February 7, 2017

The Hon. Wayne Easter, PC, MP
Chair, Standing Committee on Finance
House of Commons,
Ottawa, Ontario K1A 0A6

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 recommendations to the committee's **Comprehensive Review of Canada's Tax System**.

We are pleased to provide a brief on this on topic and the results of a recent survey of FEI Canada's members. Selected charts from this survey may be found in the Appendix attached. In brief, our members told us that:

- 69% rate the current Canadian corporate tax system as complicated;
- 71% agree each industry should have a similar tax base;
- 88% agree each industry should have a similar tax rate;
- 62% say smaller companies should have preferential/lower tax rates;
- 66% say smaller companies should have a simpler tax reporting system, such as defining taxable income as equal to accounting income;
- 79% are in favour of consolidated tax returns;
- 68% agree they would be willing to forgo some or all deductions if corporate income tax rate were lowered;
- 78% agree they would be prepared to settle tax disputes during the field audit process to avoid tax resolution procedures.

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 were drafted by members of our Policy Forum, composed of experts in these areas of responsibility.

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

Yours sincerely,

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

Norm Ferguson, CPA, CMA
Chair, Policy Forum

INTRODUCTION

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

An enormous amount of legislation was amassed over the century, as provisions were added by governments attempting to create a fair tax system, responsive to priorities of the day. However, in striving 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 ("the Act"), the time has come to review the 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, but 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 not an attempt to cover all aspects of a simplification process, FEI Canada would like to offer thoughts on principles that would form the foundation of this initiative.

1) Competitiveness

The taxation system must allow Canadian business to operate in a competitive global environment, where flow of capital is widespread and investors seek returns in varying jurisdictions.

To this end, tax rates higher than those of Canada's immediate trading partners will discourage new investment and, potentially, transfer jobs abroad.

Lower rates, with limited deductions, and the uniform application of those rates across all industry sectors, would achieve: (i) transparency and ease of understanding; and (ii) an improved platform for investment in growing businesses, as opposed to investing in those favoured by the tax system.

FEI Canada considers that broadening the tax base by reducing both rates and deductions should be largely neutral to tax revenues collected.

2) 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 CCA 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 five 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 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 obligation. Another example relates to the 50% add back of meals and entertainment expenses. These general rules, as well as other provisions, have 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 simplification. One must question the value of certain reporting required. For example, an inactive corporation held for future transactions should have a one page tax filing declaring the company is inactive and has no revenue, rather than having to file a comprehensive return. Also, a major step to simplification would be to allow companies below a certain threshold of income and/or assets to file based on accounting income with only a few minor adjustments.

d) Organization

As the Act has grown, its general organization has greatly deteriorated. A general reorganization of the Act should be undertaken. A priority should be to improve the indexing and cross-referencing on sections of the Act. This would make it easier to carry out key word searches on tax applications and would likely be more amenable to digital interrogation. Another measure 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 Act more user-friendly and significantly save time for both tax practitioners and auditors.

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3) 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 Act. Clear intention would improve both compliance by taxpayers and enforcement by the government.

b) Clarification
There are many sections in tax legislation with words leading to different interpretation and 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 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. These "holes" must be cleaned up with amending legislation, and there must be a mechanism for the continuous improvement of the legislation on a timely basis which would mean no later than once per year.

4) Administration
In addition to the increase in complexity of tax legislation, our members have experienced an increase in the complexity and thus administration of the audit and dispute resolution process. To put this into context, the number of Notices of Objection increased 88% between the 2005-2006 and 2009-2010 fiscal years.[1]

The primary reason for these alarming statistics may be attributable to our understanding that the CRA 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

[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

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 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 CRA with the utmost urgency to reduce time and resources devoted by both the government and taxpayers to resolve audit disputes.

CONCLUSION

FEI Canada members are ready to help streamline tax policy, the reporting process and the audit process. We suggest progress in these areas will help Canada become more competitive in our increasingly unpredictable global economy.

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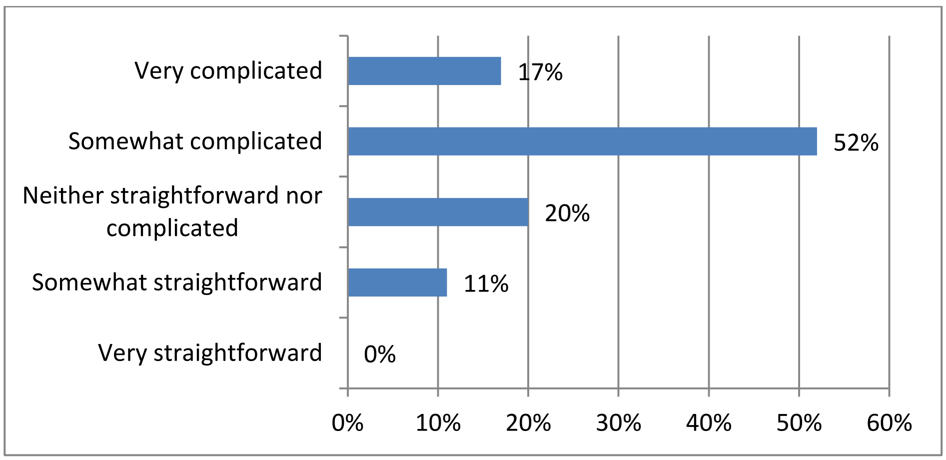
APPENDIX A

FEI Canada was invited by the House of Commons Standing Committee on Finance to provide recommendation regarding its Comprehensive Review of Canada's Tax System. In preparation for the development of these recommendations, FEI Canada surveyed its more than 1,500 members across Canada, representing all sizes and sectors of the economy. Selected members' comments are included below.

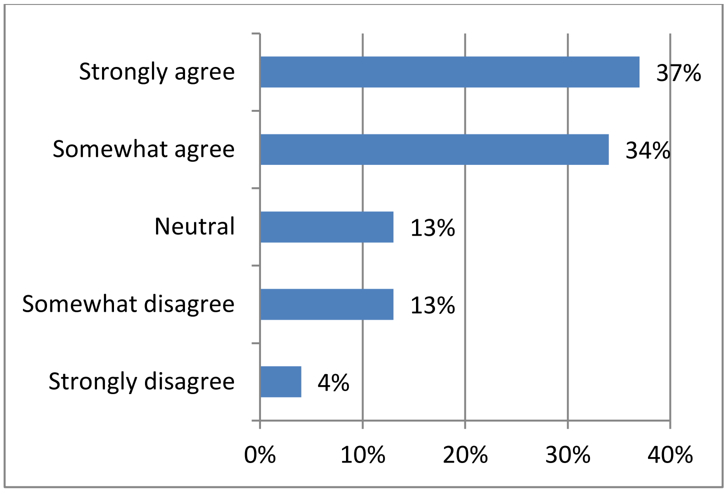
Overall, how would you rate the current Canadian corporate tax system?



"We want to pay our fair share of taxes but we should not have to spend tons of time and hire professionals to do so."

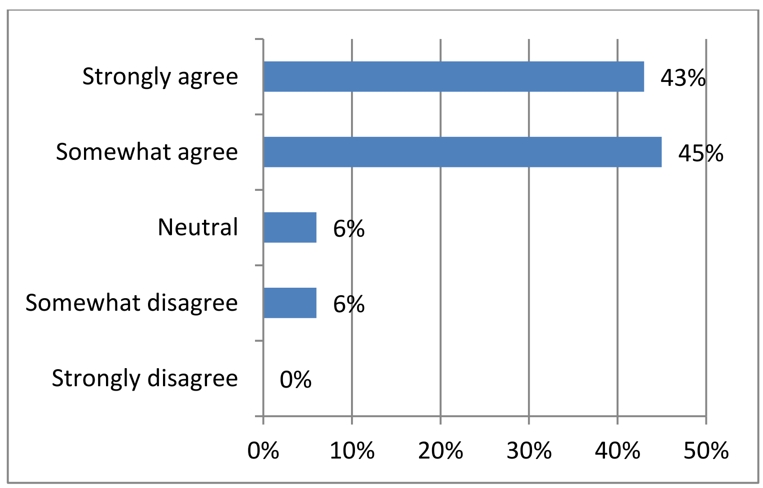
"Revisit integration and make sure rates are adjusted so that taxes are fully integrated from corporate to individual."

Each industry should have a similar tax base:



Each industry should have a similar tax rate:

"Assuming that taxes were to be used solely for the purpose of collecting revenue for government, one tax rate should apply to all businesses."



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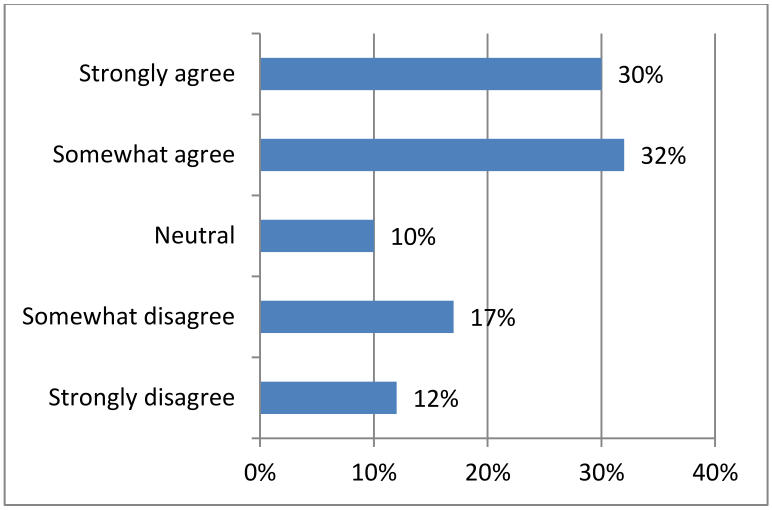
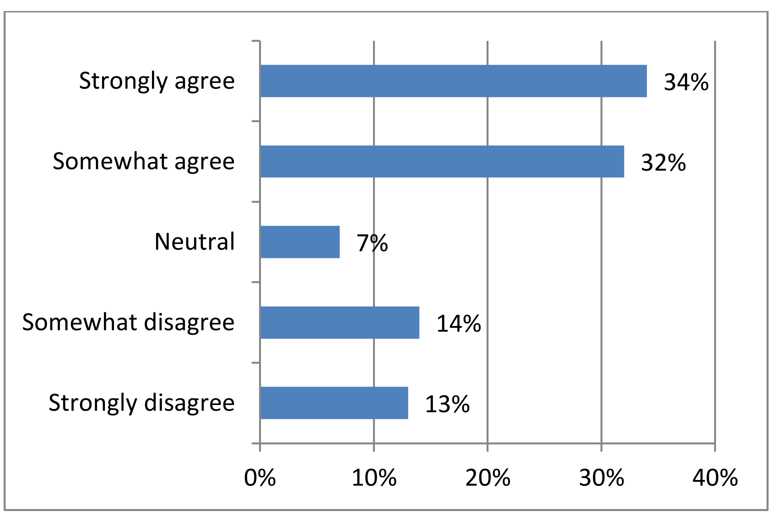
Smaller companies should have preferential/lower tax rates:

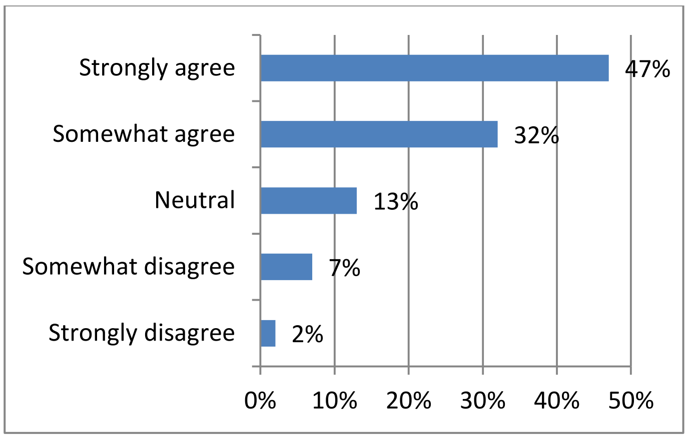


"They need to find a way to make it a lot easier for small companies who don't have the time, money and expertise to file detailed tax returns."

Smaller companies should have a simpler tax reporting system (such as defining taxable income = accounting income)



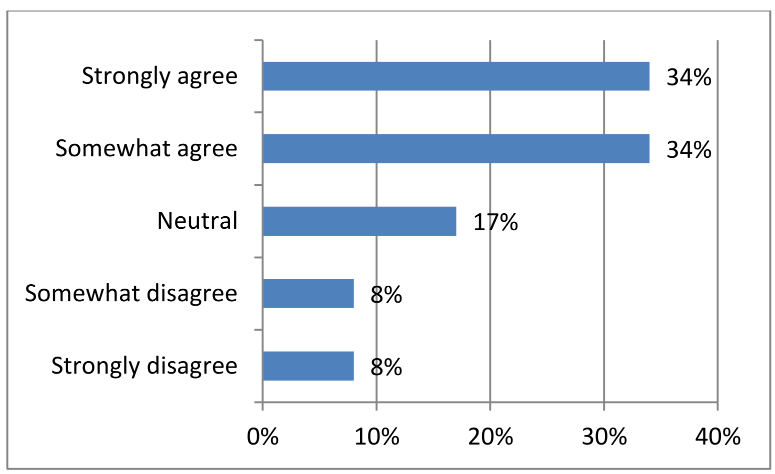
Canadian corporations should be allowed to file corporate income tax filings on a consolidated basis e.g. parent companies with subsidiaries.



"Allow tax and sales tax consolidation within a group."

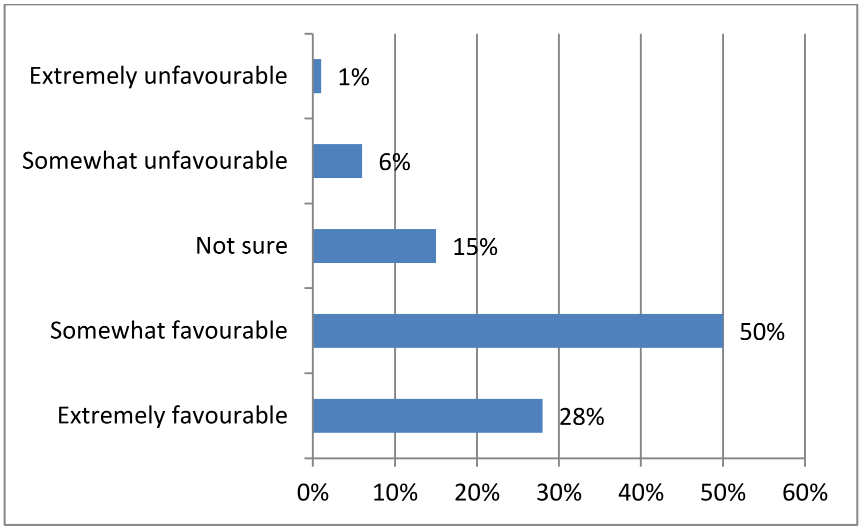
"This would allow for economic substance to govern the legal structure. Consolidated financial statements would support the tax return and eliminate the need for multiple tax returns and separate legal entity financial statements."

For simplicity, I would be willing to forgo some or all deductions if our corporate income tax rate was reduced.



"Adjust the rates to eliminate most deductions, while remaining revenue neutral."

To what extent would you be prepared to settle tax disputes during the field audit process, to avoid tax resolution procedures?

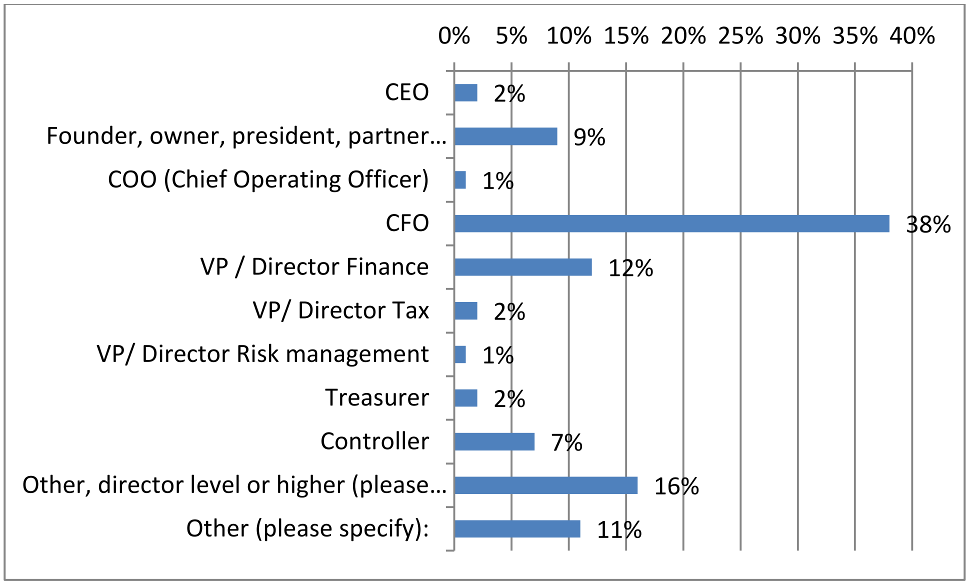


"Return to a system that allowed more open dialogue with CRA - auditors now take hard positions and simply pass files on up the line – which forces taxpayer appeals and legal time and fees."

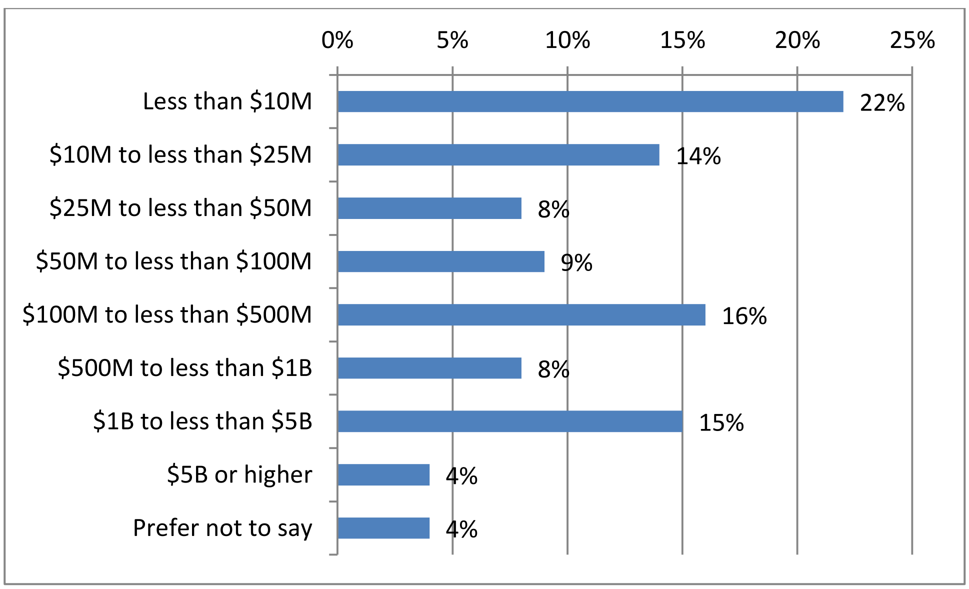
"Auditor is familiar with the situation so allow to settle and reduce the need for ongoing process."

"Would need highly skilled and objective field auditors for this to be successful."

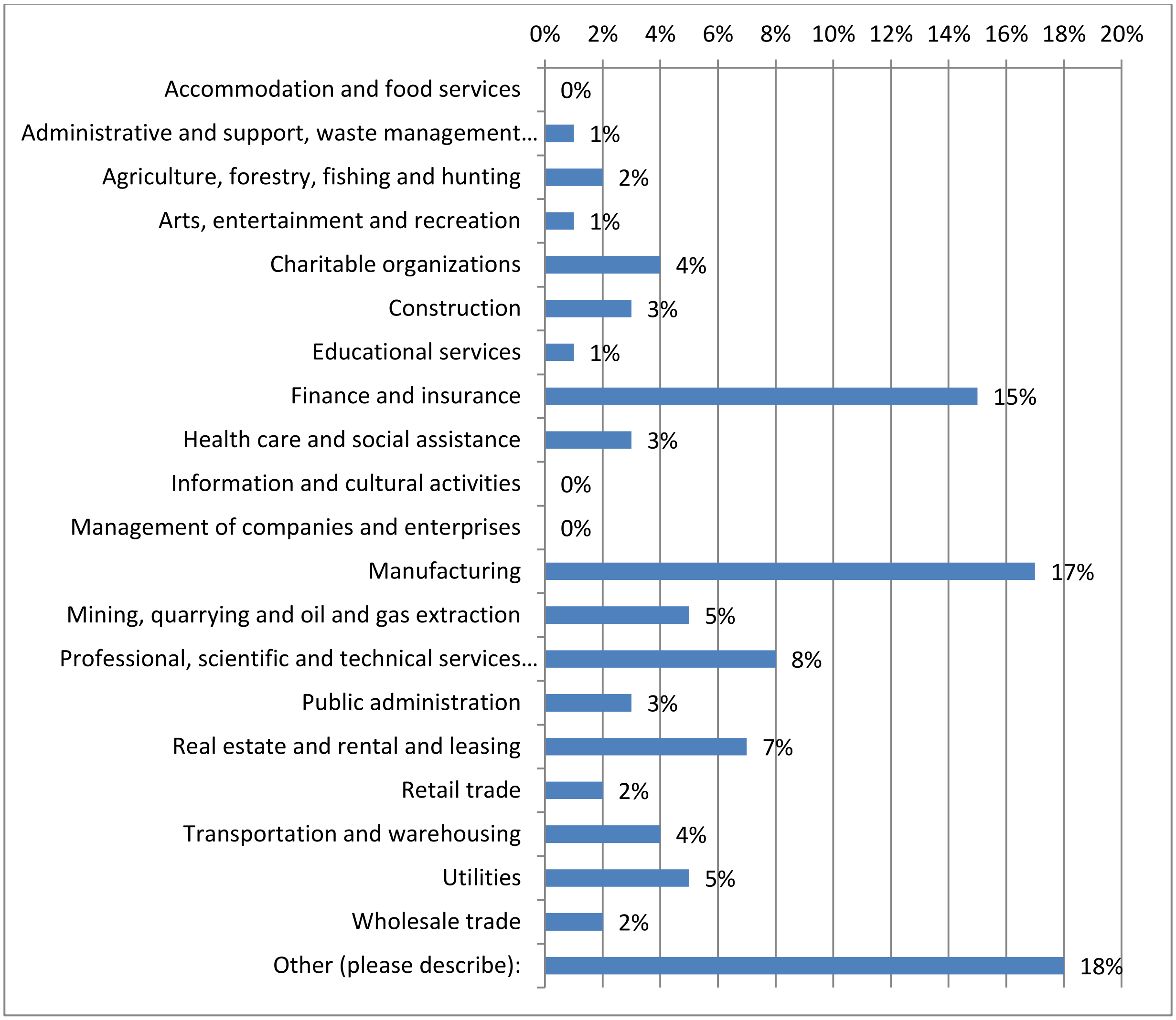
Demographics:



Revenue:



Industry:



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