

## International Tax Policy— April 2008 Consultation Paper

The Advisory Panel on Canada's System of International Taxation issued its consultation paper, [Enhancing Canada's International Tax Advantage](#), on April 25, 2008. The paper poses important questions about Canada's international taxation system and provides the Panel's initial views on a framework for improving the system. This *Tax Memo* outlines the key points.

The Panel was formed in response to a 2007 federal budget proposal. Its mandate is to make recommendations to assist the government establish an international tax policy framework for investment:

- abroad by Canadian businesses; and
- into Canada by foreign businesses.

The objective of the Panel's recommendations will be to improve the competitiveness, efficiency and fairness of Canada's system of international taxation, minimize compliance costs for businesses, and facilitate administration and enforcement by the Canada Revenue Agency.

Public comment on the consultation paper must be submitted by July 15, 2008. The Panel will provide its recommendations by December 1, 2008.

### The Current Tax Environment

In evaluating Canada's current tax environment, the Panel observes that Canada's move to lower corporate rates and its objective of achieving the lowest effective tax rate on new business investment in the G7 (i.e., the United States, Japan, Germany, the United Kingdom, France, Italy and Canada) both support a competitive international tax policy. The Panel also stated that Canada's tax policy must anticipate change in the global tax environment and have the flexibility to adapt accordingly.

### Tax Policy Framework

The Panel presented six initial views on a framework for developing Canada's international tax policy:

- **Approach to change** – Overall, Canada's international tax system has worked well. Only areas where significant improvements can be achieved should be changed.
- **Foreign investment** – The tax system should attract foreign investment. To do this, it should create a level playing field for domestic business activity carried on by foreign and Canadian businesses.
- **Outbound international tax rules** – These rules should maintain and enhance the competitiveness of Canadian businesses operating abroad.
- **Certainty and simplicity** – Tax legislation and administration should provide certainty and simplicity for taxpayers. Complexity should be avoided except, for example, when it is necessary to protect tax revenues.
- **Canada's international corporate and withholding tax regimes** – These regimes should be compared regularly to international norms. Global trends and changes should be anticipated.
- **Fairness** – Fairness in the international context needs to be clarified. The guiding principle suggested ("horizontal equity") is that taxpayers in similar situations should be treated similarly.

## Areas for Review

The Panel identified specific areas that require review. Its comments are summarized below.

### Outbound investment

Canada's international tax system for outbound investment should be retained as the basic foundation for this investment. The Panel will focus on improving the system's efficiency, simplicity and competitiveness. In particular, it will consider:

- the taxation of foreign affiliate dividends, including the scope of the exemption;
- the treatment of capital gains from the disposition of shares of foreign affiliates; and
- the allocation of costs to foreign source income.

### Inbound investment

Canada's tax rules should balance the desire for domestic and foreign businesses to obtain similar treatment while ensuring that Canadian-source income is properly measured and taxed. The Panel will consider:

- the taxation of interest expense incurred by foreign-owned Canadian corporations; and
- inbound treaty shopping.

### Withholding taxes

The Panel will review the reduction or elimination of withholding taxes on payments of non-arm's length interest, dividends and royalties to residents of other countries:

- bi-laterally, through its tax treaty network; and
- unilaterally, by amending Canada's tax laws.

## Tax-exempt organizations

The Panel wants to understand whether the increased outbound and inbound investment by tax-exempt organizations raises any issues that have to be addressed in assessing Canada's international tax system.

### Administration

To improve process, administration and/or compliance, the Panel will review the following aspects of Canada's international tax system:

- Canada's transfer pricing rules;
- withholding tax requirements for foreign services providers; and
- the collection of information by the Canada Revenue Agency.

### Other issues

The Panel acknowledges that some relevant issues may not be addressed in the consultation paper. Interested parties are invited to raise these issues in their submissions or in roundtables.

## Next Steps

Written submissions on the consultation paper will be accepted until July 15, 2008, and will be posted on the Panel's website ([www.apcsit-gcrfi.ca](http://www.apcsit-gcrfi.ca)). The Panel will provide its recommendations to the Minister of Finance by December 1, 2008.

## For Help

To discuss the issues raised by the Panel and how they may effect your particular situation or other international tax issues, please contact your PricewaterhouseCoopers adviser or any of the following individuals.

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