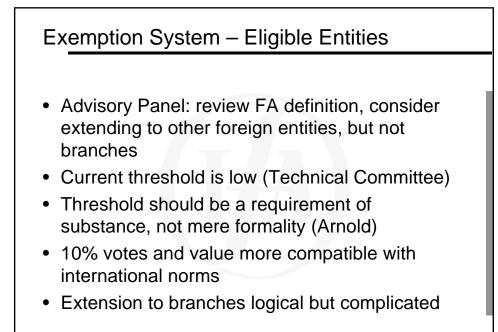
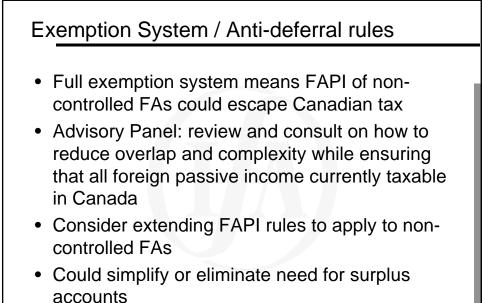
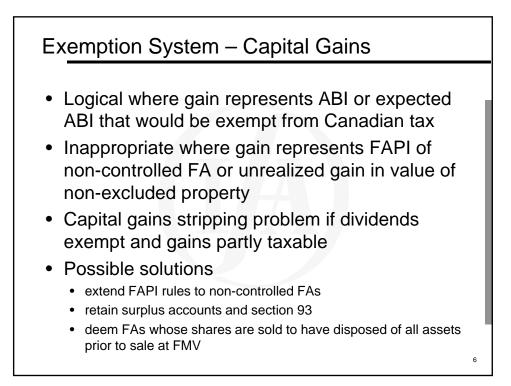


Exemption System

- Widespread support for exemption system, which involves little change from current system
- TIEAs rightly regarded as separate issue, but good reasons to encourage information sharing
- Expanded exemption system increases pressure on
 - foreign affiliate definition
 - anti-deferral rules
 - base erosion and transfer pricing rules
 - interest (and other expense) allocation rules

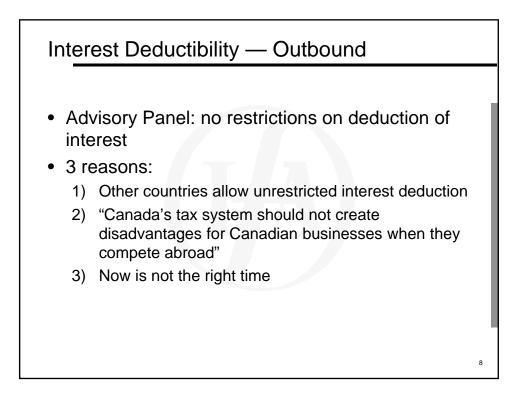


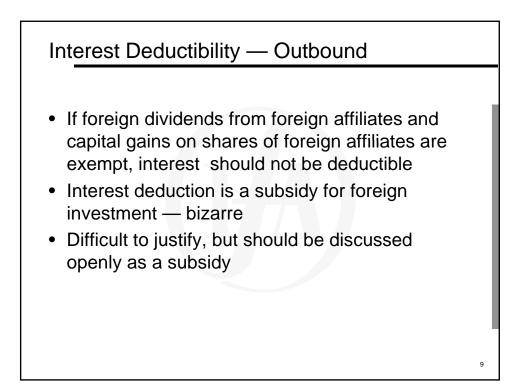


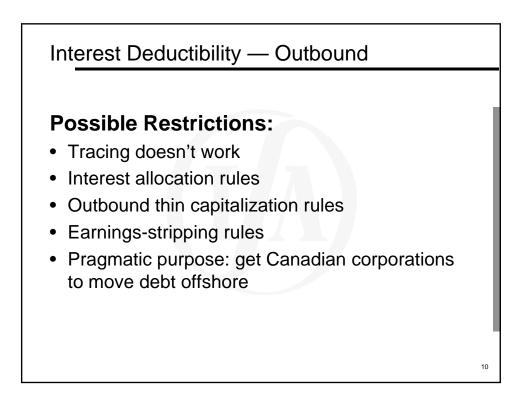


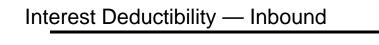
Exemption System – Capital Gains

- Arguably inconsistent to exempt gains on sale of FA shares but not shares of Canadian corporations (particularly where gain represents increase in value of a FA)
- Consider consequential changes: capital dividends, refundable tax, loss limitations
- Added pressure on inbound interest deductibility rule – if proposal is to deny interest related to "bad" foreign investments

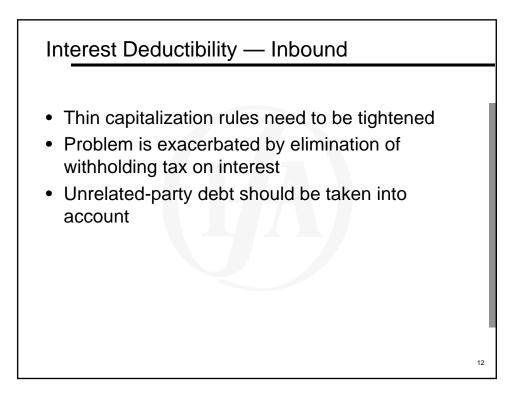






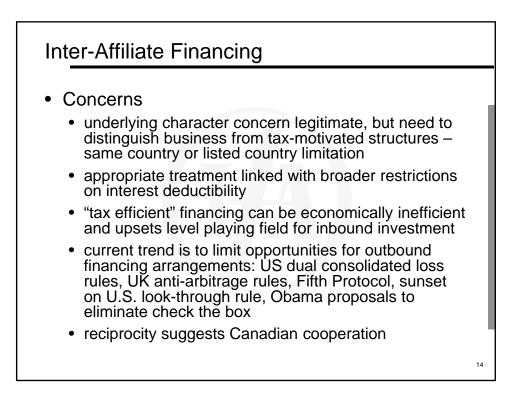


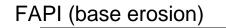
- Advisory Panel: thin capitalization rules are "sound in principle and appropriate in scope"
- Debt/equity ratio should be reduced to 1.5:1
- Rules should be extended to partnerships, trusts, and branches
- Rules should not take into account unrelatedparty debt and guaranteed debt
- Anti-avoidance rule to deal with debt dumping



Inter-Affiliate Financing

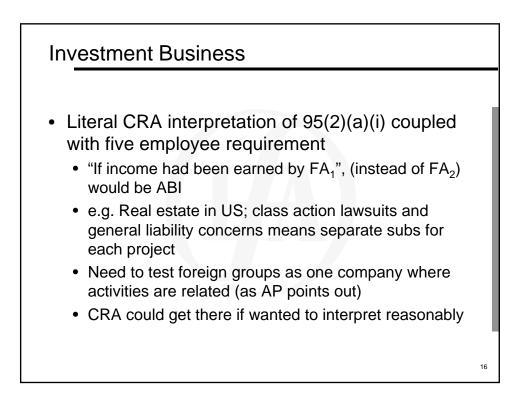
- Advisory Panel: retain 95(2)(a)(ii) as is and repeal 18.2
- Reasons:
 - preserves underlying character of ABI in global context
 - outbound financing arrangements available in other countries (U.S. check the box and look through rule, UK entity-based regime)
 - competitiveness
 - minimization of foreign taxes irrelevant from Canadian perspective





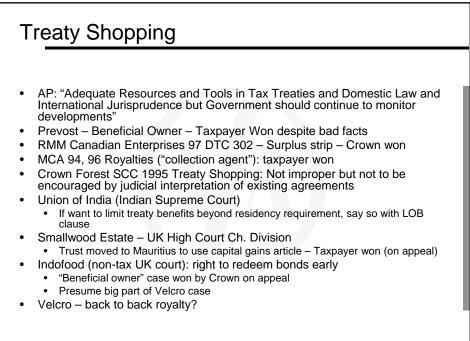
- AP: Paragraph 4.123 Base erosion rules OK for Canadian debt obligation, Canadian leasing and insurance of Canadian Risks
- Not ok: sale of foreign goods to Canco by CFA/FA where goods not originated solely in it's jurisdiction
 - Transfer pricing (ITA 247) to be guardian of Canadian FISC
 - AP: "more can be done" not sure what they want done (better ABI definition?).
 - If go with full ES system/territorial system, huge pressure on TP rules. AP saw TP issues (4.122)
 - 4.125: if FAPI applies to non-CFA "consider how rules should apply differently": What they are focusing on?
 - RGT: hard to see how will <u>not</u> be revenue loss. TP yields a range of values. So taxpayers will aim high on sales to Canadian parent. Cases will be settled in the middle-means loss of Canadian revenue. Real issue is whether business benefits outweigh loss.





FIEs and NRTs

- Not Salvageable
 - Need to start over
 - Drafting is simply too bad conceptually and technically
- FIE: If FAPI applies to FA, then much narrower scope
 - · Go with purpose test
 - Probably need "tracking" rule
 - Impute return like old 94.1 unless election to pay on actual earnings
- NRT: deemed residence concept unacceptable and commercially disastrous
 - Limit taxation impact to Canada/Canadians
 - · Extraterritoriality of proposed rules repugnant
- Overlap
 - Avoid and if must, then definitions must at least be consistent as between FAPI, FIE and NRTs
- Do not see evil of sheltering passive income with active losses
 - · really did lose money
 - a buck is a buck
- Tolerate some slippage

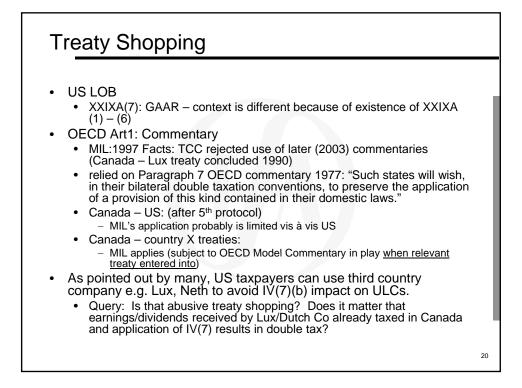


17



- MIL 2006 TCC
 - Paragraph 72: nothing inherently improper in selecting one foreign regime over another. "(referring to" dicta in Crown Forest SCC)
 - Paragraph 74: "MIL's reliance upon a treaty provision...cannot be viewed as being a misuse or abuse. Canada if concerned,...instead of applying ITA 245 should seek recourse by attempting to renegotiate selected tax treaties."
- MIL F.CA 2007
 - Paragraph 5 "We are unable to see in the specific provisions of the ITA and the treaty...Interpreted purposively and contextually and support for the argument that the benefit obtained by MIL was an abuse or misuse of the object and purpose of any of those dispositions."
 - Paragraph 7 If the object of the exempting provision was to be limited to...it would have been easy enough to say so.
 - Paragraph 8 To the extent that Crown argues that the treaty should not be interpreted so as to permit double non-taxation, the issue raised by GAAR is the incidence of Canadian taxation, not the foregoing of revenues by the Lux fiscal authorities.



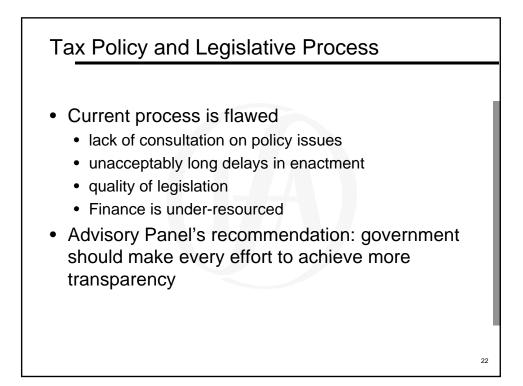




NRTs

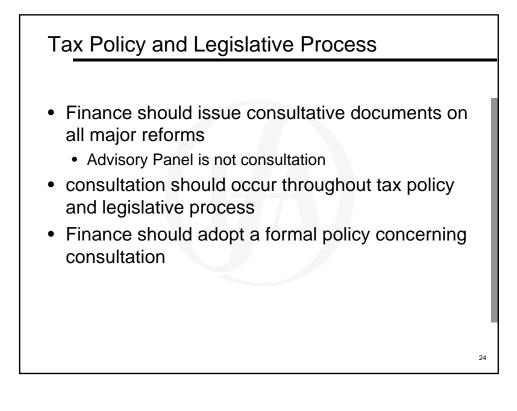
- Julien Sept 2008 Art IV(3) no order granted to force CRA to negotiate (Unenacted ITA 94)
- RCI Trust 2009 (ITA 116) : Deemed residence not "a criterion of a similar nature". Barbdos Trust with indirect Cdn beneficiary. Fed Ct ordered CRA to determine whether shares treaty exempt property but based on trust being solely Barb resident

21





- Tax policy process should be improved
- Finance should conduct its own internal review
- There should also be an external review
- Reviews should propose changes and be made public
- Canadian Tax Foundation Committee to study the process





- Tax Policy Review Board should be established to supplement tax policy work done by Finance
- Quasi-independent from Finance and CRA, but close co-operation is required
- Issues referred to Board by Finance
- But sufficient resources and authority to carry out projects on its own

