

Minister
of National Revenue



Ministre
du Revenu national

Ottawa, Canada K1A 0A6

MAY 29 2017

The Honourable Wayne Easter, P.C., M.P.
Chair of the House of Commons Standing Committee on Finance
House of Commons
Ottawa ON K1A 0A6

Dear Colleague:

The following information is pursuant to the motion adopted by the Standing Committee on Finance on April 10, 2017, and further to the Government's Response (tabled in the House of Commons on February 22, 2017, pursuant to Standing Order 109) to the Sixth Report of the Standing Committee on Finance entitled "*The Canada Revenue Agency, Tax Avoidance and Tax Evasion*". I am pleased to provide a report on progress in response to recommendations 1, 3, 5, 8, 9 and 14 of the Sixth Report.

The Government thanks the members of the Committee for their continued interest and attention to the Canada Revenue Agency's (CRA's) efforts to combat tax avoidance and evasion.

Tax evasion and aggressive tax avoidance remains a significant, global multi-billion dollar concern. As part of its commitment to cracking down on aggressive tax avoidance and evasion, the CRA will continue to build its capacity to detect and crack down on tax cheats. Furthermore, the Agency is committed to transparently communicating its activities and results to Canadians - to not only inform and improve its approaches over time - but to ensure a tax system that is responsive and fair for all.

Please find enclosed the Government of Canada's report on progress.

Sincerely,

A handwritten signature in blue ink, appearing to read "Diane LeBouthillier".

The Honourable Diane LeBouthillier, P.C., M.P.
Minister of National Revenue

REPORT ON PROGRESS: COMMITMENTS MADE IN THE GOVERNMENT'S RESPONSE TO THE SIXTH REPORT OF THE STANDING COMMITTEE ON FINANCE (RESPONSES TO RECOMMENDATIONS 1, 3, 8, 9 AND 14), AND ON RECOMMENDATION 5, AS SET OUT IN THE SIXTH REPORT

INTRODUCTION

On behalf of the Government of Canada, on February 22, 2017, the Minister of National Revenue tabled the Government's Response to 14 recommendations contained in the Sixth Report of the Standing Committee on Finance entitled: *The Canada Revenue Agency, Tax Avoidance and Tax Evasion: Recommended Actions*.

On April 10, 2017, the Standing Committee on Finance adopted the following motion:

"Given the Government's Response to the Sixth Report of the Standing Committee on Finance entitled: The Canada Revenue Agency, Tax Avoidance and Tax Evasion: Recommended Actions, tabled in the House of Commons on October 26, 2016, and specifically the following commitments set forth in the response:

- a) Concerning the Committee's first recommendation, the Minister of National Revenue committed to conducting a review of the advance tax ruling process by March 31, 2017;*
- b) Concerning the Committee's third recommendation, the Minister of National Revenue committed to reviewing the negotiated settlements guidelines and to conducting a full review of the Voluntary Disclosures Program by March 31, 2017;*
- c) Concerning the Committee's eighth recommendation, the government committed to announcing the outcomes of its review of tax expenditures in Budget 2017 on March 22, 2017;*
- d) Concerning the Committee's ninth recommendation, the Minister of National Revenue committed to reviewing the current Memorandum of Understanding between the CRA and PPSC and to updating it as appropriate; and*
- e) Concerning the Committee's fourteenth recommendation, the Minister of National Revenue committed to conducting a review of CRA instruments that deal with the issues of conflict of interest and post-employment and tasked a senior-level inter-disciplinary post-employment committee with implementing the action plan items within an aggressive timeline;*

That the Committee invite the Minister of National Revenue to report in writing on the progress made on her commitments in response to recommendations 1, 3, 8, 9 and 14 set out in the Sixth Report of the Committee."

The Government of Canada is pleased to provide a report on progress on the above-noted recommendations. In addition, the Government of Canada has also included information relating to recommendation 5, that *"The Minister of National Revenue report to the House of Commons Standing Committee on Finance regarding the progress of audits in relation to the "Panama Papers", before 1 June 2017."*

CANADA'S FIGHT AGAINST TAX AVOIDANCE AND EVASION

Through Budget funding in 2016 and 2017, the Government of Canada has committed, and is proposing, to invest close to \$1B on cracking down on tax evasion and combatting tax avoidance at home and abroad. This additional funding is expected to have federal revenue impacts of \$2.6B over five years for Budget 2016, and \$2.5B over five years for Budget 2017.

This report on progress demonstrates the Government of Canada's commitment to cracking down on aggressive tax avoidance and tax evasion.

The following document provides a report on progress for each of the above-noted recommendations. For ease of reference, the individual recommendation and the initial Government Response (as tabled on February 22, 2017) preface each report on progress.

Recommendation 1: *“The Minister of National Revenue conduct a comprehensive review of the advance tax ruling process. As part of that review, the Minister should identify ways in which efficiency and timeliness could be improved, costs could be reduced and effectiveness could be increased. This review should be completed by 31 March 2017.”*

Government Response (as tabled on February 22, 2017): *“The Government of Canada supports this recommendation. The CRA understands that tax certainty is important and that advance income tax rulings promote voluntary compliance. The Government of Canada is also committed to the global effort to address BEPS [Base Erosion Profit Shifting], led by the G20 and the OECD. Under the BEPS initiative, the CRA will exchange information on advance income tax rulings with other tax administrations to help ensure early awareness of tax planning that impacts the relevant countries. Canada made its first exchanges in December 2016.*

The CRA will conduct a review of its advance tax ruling process by March 31, 2017. The review will include engaging relevant external stakeholders to obtain feedback on the timeliness and effectiveness of the process and to identify possible improvements. The review will also consider the effectiveness of the Pre-ruling Consultation service, which has been in place since 2013. This service provides an opportunity for taxpayers to discuss a transaction prior to submitting a formal ruling request. Its goal is to make the process more timely and efficient by providing taxpayers with an early indication of the CRA position prior to submitting a formal request and to ensure that all relevant information is then submitted.”

Report on Progress:

The CRA has conducted a review of the advance income tax ruling process, which included consultations with a number of stakeholder associations. The advance income tax ruling regime is an administrative service offered by the CRA that benefits taxpayers by providing tax certainty in advance of carrying out transactions. As a result of the review, the CRA has determined that there are opportunities to improve the process. Key changes to the advance income tax ruling process are currently being finalized by senior CRA officials with the intention of implementing changes before the end of the year.

The key changes are:

- The CRA will implement more frequent and better communications between the taxpayer and the CRA, including a meeting with taxpayers to be held within 4 weeks of receipt of an advance income tax ruling request. Such a process would supplement the current pre-ruling consultation service. The objective of this change is to improve the CRA's engagement, provide an earlier indication of the CRA's view on the ruling requested and provide earlier feedback on the quality and sufficiency of the tax submissions for the ruling requested.
- The CRA will increase awareness on the advance income tax ruling process by conducting workshops at tax conferences and/or courses sponsored by national tax organizations; reviewing and updating the advance income tax ruling process Information Circular (IC 70-6) more frequently to provide clearer instructions on the process requirements, including revisions resulting from this review; and providing a sample “best practice” advance income tax ruling request. The objective of this change is to improve the quality of advance income tax ruling submissions in order to avoid undue time delays.

- Though the CRA will retain and meet the current 90-day service standard for advance income tax rulings, the standard will be amended to exclude complex tax policy issues that cannot typically be completed within this time, namely, those that require a formal referral to the CRA's General Anti-Avoidance Rule Committee, the Department of Finance or the Department of Justice. The objective of this change is to set expectations for taxpayers at the outset by providing them with a better indication of the timelines by which those advance income tax rulings can be completed.
- The CRA will develop guidelines for the provision of advance income tax rulings on questions of fact. The objective of this change is to clarify public guidance and provide taxpayers with parameters on which "question of fact" can be addressed.
- The CRA will develop guidelines for instances where it refuses to rule on the tax consequences of transactions for which there is little or no ambiguity and/or the position of the CRA is, or should be, well known to taxpayers. In this regard, the CRA will clarify generic guidance on common tax arrangements. The objective of this change is to limit requests for advance tax rulings to the unique aspects of otherwise common arrangements.
- To ensure that the CRA continues to provide accessible and high quality advance income tax rulings, where a taxpayer has not responded either to a request for additional information within 30 calendar days, or it has not been properly prepared or supported with adequate representations, the file will be closed.

Recommendation 3: *“The Canada Revenue Agency conduct a comprehensive review of its Voluntary Disclosures Program. As well, it should review the guidelines that are used to determine whether to pursue litigation or to seek a settlement with individuals or organizations that have engaged in tax avoidance or tax evasion. These reviews should be completed by 31 March 2017.”*

Government Response (as tabled on February 22, 2017): *“The Government of Canada supports this recommendation. Both voluntary disclosures and audit settlements require expertise to balance competing objectives, such as fairness, legal risk, revenue maximization, and deterrence.*

Voluntary Disclosures Program

The CRA will complete a review of the Voluntary Disclosures Program (VDP) by March 31, 2017. Further to the spring 2016 Committee hearings, the Minister of National Revenue sought input from the Offshore Compliance Advisory Committee (OCAC), an independent expert advisory committee providing her and the CRA with recommendations to combat offshore tax evasion and aggressive tax planning, including on the VDP. The OCAC provided its first report to the Minister on December 5, 2016, on the subject of the CRA’s VDP.

The Minister and the CRA will leverage OCAC’s recommendations as part of the review. It is expected that the review will result in some changes to tighten the criteria for acceptance into the program, which is consistent with the CRA’s strategic direction. The CRA will also share any proposed changes to the VDP with Canadians for input after completing the review, given the importance of this issue.

Audit Settlements

The CRA strives for effective and efficient resolution of audit files; the CRA only settles audit files on a principled basis in accordance with legislation that we administer (Income Tax Act, Excise Tax Act and other fiscal legislation).

As it is equally important for the CRA to be transparent about the process of negotiated audit settlements, the CRA will review its guidelines by March 31, 2017. With regards to tax evasion cases, these criminal matters are handled by the Public Prosecution Service of Canada.”

Report on Progress:

The Government of Canada has conducted a review of the VDP and of the negotiated audit settlements guidelines.

Voluntary Disclosures Program

The Agency is proposing several changes to tighten the access to the VDP and the relief that can be provided in order to ensure that the program continues to promote appropriate taxpayer behaviour.

As part of its review of the VDP, the CRA leveraged the advice and recommendations made by the OCAC in its report on the VDP issued in December 2016. The OCAC endorsed the continuation of the VDP as an integral part of the CRA's administration and enforcement regime, and proposed to tighten the criteria for acceptance into the program to ensure fairness of the tax system.

In an effort to transparently communicate our activities to Canadians, the CRA will soon make its revised VDP policy available on the CRA's website for external consultation.

Following external consultations, the CRA will finalize its revised VDP policy in the fall of 2017. Canadians will be advised of the release of the updated policy and its implementation date at that time.

Audit settlements

The CRA has completed a review of its written internal guidance on the audit settlement process, in consultation with the OCAC, and will update its guidance on the audit agreements and the waiver of objection rights, by October 31, 2017. The changes will provide an opportunity for the CRA to update procedural aspects and terminology contained in the guidance to improve the governance of the audit settlement process.

The key change is the launch of an audit settlement approval process in the fall of 2017, which will involve mandatory referrals to a new Audit File Resolution Committee (AFRC) in certain circumstances, such as cases involving significant dollar amounts and/or international transactions.

The AFRC's mandate will be to formalize oversight and due diligence over the settlements, to support the reasonable application of the tax laws to ensure protection of the tax base, and to provide consistency, predictability and fairness to the settlements in the context of the income tax system. The AFRC will include senior representatives from the CRA headquarters, regions and the Department of Justice.

Recommendation 8: *“The federal government, in an effort to reduce complexity and any inequities that distort behaviour and can lead to tax avoidance or tax evasion, accelerate its review of the Income Tax Act and expeditiously implement initiatives aimed at simplifying the income tax system. This review should be completed by 30 June 2017. The House of Commons Standing Committee on Finance should study those initiatives and any resulting proposed legislative amendments as part of its planned review of the Act.”*

Government Response (as tabled on February 22, 2017): *“The Government of Canada supports this recommendation. In recognition of concerns that have been expressed regarding the efficiency, fairness and complexity of the tax system, the Government of Canada announced, in Budget 2016, the undertaking of a comprehensive review of federal tax expenditures over the coming year. The objective of the review is to ensure that federal tax expenditures are fair for Canadians, efficient and fiscally responsible. This review is part of a broader Government commitment to eliminate poorly targeted and inefficient programs, wasteful spending, and ineffective and obsolete Government initiatives.*

The review of federal tax expenditures is led by the Department of Finance, with the support of a group of external experts. The Government will update Canadians on the outcomes from the review through Budget 2017.”

Report on Progress:

Budget 2017 takes initial action to implement changes resulting from its comprehensive review of federal tax expenditures. More specifically, Budget 2017 announced actions to further enhance the fairness, efficiency and effectiveness of the tax system, including the elimination of 12 tax expenditures and modifications to 6 other measures.

Measures eliminated in Budget 2017:

- Accelerated deductibility of some Canadian Exploration Expenses
- Additional deduction for gifts of medicine
- Use of billed-basis accounting by professionals
- Exemption for insurers of farming and fishing property
- First-Time Donor's Super Credit
- GST/HST rebates for tour package accommodations
- Investment tax credit for child care spaces
- Non-taxation of allowances for members of legislative assemblies and certain municipal officers
- Non-taxation of benefits in respect of home relocation loans
- Public Transit Tax Credit
- Reclassification of expenses renounced to flow-through share investors
- Surtax on the profits of tobacco manufacturers

Measures modified in Budget 2017:

- Caregiver Credit
- Infirm Dependant Credit
- Family Caregiver Tax Credit
- Disability Tax Credit
- Application of the GST/HST to taxi and ride-sharing services
- Tuition Tax Credit

The measures proposed in Budget 2017 will lead to a simpler and fairer tax system, and will make existing tax measures more effective and accessible to Canadians.

The Government remains committed to building a fair tax system that benefits the middle class and those working hard to join it. Going forward, the review of federal tax expenditures will continue to inform the Government's ongoing work to make the tax system simpler, fairer and more efficient.

As indicated in Budget 2017, the Government will continue in 2017 to take concrete steps to close tax loopholes, crack down on tax evasion, improve tax relief for the middle class, and eliminate measures that are ineffective and inefficient, and that disproportionately benefit the wealthy. Notably, Budget 2017 highlights a number of tax planning strategies that make use of private corporations, and indicates that the Government will be further reviewing the use of these strategies. As announced in the Budget, the Department is preparing a consultation paper that will set out the nature of these issues in more detail as well as proposed policy responses. Also, as part of the whole-of-government review of business innovation programs that was initiated in Budget 2017, work will be undertaken in parallel to review the Scientific Research and Experimental Development tax incentive program to ensure its continued effectiveness and efficiency.

Recommendation 9: *“The federal government take steps to improve coordination between the Canada Revenue Agency, which investigates situations of possible tax evasion, and the Department of Justice, which prosecutes cases of tax evasion.”*

Government Response (as tabled on February 22, 2017): *“The Government of Canada supports this recommendation. The Public Prosecution Service of Canada (PPSC), not the Department of Justice (JUS), is responsible for the prosecution of tax evasion. A close relationship between the CRA, JUS and PPSC ensures that cases investigated and referred for prosecution are of the highest quality. The CRA will review the current Memorandum of Understanding between the CRA and PPSC and update it as appropriate to enhance cooperation and engage on ways to advance cases.*

With the Budget 2016 investment, the CRA will increase cooperation with JUS and PPSC. The CRA will seek the assistance of dedicated JUS lawyers on various regulatory, legislative, and policy issues throughout the criminal investigations stage of cases of alleged tax evasion.”

Report on Progress:

The CRA has updated the current Memorandum of Understanding (MOU) between the CRA and PPSC, with the intention of finalizing and signing a revised version by September 30, 2017.

The MOU will enhance the communication between the organizations and clarify responsibilities from the commencement of a criminal investigation through to verdicts and sentence rendered. The processes outlined, along with service standards, will enable both organizations to work cooperatively while respecting each other's roles, to ensure a timely completion of a case that meets the principles of justice.

The MOU will be used as a tool to achieve the important public policy goal of compliance with tax laws through effective investigations and prosecutions, and to ensure that the appropriate cases are criminally investigated and prosecuted. Once signed by all parties, the MOU will set a solid foundation to address areas of mutual interest and will serve to enhance the working relationship.

Recommendation 14: *“The Minister of National Revenue conduct a broad-based review of the Canada Revenue Agency’s code of conduct for current employees and employees who are leaving the Agency. This review should be completed by 31 March 2017.”*

Government Response (as tabled on February 22, 2017): *The Government of Canada supports this recommendation. The CRA recognizes the importance of integrity, maintaining Canadians’ trust, and has already taken action.*

In May 2016, the Minister of National Revenue tasked the CRA Board of Management with conducting a review of CRA instruments that deal with the issues of conflict of interest and post-employment. This included the CRA Code of Integrity and Professional Conduct, and the Directive on Conflict of Interest, Gifts and Hospitality, and Post-employment. This review and the associated summary of observations have been completed and highlight opportunities to strengthen the CRA’s post-employment instruments and approach to post-employment situations. An action plan has been developed, and a senior level inter-disciplinary Post-employment Committee (PEC) has been struck. The PEC is tasked with implementing the action plan items within an aggressive timeline.”

Report on Progress:

A review of CRA instruments that deal with the issues of conflict of interest and post-employment was completed. As a result of the review, an action plan was developed and an executive level post-employment committee (PEC) was formed and tasked with implementing the action plan items. The PEC includes representatives from corporate and program branches, and from the regions.

To date, completed action items are as follows:

Language was added to the Directive on Conflict of Interest, Gifts and Hospitality, and Post-Employment to articulate management responsibility vis-à-vis the post-employment process, and a comprehensive communications package was shared with all CRA managers.

- The first quarterly report on management compliance with the newly articulated post-employment responsibilities was delivered to the CRA’s Board of Management in April 2017. Subsequent reports will follow quarterly.

PEC also has several action items in progress, which it intends to complete over this fiscal year as follows:

- Using an established risk assessment protocol, the CRA has determined which program areas may pose greater risks for post-employment issues. Targeted approaches to address identified risk areas are being drafted.
- A draft plan to engage external stakeholders on the post-employment obligations and restrictions applicable to former CRA employees.
- Draft procedures for capturing situations where former CRA employees attempt to gain privileged access or preferential treatment.

Recommendation 5: *“The Minister of National Revenue report to the House of Commons Standing Committee on Finance regarding the progress of audits in relation to the “Panama papers.” The report should be made before 1 June 2017.”*

Government Response (as tabled on February 22, 2017): *“The Government of Canada supports this recommendation. The CRA had received information from a number of sources prior to the International Consortium of Investigative Journalist’s coverage of the Panama Papers. Through active international collaboration and domestic sources, the CRA has gathered additional information during 2016, including from Canadian banks. The CRA has analyzed over 11.5 million documents leaked through the media related to the Panama Papers and identified over 2,600 records with a link to Canada. There are 85 taxpayers identified for further review; 60 of these taxpayers are under audit.*

The CRA continues to collaborate with other jurisdictions and is leading the detailed work on mapping the structure of the tax schemes. While the complexity of the audits make it unlikely that any will be fully resolved by June 1, 2017, the CRA will report on its approach, results to date and other project findings.”

Report on Progress:

The Government of Canada is pleased to report on the progress of audits and criminal investigations in relation to the Panama Papers.

The CRA is working in close collaboration with its domestic and international partners to share findings on the Panama Papers and is committed to supporting any ongoing international audit or investigation, where warranted. For example, in January 2017, CRA participated in the largest simultaneous exchange of information under tax treaty, through the OECD’s Joint International Task Force on Shared Intelligence and Collaboration (JITSIC).

The CRA has been able to conduct risk assessment on 1,300 names to date. Of these names, 860 were determined to be non-residents of Canada; for those where residency was determined, the CRA is in the process of sharing some of the information with the resident country, provided a tax treaty exists.

As of April 1, 2017, there are 122 audits underway and several criminal investigations are ongoing involving both participants and facilitators. The CRA is leveraging the expertise of its Promoter Compliance Center to identify any Canadian promoters associated with these offshore structures and has already publically stated that barring any exceptional circumstances, the CRA is not in a position to accept VDP requests from taxpayers involved in the Panama Papers.

In addition to the ongoing criminal investigations, the CRA has also identified 64 other potential files that warrant further review to determine links to offshore files or transactions and assessment potential for further investigation.

These audits and criminal investigations are very complex and may take years to complete.

In criminal investigations, the complexity, amongst other things, rests with following the money and legally obtaining the evidence from various jurisdictions in order to prove beyond a reasonable doubt that tax evasion has been committed. The CRA cannot disclose any further information on the ongoing audits and criminal investigations nor the investigative steps that are being taken as this would jeopardize any ongoing work in Canada or elsewhere in the world.