

*Income Tax Act*

During the Rasminsky-Lawson study representatives of the Canadian Banking Association met with them on several occasions. The study was delivered to the Government in May, 1985, but not released until March, 1986.

The study concluded that Canadian efforts to develop an international banking centre would meet intense competition from the existing centres and from other places with potential as great as ours, and that it would be unwise to force the issue by vigorous tax competition. If the view is taken that rich priorities should be given to increasing Canada's role in international financial affairs, it was their opinion that the way to pursue that goal is to take care that the tax arrangements in Canada are no less favourable than they are in the major international banking centres and that foreign banks in Canada are given as much flexibility for their international operations as they are given in those centres.

Following on that point, many observers have suggested that if Canada really wants to increase the activity of our banks in foreign affairs and if some of the business now done in the Caymans and such places is to be brought back to Canada, the real answer is to make some changes in the withholding tax. There is no mention of that in this measure before us. It is a very simple, limited measure that will give a tax break to Canadian banks in respect of deposits from or loans to foreign customers, transacted in an international banking centre. It is a measure that excludes most of the paper, where the real activity is at the present time. In fact, it is a boondoggle, not any kind of enhancement of the roles of those two cities.

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The measure before us will not enhance the role of our banks in international banking. If the Government really wanted to bring back offshore business, it would negotiate the bilateral tax treaties providing for exemption from source country taxation on commercial loan interest payments flowing between the two contracting states.

Let me quote from the expert I mentioned before, Mr. McKie. In a recent interesting article on European taxation, he also gives the history of IBC's. Let me quote a little of the history to point out how different the situation in New York was before the establishment of international banking facilities there, and our present situation. Mr. McKie refers to the efforts of New York state bankers between 1978 and 1981 to obtain legislative authority for the creation of a free banking zone in the state so they could compete with the so-called cubicle banks abroad. He said:

Under the proposal, banks would be allowed to establish special facilities in New York to conduct foreign transactions without paying state franchise taxes or being subject to federal reserve rules or deposit interest ceilings.

I would emphasize that those were the key changes that the American banks wanted at that time, but the proponents were not seeking any federal income tax concessions. Somehow, with this strange measure before us, we find federal income tax concessions being offered to banks who do not want them, and never asked for them, as an encouragement to do a very

limited amount of business which is very finite, while there is no incentive here to do the really profitable business.

I return to Mr. MacKay's account of what happened in New York:

Persuaded that these international banking facilities would generate jobs and spillover benefits, even the state's tax commissioner became an advocate of the proposal. The inevitable outcome was that in December 1981 appropriate legislation was enacted, bringing IBF's into existence, not only in New York but in many other states as well. Foreign banks, including Canadian banks, created IBF's in the U.S. The development and growth of U.S. IBF's is interesting, but it is generally agreed that the great expectations of the advocates have not been realized.

That, however, is another story which seemingly escaped the notice of the Canadians who were enthusiastically advocating international banking entities in Canada using all the U.S. hyperbole that so soon proved to be illusory.

Mr. McKie goes on to discuss various meetings in 1981 and so on. The banks continued to be less than enthusiastic about the IBC proposals. The requests for IBC were coming from chambers of commerce and others. People who had heard all the New York estimates of job creation naturally wanted this good thing for their communities.

According to Mr. McKie, as far back as 1983, the banks explained that:

—unlike the U.S. banks, they were not inhibited by banking regulations in their international transactions, and that freedom from Canadian income tax on an IBC's profits would not be any great incentive when the major hurdles to handling international operations from a Canadian permanent establishment were Canada's foreign tax credit procedure and the gross withholding taxes imposed by foreign countries on loan interest flowing into Canada.

That was the position which the Finance and Economic Affairs Committee took. The finance committee examined the whole issue of international banking centres. We went to New York, where we had extensive consultations with bankers, with people in various commercial institutions, and with the New York tax authorities. The finance committee's unanimous report was that this measure before us, which gives federal income tax concessions to banks, which either in Vancouver or Montreal make loans to or take deposits from foreign customers, is unlikely to do very much to bring back offshore banking business to Canada or unlikely to do anything to enhance economic activity in those two cities.

Montreal and Vancouver have very interesting geographical positions; Montreal in relation to Europe, Vancouver in relation to the Pacific Rim countries. They are both cities with high rates of unemployment. I am sure that every Member in the House would support the Government's desire to help those cities revitalize their economies and create jobs. This measure will not do it. This is a boondoggle which has been sold to people in Montreal and Vancouver as a job creator, which it is not. The Government has set city against city, region against region, for no reason whatsoever.

There is a long list of people who advised the Government that this measure would not do anything constructive, but did advise the Government on ways to bring international banking business to Canada if it wanted to do so. All this advice has been ignored.