Recommendation

The current 45 per cent ceiling on provisions allowable for tax purposes should be retained, but banks should be able to claim an additional loss on the difference between the amount already claimed and the total loss only when the Third World assets are written down or sold in ways which reduce the burden on the debtor countries.

Response

The Government believes that the effects of changing the tax code in the manner suggested in the Report would likely have little effect. Those Canadian banks which have already sold off most of their developing country loan portfolios would not be affected by the proposed change in the tax code. The other Canadian banks which continue to hold relatively large amounts of sovereign debt have been active users of Brady Plan operations or other conversion options. As a result, they are already disposing of their loans in ways which provide benefits to debtor countries.

Other dispositions, such as on the secondary market, can also have a benefit for the debtor, for example, when the debt is used to engage in the financial restructuring of distressed domestic corporations or when the ultimate result of a sale in the secondary market is a debt-for-equity swap. Changing the tax provision would merely change one favourable type of disposition now taking place in the secondary market for another with no additional net benefit for the debtor country.

A final concern is that skewing tax relief in the manner proposed would run counter to the broad tax policy objective of promoting and preserving tax neutrality. As a result, a bank could be penalized by being denied a legitimate deduction from income because of a loss, which is currently available to all financial institutions on other loans regardless of their origin.

Recommendation

Canada should advocate the adoption of additional debt concessions by the Paris Club members on official bilateral debt, in particular for the poorest and the most seriously affected. In responding to this recommendation the Government should table detailed proposals showing how they will apply to Canada's loans.

Response

The Government agrees that many debt-distressed, low-income countries need additional debt reduction. Canada favours debt reduction which is linked to economic reform and measures to foster sustainable development, including the use of counterpart funds.

At the Houston Economic Summit, leaders recommended that the Paris Club review additional measures to alleviate the debt burden in including a review of Toronto Terms for the poorest. Since then the U.K. and the Netherlands have made specific