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THIRD SESSION—TWENTY-EIGHTH PARLIAMENT

1970-71

THE SENATE OF CANADA

PROCEEDINGS

OF THE

STANDING SENATE COMMITTEE ON

BANKING, TRADE AND COMMERCE

The Honourable SALTER A. HAYDEN, *Chairman*

No. 36

WEDNESDAY, OCTOBER 6, 1971

Second Proceedings on:

"Summary of 1971 Tax Reform Legislation"

(Witnesses—See Minutes of Proceedings)

24206—1

THE STANDING SENATE COMMITTEE ON
BANKING, TRADE AND COMMERCE

The Honourable Salter A. Hayden, *Chairman*

The Honourable Senators,

Aird	Grosart
Beaubien	Haig
Benidickson	Hayden
Blois	Hays
Burchill	Isnor
Carter	Lang
Choquette	Macnaughton
Connolly *(Ottawa West)*	Molson
Cook	Smith
Croll	Sullivan
Desruisseaux	Walker
Everett	Welch
Gélinas	White
Giguère	Willis–(28)

Ex officio members: Flynn and Martin

(Quorum 7)

Order of Reference

Extract from the Minutes of the Proceedings of the Senate, September 14, 1971:

"With leave of the Senate,

The Honourable Senator Hayden moved, seconded by the Honourable Senator Denis, P.C.:

That the Standing Senate Committee on Banking, Trade and Commerce be authorized to examine and consider the Summary of 1971 Tax Reform Legislation, tabled this day, and any bills based on the Budget Resolutions in advance of the said bills coming before the Senate, and any other matters relating thereto; and

That the Committee have power to engage the services of such counsel, staff and technical advisers as may be necessary for the purpose of the said examination.

After debate, and—

The question being put on the motion, it was—

Resolved in the affirmative."

Robert Fortier,
Clerk of the Senate.

24206—2

Minutes of Proceedings

Wednesday, October 6, 1971.

(43)

Pursuant to adjournment and notice the Standing Senate Committee on Banking, Trade and Commerce met this day at 9:30 a.m. to further consider:

"Summary of 1971 Tax Reform Legislation".

Present: The Honourable Senators Hayden (*Chairman*), Aird, Beaubien, Benidickson, Burchill, Carter, Connolly (*Ottawa West*), Cook, Desruisseaux, Flynn, Gelinas, Giguere, Haig, Hays, Isnor, Lang, Molson, Smith, Sullivan, Walker and Welch—(21).

Present, not of the Committee: The Honourable Senator Heath—(1).

In attendance: The Honourable Lazarus Phillips, Chief Counsel; Mr. C. Albert Poissant, C.A., Tax Consultant.

Upon motion it was Resolved that 1000 copies in English and 400 copies in French of these proceedings be printed instead of the usual 800 English and 300 French copies.

WITNESSES:

The Canadian Chamber of Commerce:

Mr. Neil V. German, Q.C., President;
Mr. Brock Bradley, Chairman, Executive Council;
Mr. H. P. Crawford, Q.C., Chairman, Public Finance and Taxation Committee;
Mr. D. M. Parkinson, member, Public Finance and Taxation Committee;
Mr. C. B. Mitchell, member, Public Finance and Taxation Committee;
Mr. C. Gajewski, member, Public Finance and Taxation Committee;
Mr. E. Newman, member, Public Finance and Taxation Committee;

Secretariat: (C.C.C.)

Mr. C. H. Scoffield, General Manager;
Mr. D. J. Gibson, Manager, Policy Department.

At 11:20 a.m. the Committee proceeded to the next order of business.

ATTEST:

Frank A. Jackson,
Clerk of the Committee.

The Standing Senate Committee on Banking, Trade and Commerce

Evidence

Ottawa, Wednesday, October 6, 1971.

The Standing Senate Committee on Banking, Trade and Commerce met this day at 9.30 a.m. to give consideration to the Summary of 1971 Tax Reform Legislation, and any bills based on the Budget Resolutions, in advance of the said bills coming before the Senate, and any other matters relating thereto.

Senator Salter A. Hayden (*Chairman*) in the Chair.

The Chairman: Honourable senators, I call the meeting to order. This morning we have the representatives from the Canadian Chamber of Commerce to present their brief in connection with our consideration of Bill C-259.

Sometime during the morning, I expect that either the Honourable Mr. Pepin or someone delegated by him will come in to express their views in connection with three amendments to the Employment support bill, which we discussed last evening. When that happens, I suggest we interject it into our proceedings—it may take about ten minutes—so that we can report that bill this afternoon.

Hon. Senators: Agreed.

The Chairman: Furthermore, we adjourned the consideration of the private bill, S-22, to incorporate United Bank of Canada, until this morning. However, we had given an appointment to the Canadian Chamber of Commerce for 9.30 this morning. Our procedure should be, therefore, to go ahead and hear them and finish their presentation. I suggest that we fix 3 o'clock this afternoon to hear further representations from the United Bank of Canada.

Senator Beaubien: The Senate will sit at 2 p.m.

The Chairman: I do not think it will be a long sitting. Therefore, 3 o'clock would be a good time. The main point is that, having brought the United Bank of Canada representatives here, we should dispose of them today. Is that agreed?

Hon Senators: Agreed.

The Chairman: Honourable senators, I think we should have a motion for the printing of the proceedings.

> Upon motion, it was *resolved* that a verbatim report be made of the proceedings and to recommend that 1,000 copies in English and 400 copies in French be printed.

The Chairman: Honourable senators, the Canadian Chamber of Commerce delegation consists of Mr. Neil V. German, Q.C., President of the Chamber; Mr. Brock Bradley, Chairman of the Executive Council; Mr. H. P. Crawford, Q.C., Chairman of the Public Finance and Taxation Committee; Mr. D. M. Parkinson, Mr. C. B. Mitchell, Mr. C. Gajewski and Mr. E. Newman, members of the Public Finance and Taxation Committee; and two members of the Secretariat; Mr. C. H. Scoffield, General Manager; and Mr. D. J. Gibson, Manager, Policy Department.

We have established a practice here that we hear a summation or a statement, rather than hear the brief read. The brief has been in our hands for quite a while and we can enter into a discussion on it a little later. I understand Mr. Crawford will make the opening statement.

Mr. H. P. Crawford, Q.C., Chairman, Public Finance and Taxation Committee, Canadian Chamber of Commerce: Mr. Chairman and honourable senators, when you read the submission you probably noticed, that for the most part it was extremely detailed, in terms of suggesting that the wording of a particular subclause, a particular paragraph of a particular subsection, may be inappropriate. It seems better that I should state what we regard as several of the more important points in the submission.

First of all, I would refer you to the general points made, commencing on page 2. There are four recommendations there. Recommendation 1, in substance, is our suggestion that the procedure of the Department of National Revenue for issuing information bulletins and stamp tax rulings, in the context of tax reform and uncertainty at this time, is even more significant and more important than it has been heretofore under the existing law.

Since that was written there have been one or two developments that make this even more troublesome. For reasons that I think are understandable the Department of National Revenue has indicated that it will be some time before it can issue any interpretation bulletins, because it is going to take the department some time to organize and decide how it is going to interpret various provisions. Moreover, for advance rulings they are reluctant to do so for the same reasons.

It is important, however, particularly in view of the complexity of the various provisions and the inevitable difficulties that will result when particular problems are being worked out by corporations in their planning and because inconsistencies are inevitably discovered in legislation, that the Department of National Revenue be prepared at least to issue on the old basis informal rulings of some sort.

The Chairman: I might say at this point, Mr. Crawford, that before we are through we will very likely invite some

of the officials from the Department of National Revenue in order to ask them how they are going to approach the consideration of this matter, because they have a number of problems to settle. They have the fair market value question to settle in a big way. From what I understand they may transpose the present facilities they have in that regard in relation to estate tax and import into this field those men who have had experience. But the best way of finding out how they propose to approach the problem is to get them in here and ask them. We will do that before we finish our hearings.

Mr. Crawford: I agree with that idea, Mr. Chairman. The point that I am making is one that has been made by many others, namely, that they do have a difficult problem. You find, for example, that if you sit down to plan transactions in many areas such as foreign affiliates in terms of putting them together, there is to be no roll-over and you find as a result that there are many areas, including foreign affiliates, where there seem to be inconsistent provisions in the legislation, and to decide which ones will be applied, and so on, is very difficult. That is just one illustration. We certainly agree with the approach that we should find out from the Department of National Revenue what they intend to do, and we would urge that you encourage them to try to come up with a system of at least issuing informal rulings. Indeed, that might be combined with item 4 of our particular recommendations on page 3, that during the early years of this new system there be a certain amount of leniency in the assessing process.

It has been stated to us that there will be this leniency inevitably, but the difficulty with that is that the assessing process sometimes occurs four or five years later, and, when the assessor goes in he practises interpretations which were unclear two or three years previously but have since been formulated and at least in the mind of the departmental officials are fairly clear, and this can present numerous problems.

The Chairman: A few days ago in our consideration of this bill we were discussing the aspect of the bill dealing with the distribution of undistributed income in hand at the 1971 year, and we were informed that there is a very severe penalty in that, if you are one cent over the amount of your 1971 undistributed income, even though you have honestly calculated at that amount and have paid your 15 per cent tax, which then opens the door to let you do this, you would be subject to a 100 per cent penalty. In other words, the whole amount would be subject to tax, I assume.

Mr. Crawford: That point is dealt with on pages 6 and 7 of our submission, Mr. Chairman. Several suggestions are made as to how the resulting possible hardship you refer to could be dealt with.

The Chairman: Would you care to speak to that now?

Mr. Crawford: I would prefer to finish the two introductory points first, if I may.

The Chairman: All right.

Mr. Crawford: I appreciate that it is probably not of direct relevance to your committee, Mr. Chairman, but it would be helpful in our opinion if the minister, or his assistant, in explaining the bill either here or before the Commons could make available at an early date at least the amendments they have drafted up to that time. That would certainly be preferable to waiting until you get to section 248 to find out how it is going to be amended, because that might be pretty far along. Again, we do appreciate that they have a problem if they have not all of the amendments drafted or if they are changing them subsequently, but, certainly, if something could be done in that area it would be a help—certainly, if you could get at least the amendments that have been settled at this time so far as the Department of Finance is concerned.

Senator Connolly: We have made that suggestion already.

The Chairman: I can tell you, Mr. Crawford, that in the course of the discussion at the last meeting there was a resolution in the committee requesting the Government Leader in the Senate to make to the Minister of Finance the request that the amendments which have been settled be tabled in the course of second reading rather than, in accordance with the usual practice, having them presented in relation to particular items in the bill. We have indicated in the supporting material, which is now in the hands of the Minister of Finance, that, if January 1, 1972, is to be a realistic date for the coming into force of this bill, we should have this material early in committee and the people who are going to make representations should have it early. Otherwise there will be inevitable delays. Certainly, our purpose would be defeated if we permitted ourselves to be stampeded without having that material and allowed ourselves to be crushed against that deadline of January 1. We are not going to permit that to happen so far as we are concerned—that, at least, is my feeling of the temper of the committee.

Mr. Crawford: I can see that it would be very frustrating for your committee, Mr. Chairman, if you were instructed to see how you could amend a section and found out subsequently, perhaps four weeks later, that they were already amending it in the Department of Finance.

Senator Connolly: Have you made any representations either to the Department of Finance or to the Department of National Revenue, Mr. Crawford?

Mr. Crawford: The Chamber of Commerce had a meeting with the Minister of Finance and one of his assistant deputies.

Senator Connolly: In respect of the material you have given us here?

Mr. Crawford: Yes.

Senator Connolly: Was there any indication that any of the points you have raised here are to be amended?

Mr. Crawford: Yes. The Minister of Finance indicated that his officials were in agreement with a great many of the technical points and that amendments were being drafted.

Senator Connolly: But you have not seen them.

Mr. Crawford: No.

The Chairman: There is a follow-up question there, if Mr. Crawford wishes to answer it; would he care to indicate to us which were the sections to which he got that reaction?

Mr. Crawford: I am afraid the minister was not that specific, Mr. Chairman. He said there would be many amendments. We did ask him if he could indicate the areas, but the only area he indicated was the partnership area, in which he said there were going to be substantial amendments. However, he did not so indicate specifically with respect to any other area. I think a lot of people are assuming there will be many amendments in certain areas, but nobody is being quoted.

The Chairman: Perhaps you could correlate what the minister had in mind with what you were talking about when he made that statement.

Mr. Crawford: It is almost impossible, in the context.

Senator Walker: Was he just being pleasant, making a general statement?

Mr. Crawford: Senator, I have been at several meetings with his officials—

Senator Walker: Before that?

Mr. Crawford: Before that, discussing various aspects with them, and obviously there are going to be many amendments. Many of the items in this submission do not go to policy. They go to technicalities, and in that case I do not see any particular reason why they would not be amended. When we get our work near the end of July and early August, if, according to our interpretation, there were a technical problem that needed to be righted, I do not see why it would not be amended.

The Chairman: What do you include in a technical problem? I understand what you mean by policy, but how broad is the statement of technical problems? Do you mean just the failure to put in a comma, a semi colon or a period or a crossing of a "t"?

Senator Connolly: I suppose it would mean a conflict between sections, such as you describe here under section 24, good will. That is a technical amendment in your opinion.

Mr. Crawford: Yes. Mr. Chairman, you have touched on a very difficult problem, in crossing the line from a technical problem to a policy problem. I suppose in a way it is a matter of judgment for the person dealing with it as to how he regards it. You can approach things as technical matters, but they may turn out to be policy matters. I do not think I can state a general rule as to which side of the line it would fall on.

Senator Connolly: Generally speaking, your technical problems arise out of the draftsmanship of the sections, do they not?

Mr. Crawford: Yes. There is one item we want to speak to here which in a sense is technical and in another sense is very important in terms of policy. I refer to the very limited corporate reorganization role-over provisions. There is a very broad policy aspect here, but there are also, of course, many technical aspects to it.

Finally, in the opening part, Mr. Chairman, we would hope that either here or in the House of Commons the minister or his representatives would make some statements as to the more complicated parts of the statute—not in detail but as to what their general philosophy is and what their approach is in this area. In fact, if we had had that earlier, some of these complex provisions that so many people have criticized might have been much more understandable because in reading them we would have known what their general purpose was.

The Chairman: Well, Mr. Crawford, perhaps what I am about to suggest would meet the problems that you are referring to. We would propose in committee to have the departmental officers here and have them give us the objectives of the particular sections that have been discussed.

Mr. Crawford: That would be very helpful, Mr. Chairman, particularly since your proceedings are available and could be distributed to the public.

Coming now to specific points, let me speak first of all on what might appear to be a rather small point but is one which appears to be causing a great deal of concern and anxiety. I am referring now to the so-called departure tax which is dealt with on page 31 of our submission. This is the tax that applies where if you are a resident in Canada and cease to be a resident, you are then deemed to realize any accrued but unrealized capital gains at that time except with respect to property that would be subject to capital gains tax if you were a non-resident. I think many of us in our practice—and I am sure, Mr. Chairman, if you follow this up you will find it to be the case—are receiving perhaps more calls about this problem than any other. There are executives who are reluctant to come to Canada because of what this could mean when they leave, and there are Canadians who are reluctant to leave for a two-year posting in England or Australia or the United States, or Canadian residents who are citizens of foreign countries and who are here now and who are suggesting to their corporate employers that they should leave by or shortly after valuation day so that this provision would not apply to them.

It is also unsatisfactory in several respects in terms of some of the countries with which we have tax treaties, particularly the United States and the United Kingdom—and there may be others—where they prohibit the imposition by Canada of a capital gains tax on residents of, say, the United States. That does not prohibit Canada imposing a capital gains tax on a resident of Canada at the time he ceases to be a resident, but if he makes the election to defer the tax until he realizes on the property, which could be some years later, and puts up the security, then at that later time he is a resident of the United States and not of Canada, presumably under the treaty he is protected from capital gains tax in Canada and will get his deposit back. Then there is also the problem of getting credit.

The Chairman: At that point you are assuming that this exemption in respect of capital gains will be included in any new treaties or amending treaties negotiated.

Mr. Crawford: No, I am assuming that the treaty will not be renegotiated before it becomes a problem for one or two taxpayers—at least that or the assumption you make,

one or the other. We find it troublesome, and we have suggested that temporary residents might not be subject to this tax. There are various ways it could be dealt with. We appreciate that no solution can be perfect, but we quarrel with the decision arrived at.

The Chairman: Well, a departing Canadian who is changing his residence from Canada to another country may find himself in the position where for Canadian tax purposes there is a deemed realization, and he has made a profit or a loss, and he can pay taxes on that at that time. But in fact he has not disposed of the asset. At a later period in the country where he becomes a resident, if he disposes of it and they have a capital gains tax, he may be subject to another gains tax without any credit.

Senator Connolly: Then what you are suggesting, Mr. Crawford, is that there should not be any deemed realization if he is going for a period of, say, two years.

Mr. Crawford: You are quite right. If you are here up to two years and then leave again, either you are treated as not having been a resident for the purposes of deemed realization or there should be no deemed realization. There are various solutions to it.

The Chairman: Well, Mr. Crawford, did you notice the solution we suggested in our report on the White Paper in paragraph 17 on page 60? There we said:

> 17. In view of the need of Canada to attract investment capital, the Committee strongly recommends that all of the White Paper doctrines of tax on unrealized appreciation should be eliminated. The Committee, therefore, recommends the removal from the proposed capital gains tax of
>
> (*a*) the five-year revaluation rule . . .

Now that has been done. And then in the next paragraph it says:

> (*b*) the deemed realization of capital gain or loss on individuals giving up Canadian residence . . .
>
> (*c*) the deemed realization of capital gain or loss on the value of gifts . . .

So, we were with you at that time. Are you now going so far as to say that deemed realization on departure should be eliminated?

Mr. Crawford: We do not in our submission. I think in this submission we were looking at what we thought was in the realm of possibility in terms of influencing the Minister. I think we probably would go that far. But we might think that by doing so we would have less chance of achieving any results in influencing the process of legislative change, but we could be wrong in that judgment.

The Chairman: Obviously what the bill proposes does not meet your view of what should be in the bill. So if you were asked to rewrite this provision, what would you suggest?

Mr. Crawford: If I had a free hand to rewrite it I would suggest what this committee did in its report that you have referred to.

The Chairman: That is a nice attempt to avoid the effect of my question. But my question was; in the light of your attitude, that is that you wanted to stay within the realm of what was possible, and putting it to you on that basis of staying within the realm of what is possible, and accepting the principle of dealing with people departing from Canada and establishing residence elsewhere, how would you rewrite it so as to cure the objections you have raised?

Mr. Crawford: We would obviously insert in the bill that temporary residence for a period of, perhaps, two years would not be subject to it. We would also look at the basic purpose which to many of us involves Canadian residents who have accrued, but not realized, substantial gains upon going to live in tax-havens. If they go to live in a country with which Canada has a tax treaty, perhaps there should be no deemed realized gain.

Senator Connolly: Can you possibly go that far? Would you not say that if there is a tax treaty between Canada and the country in which they take up residence, presumably they would be saved from the effects of double taxation? Would such a treaty not include that?

Mr. Crawford: Until the treaty could be negotiated, or renegotiated with whatever results might flow from that, which would save it from the effects of double taxation, I would say if you go to a treaty country, most of the treaties, with perhaps one exception, which Canada has today are not with tax-haven countries, or are not with countries that do not levy taxes. Therefore, the person who leaves Canada to go to a country with which we have a treaty today would not ultimately achieve a big tax saving. It is true it might go to a country other than Canada. So, until a treaty could be renegotiated, or until a new treaty could be negotiated, I would exempt it with respect to treaty countries.

Senator Carter: Mr. Chairman, there would not be double taxation if the treaty country did not have a capital gains tax?

Mr. Crawford: That is true.

Senator Carter: What would be the position then?

The Chairman: Are you thinking about tax credits in these circumstances?

Mr. Crawford: Yes.

The Chairman: If a Canadian should establish residence in the United States and he takes his assets with him, and there is a deemed realization and he pays his tax on the gain here when he leaves Canada, and he realizes a capital gain a couple of years later in the United States and is subject to tax on it, how would you apply the tax credit if you say he should be entitled to a tax credit in Canada? Should the bill provide in those circumstances that the Government of Canada should go back and refund him?

Mr. Crawford: If you are negotiating a treaty with the United States, the Canadian approach is perhaps correct, that it would be subject to tax on the gain accrued while a resident in Canada and would be paid to the Government of Canada; and a gain subsequently accrued in the United States would be subject to the United States tax.

The Chairman: There would be no question of applying the tax credit in those circumstances, is that correct?

Senator Connolly: And there would be no double taxation.

The Chairman: No, because he would have paid tax on the accrued gain in Canada up to the time that he leaves; and the only way he would have a further capital gain in the United States would be if he realized a gain on a subsequent sale as against the value at the time he came into the United States.

Senator Beaubien: Mr. Chairman, what would happen if he had a gain when he left Canada, and then he realized a loss during the time he was in the United States?

The Chairman: If he had other capital gains in the United States, I would think that he would dispose of them in the United States.

Senator Beaubien: But assuming he only had one asset.

Mr. Crawford: Part of the difficulty arises with the United States tax system whereby a person becoming a resident in the United States, or subject to tax in the United States, is considered to have a cost base which relates back to his original acquisition cost even if this were 10 or 15 years earlier.

The gain that had accrued while he was a resident of Canada will be taxed. It is a very complex problem, Mr. Chairman. I am sure the committee wrestled with it when preparing your earlier report and there are no easy answers.

The Chairman: We cannot write the U.S. tax laws; we can only attempt to remedy some of these situations by means of the tax treaty.

Mr. Crawford: In part it is a matter of balancing an imperfect tax system and resultant imperfect situations in that system, with the desirability, to the extent those making the judgments consider it to be desirable, of enabling people to be transferred or moved about between jurisdictions without imposing too many roadblocks.

The Chairman: Your suggestion of granting an exemption or exception to those Canadians who establish residence outside Canada is of a temporary nature, in the sense that it may arise from their employment and at some subsequent time they may return to Canada.

Would there be inherent in that any basis upon which an exemption could be allowed? The two-year period for an exemption may not really deal with the situation.

Mr. Crawford: That is true.

Senator Hays: Mr. Chairman, when persons from the United States, France or these other countries come to Canada, what is the situation with respect to capital gains? Could we consider the situation in reverse?

The Chairman: Have we dealt with the reverse situation?

Mr. Crawford: You make a very good point, senator, which I might have made earlier. It is my understanding that most of the countries which impose a capital gains tax do not in that case.

Mr. D. J. Gibson (Manager, Policy Department, Canadian Chamber of Commerce): It was my understanding that the United States taxes citizens, not just residents. A citizen of the United States who came to Canada would be liable for capital gains tax in the United States.

The Chairman: As long as he remains a United States national, wherever he may be in the world he is liable for United States taxes.

Mr. Gibson: So they still have him in the net.

The Chairman: He does not file a return and pay the tax if he decides he will not return to the United States at any time, because it could not be enforced. However, if he hopes to return to the United States, he had better keep up his income tax returns.

Senator Hays: Are there examples of the various countries who see fit to send people to Canada? Would that not be the best approach? I do not believe we can expect much better than the treatment our people receive in other countries.

Mr. C. Albert Poissant, Tax Consultant to Committee: A very good booklet dealing with capital gains in other countries is contained in the Carter Report. It illustrates the treatment of other countries such as Germany, France, England and the United States. It is true that the citizen rule for which there is no counterpart here exists in the United States. It is an avoidance rule applied in the case of a person moving out of the United States to obtain the capital gain while outside. This will attract capital gain in the States for ten years after the person leaves. In other words, they cannot leave the United States for the purpose of having the capital gain outside, because it is not deemed to be a capital gain realization at the time they leave the States.

The Chairman: I should have announced this earlier, that the speaker was Mr. C. Albert Poissant, who has been retained as tax consultant to the committee.

Senator Isnor: From the Canadian point of view those affected comprise a very small percentage, do they not?

Mr. Crawford: That would be true.

Senator Isnor: You, as the Canadian Chamber of Commerce, are representing to a very large extent Americans who might be affected by this, am I right?

Mr. Crawford: I have to ask how our percentages in the Chamber line up. It is not only U.S.-controlled subsidiaries who transfer employees, and this can be helpful to Canada in terms of learning know-how, new methods, and so on. However, there are Canadian companies with international operations who move their employees abroad from time to time on a temporary basis.

I would certainly concede that you are perfectly right that as a percentage it is very small.

Senator Isnor: Mr. Chairman, I cannot for the life of me see why the Canadian Chamber of Commerce should be involved to this extent.

The Chairman: Well, senator, if the bill deals with the situation in what appears to be a fair and equitable fashion, then I do not suppose there could be any quarrel. There may be a large number of Canadians, which I suspect to be true, who establish residence outside Canada for many reasons, such as health. I think you might be surprised at the numbers. Therefore if they are dealt with fairly in making the change, we are not concerned. If there are unfair aspects, we should consider them.

Senator Lang: Many Canadians of advanced years and very modest means leave the country in the last years of their life for health and climatic reasons. They might be literally prevented from making such a move by this provision. I believe that there are many more people in this category than my colleague suggests. They represent a sizable segment of our population, a segment which is not affluent in any sense of the word and they could be seriously hurt.

Mr. Crawford: If I could speak to this on a note of idealism: in an increasingly interdependent world within which it is becoming important to understand various cultures, it would be in that sense important to have a system which did not prevent the mobility of people between countries.

Mr. C. H. Scoffield, General Manager, Canadian Chamber of Commerce: I am not sure I understand the question, or the point made. I will at least make the comment that the preponderance of companies in the Canadian Chamber of Commerce represented by us today are purely and simply Canadian companies. We are not here speaking for companies that are members of chambers which are largely international, have American operations or are subsidiaries of American companies. The large proportion of the members for whom we speak are purely and simply Canadian companies.

Mr. Crawford: The next area of our submission is page 15, headed: "General Assessment of Provisions Dealing with Acquisitions and Reorganizations." From your earlier studies, you are no doubt aware that one of the difficulties in any tax system that imposes a capital gains tax is in determining when a change in investment should be imposed for tax purposes and when it should not.

Most people would say that any movement of assets or shares between or among wholly-owned subsidiaries are up to the parent company, and, since the basic economic interest remains the same, should result in what is commonly referred to as roll-overs without any gained realization at that time. When I say "most people," that is probably going too far. I should say "many people."

The provisions of the bill are very limited with respect to roll-overs. No doubt you will discover that when you discuss the matter with the Department of Finance officials.

There are very difficult judgment areas involved in determining when you should be entitled to tax-free roll-overs. Once they get the new system under way, I hope that in the course of the next two or three years they will slowly broaden the areas where they can effect tax-free roll-overs.

If it is done that early it should not be serious, because in most cases the gains built up after valuation date will not be substantial.

This is an area which, in our submission, causes difficulty in terms of the efficient operation of a business. It will also create many distortions. Some people will be able to do roll-overs, and other people will not, for reasons that have very little substance.

If you happen to have companies incorporated in one jurisdiction, or in a jurisdiction that permits you to re-incorporate in the area where the other company is incorporated, you can amalgamate in certain instances and get a tax-free roll-over. On the other hand, if you cannot amalgamate the companies, you may not be able to achieve a tax-free roll-over.

There are no roll-over provisions with respect to foreign corporations or foreign affiliates. On the other hand, if your foreign corporation is incorporated in a jurisdiction such as Delaware and can be re-incorporated in Ontario, presumably you can get it re-incorporated in Ontario and amalgamated with your Ontario parent company, or with your other interests in Ontario, and you may perhaps get a tax-free roll-over.

There are provisions for tax-free roll-overs in and out of partnerships. Here, if you happen to be so structured as eventually to achieve, by rather artificial means, the setting up of partnerships, of rolling into partnerships and then rolling out of partnerships and liquidating them into other corporations, this will create a lot of distortions. I realize that it is a difficult area to deal with.

I would remind honourable senators that the bill came out in June.

The Chairman: On June 30.

Mr. Crawford: We were told, in terms of technical matters, that our submissions should be in by late August. Therefore we did most of our work, in terms of the committees involved in putting this together, by the end of the first week of August. In the time that was available to us we did not have sufficient time to work out any positive recommendations in the roll-over area.

One suggestion that has been made is that until the system matures a little, and until more provisions can be developed regarding roll-overs, there should be a roll-over somewhat similar to the system existing in the United States where, in fact, you have to get a ruling; and if you can get that ruling and it does not appear to be avoiding tax, and so on, the minister can authorize you to have a tax-free roll-over.

The Chairman: If consolidated returns are validated for tax purposes, would that assist the situation?

Mr. Crawford: Consolidated returns help a great deal, if in terms of a loss in one company and a profit in another. You do not necessarily help your corporate organization where you have assets in one and you want to amalgamate the operation, or where they are subject to a low-cost base and a fairly high value. It would be of some assistance, but it would not help the problem.

The Chairman: It would not get to the root of the problem. For the purpose of the record, I should point out that in our report on the White Paper on this question of roll-overs we dealt with this question on page 61, paragraph 20. I suggest that honourable senators might like to read that section at their convenience.

Mr. Crawford, I will put the same question to you again: You have called our attention to this problem. What do you suggest should be done?

Mr. Crawford: I am now speaking personally, because the chamber did not have time to formulate any specific recommendations in this area.

I am not familiar with the parliamentary process, but if the minister could announce, either before this committee or in the house, or wherever it is appropriate, that the Government recognizes that the roll-over provisions are very limited, and that they are proceeding to develop and extent the provisions in the first or second amending bill to the tax reform act, that further roll-over provisions will be introduced, then that would be helpful.

I have another suggestion to put forward, which I made earlier. However, the Government might not have time to implement it. By regulation they might see whether they can get roll-overs by application on a discretionary basis, similar to the provisions in the United States Internal Revenue Code. It is a complex matter, and they may not have time to do it at this time.

There are no easy answers. We think that the Government has come down too strongly against roll-overs. We suspect that it was due in part to lack of time to consider further provisions and to study the operation of the bill in this area. It is a problem, particularly when dealing with foreign businesses, where there are no roll-over provisions. You might find, perhaps, that you have operations based in the Netherlands and, for reasons completely unrelated to Canada or unrelated to tax, the centre of your corporate activity abroad should be based in France or in the United Kingdom, or somewhere, and to move that operation is going to involve substantial tax if there are any accrued gains.

The Chairman: We suggested in our report on the White Paper with respect to this question of roll-overs that in so far as foreign companies are concerned the taxation provisions should not apply unless the purpose was tax avoidance. Would you subscribe to that?

Mr. Crawford: I wonder, Mr. Chairman, if you would repeat the question?

The Chairman: I will give you the exact wording. At the top of page 62 of our Report on the White Paper we state:

> . . . The Committee recommends, however, that where the roll-over transfer is to a foreign entity, the free roll-over provisions should only apply where the purpose of the transaction is not primarily for the purpose of avoiding Canadian taxes.

Mr. Crawford: Yes, I certainly would subscribe to that. The context of our limited roll-over provisions which we have does not fit because it is more or less built on the assumption of many broader roll-over provisions.

The Chairman: Mr. Poissant, are you prepared to add anything to this discussion?

Mr. Poissant: I would just say that I agree with the points made in the brief, and I do think that the recommendation which was made verbally, that roll-overs be obtained free of tax after a ruling, is a good point.

The Chairman: In other words, the minister would have some discretion in the matter?

Mr. Poissant: Yes, and it would permit some natural roll-over to take place without having to attract taxation.

Senator Connolly: Just to simplify and to use an example, Mr. Chairman, and it may be too crude, but if you take the case of a merger of a Canadian parent company and a subsidiary, and the subsidiary has capital gains which were realized at the time, there would be tax if those assets which are the subject of the capital gains are taken over by the parent company. It is proposed under the law now that capital gains are deemed to be realized at the time of an amalgamation or merger, and, if that is the case, is not the revenue protected just as well by having the parent company or the company that results from the merger held responsible for the gains based on the gain record which was developed by the subsidiary as well as by the parent?

The Chairman: Do you have any comment on that, Mr. Poissant?

Mr. Poissant: No, I have no comment to make on that. You are saying that as it is suggested in the law now there would be this realized gain?

Senator Connolly: I understood the witness to say that once a merger takes place then any gain made by any of the mergered companies is deemed to have occurred at the time of the merger.

Mr. Poissant: That is true.

Senator Connolly: I understand this is what he said. If the resulting company is saddled with the gain or loss history compiled by the subsidiary which was merged with the parent, then, there would be no loss to the treasury. When the gain is in fact realized the tax would be exigible.

Mr. Poissant: That is what they are asking. Am I correct, Mr. Crawford, in that what they are asking is that the gain is not realized or deemed to be realized at the time of the merger but that it is realized at the time the gain is actually disposed of by the parent company?

Mr. Crawford: The loss, Mr. Chairman, to the treasury is, of course, in the form of a tax deferral. The treasury may get this tax in year 20 rather than year one, and this does obviously involve a loss.

Mr. Poissant: If the roll-over is permitted the treasury will eventually get this tax if there was any tax.

Senator Connolly: Are you saying, then, that the purpose of the section in the act as we now have it is to get the tax sooner and nothing more?

The Chairman: That is the effect.

Senator Carter: Mr. Chairman, this clause is designed against specific situations where companies buy or acquire assets and never sell them, is it not? In other words, they could go on forever accumulating assets and never paying any capital gains tax as long as they do not sell the assets. My understanding is that this section is aimed at that type of situation.

The Chairman: This is a generalization, senator. Let us take a specific situation. Supposing you have a manufacturing company manufacturing a number of different commercial products and it has acquired subsidiary companies who are in some of these fields, and they then reach the stage where they decide to put them all together, once you look at the picture as being that of a manufacturing company, a manufacturing company does not ordinarily engage in the business of buying and selling its assets. It may have a portfolio of investments which it has to deal with, but if the companies are put altogether they are put together for the purpose of carrying on in a larger or better or more efficient way their manufacturing or processing operations. At that stage there may have been a deemed realization on an accrued gain in value, and it is at this point that we have to look at it and decide whether it is reasonable or not.

Mr. Poissant: In a general way, you are correct. It comes back also to this five-year revaluation provision, and also to the economic implications of locking-in assets and having people reluctant to realize on them, and all that flows from that. You have to look at that philosophy and that problem when you look at this; there is no question about that. But as the chairman has pointed out, when they are all down below as subsidiaries, not being able to move them back and forth does not seem to have much implication, in terms of the lock-in, economically.

Senator Lang: Mr. Chairman, I can conceive that such a corporate organization might be necessary for the purpose of public financing where it is an issue on the market and this might seriously inhibit a company and render it impossible to obtain additional capital which it might require.

Senator Beaubien: Mr. Chairman, does our legal counsel think that if Company A wholly owns Company B there would be a tax on the capital gains deemed to be realized are on the assets of Company B?

Mr. Crawford: I should speak to that, Mr. Chairman. If Company A wholly owned Company B, there is a roll-over provision where you can liquidate Company B into Company A. If Company A owns companies B and C and you wanted to move assets from B to C, as pointed out on page 6 of our submission you will probably have a realized capital gain; it comes under interfiliate transfers. There are some roll-over provisions. It is just that they are very limited and will operate accidentally to permit certain types of organizations to do roll-overs where persons who happen to have a slightly different structure will not be able to do this. I appreciate it is easier to criticize than to solve this problem.

Mr. E. Newman, Member, Public Finance and Taxation Committee, Canadian Chamber of Commerce: I think one of the important points is that if Company A is moving assets down to Company B there is no roll-over; the roll-over is only on the way up.

The Chairman: On the way up, yes.

Mr. Newman: It does not make sense in terms of equity or for any other reason to me.

Mr. Crawford: Perhaps I can illustrate the logic of it in this way. There is a roll-over provision if the sole proprietor incorporates a company, transfers his business to the company and ends up by owning more than 80 per cent of all classes of stock in the company. However, if two or three individuals who may have sole proprietorships or capital to contribute in terms of assets want to move into a corporation, they will all end up with, say, 20 per cent each, or 33 13 per cent each in the corporation; there is no roll-over provision, but they could go into a partnership first, have a roll-over into a partnership, and the partnership could have a roll-over into the corporation. There are provisions where you can do indirectly what you cannot do directly. Again, it is very difficult not to do this in structuring a tax system, and I am not saying it is easy.

Another area that I think may have important economic implications is that it is possible in the United States, and other countries I believe, to do a share exchange takeover bid, whereby if there is no cash boot the shareholders of company A can exchange their shares of company A for shares of company B and have a roll-over; that is they keep their original cost base. Whereas, under our system on a share exchange takeover bid I guess the bidder will have to pay more to pay the tax of the shareholders acceptance, because there will be a deemed realization. It can be said that this is where the lock-over implications come into play. In one case it makes the takeover bid more difficult and may frustrate putting together more efficient corporate units. In the other case, however, it forces a realization at that time, and therefore tends to avoid building up big potential gains in the future.

The Chairman: Are there any further questions on that? What is the next point, Mr. Crawford?

Mr. Crawford: I think I have addressed myself to the points of significance that I wanted to speak to. I do not know if any of my colleagues would like to speak to any others. Otherwise, if you have any questions we can deal with them.

The Chairman: I would like to ask you one question. We have dealt with several points that you have developed. There are quite a number more in your brief, and you are only selecting these to deal with. How do we rate the others in importance and the attention we should pay to them?

Mr. Crawford: I think the others are largely technical, but in some cases with important implications. No doubt the committee and your advisors can review them. Some of them are simply a matter of improper references. Take the one on clause 24, good will, on page 3, to illustrate this . . .

The Chairman: I have just picked one in a hurry. On page 22 you deal with moving expenses and you refer to clause 62(3). That says:

> . . . "moving expenses" includes any expense incurred as or on account of . . .
>
> (*d*) the cost to him of cancelling the lease, if any, by virtue of which he was the lessee of his old residence.

What you have suggested is that he may not cancel the lease, he may be able to negotiate a sub-lease, and there-

fore the wording should be a little more general; that is, that it should provide not only for the cancelling but should also say, "or otherwise disposing of". To give real meaning to it, the suggestion would appear to be a fair and reasonable one, that however the person incurring moving expenses and has a lease deals with it, whether by cancellation or by negotiating a sub-lease, if it costs him anything to do it it should be an allowable expense.

Mr. Crawford: I would hope that that type of point will be picked up by the amendments that are now being or have been drafted. You can get around it in most cases, if you can get a sub-tenant and you are going to lose your expenses by sub-letting, if you have to sub-let for less than the rental obligation and the landlord co-operates you can make a new lease. The people who will get caught will be those whose landlord will not co-operate. In Ontario, for example, a landlord is not entitled to withhold his consent with respect to sub-letting in the way he heretofore has been. Or it may be the person who is not informed and gets trapped by sub-letting.

The Chairman: A lot of these section references deal with situations for purposes of, I would say, clarification.

Mr. Crawford: Yes.

The Chairman: Is there any other person in your delegation who would care to add anything?

Mr. Newman: I have not spoken to my colleagues about this, and I am not a tax specialist or expert by any means. I have taken a two-day wonder course about it to acquaint myself with the complexities of the legislation. I am struck by some of our adherence to old rules. I am thinking particularly of forward averaging which is offered as equity for a taxpayer whose income bounces up in one year. I notice that the annuity to be deducted for forward averaging must be purchased durir.g the taxation year or within 60 days, which is the symmetry of the registered savings plan and so on. I suspect that a great many taxpayers will not know that it is to their advantage to buy such an annuity within the 60-day period. They will probably be preparing their tax returns in late March or early April. I do not think there could be any loss to the treasury if they gave the taxpayer an opportunity to acquire the equity they are offering. I think that would be a very simple thing.

The Chairman: You mean without any time limitation?

Mr. Newman: No, I would say 120 days from the date of filing the tax returns.

Senator Hays: Taken to April 30.

Mr. Newman: The following year.

The Chairman: There would appear to be sense in that. Is that dealt with specifically in your brief?

Mr. Crawford: I do not believe it is.

The Chairman: We have a note of it on the record now. Is there anything else you want to add?

Mr. Newman: No, that is fine, sir.

The Chairman: What about the other members of your committee? You are here for the purpose of telling us what your problems are as you see them and directing our attention to them.

Mr. Newman: There is one point which I do not believe is covered in the brief. It refers to foreign tax credits.

The Chairman: In which section?

Mr. Newman: I do not believe it is covered. There will be an inability to group foreign tax credits in Canada, by proceeding on a country-by-country basis. In a situation where a company may have operations in many countries and may pay foreign tax in one jurisdiction and is unable to offset that against some loss in another jurisdiction, there may be taxes paid which would not otherwise be payable. The United States system provides an election of either a grouping of countries or of individual countries. This is not provided for in our present system under this bill.

The Chairman: Let us take an illustration. Supposing you have a Canadian company that has operations in the United States through a subsidiary company—this is the sort of thing you are thinking about—then they have operations in Australia through a subsidiary company, and operations in the Netherlands through a subsidiary company. Let us say that in two of them they have earnings and profits and they bring them home in the form of dividends; and in the third one they have a loss so that there is nothing to bring home. Is that the sort of situation you are talking about?

Mr. Newman: Yes. I think it is a clearer situation, sir, if you think in terms of a branch operation. It is much clearer there. Therefore, if you have tax in one country and a loss in another, you will not be able to offset these to get the maximum value in Canada.

The Chairman: The simple answer is that if they are limited companies they do not have to bring the income home.

Mr. Newman: That is true.

The Chairman: On the branch operations, those would be earnings or income of the Canadian company. Is not that right, wherever the operation is?

Mr. Newman: Yes.

Senator Beaubien: Mr. Chairman, then the loss would be offset.

The Chairman: You would think so. Mr. Poissant, what have you to add there? If you have branch operations of the Canadian company in three or four countries in the world and in one of them you have a loss, the earnings made in those branches are earnings of the Canadian company under the definition of income?

Mr. Poissant: They would be, yes. They are.

Senator Beaubien: The loss would be, too, then.

The Chairman: In those circumstances, I can understand how to deal with the earnings. They would swell the

Canadian income. How about the losses? How does the bill deal with the losses in a branch?

Mr. Poissant: If I am right on this, Mr. Chairman, they would be the same; but if you permit me, I do not think that is the point Mr. Newman is raising. Am I right?

Mr. Newman: That is right.

Mr. Poissant: You are raising the point that the tax credit, the tax itself, is to be worked out individually by each country. Is that what you are raising?

Mr. Newman: Yes.

Mr. Poissant: And you say there may be cases, as in the United States, where they have an election, whereby you can pool that as income from various sources, but only for purposes of credit of the tax itself. Am I right?

Mr. Newman: That is right. If you have a situation, Mr. Chairman, where you have a profit in one country and a loss in another, then the profit and the loss would be taken together and offset. But if you have had to pay foreign taxes in the country in which you have made a profit, then in Canada's case you would not be able to offset your foreign source income, which would be positive in one country; and you cannot offset the loss, so you would have no foreign source income and no foreign tax credit in that year, because you cannot merge the two operations for Canadian purposes.

Mr. Poissant: Even, Mr. Chairman, when they are not operating as branches. That is because they are different companies—or it could be different branches too.

Mr. Newman: Yes, or branches.

The Chairman: In looking at the Clarkson, Gordon & Company analysis of this bill, under the title "Tomorrow's Taxes", dealing with this question, on page 198, at the top of the page, section K53, they say:

> Under the proposed legislation, income from a business carried on in a foreign country through a branch will continue to be subject to Canadian tax. Similarly, business losses of foreign branches will continue to be deductible against other income of the Canadian taxpayers. However, a number of significant changes have been made relating to the tax credits to be allowed in respect of foreign income taxes imposed on foreign business income.

Your question was addressed to the question of the extent of the tax credit that you might get where you have earnings subject to tax in a branch in a foreign country.

Mr. Newman: Yes, sir.

The Chairman: If you have earnings subject to tax in a branch in the United States, you would be subject to United States tax there.

Mr. Newman: Yes.

The Chairman: If the United States tax were more than the Canadian tax when it is brought home, you would only get a tax credit at the Canadian rate. Is that the point you were making?

Mr. Newman: No, not quite, sir. It is a situation where, in calculating all overseas profits, there may be a situation in which inadvertently your foreign source income, in the calculation for a foreign tax credit, does not give you any relief; whereas if you were able to combine the results, you would get relief. If Canada will insist on treating each country on its own, you do not have the ability to combine this, as in the case of the ability in the United States.

Senator Connolly: Could we take an example. Suppose you made $100 in the Netherlands and $100 in England and you have branches in each of these two countries, and you bring in $200, that becomes taxable in Canada.

Mr. Newman: Yes.

Senator Connolly: But if you have a loss of $100 from the Australian branch, it is ignored. You cannot say that your net income from the three branches is $100; you have to say it is $200 and your loss does not figure in the tax calculation. Is that the point?

Mr. Newman: Yes, part of it, sir.

Senator Isnor: Is that a true picture, to say that you cannot get credit? If the parent body is in Canada and there are branches in three countries and one of those branches has a loss you cannot get credit for it? The Canadian company cannot combine?

Mr. Newman: It would combine.

Senator Isnor: And get credits?

Mr. Newman: The point is this, there are foreign taxes which will exceed Canadian taxes in some situations, either because of the difference in the method of calculating income or rate. If you have two countries and you have income from all sources, you may well find that, if you look at one country in isolation, you will not get full credit from Canada, because the tax rate exceeds the Canadian tax; whereas if you were able to combine countries A and B, the rate would then be less than the Canadian tax and you would get the full credit in Canada.

Senator Beaubien: That is the point the Chairman made.

Mr. Newman: It is quite an important one, in the case of multi-national corporations.

The Chairman: Yes, but, Mr. Newman, if I have a loss in one country and a profit in two countries, the loss is referable to the Canadian taxpayer.

Mr. Newman: Yes, sir.

The Chairman: And his income overall in Canada would be less by reason of the amount of the loss.

Mr. Newman: That is right, sir.

The Chairman: Then, when you move on to taxable income, he is getting some recognition for the loss. He is bringing it home, is he not?

Mr. Newman: Yes.

The Chairman: All he has to do then is have earnings in Canada.

Mr. Newman: He has to have a foreign income and a tax rate on it, which does not result in any disallowance of that tax in Canada.

The Chairman: Do you mean if he has losses and profits abroad, in branch operations, overall he must come up with income. In other words, the loss in one of the foreign countries could not be used to eat up the income.

Mr. Crawford: Perhaps we could state it this way, Mr. Chairman: if in foreign country A the tax imposed is 53 per cent and in foreign country B the tax imposed is 45 per cent, and our rate is 50 per cent, you will not get any credit in foreign country A for the amount their rate exceeds ours, nor will you get any reduction either in foreign country B, but you will pay 6 per cent extra tax if their rate is lower than ours.

Senator Hays: Does the same situation apply if you are an individual?

The Chairman: How do you mean? An individual in Canada?

Senator Hays: Yes, who has an operation in Australia, for example.

Mr. D. M. Parkinson, Member, Public Finance and Taxation Committee, Canadian Chamber of Commerce: With respect to earnings on a country-by-country basis you end up paying the taxes in the foreign country or the taxes in Canada, whichever is the greater, and this is in toto.

The Chairman: Yes, that is right. You get no credit for the excess over the Canadian rates. Is it your suggestion that you should?

Mr. Parkinson: That was Mr. Newman's point.

The Chairman: Certainly you would if you pooled all the earnings outside of Canada.

Senator Connolly: It is really a matter of averaging rates, is it not?

Mr. Crawford: Maybe it is a policy matter. It depends on how you look at it, really.

Senator Connolly: Mr. Chairman, perhaps with the Canadian Chamber of Commerce we should make the point that we in this committee and in the Senate are, and should be, conscious of the fact that more and more Canadians are getting into multi-national organizations, particularly corporate organizations.

The Chairman: We are going to hear people to whom we have given appointments who are carrying on multi-national operations.

Senator Connolly: We want to make it as efficient as we can. We are very conscious of that in the Senate.

Mr. Crawford: The final general point of our submission, Mr. Chairman, is that we did not have time in dealing with this really to deal with the international foreign source income problem. Since then many of us who are in practice realize that there are many problems in this area, and I am sure that when these other groups come before you they will bring those problems to your attention.

The Chairman: I can tell you, Mr. Crawford, that we realize the importance of the international income aspect and we did deal with that in our report on the White Paper. In addition to that tomorrow morning we are going to become students and be lectured by people who understand this area thoroughly. One of the subjects we will be dealing with will be the international income problem. We do want to be equipped. Certainly, we are grateful to you for bringing this to our attention.

Are there any other points that any member of the Chamber would care to develop?

Mr. Parkinson: If I may speak once more, Mr. Chairman, one of the items I am sure will be brought up by multinational corporations or international corporations is the question of foreign accrual property income. Ostensibly this is to stop the moving of assets to tax havens and building them up there. I suspect there has been a certain amount of that going on.

The definition of foreign accrual property income includes a dividend received by one foreign subsidiary from another foreign subsidiary, which is merely the passage of the business income within the consolidated group of countries. But by their definition they have suddenly tainted this income, which was untainted when it was first earned, and that creates a flow-through to be taxed in Canada immediately upon the dividend being received by the foreign subsidiary.

The Chairman: Whatever is the sum total of the earnings.

Mr. Parkinson: Yes. It is all business income and it is all untainted, but as it moves from one foreign subsidiary to another it gets the taint. I imagine you will hear quite a bit about that.

The Chairman: I think we have to look at the other aspect as well, that in the so-called tax havens there may very well be an introduction of taxation. I expect that many of them, when they give thought to this, will introduce a system of taxation because they can collect taxes in that country, and then you can get your tax credit here in Canada, and the one who will be the loser will be Canada.

Mr. Crawford: The sad part of that, Mr. Chairman, is not so much with respect to the tax havens as with respect to the developing countries. One or two departments of our Government are trying to encourage investment in and foreign aid to developing countries, and this system is rather rough on such investment in those types of countries.

Senator Connolly: Why?

Mr. Crawford: Because at the present time Canada does not have any tax treaties with developing countries, and those countries, in order to encourage industry, do not for the most part impose any tax or any substantial tax. Many of them do not. So a Canadian company starting operations in one of those countries will only pay tax on its business income in the developing country in accordance with the tax there, say, 10 per cent. To flow its earnings

back to Canada it will pay tax on the additional 40 per cent, thereby making a very difficult system for the economics of investing in a country like that.

Senator Connolly: Therefore, there is no encouragement for Canadians to invest in that developing country.

Mr. Crawford: That is true. The answer to that is that we are going to negotiate tax treaties with developing countries and, if that is possible, that will solve the problem because then your earnings could flow back tax-free. If by 1976 they have not negotiated the tax treaties, and if the same policy continues, then they should extend the time. I think it is even the philosophy of the Department of Finance that, where you are not talking about tax havens but are speaking in terms of overall economics, the country where the money is earned should be the jurisdiction that is looked to for the maximum rate of tax. This is just a lever to negotiate foreign tax treaties, primarily.

The Chairman: Our counsel has handed me a memorandum in connection with Bill C-259 dealing with foreign accrual property income, which is referred to as FAPI. Apparently many people lean to the alphabet to describe these things. This very short memorandum does pinpoint the problem:

> With respect to foreign accrual property income (FAPI), the appropriate definitions—

that is, definitions of the bill—

> could result in well over one hundred per cent of FAPI being taxes to resident Canadian shareholders where the foreign affiliate or affiliates concerned have more than once class of shares. This problem is compounded where one or more of the foreign affiliates is a trust with various types of income and capital beneficiaries. Appropriate amendments must be made to ensure that under no circumstances does FAPI income bear a Canadian tax in excess of one hundred per cent of the FAPI income.

Now, I do know from having done some forward reading that at least one of the submissions that will be made to us deals with this very situation where the exposure they estimate will be in excess of 100 per cent of the income. Then, continuing:

> In addition, some relief should be given for those situations where, as a practical matter, the FAPI, even though technically taxed to the Canadian resident, will never be received by such resident.

Then in relation to FAPI on capital gains, there is this:

> Capital gains are by definition considered part of FAPI and the treatment thereof is misleading since it would appear at first glance that when taxed as FAPI to a Canadian taxpayer, only one-half of the gain will be taxable. Since, however, in the case of individuals there are no appropriate offsets when a dividend out of such capital gain is actually made, the net result is that where a Canadian individual taxpayer has FAPI through a foreign affiliate and such FAPI consists of capital gains, the capital gains will ultimately be taxed to the Canadian individual shareholder in the same manner as though the FAPI was ordinary income. Appropriate amendments should be made to see that individual shareholders of foreign affiliates bear only the capital gains tax rate on that portion of FAPI which is capital gains.

Mr. Crawford: That, Mr. Chairman, well illustrates the problem raised earlier as to whether you are going to get the amendments. These FAPI problems have been brought to the attention of Finance.

Senator Connolly: Could I make a suggestion with respect to that, Mr. Chairman? Might I suggest that not now but perhaps at some future time our counsel might be good enough to take us through that memo together with the appropriate sections and point out the difficulties that arise.

The Chairman: Yes, and I want our counsel to feel that his position here is such that if he has something that he wants to direct our attention to at any time we want him to do so.

Mr. Crawford: Mr. Chairman, the CCH analysis does a very good job of going through those sections.

The Chairman: Is there anything else that any other member of the deputation or even those members who have already spoken wishes to add?

Senator Connolly: I take it that you gentlemen have read a good deal of the literature that has come out on this matter. Is there any one particular publication that you think is superior to the others—without making invidious comparisons?

The Chairman: Well, now, you should be a little hesitant on that, Senator Connolly, because our tax consultant, Mr. Poissant, has been indentified with a publication which I have read and copies of which have been furnished to all members of the committee. It deals with corporation taxes and with the treatment of corporate distributions in the hands of Canadian shareholders. Of course I am not suggesting that you should not look at all the others, because I have tried to wade through them with more or less success, but this is going to be basic, I should think, seeing that Mr. Poissant is our advisor but we can make comparisons, and say, "Well, what have you to say about this?"

Mr. Parkinson: Senator Molson has a very nice book, sir.

The Chairman: Senator Molson will make his contribution I expect.

Senator Hays: I wonder if the Chamber of Commerce have now decided that we would be better off without a capital gains tax.

The Chairman: You know, senator, I was wondering when you were going to bring that up. You were really hard shell on that the whole way through. You were utterly, completely and very vocally opposed to capital gains tax.

Senator Hays: It is an estate tax on the living.

The Chairman: Yes.

Senator Hays: The old one used to be on the dead.

The Chairman: Well, it didn't make way so I think we have to live with it and do the best we can in connection with its application.

Senator Isnor: Mr. Chairman, might I inquire from the President of the Chamber of Commerce if he has any representative from east of Montreal?

Mr. Neil V. German, Q.C., President, The Canadian Chamber of Commerce: No.

Mr. Crawford: Perhaps I might qualify that by saying that although I am from Toronto I spent a great deal of my life quite far east of Montreal.

Hon. Lazarus Phillips, Q.C., Chief Counsel to the Committee: Mr. Chairman, might I, through you and honourable senators, put this question to the Canadian Chamber of Commerce. In going through this act it seems to me that the most redundant section and the one most badly drafted is that dealing with partnerships. You have touched on that, Mr. Crawford, in your discussions with the Minister.

Mr. Crawford: Where the deemed amount is not the deemed amount but the actual amount?

Hon. Mr. Phillips: Incidentally, as one example, I do not think the word "partnership" is even defined, although we have a special section of the law dealing with it. But to this day we do not even know if a joint venture is a partnership. I mention that as an example of the, shall we say, looseness of the draftsmanship, which is obviously due to lack of time rather than to any particular attitude which does not exist in any department of government. It simply results from the problem of time and draftsmanship.

The second section which is horrendous on account of its consequences is that dealing with foreign source income of Canadians rather than with the income of non-residents, which is also troublesome, from Canadian sources. But particularly the incomes of Canadians from foreign sources is horrendous in some of its consequences in that it is quite possible, I think, from my reading of the act that redemption of shares in the foreign company under certain conditions constitutes taxable income on the total amount, unbelievable as it may be. We will deal with that in due course.

The reason I have asked the Chairman to allow me to say a few words through this committee to the Chamber of Commerce is to see whether they would like to consider a submission to the Minister that in view of the trying problem that is involved, that for the present, aside from the technical amendments which the Minister has offered, relief should be granted to at least (*a*) the subject matter of roll-overs, which has been dealt with today, (*b*) the question of reconsideration of consolidated returns, which in my humble opinion will solve a considerable number of problems not dealt with this morning, and (*c*) the complete suspension by way of deletion from the bill for the present of that part which deals with partnerships and that part which deals with foreign source income. The matters of partnerships and foreign source income of Canadians run right down the line as dealt with in the act under special Chapter K and might well be suspended from the bill for the present until such time as opportunity is given for more detailed study of this very, very important section of the bill in its relationship to international operations in all directions.

Senator Beaubien: Mr. Phillips, would you suggest that the present act would apply then?

Hon. Mr. Phillips: Yes, in terms of the deletion of these sections for the present. I feel that the present bill, with these deletions, can be harmonized without too much trouble, particularly since we have trained officials who can work under the pressures of draftsmanship. I am not trying to be facetious about this bill, because we are dealing with serious matters, but we could well delete the entire section dealing with partnerships, the entire section K, press for consolidated returns, press for the vital problem of the extension of roll-over provisions, and harmonize the bill to fit in with what I have just said. If one wanted to be colloquial, I feel we could then live with the bill in some form, and this would give us an opportunity to study more carefully some of the more complicated provisions.

I am asking, Mr. Chairman and honourable senators, that the Chamber of Commerce, which is such an important institution, consider this further, even at this late stage, and present supplementary representations to the minister.

The Chairman: If you could find it possible to do this, that would be very much appreciated.

Mr. Crawford: Certainly, the learned gentleman's points are well made. Dealing with partnership, as an example, I do not think that anybody has even looked at some of the problems that are obviously doing to be thrown up. For example, it would appear that you could avoid the thin capitalization rules by having a partnership and avoiding the existing structure. I am sure that the Chamber will give very careful consideration to this and take whatever action they feel is proper.

The Chairman: Mr. Phillips has used the word "delete". Perhaps it would be more appropriate at this time to speak of suspending the operation on the bringing into force for a definite period of time.

Hon. Mr. Phillips: Mr. Chairman, I am sure that I need not say, through you, that these observations which I have made are purely personal to me, and they obviously do not represent the views of any member of this committee because it has not been discussed in Committee at all. These are purely my observations as an individual, but I take advantage of this situation because you gentlemen are here today representing this important body.

The Chairman: Honourable senators, it would appear that the representations of the Chamber of Commerce have been completed. We may have saddled them with additional work, if they find they are able to take it on, and if they are, we would welcome what they have to submit.

I want to thank you gentlemen very much for coming here today, for the work you have done and the presentation you have made. Thank you very much.

Mr. German: Mr. Chairman and honourable senators, we appreciate very much the opportunity of making this presentation and being with you on this occasion. I would

point out, for the benefit of one honourable senator, that I have been president only since September 28, and Mr. Gordon Archibald of Halifax was the president previous to that time.

The Chairman: Now, perhaps we have given this the proper eastern flavour. Are you satisfied with that?

Mr. German: Yes. Thank you very much.

The Chairman: Honourable senators, please do not leave yet. There are a few things about which I want to report to you, and then we need to consider the several clauses in Bill C-262, which we were dealing with last evening, which were stood until today. I want to be able to report the bill to the Senate this afternoon, so we should complete our consideration of it this morning. This committee is sitting at 9.30 tomorrow morning, and we will be continuing with our witnesses of last week, Mr. Scace and Mr. Stephen Smith in this room. We have several very interesting and important subjects to be dealt with—for instance, general matters relating to estates, real estate, and corporate acquisitions. I can tell you that inherent in this problem so far as the United States is concerned are some very important and complex questions that need to be considered. Then we have international taxation, which we have been talking about this morning, which is a very important consideration in Canada now.

We then have international taxation, which we have been discussing this morning, and which is a very important consideration at present in Canada. We also have resource industries. We would hope to complete all that by 1 o'clock tomorrow.

The other point I wish to make is that we have fixed appointments for succeeding weeks, having made definite arrangements with organizations to October 28.

Senator Beaubien: Could we have a list?

The Chairman: Yes, I will arrange for you to receive a list. However, I am more concerned now with regard to next week. We have confirmed appointments for Wednesday of next week to the Canadian Federation of Agriculture and the Canadian Construction Association. For Thursday, October 14, we have confirmed appointments for the National Association of Canadian Credit Unions, the Co-operative Union of Canada, and the Allstate Insurance Company of Canada.

Now, that is just for next week. I stress this particularly now, because I have heard rumours that it is possible that the Senate may not be sitting next week. Against that possibility, having confirmed these appointments and this subject matter being very important, will I have a quorum for the meetings next week in the event the Senate is not sitting? Yes; I can see by your response that we will have a quorum. Thank you on that point.

You might be interested in knowing of some of the other appointments. During the week of October 20, on the Wednesday we have the Canadian Jewish Congress, Massey-Fergusson Limited, which is multinational with international income, and The Canadian Mutual Funds Association. On Thursday, October 21, the Canadian Bar Association and the Independent Petroleum Association of Canada will appear. On the 27th we will have ALCAN, which will be international income, Bethlehem Copper Corporation Limited, The Canadian Gas Association and, tentatively, the Canadian Export Association. On October 28 we have the Canadian Petroleum Association and the Mining Association of Canada.

The volume of requests to appear at hearings indicates that it may be necessary at the beginning of November, or even in the last week of October, to add another day of hearings per week, maybe Tuesday. We should endeavour to conclude our hearings by the middle of November, as we will need some time to prepare our conclusions, after which they will be discussed with the committee. I certainly do not consider two weeks to be too long a period for that.

Senator Connolly: Hopefully we will have the amendments by that time.

The Chairman: I believe I informed you earlier that I had submitted in writing to the Government Leader in the Senate the substance of the resolution passed by the committee last time. That submission stressed the importance of having this information as early as possible, in order that the hearings may be expedited.

The Committee adjourned.

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THIRD SESSION—TWENTY-EIGHTH PARLIAMENT

1970-1971

THE SENATE OF CANADA

PROCEEDINGS

OF THE

STANDING SENATE COMMITTEE ON

BANKING, TRADE AND COMMERCE

The Honourable SALTER A. HAYDEN, *Chairman*

No. 37

WEDNESDAY, OCTOBER 6, 1971

Second and Final Proceedings on Bill S-22,

intituled:

"An Act to incorporate United Bank of Canada"

REPORT OF THE COMMITTEE

(Witnesses—See Minutes of Proceedings)

THE STANDING SENATE COMMITTEE ON
BANKING, TRADE AND COMMERCE

The Honourable Salter A. Hayden, *Chairman*

The Honourable Senators,

Aird	Grosart
Beaubien	Haig
Benidickson	Hayden
Blois	Hays
Burchill	Isnor
Carter	Lang
Choquette	Macnaughton
Connolly *(Ottawa West)*	Molson
Cook	Smith
Croll	Sullivan
Desruisseaux	Walker
Everett	Welch
Gélinas	White
Giguère	Willis–(28)

Ex officio members: Flynn and Martin

(Quorum 7)

Order of Reference

Extract from the Minutes of the Proceedings of the Senate, June 15, 1971:

"Pursuant to the Order of the Day, the Honourable Senator Robichaud, P.C., moved, seconded by the Honourable Senator Macnaughton, P.C., that the Bill S-22, intituled: "An Act to incorporate United Bank of Canada", be read the second time.

After debate, and—

The question being put on the motion, it was—

Resolved in the affirmative.

The Bill was then read the second time.

The Honourable Senator Robichaud, P.C., moved, seconded by the Honourable Senator Macnaughton, P.C., that the Bill be referred to the Standing Senate Committee on Banking, Trade and Commerce.

The question being put on the motion, it was—

Resolved in the affirmative."

Robert Fortier,
Clerk of the Senate.

24208—2

Minutes of Proceedings

Wednesday, October 6, 1971

(45)

Pursuant to adjournment and notice the Standing Senate Committee on Banking, Trade and Commerce met this day at 3:00 p.m. to further consider the following Bill:

Bill S-22 "An Act to incorporate United Bank of Canada".

Present: The Honourable Senator Hayden (*Chairman*), Beaubien, Benidickson, Burchill, Carter, Connolly (*Ottawa West*), Cook, Desruisseaux, Gelinas, Haig, Hays, Isnor, Lang, Molson, Smith, Sullivan, Welch and White—(18).

Present, not of the Committee: The Honourable Senators McNamara and Robichaud—(2).

In attendance: E. Russell Hopkins, Law Clerk and Parliamentary Counsel.

WITNESSES:

United Bank of Canada:

Mr. B.V. Levinter, Q.C., Counsel;
Mr. Dennis Dwyer, President, Chartec Limited;
Mr. Robert Wilson, member, Chartec Limited;
Mr. Bernard Charest, member, Chartec Limited.

Upon motion it was Resolved to report the said Bill without amendment.

At 4:40 p.m. the Committee adjourned until Thursday, October 7 at 9:30 a.m.

ATTEST:

Frank A. Jackson,
Clerk of the Committee.

Report of the Committee

Wednesday, October 6, 1971.

The Standing Senate Committee on Banking, Trade and Commerce to which was referred Bill S-22, intituled: "An Act to incorporate United Bank of Canada", has in obedience to the order of reference of June 15, 1971, examined the said Bill and now reports the same without amendment.

Respectfully submitted.

Salter S. Hayden,

Chairman.

The Standing Senate Committee on Banking, Trade and Commerce

Evidence

Ottawa, Wednesday, October 6, 1971

The Standing Senate Committee on Banking, Trade and Commerce, to which was referred Bill S-22, to incorporate United Bank of Canada, met this day at 3 p,m. to give further consideration to the bill.

Hon. Salter A. Hayden (*Chairman*) in the Chair.

The Chairman: Honourable senators, I call the meeting to order.

You will recall that on the last occasion we were considering this bill we requested the feasibility studies, and so forth, and I understand these are available today.

Mr. Levinter, are you ready to continue?

Mr. B. V. Levinter, Q.C., Counsel: Mr. Chairman, I understand that there were two facets which the Senate was interested in: The first was with regard to the financing, and the second was with regard to the projections which I would prefer calling our goals over a five-year period.

If I may, Mr. Chairman, I would like now to call upon Mr. Dennis Dwyer, the President of Chartec Limited, who has done our financial study and who is perhaps in the best position to give you an outline as to what Chartec Limited has done. He can then answer any questions that might be in the minds of the honourable senators.

The Chairman: Has this been developed in any statement?

Mr. Levinter: Mr. Dwyer has a short statement. In order to get to the meat of the matter so that we are aware of the questions you want answered I would suggest that he give you this brief outline, and then any questions can be asked.

The Chairman: Honourable senators, this is Mr. Dennis Dwyer, the President of Chartec Limited. Chartec Limited is the organization that was referred to in our previous hearing as having conducted certain studies in connection with the feasibility or the practicability of a bank of this kind and its operations having regard to the present state of the market, and so forth.

Mr. Dwyer, I have identified you to the committee. If you want to add anything further to your identification, go ahead.

Mr. Dennis Dwyer, President, Chartec Limited: Thank you, Mr. Chairman. Mr. Chairman, honourable senators, I am appearing before you today along with Mr. Robert Wilson, C.F.A. and Mr. Bernard Charest, both of whom are my partners. We appear before you as independent financial counsel retained by the provisional board of the United Bank of Canada to assist them in making the proper arrangements for the raising of the bank's capital.

Let me introduce the members of our firm. Mr. Bernard Charest joined us in 1969. He has been in the investment business since 1955. His major role in our firm is as an investment manager for client's security portfolios. He is also retained as an investment adviser to outside institutions.

Mr. Robert Wilson joined me in 1968. He has been actively engaged as a security analyst and portfolio manager since 1948. His responsibilities in our firm involve the management of funds entrusted to our care, advising our institutional clients, and using his past expertise in specific financial counselling assignments, such as our present one.

My background in the investment business began with Greenshields Incorporated in Montreal in 1959. I became sales manager in 1963 and held that position until 1966. I then spent some time with Hodgson, Robertson, Laing & Co. investment counsel, of the same city. By 1967 I went into business for myself as a financial consultant.

Mr. Wilson, Mr. Charest and myself bring to the provisional board of the United Bank a total of some 50 years' experience in dealing with the investment house, the stockbroker, the investing institution and the investing public.

Our mandate from the board was quite clear. One, the ownership of the bank was to be as widely held, by as many Canadians as possible. Two, the bank was to have an initial capitalization of at least $20 million. Three, the provisional directors were in no way to control the bank financially. Four, our firm and its own members, were to have no financial interest in the actual sale of the shares.

Also, the board was interested to know if the bank would receive broad investor support, in view of its socio-economic policies. We discussed our mandate with 71 people representing 28 investment houses, brokers, and 18 institutions. We considered that this group represented a good cross-section of the most responsible people in the investment field. A few were negative, many more were positive, and of these a substantial number were very enthusiastic.

The comments made by those who were positive may be summarized as follows: One, investor interest in Canadian chartered bank shares in general is high, in view of the high return on capital investment. Investor interest in the United Bank, solely on the grounds of the provisional board's responsible and deliberate actions to date, has given the impression that the investor believes that the basic policies of the bank will ensure a profitable operation.

Two, one crucial factor in investor interest has been the desire expressed by the provisional board that no one group, or small combinations, will control this particular bank. Our mandate specifically stated this objective and

this met with great acceptance and enthusiasm amongst the people whom we saw.

Three, institutional investors, brokers and dealers are particularly conscious of the role that they can play in realizing what so many Canadians want at this point in our history, that is, a broader genesis and control of emerging Canadian industry. With their leadership, a public issue will be successful.

Four, the deliberate attempt by the founders to involve a group of Canadians from all walks of life, to ensure the bank's particular responsiveness to the changing Canada of the seventies was fully endorsed.

Finally, the regional concept of the bank found great acceptance.

Honourable senators, I believe it is important that I stress that the great body of investment people viewed the policy of the United Bank in this regard as a strength and not a weakness, as this policy is particularly in tune with the general socio-economic views now being expressed widely across our country. These many meetings with investors suggested a logical step by step process, so as to enable the bank to raise the required funds.

The following is a summary of that plan:

One, after the granting of the charter, management will make itself known to the investment community and will meet with them individually and collectively to explain the actual operations of the new bank.

Two, following this, investment dealers who have already indicated a desire to be major underwriters will be selected by the provisional board.

Three, subscriptions from investing institutions will be accepted and, following this, subscriptions from private individuals will be accepted.

It must be appreciated that because the bank does not yet have a charter, specific commitments cannot be obtained. The result of our survey indicates, however, that $20 million can be raised.

Mr. Chairman, I shall be pleased to answer any questions which may be put.

The Chairman: Mr. Dwyer, you said there was a general acceptance of the regional concept of the bank. What do you mean by that?

Mr. Dwyer: I mean, sir, that the investing people that we saw, and more particularly the institutions than the dealers, were very conscious of the necessity for very close development ties between the granters of credit and the people who wish to borrow. And they felt that the policy was a rather deliberate policy as expressed by the provisional board, that this was a very key part of the operations of the bank, to be very sure they are aware of the concerns of their particular areas. The investment people viewed this very positively.

The Chairman: But, Mr. Dwyer, let us get down to cases. You have been talking about a regional concept. When Mr. Levinter was talking, he was talking about a regional concept in relation to the receipt of deposits and the making of loans.

Mr. Dwyer: That is right, sir.

The Chairman: You are talking about a regional concept being attractive to investors. I did not ask you about the investors. I asked what makes a regional concept. First of all, is the regional concept of the bank such as Mr. Levinter has said—that is, you accept deposits in a region and you make your loans in the area from which you have received the deposit. Is that your concept, too?

Mr. Dwyer: Yes, it is.

The Chairman: That is why I asked Mr. Levinter on the last occasion whether this was a new philosophy in banking—that is, that you collect money in an area and you loan it in that area even though there are better opportunities to make money in other areas. He said no to that.

Mr. Dwyer: No, sir, I think he said that, wherever possible, as a deliberate act, given a good and a responsible banking practice, that the bank would exhaust, as it were, every effort to ensure that the money was returned to the area from whence it came. Why the investors are interested in this is because this should engender deposit loyalty. And a bank grows because of its ability to attract deposits. One of the questions I was repeatedly asked was: Where are the deposits to come from? Our answer was to explain that particular policy.

The Chairman: When I asked Mr. Levinter he expounded on the concept of the Provisional Board of Management and he said:

> — we have considered that if deposits are made in, let us say, Nova Scotia, the money raised in Nova Scotia by way of deposit should first be made available—again, within guidelines—to people who need loans there and for the development of the Province of Nova Scotia, instead of bringing it down here for the development only of Ontario or only of Quebec.

Now that was his pronouncement of principle. So then I said to him:

> The directors of this bank will be dealing with money that has been invested by shareholders. Do you subscribe to the principle that they should follow the regional theory of investment, even though investment opportunities and earning capacity are greater in another area than where the money was raised?

His answer was:

> No, sir. I was talking strictly about deposits. We must remember that the overall concept must be the success of our bank.

I have a question which bothers me—and I can ask Mr. Levinter later, of course—but it is whether he was drawing a line between money that comes in from shareholders for investment, and you will be free to invest that anywhere, and money that you collect by way of deposits which you would loan out only in the area where you collect deposits. Is that your concept of regional investment?

Mr. Dwyer: Well, I would like Mr. Levinter to answer that question because it is a question of board policy.

The Chairman: No, I want you to answer.

Mr. Dwyer: I am not trying to avoid it, sir.

The Chairman: You have just expressed an opinion and I want to know what is behind it.

Mr. Dwyer: The people that we saw were concerned that the policy not override profitable banking. But at the same time they were very interested that the policy existed and they did not, and I do not think that I do and I do not think that any investment person would try to artificially divide between the capital of the bank and the deposits. I think that would be a very, very difficult thing for management to try to do. But I think the intent, and the very strong intent, that the bank make every effort to employ these funds in the area from which they came is a very positive thing.

The Chairman: Senator Cook the other day said, and I am wondering whether you investigated this:

> I think the history of banking will show that most banks which tried the regional theory either failed or merged.

Have you made a study of the operations of banking and its development throughout Canada to be able to express any view in relation to what Senator Cook said?

Mr. Dwyer: My partners and I as security analysts have naturally looked at banking, and I think when that remark was made, it was probably intended to isolate those banks that only dealt in a certain region. This bank will be a national bank with a strong regional flavour. I think this is rather a different thing.

The Chairman: What do you mean by "a strong regional flavour"?

Senator Beaubien: What region are you contemplating?

Mr. Dwyer: The head office of the bank as proposed is in the City of Toronto, but I believe our Provisional Board expressed the thought that in the first year of operation there would hopefully be a branch in Halifax, in Montreal, in Toronto, in Winnipeg and Vancouver.

Senator Beaubien: That is quite a big region, from Halifax to Vancouver.

Mr. Dwyer: Well, the Halifax area would be considered in this sense to be a region as would the Vancouver area be considered a region.

The Chairman: You see, Mr. Dwyer, from what has been said so far, from what you have said and from what Mr. Levinter has said, the regional concept is dictated to you. You do not choose it because the regional concept, according to Mr. Levinter and you support it, is where you get the deposits; that is where you will loan the money. You accept that as the definition and surely this is the way we have to look at it, and see whether it is practicable or not. If you meld this regional concept of collecting deposits in an area and loaning in that area with what is also said—that is that the bank has a national concept—what money would be used for that national concept? Are you going to rob the regional area? What are you going to do?

Mr. Dwyer: No, sir. I think it is not only possible but it will in fact happen that in any one area and perhaps especially in certain wealthier areas, the amount of deposit money coming in will probably be able to be used all in that area because of the amount of industry that exists there. But I think at the same time the amounts of money coming from, shall we say, less-developed areas would require harder work for its investment. There will always be an extra pool. It will always exist. But I think it is the intention—and I think that is the important thing here, that when we saw the investment people, we never for a moment suggested that for every dollar of deposit coming from region X, that same dollar plus a multiple will go back to that particular area.

Senator Molson: Mr. Chairman, I think the philosophy is excellent, but I would like the witness to explain to us in what way this differs from the practice of the existing chartered banks, because I fail to find any material difference.

Mr. Dwyer: Initially, sir, it will be a difference in size, right from the start, I think it is fair to say that a smaller organization just by its very nature tends to move more quickly. I think one possibility is that you may find that your limits may not be as different as they are, for example, if you had a head office, say, here in Toronto. I suggest that this is a matter not for us but for management, but the loan limit in Toronto may not be two or three times the loan limit for management in Winnipeg. That may be a difference. As I understand the present chartered banks, the loan limits in different areas tend to be different.

Senator Molson: Not because of the areas, but because of the different circumstances and size and so on. I am talking not about the size of limits and so on, but about the philosophy you have expressed that this bank is going to make a new move in that it is going to try to relate deposits to loans. I have been led to believe that this is a fairly general practice in banks, and so I asked you what the difference is and you did not answer my question so far.

Mr. Dwyer: Let me try again, sir. I think it is a fairly general practice, and as you know some statements have been made in the press by other provinces about the amounts of money that were supposed to have been taken out, and these have been questioned by some of the chartered banks, and I think rightly so. The only thing I am trying to say here is that this policy has been enunciated as a policy. Now I do not think the other chartered banks have as yet enunciated that as a policy. I think it happens perhaps a lot more than is publicly believed.

The Chairman: What is the difference? If this happens, what is the difference whether they enunciate it as policy or not?

Mr. Dwyer: Sir, if I may, the reason for enunciating it is because these people have not normally been involved in banking at the board and management level, as Mr. Levinter has said. The communities which they represent wanted to know what the policy of the bank was in this regard. Therefore, it was reasonable for the provisional board to make such a statement of policy.

Senator Benidickson: Mr. Chairman, we have several experienced directors of banks on this committee. From their experience, when these banks are as old and as large as they are, and with as many branches as they have, can

they determine a relationship between where they lend money and where they get their deposits?

The Chairman: I would assume that you lend where the advantage is.

Senator Benidickson: Yes, I would agree, and where you get the interest and the loan repayments.

The Chairman: When I asked Mr. Levinter that question he agreed with the statement I made, that you go where you make the money; and if you have any other policy, you are going to fall flat on your face ultimately.

Senator Connolly: Mr. Chairman, would the witness say that so far as the lending policy of this bank would be concerned that basically the bank would follow the normal banking practice, looking first to such things as the prospects of the borrower, the security that he offers, and the kind of covenance that he can give. And, assuming for the sake of argument that there are applications for loans from British Columbia, Ontario, and from Nova Scotia, and all of these applications satisfy the general banking criteria—which I may not have exhausted, but which are reasonably representative perhaps—then the policy would be to say, "Since we have a greater volume of deposits from the Toronto branch than from the Nova Scotia branch, we should first of all, favour those Toronto applications." They might then say, "Even though we have not sufficient deposits to justify a loan to a proposed borrower from Nova Scotia, we are pretty short on loans in Nova Scotia. Perhaps we had better pay some attention to the geographic factor and make a loan there." Is that the way it is going to work?

Mr. Dwyer: I would think so, yes.

Senator Connolly: In other words, geography is a secondary consideration for the granting of a loan?

Mr. Dwyer: That is right, a loan has to stand on its own two feet.

Senator Connolly: I do not use the word in any objectionable sense, or in a sinister sense, but, in a sense, that will be a political decision as to whether you should approve a loan in Nova Scotia rather than Ontario—political because of the geographic factor perhaps. I think we mentioned also the other day that the ethnic factor comes into play here.

The Chairman: I was going to come to that later.

Senator Connolly: All right, we will stick with the geographic factor.

The Chairman: I was wondering, Mr. Dwyer, supposing the first branch of this bank is opened in Toronto and they get substantial deposits. Following the principle of lending does that mean that most of your loans would be made in Toronto? If there is no question of the quantity of money you have to lend, would you not find good loans in the Toronto area? Then supposing you open up the next branch in Halifax ___

Senator Benidickson: Let us give ethnic consideration to this also, and let us say Sudbury instead of Halifax. I do not see how you can separate discussion of new emphases of a geographical or ethnic nature if they are new emphases.

The Chairman: Let us go along with free-wheeling. The first question that we have to settle on the ethnic matter is how we are going to achieve ethnic representation.

Senator Molson previously asked the question as to how they were going to maintain that in their solicitation of investment.

Senator Benidickson: There are two sections of the community who feel, rightly or wrongly, that they have been rather neglected in the banking system of this country on regional and ethnic bases. Have people been approached as possible investors on the basis that certain ethnic groups are inadequately represented on the boards of directors of our banking system at the present time? Has that been part of the approach for capital funds?

Mr. Levinter: We are not making any direct effort to appeal to any of the ethnic groups, with regard to either financing or loans. It is not an ethnic approach. It is a cosmopolitan approach. In other words, it is a blending of all the people in banking, both in a financial way and in the operations of the bank.

I can say that there will be no favouritism given to the ethnic group as opposed to another ethnic group with regard to loans. The only value attached to a cosmopolitan approach lies in a board of directors, which sets policy, understanding the needs of the various people it represents and of which it is a part. I am totally against, favouritism being given because someone is Polish or is Italian. Nor it is a fact that any individual will become president by reason of his ethnic background. But by reason of his ethnic background, nothing shall hinder him from becoming president. In other words, we want to involve everybody.

Senator Benidickson: It may have hindered them in the past.

Mr. Levinter: I would prefer not to make a comment on this.

Senator Benidickson: But I would.

The Chairman: On the last occasion Senator Molson asked the following question:

> Might I ask whether it is proposed in your by-laws, or through any other way, to limit the ethnic makeup of your board or management? How do you expect to perpetuate this situation which you are now starting with a provisional board, which no one can quarrel with? How do you expect that it will continue? Where do you think you will be in five or ten years, or in the future? Do you think you will be able to continue in this way?

And Mr. Levinter replied:

> I do, from a practical point of view. Firstly, our goal is to have mass distribution of stock so that nobody has control of the bank.

So far as I am concerned, that is a very indefinite and inconclusive answer. How do you maintain the ethnic com-

plexion unless you have participants in the form of bankers, shareholders and directors who have various ethnic origins?

I am not criticizing whether or not they have ethnic origins. This has been put forward as a basis as to why the charter should be granted. Therefore I want to know what value there is in that representation. The same thing applies when we talk about a reasonable concept of operating a bank. I am not criticizing it one way or the other. I want to know its value in terms of assessing the possible success of the bank. That is all.

I want to see whether it is a practical thing. If not, ultimately we may have to look at this as an application by a certain group of people, and consider whether they should be granted a charter or not, not leaning on the regional concept at all, not leaning on the ethnic group concept at all, because on close analysis they may not stand up, and it would not appear that they do stand up. I am sorry that I am intruding.

There is one question I wanted to ask, if I may. You talk about the investment in such a bank being attracted up to $40 million. As we said the other day, the Bank of British Columbia finally ended up with $12½ million. They had the Premier of the Province of British Columbia behind them. Here he told us, when they were applying for a charter, that they would have no trouble getting $400 million. There is a big gap between $400 million and $12½ million. What makes you so sure that you can get $20 million?

Mr. Dwyer: First of all, we have spent a great deal of time talking privately to a very large number of people, whom we have known over a long period of time, explaining very carefully the aims and objectives of this bank, and the desire to broaden the Canadian banking system in general. We have not made any extravagant claims about $400 million, or $100 million. Anybody who was in the investment business at the time of the issue of the Bank of British Columbia would have their own ideas as to why the money was not raised.

The Chairman: I was not asking you why it was not raised.

Mr. Dwyer: I am just saying that we have done this very quietly and, we hope, responsibly. We found among a lot of people in this country, a lot of investment people, a desire to see a broadening of the banking system, and, to answer your question to Mr. Levinter if I may, to see how the complex of people at the management and board level will be maintained. I think one only has to look at the States to see how certain institutions that were started there have become great big companies, by the very nature of the initial board and policies of these companies, which have continued to attract people from a wider spectrum than other companies.

I think those looking at this bank and seeing the sort of people who are founding it, will say, "These men are prepared to commit themselves. I would like to be involved." Believe me, that will happen, because many of the investment houses that we saw have very large clientele in certain areas, and a number of them have had people actually phone in. We have not been out trying to sell bank stock. We have merely been telling the story of the bank and saying why we think it would be good for the country.

The Chairman: I assume part of the story you have been telling has been singing the virtue of the regional concept.

Mr. Dwyer: That is one thing.

Senator Benidickson: And perhaps the ethnic concept.

The Chairman: And singing the virtues of the ethnic concept.

Mr. Dwyer: Certainly, sir.

Senator Benidickson: I was going to ask a question. There are people more knowledgeable than I about this, but am I right in my thought that perhaps the largest bank in the United States today is the Bank of America, away from New York and organized by an Italo-American?

Mr. Dwyer: Yes, and that is an ethnic bank.

Senator Benidickson: That is on the west coast, in California.

The Chairman: Are there any other questions on this aspect?

Senator Molson: I would like to follow up a little more on the regional aspect. I do not quarrel with this. As a matter of fact, I think it is very desirable in this country under the circumstances. I question how far it is possible, how far it is to go. I also repeat that I believe this is in very large measure a practice of the banks today. I would point out the wheat trade gets loans aggregating at times $800 million. Is it suggested that that money comes from the Prairies? I suggest to you that that is money from elsewhere; the deposits do not match the loans in this case. The CPR would have ended up in Westmount if there had been a completely regional practice in banking a long time ago. I think that to a large degree this applies today. I believe it is a very valid objective. I hope it can be worked out by this group.

The same thing applies to the question that I raised and which you have just mentioned about the ability to continue an ethnic character in relationship and proportion as time goes on.

Quite frankly, I have to question in my own mind whether some of these quite laudible objectives will be diluted and will disappear as the bank gets underway. However, that is not sufficient in my mind to say that there is anything wrong with the proposition that is put forward by these gentlemen.

The Chairman: No, all it means is that you may have to look at the application in the light of an application from the people who are making it and the feasibility of it, forgetting the other things that they are urging, even about ethnic participation and about matching deposits with loans, which certainly has not proven to be a good banking theory.

Senator Benidickson: Perhaps in the past there has been regional under-lending, or at least the feeling of that in certain regions.

Senator Cook: Mr. Chairman, I do not oppose the application in any way, but I do agree with your remarks and those of Senator Molson in that, after all, a bank is a custodian for its depositors. It is not the money of the shareholders which the bank lends but it is the money of the depositors. If the bank adopts any principle other than making a loan which is a sound risk, if the bank operates on a regional basis or an ethnic basis and gives loans that are not sound risks, then that bank is going to be in trouble as sure as we are sitting here.

Senator Burchill: Mr. Chairman, in the region I come from in the Maritimes people tend to feel and complain that banks do not look after them very well. Although two of the biggest banks had their beginnings in Halifax, their head offices are now located in Montreal and Toronto and the people of the Maritimes have a feeling that these banks have moved away from them. Their complaint is that the banks do not know enough, or seem to know enough, about the economy of the regions which are far distant from them. In other words, they measure us by the tempo of the economy in which they live. I have spent many hours talking to bank officials at their head offices, pleading with them to become more familiar with the life style and way of life in the Maritimes. I have done so because we feel that sometimes we are at a disadvantage owing to the fact that we are too far away from those who make the policies of the banks.

The Chairman: Senator Burchill, are you suggesting that the policy of the banks that are in existence today is not to make good loans in every area where they can possibly make those loans?

Senator Benidickson: I am glad you and a previous speaker with banking knowledge used the word "today", Mr. Chairman. I am old enough to recall, and you have spent enough time in western Canada to know, that there has been in my time in the west this feeling such as Senator Burchill describes for the Maritimes. It may be that that is not the feeling today, but it was the feeling in recent years, and not too long ago at that. Rightly or wrongly, there was a very strong feeling in western Canada in cities like Winnipeg and Vancouver, where bank charters have been applied for in recent years, that if money was scarce it was because the borrowers were looked at first in the regions where the national banks had their head offices—in Toronto and Montreal.

The Chairman: Well, that is just what we heard when the Bank of Western Canada applied for its charter.

Senator Benidickson: With Toronto money, unfortunately. But the Bank of British Columbia has a little different record.

Senator Connolly: Mr. Dwyer, you are familiar with the provisions of the Bank Act.

Mr. Dwyer: Not entirely, sir, although I was brought up on it.

Senator Connolly: I assume in undertaking this investigation for this group you became reasonably familiar with its provisions.

Mr. Dwyer: Yes, sir.

Senator Connolly: You know what is required of a bank in order to meet the statutory demands.

Mr. Dwyer: Yes, sir.

Senator Connolly: What you have told us is that you made investigations in the financial and commercial communities. Are you satisfied, first of all, that this bank will be operated in a manner which will meet the requirements of the statute?

Mr. Dwyer: Yes sir, I am.

Senator Connolly: Are you satisfied also that the investing public and the depositing public will be served in the manner in which banking institutions should serve?

Mr. Dwyer: Yes sir. Particularly on that point I refer to Senator Hayden's remarks with regard to the bank charter passed on the basis of the people, rather than any of the concepts. One of the things that seemed to convince the people that we saw that this was an honest, if you will, straightforward, no nonsense undertaking, was that the sponsors have in no way attempted to control the bank, either politically or financially. I have checked the testimony of some of the previous hearings before this committee where it expressed very great concern regarding the control factor in some previous applications. In this application there is no such control desire.

This is one of the reasons why investors look upon this kind of bank which, after all, will have a professional management and a board which would be deliberately representative of all sections of the public, as being something which will attract investors.

Senator Gélinas: When you mention investors, do you mean institutions, or investment dealers with whom you have been in contact?

Mr. Dwyer: Both, sir.

Senator Gélinas: Some people have told you, I suppose that the banking system could be enlarged and it would be very beneficial?

Mr. Dwyer: Yes sir.

Senator Gélinas: Is that for the two reasons you mentioned, both the regional concept and the ethnic concept?

Mr. Dwyer: Also to generally broaden the credit-granting base. Many investment people who are concerned with the development of industry in this country feel that any responsible broadening of the credit-granting base is good for the country, that any innovation will raise the general level of excellence of banking in Canada.

Senator Gélinas: Is there a language barrier involved in the ethnic concept?

Mr. Dwyer: No sir; as a matter of fact, as you know, the provisional board is made up of persons speaking a number of languages. In fact, one could say this, that in the future one would hope that the language attitude would be one of at least being able to bring in perhaps newer Canadians who will not speak either one of the official languages, but will be able to train themselves.

Senator Gélinas: I think they can get along with the present system as far as language is concerned.

Mr. Dwyer: I do not think there is any implicit policy that the board has taken with respect to language.

The Chairman: I would think you would have to acknowledge that no one would suffer as a result of a lack of communication due to language if he went into any existing branch of any existing bank.

Mr. Dwyer: All of the existing banks have people on their staff who speak Italian and German.

Senator Benidickson: Many of the big banks have directors who are not resident in Canada. That is correct, is it not?

Mr. Dwyer: I believe so, yes.

The Chairman: Some directors.

Mr. Dwyer: Not very many.

Senator Molson: There would be very few.

Mr. Dwyer: Would these not normally represent overseas correspondent connections and that type of thing?

Senator Molson: No. Most banks have the odd overseas director. I have not looked at any of them recently, but I think if you do you will find that 90 or 95 per cent of the members of the boards of the chartered banks are Canadian, pure and simple.

Senator Benidickson: I would agree with that. I just simply said that many of the banks have non-resident directors.

The Chairman: And all I said was "some non-resident directors".

Senator Connolly: From your investigations —

The Chairman: Wait a minute, senator; Senator Hays asked to be heard a short time ago.

Senator Connolly: I am just finishing my question.

The Chairman: Senator Hays?

Senator Hays: Mr. Chairman, if this particular area has been exhausted I would like to ask some questions. These questions have probably been asked already, but I was not present at the last meeting.

If Senator Hayden, Senator Molson and Senator Beaubien were to start a bank and they applied for a charter I would take a flyer on it. I would be particularly interested to know the principals behind this, as to who is going to start this bank. In the first place, I think management and direction are the most important factors, and also the confidence that you have in these people if this bank is ever going to get off the ground.

The Chairman: Mr. Levinter is here. Ask him the questions.

Senator Hays: These people should have supporting evidence to let us know exactly what their methods are; how involved they are going to be personally; and what they have done in the past.

I realize that small acorns into great oaks grow, but it seems to me that this is the most important aspect of any group that is starting any organization. Who are the principals? How is it going to be managed? Is it going to get off the ground?

The Chairman: Who is going to run it?

Senator Hays: Who is going to run it, yes, and I think this philosophy can change. I would hope that it would if they found they were making errors. In other words, if it was found that one venture was not profitable, then they would move their money into another venture. How safe is the money going to be? Are they going to lend it? Will it be a money-making proposition for those involved in the bank and for those using the bank? It seems to me these are very important questions to be asked of anyone who is asking for a bank charter.

The Chairman: Mr. Levinter?

Mr. Levinter: I appreciate your concern, senator. Without proper management the bank will not get off the ground. However, I am in a difficult position. One can only take my word for the fact that I have a gentleman who is a senior man in Canadian banking and who is intimately familiar with, not only operating a bank but who is also equipped to set up a bank. Naturally, I cannot disclose the identity of this man, but as soon as the charter is granted his identity will be made known. Bear in mind that no one can cause any harm to the public until Mr. Scott's department and the Governor in Council give their approval to the charter.

This is not a question of a cat-and-mouse game; this gentleman has an extremely responsible position in banking and you can well understand that if something should happen here or in Parliament it could ruin a man's career in Canadian banking. We have assessed this man. Mr. Dwyer has met this man, as have both Mr. Lasalle and Mr. Scott. Mr. Scott saw him yesterday.

I have Mr. Ryley present today. He is a partner in the firm of McDonald Currie & Co., and he has been an accountant for some 20 years. He has met our management and he has looked over our proforma goals, our objectives, our proforma balance sheet, and our profit and loss statements. He is available here to give you an opinion as to his views with respect to how our management is going about this. I can unequivocally say to you that I am very lucky to have such a man. It was a great stroke of luck, a great experience. He has great know-how and is very methodical.

I can also say that we have commitments for senior accountant, and so on. I may say that they are all coming from the present banking system—and I do not mean from the lower echelons, I am talking about the upper echelon.

We have commitments, I believe, from consumers. The manager has set out an organizational chart for me, so that I would be able to discuss this to some degree. We have, I believe, a consumer credit man available to the bank. We have a chief accountant now available to the bank and, remember, this is even before we get a charter.

We are not through the Senate, yet we have these commitments.

We have a president who is topnotch; we have a vice-president in charge of administration already. I am advised by the president that there should be no difficulty in getting an investments man, a money man, an international manager, personnel manager and so on. My management knows how to get these people. I do not. I am not intimate with the system.

The Chairman: Mr. Levinter, may I interrupt you for a moment? Do I understand you to say that the Inspector General, Mr. Scott, has met the person you contemplate to be either the president or the general manager? Is that right?

Mr. Levinter: Yes. I took the liberty of introducing him to Mr. Scott.

The Chairman: So it will be open to us, in our own right, to have the Inspector General come here and express a view. We have had him here once already, but I believe that was before he met this man.

Mr. Levinter: Yes, but the Inspector General was king enough to indicate that he would not discuss the identity of the individual.

The Chairman: Quite apart from disclosing it, if he is ready to say he has met this man, that he knows this man and that the business ability, the banking experience and training of this man is such that he can do a good job—with all due respect, that is even stronger than when you say it, because you are promoting this.

Senator Cook: What is the opinion of the proposed president on these regional and ethnic objectives? Have you discussed that with the proposed president, how far you are going to carry out the regional concept?

Mr. Levinter: I discussed the regional concept. The president is of the view that regional loyalty is a plus in obtaining deposits, in having people generally deal with the bank—consumer credit, commercial loans, deposits, various things of that sort. He considers it as a plus.

Perhaps I did give the wrong impression at the last hearing. I did not want to give the impression that all the deposits obtained in British Columbia were going to be available for British Columbia. This has to be worked out on a ratio, naturally; but the best banking practice must be considered. A ratio of the deposits obtained in British Columbia should be available for development there, a ratio of the deposits obtained in Nova Scotia should be available for development there; but one can never overlook the overall concept that it is one bank, and that this one bank must operate and be successful.

I am not suggesting, again on a regional concept, that if 40 per cent of the deposits are made in Nova Scotia, 40 per cent should be made available there; but if there is not as good a loan available in Nova Scotia, unfortunately it cannot go to Nova Scotia.

Senator Hays: You are not going to have much to do with this. This is your philosophy now, which might completely change when this gentleman, whose name you do not wish to disclose, takes over. Am I right in this?

Mr. Levinter: No, sir. Our views do not conflict. When I first met this gentleman I explained my views, and I am trying to get away from the word "ethnic", because I was tagged with that word by the *Financial Post* when the first notice was put in the *Canada Gazette*. The squib came in as soon as they heard that it was I who was promoting it and they called it an "ethnic" bank. I am trying to get away from that because I do not like the word. It is a cosmopolitan bank; it is a Canadian bank, and inasmuch as Canada is made up of a great number of ethnic groups, I suppose one could call it an ethnic bank. But I refer to it as a Canadian or a cosmopolitan bank. That is why I qualified what I said before. Because a man is an Italian, it will not guarantee his loan in any way. But I would like to have an Italian on that board who knows the needs of his community so that we can better serve and service his community. That is what I mean by a cosmopolitan bank. If a man is a bright young man and he may be Polish or he may be German or he may be Italian, but if he wants to come into the banking business, I would like to be able to say to him, "Young man, it does not matter whether you are white, blue, green or purple, you do the job and you will get somewhere some day." That is all I want.

The Chairman: After all, the word "ethnic" has a broad application; everybody is ethnic.

Senator Hays: But I go back to my original question. I think before we vote on it and consider it, we should know exactly the principals behind the bank, who they are and what they have done and what sort of confidence we can put in them, because, after all, this is what it is all about. To me the most important thing about the whole charter is the people behind it.

Mr. Levinter: Sir, the five provisional directors are behind it and I can tell you that they are: my father, Dr. LaSalle, a gentleman who is a Polish accountant by the name of Mr. Gutkowski, a gentleman by the name of Pianosi from Sudbury and myself. The board will certainly be enlarged because we want to have an excellent board.

Senator Hays: You are all nice-looking people and you look intelligent and bright, but I would just like to see it all down.

The Chairman: You want a chart?

Senator Hays: Yes.

Mr. Levinter: I gave this last week, sir.

The Chairman: No, you gave the history of the provisional directors from almost their original birthday down to date. But what we are talking about here, if I understand Senator Hays correctly, is a chart in relation to the personnel who would be the senior operating officials of the bank. Granted you will have to put Mr. X as president because you do not want to disclose his name, but what about the others?

Mr. Levinter: But, sir, these are all people in the banking institution.

Senator Benidickson: Mr. Chairman, we do not ask this normally if we are incorporating an insurance company which eventually has vast sums of money to administer. Often we are only shown a list of provisional directors.

The Chairman: Senator, this may be your view, but Senator Hays has asked the question and certainly it is relevant. If he asks it, it is relevant.

Senator Benidickson: But I should say it has not been a universal precedent or practice in this committee to ask, before a charter is granted, who the eventual directors are going to be. Maybe it is desirable and I am not objecting to the question.

The Chairman: What Senator Hays has asked, as I understand it, is who will be the senior personnel who will be operating the bank.

Senator Benidickson: If they are coming from important jobs in the present banking system and these applicants do not get their charter, in many instances it may be very embarrassing, even catastrophic, to those people and they will lose their jobs in the existing banking system.

The Chairman: Is that the answer Mr. Levinter makes?

Mr. Levinter: Oh, yes. I am equivocal and I cannot disclose their names.

Senator Hays: It seems to me that if you are granting a charter, it is reasonable to want to know whether it is going to be a success or a failure. I do not have all that much money to invest, but when I do I look at the management first to see if my money will be safe and if it is going to be used wisely.

Mr. Levinter: Before a dollar's worth of shares are sold, yes, the management will be disclosed, but we have to have our charter first. That is all I can say. The management, of course, is very important, but I would point out that Mr. Hall was not employed by the Bank of British Columbia and they did not have a president until they had been open for six months. I am sorry, sir, I cannot give you that. I can give you our organizational structure.

Senator Benidickson: The Inspector General would not let you operate unless there was a certain amount of capital paid up which he felt was sufficient to protect the public.

The Chairman: It does not read that way. It says:

> When, at the time of the application for the approval of the Governor in Council, a sum of less than one-half of the authorized capital stock has been subscribed, the Governor in Council shall, when granting the approval, reduce the authorized capital stock to the largest multiple of one million dollars that is not greater than twice the amount so subscribed, Schedule A is thereupon amended accordingly . . .

When these people apply and indicate the quantity of capital they have subscribed, and the Inspector General compares that with what is authorized or stated to be the authorized capital, then if it does not bear a certain relationship, the authorized capital is reduced accordingly.

Senator Benidickson: Mr. Chairman, you are one of our best lawyers. I am glad you have quoted this from the Bank Act for us. That is really what I meant. The public is protected through investigations and inquiries subsequent to the issue of the charter by the Inspector General of Banks.

Mr. Dwyer: And the money is held in trust until such time as the licence is granted. So there is no way the provisional board can use these funds until such time.

Senator Benidickson: Does the cabinet itself have to come in after Parliament grants the charter?

Mr. Levinter: It is the Governor in Council.

Senator Benidickson: Yes, the same personnel.

Senator Beaubien: Mr. Chairman, I feel that the Senate's job is to look into the past histories of the provisional directors so that this committee can ensure that they are perfectly honest, respectable citizens, that they have very good histories in business, and so on and so forth. If we are satisfied with the investigation which has been made, I feel the Bank Act can look after the rest of it; but I feel that this is the Committee's real purpose.

Senator Connolly: The only thing that I would like to add to that, Senator Beaubien, is that we have asked that Mr. Dwyer, who did the investigation for this board, come here and give us an account of his investigation.

The Chairman: And he is here.

Senator Connolly: And of his own responsibility, he has said, "Yes, I am a financial consultant, and I think this is a valid proposition."

The Chairman: We asked the sponsors to bring in their financial representative to indicate the studies and projections he had made with regard to this matter. Is it the desire of the committee to hear the representative?

Hon. Senators: Yes.

Senator Cook: Who certifies the chartered analyst? Is it a degree from a university?

Mr. Dwyer: In the investment community there has been a professional designation for some time. Such an institute was started in the United States some years ago, and it was introduced into Canada in 1964. It involves having had a certain number of years' experience in other business and taking hours of courses and examinations over a three-year period.

It is the hope of the International Federation of Chartered Analysts that it will be accepted as a designation just as, say, a C.A. is. In the community this is the top analytical designation that a man can obtain.

Senator Burchill: If this gentleman meets all the requirements of the Bank Act, then I do not think that we need sit here any longer, and I move that the bill be passed.

The Chairman: The committee has already indicated that it would like to hear the auditor or the accountant.

Senator Lang: How long, on your projections, will this bank be in a loss position? Where is your turn-around point? How much of your capital is going to be eroded before you start making a profit?

Mr. Levinter: We have projected, in line with the Bank of British Columbia for the first three years. After the first three years we have no past precedent upon which to

draw. Therefore we can only set our goals for the fourth and fifth years based on management experience, taking into consideration the amount of capital raised and the base which will have been obtained after that first three-year period.

After taking into consideration an appropriation for losses of $300,000, and after paying $50,000 into a rest account, there should be a profit of $12,177 in the first year. That is on earning assets as opposed to total assets. Total assets after the first year are anticipated at $75 million.

The Chairman: What capital are you referring to?

Mr. Levinter: Twenty million dollars will be raised in the first instance. The earning assets of the bank, to come to that net profit, would be $63 million. The earning assets are made up of treasury bills, securities, day call and short loans to investment dealers which are secured, loans which include business and personal, consumer credit, mortgages, and other currencies. That is the earning assets. For the second year, which follows right in line with the Bank of British Columbia, the net would be $25,600; that is after an appropriation for losses of $850,000; plus a further $50,000 in the rest account. The net then of undivided profit would be $25,600. In the third year, after an appropriation for losses of $1 million and a further $50,000 into the rest account, the profit would be $34,409. In the fourth year, with appropriation for losses of $1,500,000 and in the rest account $225,000—

Senator Benidickson: Why does the "rest account" provision go up almost five times in that fourth year?

Mr. Levinter: As I understand it, this is a method putting away profit so that you are not taxed; you are building up the capitalization of the bank. At this point they thought $225,000, and they would have a $35,603 profit; that would be undivided profits.

The Chairman: Would this be a good place to interject? Perhaps Mr. Ryley could tell us on what basis you calculated the losses in each year.

Mr. Patrick Ryley: I think I should explain that these are the projections made by the proposed management of the bank. Our role is to review these, and really to try to determine whether they are based on reasonable assumptions, so that the appropriation for losses is the appropriation over and above, as you know, the actual losses that we expect to incur. When Mr. Levinter is quoting the balance of profits, I think most in the banking business feel the balance of revenue is more appropriately the profit of the bank. Of course, that is expressed before appropriation for losses and income taxes. I hope those remarks might clarify the position.

Senator Molson: That figure you say is expressed before appropriation for losses, but there is the appropriation to come in from the five-year experience, which would come on to administration and other charges up above.

Mr. Ryley: That is correct.

Senator Molson: So you are speaking about non-specific reserves.

Mr. Ryley: These are the appropriations for losses that banks make after this determination has been made, yes. It is a contingency appropriation.

Senator Benidickson: That has something to do with income tax?

Mr. Ryley: Not in its entirety, no.

Senator Molson: This is all done in accordance with the requirements of the Inspector General of Banks. That is what you are saying.

The Chairman: And the provisions of the Bank Act. Mr. Levinter, in making these calculations were there available the experiences of the Bank of British Columbia in those years, to see how it did in relation to its build-up?

Mr. Levinter: Yes, sir. As I say, for the first three years our projections and goals are the same as the Bank of British Columbia. What I have just indicated to you follows their pattern almost exactly, except in 1975, which is the third year, as I understand, it, as of July 1, the Bank of British Columbia had $162 million in assets. We anticipate having $7½ million more in capital, which would mean that we would have $167½ million, but by reason of our anticipated mix and our anticipated national character, instead of the $162 million which the Bank of British Columbia had as of July 1, our total assets were $180 million. This is $10 million more after the third year than the Bank of British Columbia. That is a projection of $10 million more than the Bank of British Columbia.

Senator Benidickson: Although you propose to start with 50 per cent more capital than the Bank of British Columbia eventually started with?

Mr. Levinter: Yes, but we have tried to be conservative to the nth degree in making these projections, because we want to set goals for management which are good goals. We do not want to set impossible goals. Moreover, the goals we set must be credible. So this is what management has taken into consideration. We have kept lower limits all the way down. For example, I understand that in the accumulated appropriations for losses basically they put 25 per cent more than the average banks do.

I heard a comment that you are allowed the five-year experience; but in fact we have no experience. So as a percentage of total expenses we have taken 25 per cent more, again just to be conservative all the way down the line.

The Chairman: Mr. Levinter, suppose you do not get the $20 million of authorized capital, have you looked at this on the basis of other amounts—for instance, $10 million?

Mr. Levinter: Yes, sir.

The Chairman: Would you throw up a profit figure in each year with $10 million?

Mr. Levinter: In view of the fact that I am advised by management that our first two years fall right in line with the Bank of British Columbia, regardless of the fact that we have more capital, and we still show a profit of $12,177, I would say, yes. I would say that with $10 million, of course, the bank is feasible. It is not as comfortable as I

should like to have had, because with the $20 million you can get off that much more quickly. If we were to get only $10 million, we would not put in as many branches. You cut your cloth to suit your pocketbook.

The Chairman: Have you set an objective of an amount that you must have subscribed before you would apply for your charter? You realize that under the Bank Act you may start with a minimum capital of $1 million. Have you set any amount below which you would not pursue the matter? If you got $1 million subscribed, would that mean that you would go ahead?

Mr. Levinter: No, sir. In my view it would be utterly impractical with $1 million. I would think that the break-away point would be higher than that. However, again in view of the investigations that were made there was not great consideration given to this. We considered that if we had $12 12 million there would be no problem. At $10 million I do not think there are any problems, but if we got below $10 million it would certainly have to be considered very, very carefully. This, again, would depend on -hat management advised us, what our financial consultants advised us, what our accountants advised us. If it were below $10 million and they in their wisdom considered that it would not be feasible, then we would have to accept their advice. That is all.

Senator Hays: Mr. Chairman, perhaps we could get Mr. Scott, the Inspector General of Banks, to answer the question that I asked.

The Chairman: Certainly, Senator Hays, but first I believe Senator Lang has a supplementary on this same point.

Senator Lang: Thank you, Mr. Chairman. Mr. Levinter, do you use the Bank of British Columbia experience to make your assumptions as to your rate of intake of deposits?

Mr. Levinter: Yes, sir, except that in our fifth year again in considering prognostications we use the general industry average. I can say that in using the general industry average, the percentage of deposits of total capital is 54.9 per cent. That is personal savings. At the end of five years we considered only 40 per cent of our total assets being personal savings. There were two reasons. The first was that we have to build up our deposits to the general industry average as experienced for many years. Secondly, management has indicated to us that personal savings deposits, in their opinion, as the years go by will form less and less of the total assets of banks. This is because of the general public's present knowledge of the value and interest rates which they can obtain on, for example, certificates. The general public is becoming more and more aware of the fact that it is not a very profitable proposition to keep money in personal savings in banks. Therefore, management is of the view that the trend will decline in this regard. Therefore, again in an effort to be conservative, while the industry average was 54.9 per cent in 1969, after we have been in operation for five years we believe we will have only 40 per cent of our assets in this category.

Senator Hays: Mr. Scott, in discussing the United Bank of Canada with the principal who are here today, are you satisfied with all the investigations you have carried out to this point in so far as personnel and that sort of thing are concerned?

Mr. W. E. Scott, Inspector General of Banks: At this point, Senator Hays, it is difficult and unusual to be able to carry out a full investigation; all the plans are tentative. After the act is passed, if it is, there will presumably be a period in which these people can, as they have indicated, make firm engagements and firm up their plans. There will be an opportunity later, when they apply for their certificate, to obtain a much better picture of the situation than is possible for any group applying for a charter at this point.

Senator Hays: If at that point in your investigation you are not satisfied, then the deal is off?

Mr. Scott: I do not have that power in my hands; I can only recommend to my minister.

Senator Benidickson: Do you recommend to the Governor in Council?

The Chairman: It is the Governor in Council who issues the certificate.

Senator Hays: On the recommendation of the minister, I suppose.

Mr. Scott: Yes.

The Chairman: Yes. Do you feel that you have authority under the Bank Act to carry out these investigations after a charter has been issued and before a certificate has been issued, or are you studying what money they have collected and what their authorized capital is in order to recommend to your minister on that basis?

Mr. Scott: It is usual, sir, to be in touch with the management of all new banks in that period, following the plans quite closely. Therefore one would hope to have a reasonable picture of their ability to do what they are planning by the time they ask for the certificate to open their doors.

The Chairman: I just wonder what authority you have to do that.

Mr. Scott: To keep in touch with them?

The Chairman: Yes?

Mr. Scott: I think the authority is in the act to require information, if necessary.

Senator Benidickson: Assuming that a charter is granted, Mr. Scott, then between that time and your recommendation to the minister, and also from the point of your recommendation to the minister to the point of a granting a certificate from the Governor in Council, what control is there over the funds that have been put forward by investors in the capital of this bank?

Mr. Scott: In a sense they are trust funds in the hands of the provisional directors.

Senator Benidickson: Would you periodically look and see if that trust fund is there intact?

Mr. Scott: It can be done, yes, but they would have no authority to make loans or accept deposits.

Senator Benidickson: It would be an illegal act if they encroached on that capital before the certificate was issued?

The Chairman: It would be illegal for them to do anything of a banking nature before they had their licence.

Any other questions?

Senator Benidickson: What if they pay organizational expenses out of the funds?

Mr. Scott: They may incur a liability for these expenses, but they are quite limited under the act with respect to the extent that they can pay them.

The Chairman: Are there any other questions you wish to ask Mr. Scott?

Senator Lang: Are the powers vested in either you or the minister under the Bank Act with respect to the operation of a bank comparable to those under the Trust Companies Act? Can you put in a comptroller or supervisor, if you wish, and operate it yourself, if necessary?

Mr. Scott: Within quite wide limits. The management of banks, like the management of trust companies, is responsible—

Senator Lang: Yes, I know that, but there are great powers conferred under the Trust Companies Act. I am just wondering if there are comparable powers conferred under the Bank Act.

Mr. Scott: Under the Bank Act the minister's power to put in a curator is limited to the circumstances under which he deemed the bank to have become insolvent. There is no authority for him to step into management before that situation is reached. He can express views, but he cannot act.

The Chairman: Are there any other questions?

Senator Hays: Mr. Scott, you really do not make a thorough investigation until after the charter has been issued, is that right? Your responsibility starts at that point, does it, or do you examine the principals before that point?

Mr. Scott: I believe the statutory responsibility that is laid down in the act does not start until after they have received the certificate, but, as a matter of practice, the Inspector General of Banks has been the official on whom the minister relies to keep in touch with the progress of things in the bank before the certificate is issued.

Senator Hays: Before the charter is granted?

Mr. Scott: Before and after the certificate is granted.

Senator Hays: Then you do look at those who may be applying for a charter at this point?

Mr. Scott: I would assume that would be one of the things.

Senator Hays: Have you done this?

Mr. Scott: I do not believe I know more about these people than has been stated in this committee.

The Chairman: It has been said that you have talked to the person who may be the head of this bank. Is that right?

Mr. Scott: Yes.

The Chairman: And without asking you to disclose his name, is he a man of banking experience and ability and integrity?

Mr. Scott: I have no reason to doubt that.

Senator Cook: Would it be fair to say that your department would pay particular attention to a bank in its formative years, more so than you would to a well established bank?

Mr. Scott: Yes.

The Chairman: Are there any other questions? Are you ready for the motion? Shall I report the bill without amendment?

Hon. Senators: Agreed.

The Chairman: The committee meets again tomorrow morning at 9.30, at which time we will discuss the tax bill.

The committee adjourned.

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THIRD SESSION—TWENTY-EIGHTH PARLIAMENT

1970-71

THE SENATE OF CANADA

PROCEEDINGS

OF THE

STANDING SENATE COMMITTEE ON

BANKING, TRADE AND COMMERCE

The Honourable SALTER A. HAYDEN, *Chairman*

No. 38

TUESDAY, OCTOBER 5, 1971

WEDNESDAY, OCTOBER 6, 1971

Complete Proceedings on Bill C-262

intituled:

"An Act to support employment in Canada by mitigating the disruptive effect on Canadian industry of the imposition of foreign import surtaxes or other actions of a like effect"

REPORT OF THE COMMITTEE

(Witnesses—See Minutes of Proceedings)

THE STANDING SENATE COMMITTEE ON
BANKING, TRADE AND COMMERCE

The Honourable Salter A. Hayden, *Chairman*

The Honourable Senators,

Aird	Grosart
Beaubien	Haig
Benidickson	Hayden
Blois	Hays
Burchill	Isnor
Carter	Lang
Choquette	Macnaughton
Connolly (*Ottawa West*)	Molson
Cook	Smith
Croll	Sullivan
Desruisseaux	Walker
Everett	Welch
Gélinas	White
Giguère	Willis—(28)

Ex officio members: Flynn and Martin

(Quorum 7)

Orders of Reference

Extract from the Minutes of Proceedings of the Senate, October 5, 1971.

"Pursuant to the Order of the Day, the Senate resumed the debate on the motion of the Honourable Senator Forsey, seconded by the Honourable Senator Lafond, for the second reading of the Bill C-262, intituled: "An Act to support employment in Canada by mitigating the disruptive effect on Canadian industry of the imposition of foreign import surtaxes or other actions of a like effect".

After debate, and—

The question being put on the motion, it was—

Resolved in the affirmative.

The Bill was then read the second time.

The Honourable Senator Forsey moved, seconded by the Honourable Senator Heath, that the Bill be referred to the Standing Senate Committee on Banking, Trade and Commerce.

The question being put on the motion, it was—

Resolved in the affirmative."

Robert Fortier,
Clerk of the Senate.

24210—1½

Minutes of Proceedings

Tuesday, October 5, 1971
(42)

Pursuant to adjournment and notice the Standing Senate Committee on Banking, Trade and Commerce met this day at 8:00 p.m. to consider the following Bill:

Bill C-262, "An Act to support employment in Canada by mitigating the disruptive effect on Canadian industry of the imposition of foreign import surtaxes or other actions of a like effect".

Present: The Honourable Senators Hayden (*Chairman*), Aird, Beaubien, Benidickson, Burchill, Gelinas, Grosart, Isnor, Molson, Smith, Sullivan, Walker and Welch—(13).

Present, but not of the Committee: The Honourable Senators Forsey, Heath, McNamara and Molgat—(4).

In attendance: E. Russell Hopkins, Law Clerk and Parliamentary Counsel and Pierre Godbout, Director of Committees, Assistant Law Clerk and Parliamentary Counsel.

WITNESSES:

Department of Industry, Trade and Commerce:

The Honourable J.L. Pepin, Minister;

Mr. L.F. Drahotsky, General Director, Office of Industrial Policy Advisor;

Mr. R.E. Latimer, General Director, Office of Area Relations.

Amendments to Clause 6(1) and Clause 7(2) and the possibility of inserting a review procedure in the Bill was discussed.

At 10:00 p.m. the Committee adjourned to the call of the Chairman.

Wednesday, October 6, 1971.

(44)

Pursuant to adjournment and notice the Standing Senate Committee on Banking, Trade and Commerce met this day at 11:20 a.m. to further consider:

Bill C-262, "Employment Support Act".

Present: The Honourable Senators Hayden (*Chairman*), Aird, Beaubien, Benidickson, Burchill, Carter, Connolly (*Ottawa West*), Cook, Desruisseaux, Flynn, Gelinas, Giguere, Haig, Hays, Isnor, Lang, Molson, Smith, Sullivan, Walker and Welch—(21).

Present, but not of the Committee: The Honourable Senators Heath and Laird—(2).

In attendance: E. Russell Hopkins, Law Clerk and Parliamentary Counsel and Pierre Godbout, Director of Committees, Assistant Law Clerk and Parliamentary Counsel.

WITNESSES:

Department of Industry, Trade and Commerce:

The Honourable J.L. Pepin, Minister;

Mr. L.F. Drahotsky, General Director, Office of Industrial Policy Advisor.

Upon motion it was Resolved that Clause 6(2) be amended, Clause 7 be amended by adding thereto a new subclause (3) and that amendments be made to Clause 21.

NOTE: The full text of the amendments appears by reference to Report of the Committee immediately following these Minutes.

Upon motion it was Resolved to report the said Bill as amended.

At 12:20 p.m. the Committee adjourned until 3:00 p.m. this day.

ATTEST:

Frank A. Jackson
Clerk of the Committee.

Report of the Committee

Wednesday, October 6, 1971.

The Standing Senate Committee on Banking, Trade and Commerce to which was referred Bill C-262, intituled: "An Act to support employment in Canada by mitigating the disruptive effect on Canadian industry of the imposition of foreign import surtaxes or other actions of a like effect", has in obedience to the order of reference of October 5, 1971, examined the said Bill and now reports the same with the following amendments:

1. *Page 3:* Strike out subclause (2) of clause 6 and substitute therefor the following:

"(2) Not more than two-thirds of the members of the Board at any time may be members of the Public Service within the meaning of the *Public Service Employment Act* but a vacancy occurring in the membership of the Board that has the effect of temporarily reducing the number of members of the Board who are not members of the Public Service below one-third of the members of the Board does not invalidate the constitution of the Board or impair the right of the members to act if the number of members is not less than a quorum."

2. *Page 3:* Immediately after subclause (2) of clause 7, add the following as new subclause (3):

"(3) The Chairman shall preside at any sittings of the Board at which he is present and shall designate one of the other members to preside at any sittings of the Board at which he is not present."

3. *Page 8, clause 21:* In lines 9 and 11 strike out the words "fiscal year" and substitute therefor the words "annual quarter".

Respectfully submitted.

Salter A. Hayden,
Chairman.

Report of the Committee

The Standing Senate Committee on Banking, Trade and Commerce

Evidence

Ottawa, Tuesday, October 5, 1971

The Standing Senate Committee on Banking, Trade and Commerce, to which was referred Bill C-262, to support employment in Canada by mitigating the disruptive effect on Canadian industry of the imposition of foreign import surtaxes or other actions of a like effect, met this day at 8 p.m. to give consideration to the bill.

Senator Salter A. Hayden (*Chairman*) in the Chair.

The Chairman: Honourable senators, we have one bill for consideration this evening, Bill C-262.

We have with us the Minister of Industry, Trade and Commerce, the Honourable Jean-Luc Pepin; Mr. L. F. Drahotsky, General Director, Office of Industrial Policy Advisor, and Mr. R. E. Latimer, General Director, Office of Area Relations.

Following our usual practice, I think we should first ask the Minister to make a statement.

Honourable Jean-Luc Pepin, Minister of Industry, Trade and Commerce: Mr. Chairman and honourable senators, my statement will be rather short, Senator Forsey having done a remarkable job in introducing the bill, a bill which is slightly complicated and is introduced in, I will admit, rather complex circumstances. I am sure that all honourable senators have read the bill, that they have listened to those who spoke in the debate, that they have read the debates in the other place and, no doubt, the reports of the committee of the other place which considered the bill.

If I were to introduce it now very rapidly I would simply remind honourable senators of the permanent character of the bill itself, which character Senator Forsey emphasized extremely well. I would also remind honourable senators that even if the bill is of a permanent nature, it is not temporary application, to deal with the current crisis. As soon as the surcharge disappears, obviously the bill will no longer apply.

I would emphasize that its purpose is to maintain employment. In view of some of the things that have been said, I would point out that it applies equally to all parts of Canada. It may very well be that because of the concentration of industry in Ontario and Quebec the actual benefits will be higher, on a provincial basis, in Quebec and Ontario than they would be in, for example, Western Canada.

However, I can assure you that when the provincial ministers of industry and commerce attended a meeting that I called for the purpose of discussing the U.S. surcharge they were very keen to see this bill apply in their respective provinces. Despite, what might seem to an Ontarian, its rather small size, the benefits of this bill to, for example, Prince Edward Island, will be very important in Prince Edward Island terms. I think one has to bear all these things in mind. The effects in Prince Edward Island, though immensely smaller in dollars than the effects in Ontario, will be quite large, for Prince Edward Island. All the provinces were most interested in seeing this bill passed. Mr. Evans from Manitoba, for example, expressed dissatisfaction with some aspects of the bill, but he has not called for their non-application in Manitoba; you may be sure of that.

I repeat that it is not a profit maintenance measure. If there is no likelihood of significant export dislocation at a plant, assistance will not be provided simply for the purpose of making up the reduced profitability of a company on account of the import surcharge. The profits of a company is not the preoccupation of this bill.

Senator Forsey emphasized, as both I and my Parliamentary Secretary did, that this is not an export subsidy measure. A company receiving assistance is not obliged to maintain its level of exports for the purpose of this program. It does not matter where the products are sold, whether abroad or in Canada. In the other place I indicated that there were six or seven possibilities opened to a company receiving assistance under this bill. A company can use the money to effect a change of products. A company can simply add to inventories. A company can develop markets elsewhere. A company can do a number of things.

Senator Forsey: Faire de la peinture.

Hon. Mr. Pepin: Faire de la peinture si elle le préfère.

The Chairman: On that point, Mr. Minister, the purpose of the bill is to maintain employment, but if a company is going to change various products, it will have to spend money to do so. The money that it will spend will have to be its own money, because the only maintenance it gets out of this fund is the grant to maintain employment.

Hon. Mr. Pepin: I will come back to that in a moment. Senator Manning was emphasizing the difficulties of implementing this bill. Some of us have thought of that, too. It is not news. I will come to that in a moment, if you do not mind. Let me try to finish first the few ideas I wish to express.

Obviously, as Senator Forsey also said, this will not solve all the problems faced by Canadian industry in general—not even the problems arising out of the wide-ranging economic measures recently announced by the United States. Senator Forsey emphasized the word "mitigate"—in good English and in good French, too, "mitiger".

Already damage is being created, particularly in terms of the uncertainty which exists in Canada-United States trade relations, because of these U.S. measures. A number of companies are possibly not pushing as hard their exports to the United States as they would have otherwise. A number of people in the United States may very well feel that this is a great message to them, from high above, that a new psychology has to be implemented. So, damage is actually being done. The only thing the bill can do is try to limit the damage done to employment in Canada.

Senator Isnor: Should it not be the other way, that they should be putting a special effort into it?

Hon. Mr. Pepin: Yes, but when you do not think that the benefits will be as high as they have been in the past, or were expected to be, it is human for people to tone down a bit on the efforts they were making.

Senator Walker: I missed what you said. I understood you to say "when the surtax was withdrawn". What effect will that have? You said something about that earlier.

Hon. Mr. Pepin: As the bill concerns the surtax, when the surtax is withdrawn the implementation of the bill will stop.

Senator Walker: Yes.

Hon. Mr. Pepin: I cannot tell you that implementation will stop on the very hour the surcharge is removed because there probably will be a cleaning up job to do, but that is the general idea. If a similar bill is to be invoked again, the Government will have to demonstrate that there is another crisis, that there are circumstances similar to this, as indicated in the long title of the bill.

The Chairman: And most likely provide money.

Hon. Mr. Pepin: Yes. I presume that on that occasion it would be done, as the bill exists, by special estimates.

Senator Walker: Would it be by order in council or would you have to go to Parliament?

The Chairman: I am not sure. Would you develop that, Mr. Minister? I am not sure whether it can be done by estimates, because the bill statutorily limits the amount to $80 million and limits it to 1971-72.

Hon. Mr. Pepin: The difficulty we had here was perhaps to pass this as general legislation and not mention money and go for supplementary Estimates to get the money. We thought that it would be more democratic to put that particular amount of money needed for the next six months in the bill, with the clear understanding that when that period of time is over, or even if not enough money is being provided by this bill, the Government would have to go the supplementary Estimates way to get more money.

Senator Walker: You would have to go before Parliament for more?

Hon. Mr. Pepin: Yes.

The Chairman: There is a question we can settle at that time, whether you can go by way of Estimates at that time, where there is a statutory limit in the bill; but that is not the subject-matter tonight.

Senator Benidickson: No, but the Government Leader referred to a ruling in the other place, in the House of Commons last year, about limiting the power of legislation by limiting the amount which can be voted. I have not checked to find out what he meant by that, but that is what he said.

Hon. Mr. Pepin: Senator Benidickson, this bill will obviously be used in very extraordinary circumstances. As you cannot anticipate extraordinary circumstances as you do for ordinary circumstances, for which you anticipate in departmental budgets, obviously you must have a supplementary Estimate to cover these extraordinary, abnormal situations.

Senator Forsey: That is what I suggested, in answer to a question by the Leader of the Opposition in the Senate; and the Leader of the Government said that on account of this ruling last year in the House of Commons, that I was not aware of, it would not be possible to proceed by way of putting something in the Estimates, and I was rather surprised.

Hon. Mr. Pepin: If the chairman is right in what he has just said, or in what he has said as being a possibility—which is, if it is true that the Government cannot vote extra money for the period of time which is covered by the bill, then obviously we would have to come back to Parliament to get extra money—

Senator Walker: You would just amend the act. In the case of the National Housing Act—I was the minister responsible for several years—if we wanted more money, we amended the act and increased the amount.

The Chairman: I only interjected the question when the minister said that this was permanent legislation. Parliament retains control by virtue of the fact that they may have to come back for money from time to time—and that is a good feature.

Senator Benidickson: Even within the current year.

The Chairman: Yes, and that is a good feature.

Senator Benidickson: Yes.

Hon. Mr. Pepin: I would have thought that, even for the six months coming, even with the amount of money allocated to it by the bill, if things should turn worse than we have anticipated, and the possibility of getting more money through supplementary Estimates was still open, it would be done in that way—but if I am not right, we will do what the law says, obviously.

Senator Walker: It is a question of the way to do it and that is not our task now.

Hon. Mr. Pepin: I do not want to state again what the three eligibility criteria are. You remember these.

Senator Benidickson: No. That was referred to. Someone said in our debates that you recited in committee, for the House of Commons, that there were three basic principles, but they are not stated in the bill. Can you put them on record here?

Hon. Mr. Pepin: I will red them. The first criterion for eligibility is that the surtax has caused or is likely to cause

a significant reduction in employment at the plant. The word "significant" there is the important word. As I said in the House, and it was repeated here, the size of the plant has no relevance. What is "significant" in a plant employing ten people may be one or two; and what is "significant" in a plant employing a thousand people may be fifty less or more. We have given a lot of discretion to the board in these matters, because it is not always easy to define these things. I will come back to the discretionary aspect of the bill, if you wish, later on.

The second criterion for eligibility is that no less than 20 per cent of the plant's 1970 output must have been exported to the country imposing the surtax and was of a class that would now be subject to the surtax. As was explained, section 15 of the bill foresees the possibility that exceptions might be made, even to that 20 per cent rule or to the other criteria.

The Chairman: Where is the 70 per cent provided? Is that by regulation?

Hon. Mr. Pepin: The 20 per cent is in the regulations. We have to establish a difference here between what is in the bill and what is in the regulations. We tried to put as much in the bill as could be covered by the bill; but this 20 per cent basis is bound to change from one situation to the other, so we kept that for the regulations.

Senator Aird: You think that 15 gives you sufficient flexibility?

Hon. Mr. Pepin: 20 per cent.

Senator Aird: No. Section 15 of the bill?

Hon. Mr. Pepin: Yes. As matter of fact, some people have said this gave the board and the Government too much flexibility. What we are saying is that there may be hardship cases. There may be a company exporting 15 or 18 per cent in Cornwall, or in some place where unemployment is very high, and in these circumstances we wanted to keep the possibility of intervening, to help it maintain employment.

Senator Walker: You are going to be swamped with applications, are you not?

Hon. Mr. Pepin: We expect over a thousand. Mr. Drahotsky and his group have a list of all the companies that would be or could be eligible. They have tried to bring it down to what is expected. It would be 1,300 in the first 90-day period, so Mr. Drahotsky tells me.

Senator Isnor: What is that 1,300 based on—previous business?

Hon. Mr. Pepin: On a survey that we conducted in the first few days following the announcement of the surcharge.

Senator Isnor: Is it on the basis of the previous business?

Hon. Mr. Pepin: Yes, on the 1970 performance. Mr. Drahotsky may explain, if you are curious, the "base period" and to the "assistance period". It is a bit complicated and I would prefer not to try it.

The Chairman: Mr. Minister, may I interject a question here? It appears to me that, the object of this bill being to maintain employment, if employment is reduced because the product no longer finds a market in the United States by reason of the surcharge, that means that those people who worked on the production of that product would have no work to do, because the company obviously would not go on manufacturing a product, if they had no market. Then the grant is supposed to maintain those people in employment.

Hon. Mr. Pepin: Yes.

The Chairman: Does it determine in what kind of employment?

Hon. Mr. Pepin: No. That is exactly the flexibility which is given to the employer.

The Chairman: But there are limits to the way you can shift employees, as I understand it, in these days of unions.

Hon. Mr. Pepin: Yes.

The Chairman: There is a limit to where you can direct employees to work.

Hon. Mr. Pepin: This point was raised in the House by the member from Kent, if I remember correctly, and my answer was that these being extraordinary circumstances, I would hope and expect that unions and employers alike would show a bit of flexibility. I suggest that this will be done.

The only case where a company will be allowed to benefit, notwithstanding the fact that the company would not maintain employment at the level of previous times, is when something rather extraordinary takes place and when the board may be asked to fix a level. I presume you are aware of the possibility of circumstances that we anticipate, such as, for example, there being a fire in a plant and only half the plant being in production as a result. Obviously, in such circumstances, you would not want to keep the company at the level of employment it had before. If the company is going through a rationalization or a modernization program, and if under this rationalization program, they need only 75 per cent of the level of employment they had previously, then in such circumstances the board has the power to fix the level at which employment must be maintained. That is, again, common sense.

The Chairman: I am sorry to interject, but I was looking at section 12. Section 12 provides for the amount of the grant, and it would appear that the measuring stick provided there is the amount which in the opinion of the board would be adequate to maintain employment by the manufacturer throughout the prescribed assistance period at such levels as those prescribed or specified by the board, as the case may be.

It says, "maintain employment by the manufacturer". So that would appear to me at the moment to limit the direction of the expenditure of this money and the employment to the manufacturing operations of the company at that time.

Hon. Mr. Pepin: That is taken in a very broad sense. The company, as I said, can do a number of things. The company can produce for the domestic market or for markets other than the US market. The company can stockpile. It can develop new products. It can paint its sheds. It can do all kinds of things.

The Chairman: I am not sure about painting the sheds or raking the leaves. You might run into trouble with the unions in that regard. As to stockpiling, well, that may be, but, if we are going to get into that issue, the stockpiling should be considered by the Government.

Hon. Mr. Pepin: Well, we still hope, and have some reason to hope, that the surcharge will be temporary. Consequently, this is not a uranium type of operation, if you know what I mean.

The Chairman: I know that. I am trying to figure out how you can suggest that the company should carry on manufacturing a product with the grant and maintain its employment when it would be necessary to stockpile because there is no market.

Hon. Mr. Pepin: If they do not consider that this is a good thing to do, then they will do something else. One has to round corners a little bit at the moment, I feel.

The Chairman: Except that we are spending a lot of money.

Hon. Mr. Pepin: Yes. You bring up the point of the behaviour of unions and I must bring up the point of the behaviour of employers. It is necessary to be intelligent. We had a good demonstration of that here from Senator Blois the other day. There was a good Canadian reaction. He said quite openly that he thought that his company could have had other ways and means to cope with the surcharge than the use of Bill C-262. So much the better, in my opinion. When I read that I applauded. I was the only plum in the room!

The Chairman: That is the old stalwartism that we like.

Hon. Mr. Pepin: Now, Mr. Chairman, if I may finish my remarks, I will be open to questions.

I have read most of what has been said in the Senate, and I notice that the point was raised that the administration of this bill would be very difficult. That point of view implied that the Government was passing the buck by throwing this to a bureaucratic board, if I remember well.

Senator Benidickson: With no appeal, apparently.

Hon. Mr. Pepin: I will come back to that particular point in a minute, if you do not mind, but my answer to the other part is that we are not passing the buck at all. We are passing a bill! Also, we have regulations attached to that bill, and the board is probably less bureaucratic than most boards. It is less, because there is an input from the outside of three members to that seven member board.

Senator Forsey: It could be more.

Senator Benidickson: Where do you find that? As I read the section, and this bothers me, there will not be any more than four technocrats or bureaucrats; the only mandatory thing there is to put on the board one outsider as chairman. You could omit having two of the three outsiders, in other words.

Hon. Mr. Pepin: I could clarify that simply by saying that we are going to have three outsiders and four officials to start with.

Senator Benidickson: But it is not mandatory. It is simply your pledge.

Hon. Mr. Pepin: That is what we intend to do.

Senator Benidickson: I would hope you would utilize the full powers here and have at least three outsiders so that we would not run into the kind of criticism that President Nixon is receiving in the United States with respect to certain aids to industry in the emergency which labour says is not benefitting them. I would hope that labour would be represented on your board.

Senator Forsey: I was going to raise that very point.

Hon. Mr. Pepin: Bill C-262 is a typical Canadian compromise; it has some officials and some outsiders. The chairman will be an outsider. The Government has experimented in the past with this mix. We have the GAAP program, which is run that way, and it has been running well. So we are doing the same thing now. I repeat that the chairman would be the outsider.

Senator Benidickson: Am I not correct in saying that if this bill is passed you would be obliged by the law to appoint only one outsider, who would be the chairman. He would be the only one you would be obliged to appoint.

Hon. Mr. Pepin: I am afraid I had not really concentrated on this fine point, a point which Senator Forsey raised in his introduction. Concentrating on what I was trying to do, which was to get three outsiders and four officials, I did not find time to dedicate to this particular, very sophisticated point. But Mr. Drahotsky might have something further to say on that.

Mr. L. F. Drahotsky, General Director, Office of Industrial Policy Advisor, Department of Industry, Trade and Commerce: Mr. Chairman, the way I read the bill there will have to be three outsiders in the seven member board.

Senator Benidickson: Where does it say that there has to be . It only says that the chairman must be from the outside.

Mr. Drahotsky: I am sorry, sir, but it also says that not more than four members may be members of the Public Service.

Senator Benidickson: My point is that it could be five. The chairman, who must be an outsider, and four bureaucrats. That still is within the bill.

Hon. Mr. Pepin: You may have a good point, but what I am saying is that I am trying to get three outsiders, one of whom will be the chairman. So that is the way it is going to look.

Senator Burchill: There is another point. It says that there is to be a quorum of three. Would that mean that the three bureaucrats could meet without anybody from outside?

The Chairman: You would have to assume that notice would be given. I cannot imagine a meeting being held without notice. No, we must assume that.

Hon. Mr. Pepin: The point raised is a good one. We have seven members on that board and the quorum is three.

Senator Benidickson: You do not have to have seven.

Hon. Mr. Pepin: I am talking facts, not legislation. You may suppose that we will have seven, because that is our intention. It may be that the three who are going to meet at a particular moment at seven o'clock on a Wednesday morning will be three officials, because they will be the only ones available at that particular moment.

Senator Aird: Mr. Chairman, I think it would meet the point raised by Senator Benidickson and be in line with the Department's thinking if the words "not more than" were changed to "at least".

Senator Benidickson: That is what I had in mind. In addition, in section 6, subsection (3) I was proposing to put in an amendment. That subsection now reads:

> The Chairman of the Board shall be appointed by the Governor in Council from among those members of the Board who are not members of the Public Service.

Now that refers to the Chairman, but I do not see anything that would make it obligatory for you to appoint three members, at least, who are not members of the public service. Therefore I was going to propose that subsection 3 of section 6 should be amended to read that the Chairman of the board and at least two other members shall be appointed from those who are not members of the public service.

The Chairman: Well, Senator Benidickson, in subsection 2, it says that not more than four members of the Board may be members of the public service. Obviously one would then assume that the other members would not be members of the public service, and one of them would be the Chairman.

Senator Beaubien: But he only has to appoint five in all.

The Chairman: No, seven.

Senator Benidickson: Not more than seven.

The Chairman: That's right.

Senator Aird: I think, Mr. Chairman, it would meet the situation if you were to change the words in subsection 2 which now read "not more than four members . . . ." to, "at least . . . ".

The Chairman: That would remove all difficulty.

Senator Beaubien: Why not just say seven and be done with it.

Senator Benidickson: I have had a suggestion from Senator Forsey, speaking on behalf of you, Mr. Minister, that you are going to have a flood of applications, as you have indicated tonight,—1,300 in 90 days. I also think it was Senator Forsey who suggested during the debate that the board may have to divide itself into panels. Therefore I see no objection to the words "at least" because you may find that you will need more than seven to constitute three panels rather than two. If you are to deal with 1,300 applications, I would not want to restrict you to seven.

The Chairman: Well, Senator Benidickson, the point you raise would be dealt with if instead of the words "not more" in section 6, subsection 1 there were substituted "at least seven . . . .".

Senator Benidickson: I would be satisfied with that.

Senator Forsey: I should like to raise another point, Mr. Chairman. Quite a number of remarks have been made by you and by others about possible difficulties with unions. I might remark parenthetically that unfortunately not all workers are organized. I should like to ask the Minister first of all whether in view of the fact that there might well be difficulties with unions in some cases and in view of the importance of this whole matter to organized labour, the Government is considering appointing competent and experienced labour representatives on this board? It seems to me to be highly desirable to do so if such persons can be found, and I am inclined to think that it is not impossible to find them.

Hon. Mr. Pepin: Well, we have three questions in front of us now and I want to be sure we remember them. I am talking now about the difficulty of administration. We are also talking about the composition of the board and Senator Forsey is asking me if one of the members will be appointed from labour.

On the last question, we are trying to do that. Fortunately or unfortunately I am also trying to get a good distribution by region and whatnot in the composition of the three outside members of the board. To be absolutely frank, one of the "labour" names I have clashes with another name I have for the same region. So I shall see Senator Forsey afterwards to find out if he has any names to suggest to me, and if anybody has some names to suggest, I shall gladly consider them. The former "Liberal-Labour" member or the House of Commons from Kenora-Rainy River may have some ideas on that subject.

Senator Benidickson: I pointed out the criticism that President Nixon is getting about his August 15 statement from labour who feel that his legislation provides hand-outs, as this does, to industry but that that does not necessarily flow through to labour.

Hon. Mr. Pepin: I am very much aware of it, and I have a Minister of Labour who reminds me of it every day.

We were talking about the composition. Do you want to come back to that later?

Senator Benidickson: No, but I should like your comments on Senator Aird's suggestion in due course.

Hon. Mr. Pepin: Can we leave it then in suspended animation and come back to it?

I was talking about the difficulties and I recognize that there will be some. I have also implied that every board in the country be it at the provincial or the federal level, has all kinds of difficulties. I just wanted to tell Senator Manning that I am quite sure that the National Energy Board and the Alberta Energy Board when they have to decide what is surplus to Canadian needs in gas or oil, also have some difficulties. So I take it for granted that this board is going to have a rather difficult task and will have to carry it out in a relatively short period of time. The only way we can solve this is by appointing good people and paying them adequately so that they will stay with us for the duration which I would hope would be very short. I want to make it clear that I have taken note of the remarks made on the difficulties of administering this bill.

Remarks have been made also on the good relations that we should maintain with the United States. This is a question of judgment, is it not?

Senator Grosart: Mr. Chairman, before we leave the particular issue we were discussing, I should like to draw attention to subclause (2) of clause 7. It says:

(2) Three members of the Board constitute a quorum.

In the discussions on the bill, it has been pointed out that the board may sit in two parts. Presumably this means that as long as there are three members of the board available, the board could sit contemporaneously in two parts. This raises the question as to whether the chairman of each board or each panel would be somebody other than a member of the Public Service of Canada. We are discussing a bill where two-thirds of what the Minister described as the basic criteria are in the regulations and not in the bill itself.

The Chairman: Senator Grosart, in connection with the point that you have raised, Senator Forsey has suggested that due to the number of applications the board may find it necessary to divide itself. There is nothing in the bill to indicate that it will sit in panels.

Senator Grosart: No, Mr. Chairman, but if I may speak to my point, the Minister said that this may happen, and his parliamentary secretary who piloted the bill through the committee stage said it would happen.

Senator Forsey: It was not original on my part.

Hon. Mr. Pepin: You are absolutely right.

Senator Grosart: This is the way the committee would function, and I am now raising the point as to whether with the committee sitting in two parts it could have three members of the public service and no member who is not a member of the public service as a chairman of one of the sections of the board. This to me is very important.

Hon. Mr. Pepin: The answer is that the Department at this time with the knowledge they have of industry and the knowledge of the number of cases that might come up feel that a board of seven members is sufficient, but that the board, however, might have to sit in panels for a short period of time. We have left it to the chairman, who is going to be an outsider, as everybody knows, to decide on who should chair the other panel.

The Chairman: There is nothing in the bill on that.

Hon. Mr. Pepin: There is nothing in the bill on that.

Senator Grosart: You may have left it to the chairman, but the chairman does not have authority under the bill.

The Chairman: Senator Grosart, a very simple change in the bill could accomplish that. You could provide that the chairman of the board shall preside at meetings of the board, or a member of the board designated by him.

Senator Grosart: I quite agree. I am not saying that this is not a situation that requires other than a minor change, but that that change ought to be made.

Hon. Mr. Pepin: Let us keep this in suspension again because I am not a legal expert; I am one of those non-practising lawyers. I will see if we can obtain a good answer to the question you raised, senator.

Senator Grosart: Mr. Minister, I seem to be raising more than one point in connection with the viability of the bill. I would like to say that I am fully aware of the problems in drafting the bill due to the urgency of the situation, and anything I say is not meant to be in any way critical. It is merely a suggestion as to how it might be improved.

Senator Benidickson: And in an emergency situation a fair amount of flexibility is required.

Hon. Mr. Pepin: This is the way I took it. I do not agree with all the remarks Senator Grosart made in his speech, but I do agree with him on that one point.

Senator Grosart: There is a difference in what one might say in the Senate and what one might say in committee.

The Chairman: You are not through with your statement, Mr. Minister.

Hon. Mr. Pepin: I would like to comment on the good-relations-with-the-United-States concept. I think these relations are quite good. I was not too clear on what the criticism was, and I stand here to be enlightened. Was it because we have cut our troops in NATO, or because I went to China, or because the Prime Minister went to the Soviet Union? When one analyzes the situation one realizes that the Americans are doing now a number of the things we have done a few months ago. So it is difficult to accept blame, firstly, for something which seemed to be supported by the Canadian population, and, secondly, for something that the Americans themselves have decided to do on second thought. It is as difficult for me to accept the blame for what we have done in our relations with the United States. I agree with you that there is always room for improvement. Then the question is: What is it that we should have done? Should we have abandoned unconditionally the safeguards of the automotive agreement? Should we have made it possible for them to sell more military equipment in Canada? Should we have let them run our industrial policy? What is it that we should have done to make our relations with the United States better than they are?

I stand here to be enlightened. I do not think we should panic and decide to accept "political union" just because of what is happening now. This is a difficult time and I feel

we must keep our cool. We must have healthy, strong, virile negotiations with the United States. That is still very much possible, and that is what we are going to do now.

Senator Grosart: Mr. Chairman, the minister seems to be directing his remarks to some remarks which I made. I assure you I did not make that suggestion. As to the suggestion that we might have brought some of this on ourselves, I do not feel that this is what is before the committee. The bill is what is before the committee. Whether we might have avoided the bill or the surcharges is another matter.

Hon. Mr. Pepin: I cannot help it, I am a politician too!

Senator Grosart: I do not feel it is necessary to enter into discussions with you on that aspect. I would like to confine my concern this evening to the bill as it is presented here.

The Chairman: Mr. Minister, two questions have been raised. One is to amend section 6 by changing "not more than" to "at least seven"; and the other one is to provide that when they sit in panels, the chairman shall preside, or some member of the board designated by him.

Section 7(2), relating to the quorum. The words would be added that the Chairman or a member of the Board designated by him shall preside at any meeting.

Senator Forsey: Would that be a third subsection?

The Chairman: No, it would be just an added sentence to section 2. It would read: "The Chairman or a member of the Board designated by him shall preside".

Hon. Mr. Pepin: May we take this under advisement?

The Chairman: Yes; how long would you like? We are meeting again tomorrow morning. Would you like to think overnight?

Hon. Mr. Pepin: What time are you meeting tomorrow morning?

The Chairman: The committee is meeting at 9.30 and will sit the whole morning. If you, Mr. Drahotsky or Mr. Latimer wish to interject it will be in order.

Hon. Mr. Pepin: I am not a great authority on parliamentary procedure, as is well known. what would be the formula? We -ould have to return it to the House of Commons.

The Chairman: Yes; the bill would have to go back.

Hon. Mr. Pepin: I am rather keen to get this going.

Senator Benidickson: We are discussing possible amendments, and I do know there is reluctance to impose the delay involved by a Senate amendment. I have been a little disturbed by the fact that "manufacturer" is defined in the interpretation section. We have listened to the debate and the proceedings in the House of Commons committee. "Manufacturer" is wisely defined there, because the bill is really for the benefit of manufacturers although in other sections, section 3, for example, the word "industry" is used twice.

In ordinary parliamentary parlance agriculture and fishing are referred to as industries, yet there have been complaints in the press, and it was Senator Manning's point, that there is a possibility of discriminations in the regions because manufacturing is not prominent in certain areas. we were told, I think by Senator Forsey, without detail, which he is not expected to have, that there is provision to aid that section of the agricultural industry and that section of the fishing industry which do not export to the United States duty-free and are therefore subject to the surcharge.

I wonder if the minister would enlighten us, first of all as to the percentage of the agricultural industry as a whole whose exports to the United States will be subject to surcharge; similarly with regard to what is known as the fishing industry, the percentage of fishing exports subject to surcharge? Could he very briefly outline the legislation that Senator Forsey reminded us exists to enable the Government, in some parallel manner, to assist those two industries, which may have a fall-off in employment by reason of the imposition of surcharge? What portion of fishing and agricultural products is subject to duty?

Hon. Mr. Pepin: I will take one-half of the answer and leave the other half to Mr. Drahotsky. The concept of manufactured in the bill is borrowed from the General Adjustment Assistance Program. It has worked well there and is expected to work well here. Mr. Drahotsky can read it, but I believe Senator Forsey put it on the record.

Senator Grosart: No, Senator Forsey mentioned only one act, the Agricultural Stabilization Act. There are other acts involved in agriculture and, presumably, others in fisheries and perhaps in other primary products.

Hon. Mr. Pepin: I have established that the word "manufactured" is borrowed from the General Adjustment Assistance Program, with which some of you are familiar. It has worked well there and is expected to work well here.

The second fact I wish to place on the record is that, using this definition, it is estimated that approximately 85 per cent of agricultural products subject to the surcharge will be covered by this bill, which is a very important point to bear in mind.

Senator Benidickson: Because it is considered to be manufactured.

Hon. Mr. Pepin: Because it is processed.

Senator Benidickson: Yes, that phrase was used in our debate, processed and unprocessed goods in these primary industries.

Hon. Mr. Pepin: That is the main idea, that if 85 per cent of the agricultural products subject to the surcharge are covered by this bill, by far the major part is covered.

The Chairman: Mr. Minister, would you not say that all phases in the fishing industry, other than the actual catching and sale of the fish as such, are processing operations, which would come within the definition "industrial operations"?

Hon. Mr. Pepin: I would say that.

The Chairman: And would not that apply with relation to agricultural products?

Hon. Mr. Pepin: Let us leave that to Mr. Drahotsky; he is fairly well paid, so he must work also!

Senator Grosart: May I ask the minister, for clarification: I believe he said 85 per cent of agricultural products?

Hon. Mr. Pepin: Yes, subject to the surcharge.

Senator Grosart: Would be covered by the act, to simplify it. My question is: is the minister saying that 85 per cent of all primary products that might be affected by the surcharge would be covered, or is he referring only to agricultural products?

Hon. Mr. Pepin: I am referring only to agricultural products.

Senator Grosart: Would the minister enlighten us as to the situation with respect to other primary products?

Hon. Mr. Pepin: That is the part I am leaving to Mr. Drahotsky. Mr. Olson, on a number of occasions, has stated that he will be taking care of what is not covered by the agricultural products, by other means and other existing legislation.

Senator Benidickson: Was that statement made last Friday in the house?

Hon. Mr. Pepin: Yes, it is page 8345 of *Hansard* of last Friday, October 1, 1971.

Senator Benidickson: That was also referred to this afternoon in our debate.

Hon. Mr. Pepin: So now we have a number of questions left from Senator Grosart and Senator Benidickson. Mr. Drahotsky will endeavour to remember them and give the answers.

Senator Heath: Mr. Chairman, may I ask the minister a question? As we are considering this bill at the moment it might be helpful if we got this information. As I understand it this is a temporary measure. I wonder if it is part of what will become the law later to cope with more difficult problems which we have not yet felt? I think of the United States being such a big buyer of our exports, the American job incentive program and DISC, which the American manufacturers themselves are heavily underwritten by the American taxpayer. Will this be an initial part of the Government's policy to assist our manufacturing exporters, or are we just looking at it as a narrow stop-gap for the present?

An answer to that would certainly help me in considering the bill, if you could give me a little help in that direction.

Hon. Mr. Pepin: Let me answer that question in a cautious way. The bill is of general permanent nature, as we have established.

Other actions "of a like effect",—that is part of the title of the bill, can be covered by the bill. That is the general proposition.

Will the job creation investment credit, or whatever the name is, be covered by this in future? It is too early to say. As you know, these two programs, that one and DISC, have evolved almost on a daily basis in the United States.

Will it be what comes out of Congress at the end of the day? Will it have "a like effect"? That will be for the Government to decide when these things come out of the US Congress.

This is the sort of situation that would have to be assessed to find out if it is "of a like effect" and consequently can be brought within the provisions of the bill.

Senator Benidickson: I am glad that question was raised, because a little earlier you said that if not within hours, then very soon after the removal of the surcharge — you did not refer to any other possible American legislation, so I assume that you were talking about the American surcharge — this bill would become unnecessary.

Hon. Mr. Pepin: With respect, I did not say that.

Senator Benidickson: Did you not say that it would not apply?

Hon. Mr. Pepin: I said the application of the bill to that particular situation, being the surcharge, would come to an end.

Senator Benidickson: I was thinking of the question that was raised regarding the effects of DISC, which might be much worse than the surcharge, if they withdraw manufacturing from branch plants in Canada and divert it to the United States, becauye of the incentives that they offer if the DISC program is approved. I also wanted to make sure that when you said "the surcharge," you were talking about the United States. However, this bill might continue to take effect, perhaps by reason of the United Kingdom putting on a surchage.

Hon. Mr. Pepin: Yes, indeed. But in this case there would have to be a decision by the Government, by an Order in Council, to apply this bill to that particular situation which you are now contemplating. It is not automatic. We would have to decide if the situation is the same or "of a like effect", and consequently could be dealt with by this bill.

Regarding the job creation investment credit, when this bill comes out of Congress, and if it is approved by the President, the Government of Canada will have to decide whether it is "of a like effect" and whether the implementation of Bill C-262 is a proper approach to that particular injury.

If the answer is yes, then an Order in Council will have to be passed and the bill would apply to that particular US decision.

The Chairman: I am not sure that it is that easy. The words "a like effect" appear also, in section 3. The primary purpose is to impose temporary import surtaxes, or to take alternative action on anything having "a like effect" or an adverse effect on Canadian industry.

You have to say what is the area affected. Here is manufacturing. Therefore, when it is by way of surtax or anything of that nature, or by way of levy or restriction, there is a limitation. The limitation is the manufacturing industry.

Senator Benidickson: That is why I wanted an answer regarding fish. I was recently travelling in an aeroplane with my friend the member for Churchill, who remem-

bered that I came from Manitoba. Since moving to Ontario, to The Lake of the Woods, I have had a considerable interest in the export of fresh water fish.

He said, "What is the narrowness of the word "industry," because it is really for manufacturers?" He, of course, has put up a strong plea for fishermen in the other place.

Perhaps the minister could tell me whether the export of fresh fish from Manitoba lakes and the Lake of the Woods, which are filleted, frozen, or sometimes sent fresh, is now subject to duty and therefore subject to surcharge?

Hon. Mr. Pepin: I will let Mr. Drahotsky answer that question. However, regarding the previous question, the decision that the Government will have to make is whether this is the same or of "a like effect", does this apply to manufacturing according to the way it is defined here; and do we cope with it by an employment maintenance program?

If the answer to those three points is "yes", we can use this bill. If it does not fit, then we must try to find other ways. Mr. Drahotsky, Senator Benidickson would like to know what will be the effect of the surcharge on the fishing industry and how is it to be taken into account.

Senator Burchill: Senator Grosart asked about other national products.

Mr. Drahotsky: I have to deal with agricultural products and fish products together, because they are covered under the same commodity classification which we use in order to establish the impact of the surcharge on these sectors.

The commodity classification or group is known as the animal and vegetable products category. It includes a wide range of commodities, including live animals, meat, fish and shellfish, dairy products, hide and skins, live plants, cereal grains, vegetables, coffee, beverages, including whiskey, and other animal and vegetable products.

In looking at this category, our analysis shows that in 1970 some 63 per cent of our exports to the United States will attract the surcharge—that is slightly over one-half.

Senator Benidickson: Have thw words "processed" or "unprocessed" anything to do with that wide recital of commodities which you have given?

Mr. Drahotsky: Let me proceed to break it down as much as I can. As a rough guess, of the 63.5 per cent that will be affected in the animal and vegetable products category, close to 85 per cent are processed; in other words, are past the raw stage, and hence would be covered by this bill.

Senator Benidickson: Because there will be a surcharge imposed on that processed product?

Mr. Drahotsky: Because they are surchargeable and are at a stage of manufacture past the raw stage. The 85 per cent is the figure the minister referred to.

Senator Benidickson: Does the fileting of fish constitute processing?

Mr. Drahotsky: Yes, it does. Any manufacturing or processing operation, whether by hand or machinery, including fileting.

Senator Benidickson: Does gutting constitute processing?

Mr. Drahotsky: Gutting presumably for the purpose of the canning operation.

Senator Grosart: Mr. Minister, I do not deny for a minute that it is the intention of the Department of Agriculture to do this. What concerns me is that this bill, which deals with employment jeopardized by this surcharge, does not cover all employment. It seems to me that the bill should cover all employment and that we should not divide our GNP producers into sheep and goats. Why do we say we are going to cover manufactured products but not all products where employment is affected? I have some objection to the definition.

Senator Benidickson: Not all industries.

Senator Grosart: I would suggest to you that you may be on dangerous ground when we come to this retaliation business. I believe you would improve your position if you were to include all employment under this one bill. We are fully aware that there may be damage done to employment by the surcharge other than to those directly in the export business. These things could be taken care of by other acts, but I would suggest to you quite strongly—and I am not suggesting it is necessary to make the amendment now—that you give serious consideration to making this bill all-inclusive by covering all employment affected by the surcharge and not to take refuge, as I think has been done, in the fact that there had to be haste and so on.

I suggest to you that the definition of "manufacturer" is not a very good one. The definition excludes change by growth or decay. This means, as I understand it, that if someone processed a product in such a way as to lengthen its life, for example, or in such a way as to inhibit its growth they would not qualify. We all know the Japanese have a marvellous product which is now on the Canadian market and which has the effect of inhibiting the growth of a plant. Why is this excluded? We know why it is excluded under GAAP act, but the GAAP definition has been brought in holus-bolus, and I suggest to you without any careful consideration as to whether it applies to the specific circumstances here.

If you will look at clause 2 the definition of "manufacturer" definitely excludes change by growth or decay. Why? Does this mean that someone who has processed a product to inhibit decay is not a manufacturer? Surely, this is not so.

I understand why you may have brought this definition in holus-bolus, but I would suggest to you that it does not apply here. I realize you had to do these things in a hurry.

Hon. Mr. Pepin: The reason why we did bring it in, as I said before . . .

Senator Grosart: You said it worked very well in that situation.

Hon. Mr. Pepin: It did work very well.

Senator Grosart: That is the poorest reason in the world, Mr. Minister.

Hon. Mr. Pepin: It worked in GAAP.

Senator Grosart: To say that it worked in GAAP is one thing, and even to say that it will work in this situation without a careful examination of the circumstances is understandable, but it is something that perhaps we as members of this committee should question.

Hon. Mr. Pepin: I simply felt that we should try to cover as much of the area affected by the surcharge with this bill. When I was informed that 85 per cent was being covered and when Mr. Olson assured me that he was taking care of the other 15 per cent, I felt justifiably relaxed. I do not think you can chastise me too much for that.

Senator Grosart: I am not criticizing you, Mr. Minister. I agree with you that under the circumstances this may well have been necessary. I would not be making these suggestions if there had not been the stress made by yourself and others as to the permanence of this bill and the fact that once this bill is passed, then by Order in Council you could make regulations to bring anything of a so-called "like effect" under it, and also the fact that there is no appeal whatsoever from this board.

Hon. Mr. Pepin: If we are to have another situation "of a like effect," obviously we can amend the regulations to take better care of that set of circumstances.

Senator Grosart: You will have to because these regulations refer to time limits, and so on.

Hon. Mr. Pepin: You are right. My answer to that in the House was that a number of other important matters were and are dealt with in that way.

Senator Grosart: It is not a good way.

Hon. Mr. Pepin: It is not a bad one. If you are willing to bring back to the house every Order in Council that is of substantial importance I will agree with you, but in that event we may disagree quite strongly amongst ourselves as to what constitutes "substantial importance." If we were to bring back everything which, according to one person in the Senate or the House of Commons, is of substantial importance, the house of Commons and the Senate would not be able to do anything else than approve orders in council. That is a "raisonnement par absurdité."

Senator Grosart: Mr. Minister, you have made an excellent beginning in bringing the draft regulations before the committee.

Hon. Mr. Pepin: Yes, I thought this was a good start. We could have done it the way other countries are doing it—that is, by the side door—but we thought that this was a great event in Canada's recent history and we thought that we would share with the House of Commons and the Senate the difficulties involved. I did more than that; I brought the regulations into committee. This is not always done, as members know. I have the best possible record!

The Chairman: Mr. Minister, we have cross-fired on this point for a while now. The simple question is: Are you prepared to strike out the clause which excludes change by growth or decay or not, and if not, tell us why and that will settle the question.

Hon. Mr. Pepin: I am quite sure Mr. Drahotsky and Mr. Latimer together can answer that question.

Mr. Drahotsky: All I can say, Mr. Chairman, is that I am unaware and cannot conceive of an operation which would be confined solely to producing marketable products by means of growth or decay, nor am I aware of such operations constituting a sizeable or significant sector of our economy. If they do exist, I am not aware of them.

The Chairman: Can I put the next question to you, then? If that is your conclusion then we can safely say we can leave it out because we could not establish processing in relation to that.

Mr. Drahotsky: If I were the minister, Mr. Chairman, I would have answered . . .

Hon. Mr. Pepin: Pretend for a while!

Mr. Drahotsky: I am flattered that the only omission in this definition . . .

Senator Grosart: I did not say that.

Mr. Drahotsky: The only shortcoming in this definition is that . . .

Senator Grosart: I did not say that either.

The Chairman: Are you inviting us to find more? I should think you would try to get along with what we have been dealing with.

Senator Grosart: Mr. Chairman, I would like to oblige, but I just picked out one example.

The Chairman: We have really shaken this one, and the minister has to make a decision. Personally, in view of the answer Mr. Drahotsky made, I think that even if there were an exclusion there, what is excluded specifically would be excluded because it would not be processing; you could not have a processing operation of that kind.

Senator Grosart: It excludes the whole technological innovations of rust-proofing and methods of resisting metal fatigue, which is a very important scientific innovation, in which Canada is highly involved. Under this, if you process metals to prevent metal fatigue, that is to prevent decay, you do not qualify.

The Chairman: I do not know; it might be arguable.

Senator Grosart: Well, that is to prevent decay. What is preventing metal fatigue except to prevent decay? Just as it is with us senators!

Senator Forsey: What about:

> . . . change including change that preserves or improves the keeping qualities of that raw material?

Surely that covers something.

The Chairman: Certainly it covers the things Senator Grosart has been talking about.

Senator Forsey: I should have thought so.

Senator Grosart: This could be well interpreted, and probably would be by the courts I suggest, as excluding freezing, which we have been told is included. Freezing is to prevent decay.

Senator Forsey: It says "improves the keeping qualities".

Senator Grosart: According to this it excludes any process that is intended to prevent a "change by growth or decay".

Senator Forsey: Are you thinking of the aging of whisky?

Senator Grosart: Oh no, that improves it; that would meet my point.

The Chairman: It seems to me from the explanation we have that striking out these exclusions would not alter the extent or scope of the definition at all. With all the other things that we say may relate, for instance change by growth, we have to look at the other language, such as:

> . . . a physical change including change that preserves or improves the keeping qualities.

We know that if you do not improve the keeping qualities you get deterioration and decay, so they are already covered.

Senator Grosart: That is what I say, it is contradictory. You allow a manufacturing process that improves the keeping qualities but you do not include one that prevents decay. It does not make sense.

Senator Burchill: Are we finished with that?

The Chairman: I think so.

Senator Benidickson: No, Mr. Chairman. I raised the general question of industry, and said that in ordinary parlance we talk about the agricultural industry and the fishing industry. I was frankly surprised that such a high percentage of our exports of agricultural and fishery products are subject to the surcharge and duty. With respect to agricultural products, the Minister of Agriculture made a statement last Friday, which I read and thought I had with me but find I have not. It was a relatively short statement, and I think it should either be read or put in the record so that people who read our record know what we are talking about. That would deal with agriculture.

Nobody has told us what help will be given to the exporters of fish that has been processed and has been subject to duty on entering the United States, and is now subject to the surcharge. I am thinking particularly of the fresh water fish from Western Canada and Northern Ontario, but I am sure the Atlantic senators will have a problem there too.

Mr. Drahotsky: Of our exports of fish and shellfish in 1970 to the United States, about 35 per cent would have attracted the surcharge had it been in effect in 1970. Practically all of these products that would be affected by the surcharge, or are affected, are processed fish products: filleted, frozen, and chilled. It is our view that practically all—we are not aware of any exceptions—would fall under the purview of this legislation and would benefit from it.

Senator Welch: You have discussed fish. Now would you tell us about fruit?

Hon. Mr. Pepin: With respect to fish, I was going to say that at the moment the prices are particularly good.

Senator Benidickson: You are not suggesting they are good just because we have had a recent Jewish holiday, are you? I am told by the fish industry that that has a great effect on fish prices.

Hon. Mr. Pepin: I can say that frozen cod, I think it is, has gone up in price from 19 cents to 44 or 45 cents in the short period I have been minister. There is no cause-effect relationship between the two facts; it is just that market conditions are much better now.

Senator Smith: Processed salt cod on the New York market is 64 cents.

Hon. Mr. Pepin: You see, it could also be understood that the exporters are in a position to absorb the surcharge on this particular item.

Senator Benidickson: For the record I want the other fact to appear, that the fishermen, by a very high majority vote, those that are organized—the Indians are not organized but approve—have gone on record as saying that they would like to be exempted from the marketing board that operates for the Prairie provinces. That must be because of price, that the net return to them is not what they thought they got prior to the institution of the marketing board.

The Chairman: This is not part of this bill senator.

Senator Benidickson: They are exporters; practically all their products are exported to the United States, and they are processed products.

The Chairman: But they want not to be subject to the marketing board.

Senator Benidickson: That is a different question.

The Chairman: That is an entirely different question.

Senator Benidickson: When it comes to price betterment currently that the minister describes, that apparently cannot apply to freshwater fish of Northern Ontario, because those in the industry are not satisfied with the prices they are getting now under this new arbitrary marketing board compared with what they were getting two or three years ago, before the marketing board was in operation. I do not know what goes on with the Atlantic exporters.

Hon. Mr. Pepin: We have established that they are covered under this bill.

Senator Welch: Now may I have an answer?

The Chairman: Now let us have an answer on fruit.

Mr. Drahotsky: Perhaps I might give the information on the type of products in the fruit category that may be affected: fresh apples, which would be taken care of under the programs of the Department of Agriculture; frozen blueberries, which would be covered under this legislation; fresh grapes other than hothouse grapes, which presumably would be covered by the programs of the Department of Agriculture.

Senator Welch: Processed apples?

Mr. Drahotsky: Processed apples do not appear to be affected by the surcharge. There may be another answer. Either they are not affected or they are not a big item in our overall export sales to the United States, but they would be eligible under the bill.

Senator Benidickson: Inasmuch as the statement by the Minister of Agriculture last Friday was not in answer to a question but was a formal statement, which if my recollection is correct was not long, could it be agreed that it either be read or be made an appendix to our minutes?

The Chairman: Is that the wish of the committee?

Hon. Senators: Agreed.

See Appendix "A"

Senator Burchill: We have heard about fish, agriculture and food.

The Chairman: And fruit.

Senator Burchill: Now, what about lumber?

Hon. Mr. Pepin: If I can establish first that pulp and newsprint are not surchargeable, consequently, the bill does not apply.

The Chairman: Does that answer your question, Senator?

Senator Burchill: No.

Hon. Mr. Pepin: Indeed, you want to know about other forest products.

Senator Burchill: Yes, because I have an inquiry from the Canadian Lumbermen's Association.

Mr. R. E. Latimer, General Director, Office of Area Relations, Department of Industry, Trade and Commerce: On lumber, most of the lumber we sell in the United STates, there will be a reduction in the United STates tariff, we expect, under the final implementation of the Kennedy Round cuts; and on the assumption they go ahead with that, they would then be duty free and not subject to the surcharge, as of January 1, 1972.

Senator Molgat: Would there be a reduction or an elimination?

Mr. Latimer: An elimination of the tariff; and with the elimination of the tariff the surcharge does not apply to these free items. That is the expectation.

Senator Burchill: A manufacturer told me the other day, who had a plant shipping 65 million feet, the production of that plant, to the United States, that they will be subject to $4 a thousand under this.

Mr. Latimer: Precisely so, as long as there is a duty in the United States on lumber. If the United States does what we expect it to do, which is to eliminate the remaining U.S. tariff in accordance with their obligations under the Kennedy Round, on January 1st of 1972, they will then be duty free and because they are duty free they will thereby be exempt from the surtax.

Senator Burchill: You expect that to happen on January 1, 1972?

Mr. Latimer: Yes.

Hon. Mr. Pepin: In the meantime, what you have in mind is eligible under the bill, because obviously it is processed. I might add to this, that the surcharge in this particular instance is not as high as 10 per cent. As a matter of fact, it is more in the area of 4 per cent, because the surcharge can never be higher than U.S. tariff "column 2", which in this particular case limits the surcharge to 4 per cent. So it is eligible, it is only 4 per cent, and the prices are fairly good at this time.

The Chairman: We have had quite a run at this bill. If we think in terms of putting all this together, we have two questions outstanding, which the minister wants to think about overnight. They would involve an amendment to section 6, where we substitute "not more than" where we say "at least 7" members of the board; and in section 7(2) where we add to the sentence by saying that the chairman or a member of the board designated by him shall preside at such meeting. The minister is going to think about those. Subject to that, is the committee ready to approve the bill?

Some hon. Senators: Agreed.

Senator Grosart: No, sir. Before the motion is put, I would like to raise one other point.

The Chairman: Very well. Which section is involved?

Senator Grosart: Perhaps it might involve section 17. It involves the whole series of sections which deal with a manufacturer making an application. There is provision for the board, under certain circumstances and in certain situations, to go outside the act. The board may waive the three basic criteria, if it so wishes. The board may, in effect, appeal from the provisions of the act. I suggest there should be an appeal permitted to a manufacturer who is refused payment. At the present time, he would be subject to a decision by a board, the majority of whom almost certainly will be public servants. He may disagree with the decision of the board and he at the moment has no right of appeal. The minister was right to call attention to the section of the bill which says that the board shall operate under the direction of the minister. This would presumably mean, and the minister has said so, that a manufacturer could appeal to him, and he would give sympathetic consideration. At the same time, I think the minister weakened his case when he said he had never given directions to a board and, by implication, he never would. My suggestion is that there should be a right of appeal. Perhaps the minister would put in a right of appeal, perhaps to a board, perhaps to a federal court, perhaps to a judge designated by the federal court.

I suggest to the minister that it is terribly important that a right of appeal be written into the bill. A manufacturer may disagree entirely with the decision of this board—which, I say, again may be dominated by civil servants. The manufacturer feels he has been badly treated. Where does he go? The minister says he may come to him and that he could deal with the board. I suggest that in an act as sweeping as this, which gives tremendous power to the board—not only temporarily but permanently, if orders in council so expand it—that there should be written into the act a right of appeal.

I am going to ask the minister to consider this.

The Chairman: Are you suggesting a right of appeal from any decision of the board, with due regard for pretty strict time limits?

Senator Grosart: Those are details.

The Chairman: Say, to the president of the Federal Court or a judge designated by him? If the minister will not take the responsibility, it should go outside.

Senator Grosart: May I expand a little on this? I am fully aware of some of the problems. I am fully aware of the fact that this board will have a fantastic number of applications, that it must have authority to act with expedition. But this applies to the highest court in the land, it applies to divorce courts and to any other court. On the argument that the board will have a lot of work to do, that it will mean that some promptness to its decisions will be requisite, applies to any decision of any court or of any body corporately known.

In putting forward this suggestion, Mr. Chairman, I would like to go a little beyond this, because we have the suggestion to the minister that he conyider certain amendments to the bill. I see some problems, problems of expedition and other problems, if we were to insist on an amendment, or on some amendments to the bill here, so that this bill would have to go back to the House of Commons. The minister might think that this could open up the whole kettle of fish again.

The Chairman: A can of worms.

Senator Grosart: I say a kettle of fish and not a can of worms. The fish would be covered here but the can of worms would not.

Hon. Mr. Pepin: The can of worms is eligible!

The Chairman: The can would be processed.

Senator Grosart: The can would be processed, but the can of worms that I am speaking of is a raw product.

Hon. Mr. Pepin: Uncanned. You are being candid!

Senator Grosart: If the Minister feels he can accept the suggested amendments, he could simply give assurance to the committee that the act would be administered in conformity with the suggestions and that in due course—and by that I mean if the act was invoked again—in due course consideration would be given to these amendments. I personally would be satisfied with that. I should like, if I could, to get acceptance from the Minister of some of the suggestions we have put forward without putting him to the long process of taking the act back to the Commons, even if he agrees with some of the suggestions that have been made. I put that forward in connection with my suggestion, which is very fundamental and with which I think, on reflection, the Minister might find himself in some agreement.

Senator Benidickson: It does not have to be long in process.

Senator Grosart: If I were the Minister, I would not want to take this bill back to the Commons, even with a small amendment.

Hon. Mr. Pepin: Perhaps I could make a few comments on that. On the first point you make, I think article 15 dealing with special cases says that the board recommends to the Governor in Council. So the recommendation to cabinet will have to come from the board; not from me. The board studies the particular situation, and if the situation does not meet with one of the criteria, or with two or three of them, then the board makes its recommendation accordingly to the Governor in Council. I have not any authority to do that. The board will do that.

Senator Grosart: I am afraid that I do not get that point.

Hon. Mr. Pepin: I mean to say that the company which feels that it has a special case to make will not make it to me. Some members of the house were afraid that I would be the recipient of claims from companies. This is not the way it is going to be. It is going to come to the board and from the board it will go to the Governor in Council. It will go as a recommendation.

Senator Forsey: That applies only under section 15.

Hon. Mr. Pepin: Yes, sir. I just wanted to straighten that out.

Senator Grosart: If I may point out, Mr. Minister, this is the section where the board is of the opinion that a grant to the manufacturer would be outside the purpose of the act.

Hon. Mr. Pepin: That is it. I was just wondering if that was clear enough in your mind.

Senator Grosart: Oh, of course.

Hon. Mr. Pepin: All right.

Senator Grosart: What I object to very strongly, if I may say so, is the fact that this board can now say that in its opinion the particular grant it wants to make is not outside the act, notwithstanding the act. This board could say in effect, if I may say so, that it could not care less about the act. It could decide that, in its "opinion"—and that is the explicit word in section 15—in its opinion the application is not outside the act.

Hon. Mr. Pepin: That is it.

Senator Grosart: I might say that the draftsmanship in sections 8 and 9 is rather more careful. In section 8(2), the draftsman has said, "to the extent deemed necessary by the Board." This is a legitimate case because he is only talking about internal arrangements. And when you come to section 9, "the Board may make such rules as may be necessary," with this I agree also. It is not what the board thinks is necessary but what actually may be necessary. Therefore, the courts may decide whether it was necessary or not. Later on in section 9 it says, "may do all things that are necessary," and that again is not what the board thinks is necessary or the minister thinks is necessary but what is in fact necessary. Therefore, it is subject to review by the courts.

On the other hand, when we come to section 15 and it says that the board "is of the opinion that a grant to the manufacturer would not be outside the purpose of the act—"

Hon. Mr. Pepin: If it is not outside, it is inside.

Senator Grosart: So, regardless of anything in the act, regardless of the 17 sections or anything else, the board decides that it can say that this application is not outside the act, and that is the end of it.

Senator Forsey: No.

The Chairman: You are not reading the whole section, senator. You must realize the limitations. If they decide that it is not without the purposes of the act, then they can go ahead and give a benefit to the manufacturer. That is beneficial.

Senator Grosart: Of course it is.

The Chairman: Well, to whom do you want to give an appeal in these circumstances?

Senator Grosart: I am not speaking of an appeal here. I am saying that in this particular case I object to any board being able to say what is inside or outside the act.

Senator Forsey: May I point out, Mr. Chairman, if I read this section correctly, that it says when the board is of the opinion it may recommend to the Governor in Council that a grant be authorized. Surely the Governor in Council has then to decide. The board does not say so and so and that is the end of it.

The Chairman: That is right. The Governor in Council will make the decision.

Senator Grosart: But this board can say to the Governor in Council, "We have decided that this is not outside the act." In the natural course of events the Governor in Council or cabinet is going to take that recommendation and I say that the board should not be put into the position of being judge.

Hon. Mr. Pepin: Who should do it, then, the minister?

Senator Grosart: The board should not interpret the act by saying that this is not outside the act.

Hon. Mr. Pepin: The board makes a recommendation to the cabinet suggesting that this is within the purposes of the act.

The Chairman: Mr. Minister, what Senator Grosart is overlooking is that, where an application is made to a board, the board has to determine whether it has any power or authority under the act to hear it. All that means is that they decide they have power to hear it. That is within the scope of the authority the board has. That is certainly the primary consideration. If you want to wipe that out, then you wipe out the whole bill. No board could function unless it could assume that it had authority.

Senator Grosart: Of course, but why then do you give it under one section specific authority to decide that this is not outside the act? It is obvious from any general reading of the bill that this is designed to allow the board to say, "Look, the act says so and so but we want to say this is not outside the act." If you read the whole bill, that is clear.

Hon. Mr. Pepin: I think you exaggerate.

Senator Grosart: I do not think I do exaggerate, because I have never seen a bill with this kind of phraseology, and I have studied a lot of bills.

The Chairman: I have seen many such bills. If I had a little time I could pick them out for you. There are laws where the first function of the board is to determine whether they have authority. I think one example is the anti-dumping tribunal. They have to decide whether they have authority.

Senator Grosart: Every board has to decide that.

The Chairman: Of course. Exactly.

Senator Grosart: Well, every decision of the board is that it is not outside the act, but I will not argue that point.

Hon. Mr. Pepin: Senator, section 15 is really there to take care of cases of the type I have indicated, for example, where the company is exporting 19.2 per cent. It is not to bring in all kinds of situations that are irrelevant to the purposes of the bill.

Senator Grosart: Let us get back to the appeal.

Hon. Mr. Pepin: The appeal, of course, is a matter that was raised, as you know, either in committee or in the house. I recall at the time what was said seemed to be so reasonable that I regretted being on the side of Caesar instead of on the side of Caesar's wife, on which side Senator Grosart is at this time. The question really is who should be the authority to whom somebody would appeal from the board. You mentioned the courts. Well, the courts may receive this sort of appeal on legal grounds to interpret the law and that sort of thing, but certainly not to interpret the factual situation that exists. The honourable judge knows ten times less about the realities of the situation in which the company is than the members of the board would. I do not see why you should appeal on factual matters.

Senator Grosart: You would wipe out 90 per cent of corporate law, if that were true. The courts do decide facts.

The Chairman: Of course, you are practising law tonight too, Senator.

Senator Grosart: I am not practising law.

The Chairman: You are having a fist at it. Not a very good one, but a fist.

Senator Grosart: I am simply trying to do my job here as a member of the committee.

The Chairman: That is right.

Senator Grosart: It is quite irrelevant whether I am a practising lawyer or otherwise.

The Chairman: Well, I am not interfering with what you are saying; I am simply pointing out certain things.

Hon. Mr. Pepin: This is certainly a very lively committee. I am enjoying it.

Senator Grosart: It does not matter whether I am a lawyer or not. I am perfectly entitled, as a member of this committee, to ask the minister questions.

The Chairman: No one has challenged your right. You are getting excited unnecessarily.

Hon. Mr. Pepin: There is obviously something arbitrary about the board's having full authority to make decisions in this case. But I do not see to whom one could appeal, and I am saying that there is a *de facto* possibility of "appealing" to the Minister. I have responsibility in Parliament for a number of these boards, and I can only recite my own experience on the subject, and I have not run into too many difficulties. If a company feels that it has not received total justice from one of the boards for which I am responsible, they come to see me and I say, "Well, I shall make very, very sure that all the facts that you bring to my attention are brought to the attention of the board; I will organize meetings and I will ask somebody from my department to support the claimant in these matters if there is reason to do so." The choice I have really is between having confidence in what the board has decided, making sure that all the facts are before the board, or substituting from my own knowledge my own decision for what the board has to decided. Now, I am not that pretentious, yet. Perhaps I shall be in the future, and if that should happen, then it will be time for you to get rid of me! But I really think that the reason governments appoint boards is to make just that kind of decision.

Senator Grosart: But, Mr. Minister, there is an appeal from many boards, and what I am suggesting to you is minimal; I am suggesting that it should be written into the act that an appeal can be made to the Minister. What you are suggesting is that when a board rules against a manufacturer, he then starts to use some kind of political persuasion rather then being able to appeal as of right. I suggest it would help you if there was written into the act a clear short statement that an appeal shall lie to the Minister, so that any representations will come to you as an appeal and as of right, and not as some kind of backdoor political persuasion. My suggestion is that simple.

Hon. Mr. Pepin: Well here I am caught between two fires.

Senator Grosart: Speaking to your second point, this does not mean that you are destroying the effectiveness of the board. It merely means that an appeal can be brought to you as of right, and then you can dispose of it in the manner which you are describing.

Hon. Mr. Pepin: But then it is not a real appeal. As I understand an appeal, it means that you have the right to go to a higher authority which is going to make a decision. I think what you are talking about is another line of communication. It is not, I suggest, a real appeal, unless my understanding of the word "appeal" does not make sense. My understanding of an appeal is that when a client is not satisfied with a decision rendered, for example, by a lower court or a lower tribunal, he can go to a higher one to get a decision. So, as I say, I think what you are talking about is another line of communication. But this already exists, and businessmen know that it exists. Let me say that every so often—every month or so—I have a personal visit from some company official unsatisfied, for one reason or another, with a decision rendered by one of the boards for which I am responsible, asking me to see to it that a second look is given to the particular matter that has been decided by this board.

Senator Grosart: But my suggestion is quite simply that they be permitted under the act to come to you as of right.

Hon. Mr. Pepin: I regret that I am, as I have already said, caught between two fires. There are some people in the house and I presume there are some here who would be tempted to say that the Minister should not be given too much authority to interfere in these matters. So I have to play safe in between the two opinions. Clause 8 of the bill says, "Subject to the regulations and direction of the Minister, . . .", so I presume I could give that type of recommendation.

The Chairman: Well, Mr. Minister, suppose we put it in this way and you can think about it. Where a board decides against an applicant—and I think that is the case Senator Grosart is talking about—the person who is affected by that decision has a right to go to the Minister to have that decision reviewed. Let us get away from the word "appeal".

Senator Grosart: That is an excellent suggestion.

The Chairman: Will you think that over and deal with it when you are giving us the answers to the other questions?

Hon. Mr. Pepin: Irrespective of the fact that it could be in the bill, I am saying that this is the way it is now being done and this is the way I expect it to be done again. Maybe that is not as good as having it specified in a clause in the bill, but bearing in mind the timetable that you have been referring to so kindly, I suggest that this probably would be good enough for the interested parties in industry.

The Chairman: Now, honourable senators, we have three points that the minister is going to look at, and the third one is the question of review of an adverse decision by the board. The minister is going to consider these three points and let us have his answer in the morning. In the meantime is it the wish of the committee that all the other sections of the bill be approved?

Senator Benidickson: Before we come to that, Mr. Chairman, the minister has indicated, and I appreciate it, that he has read our *Debates*. I am sure he will recall that Senator Grosart said he was going to concentrate on four questions. I think his fourth question was — were better alternatives available than this bill and so on. Then Senator Martin, the Leader of the Government and a member of the cabinet said he thought there were; that the United States could have used other measures other than the surcharges, and that they would have been better employed. Now my notes say, and I have not yet read *Hansard*, that Senator Martin did not state what in his opinion these other better measures were on the part of the United States. Would the minister care to make any comment on that?

The Chairman: Before the minister comments, senator, and I am not going to say that he should not, I should point out that we have the bill before us.

Senator Benidickson: Yes, but the bill is the result of an action taken by the United States.

The Chairman: It arises by reason of that action.

Senator Benidickson: Yes, it arises by reason of that action. Now a member of the Government has suggested

that from our point of view and even from their point of view they could have done this in a better way.

The Chairman: Maybe the minister does not know what Mr. Martin was thinking about.

Hon. Mr. Pepin: I really do not care to comment on this. I assume that Senator Martin may have had in mind—and I do not know this but am merely assuming it—that the Americans could have gone the way of devaluation or something like that.

Senator Benidickson: I accept that answer.

Hon. Mr. Pepin: They could also have fought inflation the way we did in Canada.

Senator Benidickson: Now, Mr. Minister, referring to clause 21, my recollection is that you made a verbal commitment to the House of Commons that you would report more frequently than the bill requires.

Hon. Mr. Pepin: On a quarterly basis.

Senator Benidickson: I can see the situation arising, if you were to report only as infrequently as this bill requires, that the board might extend aid to an employer or the owner of a business and it would be a long time before the people whom this bill is supposed to help—namely the employees—would know that that industry had been assisted and they might feel that the assistance has not gone to them in the spirit of the bill. It would not be very effective if you only reported once a year, so I would like you to repeat that undertaking.

The Chairman: Senator Benidickson, if that is the issue, the quickest and best way of obtaining the information would be publication of board decisions.

Senator Benidickson: Some members of the House of Commons requested that be done. The minister compromised and said that he would not publish each and every decision, but that he would do better than clause 21 requires. Members of Parliament, as well as the employees of the industry assisted, would receive information more promptly than is provided in clause 21.

Hon. Mr. Pepin: I must be very clear on that, because I did not promise to give detailed, industry by industry, amounts of money by amounts of money, reports. I said, after a long discussion, that I would give quarterly reports covering sectors of industry.

Senator Benidickson: That means they would be anonymous, or group reports.

Hon. Mr. Pepin: Yes, I added to this, as I have done on previous occasions with other boards for which I am responsible, that I would entertain questions, written or oral, by members of the house or the Senate and on each occasion I would go to see the company, as I have done on a number of occasions, and attempt to obtain their consent to my revealing that they have received the assistance.

Senator Benidickson: Notwithstanding that, grants to industries under, shall we say the legislation of the Department of Regional Economic Expansion, are practically individually advertised and publicized.

Hon. Mr. Pepin: You are right; there is a different situation.

Senator Benidickson: There is full publicity if an industry receives a grant to encourage it to locate in an underveloped area, or for other reasons receives a governmental capital grant. The community knows it, the potential employees and everyone else know of it. I remember that you were cautious in that regard and did not make that full commitment.

Hon. Mr. Pepin: My feeling is simply that that would be publicizing that industry "X" is having difficulties, which may not be the right thing to do. These are very special circumstances.

Secondly, I am afraid that if we start along this line now, the next step would be for me to have to publicize all research and development grants and all that is done in my department for industry. I do not think this would be in the best interests of anyone.

The Chairman: Senator Benidickson has indicated that he accepts the minister's explanation.

Are you prepared to approve the bill with the exception of the three points which the minister will consider overnight? Mr. Minister, you could have Mr. Drahotsky come in to advise us tomorrow morning.

Hon. Mr. Pepin: In the case of the amendments suggested by Mr. Grosart, I have extended myself to the fullest, short of accepting the amendment; I do not think I will be accepting it.

I will report on the other two points tomorrow, that is with respect to the quorum and the seven members.

It is a matter of being courteous enough to consult the people who conducted the drafting of these provisions.

The Chairman: What did you say with respect to Senator Grosart's amendment?

Hon. Mr. Pepin: Clause 8(1), which provides:

> Subject to the regulations and the direction of the Minister, . . .

Might for all practical purposes include the possibility of a company which is dissatisfied with the decision of the Board to ask the minister for a review.

Senator Benidickson: It has been your practice then to ask the Board to reconsider, if there is new evidence.

Hon. Mr. Pepin: For the reasons brought up by Senator Grosart.

In the case of the other two suggested amendments, I hope the House of Commons will gladly agree to them.

Senator Grosart: I am not clear, because one of the others was suggested by me. However, I would ask you to reflect on the suggestion made by the Chairman, that you write the right of a request for review right into the act. I ask you to think carefully of the very wide powers given under this act and its possible extension by Order in Council to situations we cannot even contemplate at the moment. The fact that this is a board consisting of a majority of public servants should be borne in mind. I would ask you to reflect very carefully before you reject that. I particularly

ask, if you accept my way out, if you like, that you give us an assurance with respect to these matters if you feel that for reasons of urgency, among others, this should be passed without further delay.

The Chairman: As I understand it, the minister will let us know his views on these three points tomorrow.

Senator Grosart: I just hope that at this point he will not rule out consideration of the three points.

Hon. Mr. Pepin: As a matter of fact, I am accepting your own recommendation *de facto.*

Senator Grosart: I started with that particular aspect by pointing out that you had said that "and the direction of the Minister" appeared to be a saving clause. However, this does not, I suggest, now include the right to ask for a review.

The Chairman: We must have some end to discussion. The committee has approved all the clauses of the bill except these three points, on which you can speak tomorrow, Mr. Minister.

The meeting is adjourned until 9.30 tomorrow morning.

The committee adjourned.

Ottawa, Wednesday, October 6, 1971.

Upon resuming at 11.20 a.m.

The Chairman: We now have several amendments to consider in relation to Bill C-262. Some senators present today were not here last night, so I will briefly review what took place.

The committee approved all clauses of the bill except clauses 6, 7 and 8. Certain points raised for particular consideration were indicated to the minister, who agreed to express his views to us this morning. We expect him shortly, and I will prepare you by outlining the proposals.

With respect to clause 6(1), the proposal was to strike out the words "not more than" in the third line and insert "at least". The feeling of the committee was that the wording "not more than seven" would allow four, five, six or seven to be appointed.

Subclause 2 of the same section provides that "Not more than four members of the Board may be members of the Public Service". Unless the full seven were appointed there might not exist a reasonable balance between the Public Service representation and others. The proposal, therefore, is to substitute the words "At least" for "Not more than".

It was indicated by the minister that in the course of the operations of the board it might very well sit in panels. The question then arose as to who would be the chairman of each panel. Clause 6(3) provides that:

> The Chairman of the Board shall be appointed by the Governor in Council from among those members of the Board who are not members of the Public Service.

The Chairman, if there are two panels, cannot subdivide himself and act as chairman of each meeting. Therefore our proposal was that clause 7(2) be continued to add: "and the chairman of the Board or a member of the Board designated by him shall be the presiding officer".

I see the minister has arrived. I have informed the committee of the proposal to amend clause 6(1) by substituting for "Not more than", "At least seven . . . ".

Senator Flynn: Would there be no limit? Is it at least seven?

The Chairman: At least seven; yes.

Senator Flynn: There would be no limit?

The Chairman: That is correct.

Senator Connolly: It would be a matter of judgment for the Government to decide.

Senator Flynn: Twenty members could be appointed and if some were not suitable an attempt could be made to arrange with the chairman to dispense with the services of those members. Perhaps it should be at least seven and not more than ten.

Hon. Mr. Pepin: I am grateful for Senator Flynn's intervention. I agree with him that the words "at least seven" would be open to all kinds of other possibilities.

We do not want to have more than seven, for the very simple reason that to do so would make it very unwieldy and difficult to operate.

If honourable senators do not object, we will state "not more than seven",and we will concentrate on other changes that can be brought about.

The Chairman: The words "nor more than seven" will not cure the difficulty that we see here.

Hon. Mr. Pepin: That is what I intend to deal with. The bill says "not more than seven". We felt that more than seven would make it difficult for the board to operate efficiently. We were however looking for a board membership sufficiently numerous to have, in effect, two panels. That is achieved by the words "not more than seven".

However, it may be that at other times five would be enough, and five is "nor more than seven", if I might sound a little complicated.

The main preoccupation of the committee last night was that of the "mix" between outsiders and officials.

I think we should devote our attention to clause 6(2) which says:

> Not more than four members of the Board may be members of the Public Service within the meaning of the Public Service Employment Act.

The significance of that is that on a five-member panel, four would be officials. Under clause 6(3), the chairman would be an outsider. On a board of five members you would then have four officials, and one outsider, who would be the chairman.

I understand that honourable senators do not like that provision, that they would prefer to have three outsiders on a seven-man board, and, presumably, at least two outsiders on a five-man board.

The Chairman: That is right.

Hon. Mr. Pepin: That can be accommodated by the following amendment to clause 6(2):

> Not more than two-thirds of the members of the Board at any time may be members of the Public Service within the meaning of the Public Service Employment Act.

That would cover it. If we say that not more than two-thirds should be officials, public servants, we would have two outsiders on a five-man board.

The Chairman: Two-thirds of seven would be four, because you would have an excess over three and you cannot fractionalize that.

Hon. Mr. Pepin: On a seven-man board we would have four officials; on a six-man board, four officials; on a five-man board, three officials; and on a three-man board, two officials. I repeat my suggestion, that "not more than two-thirds of the members of the board at any time may be members of the Public Service within the meaning of the Public Service Employment Act."

The Chairman: Senator Aird, you made a similar proposal last night. How does the suggestion strike you?

Senator Aird: I think it meets the consensus expressed last night. We were concerned primarily about the mix.

Hon. Mr. Pepin: If Senator Aird will allow me to continue, I think that for reasons of safety we should add to what I have read the following words:

> . . . but a vacancy occurring in the membership of the board, that has the effect of temporarily reducing the number of members of the Board who are not members of the Public Service below one-third of the members of the Board does not invalidate the constitution of the Board or impair the right of the members to act if the number of members is not less than a quorum.

An outside member might resign because he has insufficient time to do the job, or because he thought it was easy and he finds that it is tougher than he expected. The board would then be unable to operate until another member was appointed.

The Chairman: A few more words should be included in the suggested amendment, that when there is a resignation the Government should act within a reasonable time to find a successor.

Hon. Mr. Pepin: That is the sort of difficulty we find ourselves in when we make changes.

Senator Flynn: The solution to the problem might lie in saying "at least seven and not more than ten".

Hon. Mr. Pepin: But that does not solve my problem, because at times I might want less than seven. If you say "at least seven", you will be ordering me to have at least seven.

Senator Flynn: It is possible that their appointment might be on a temporary basis.

Hon. Mr. Pepin: All these appointments will be on a temporary basis.

Senator Flynn: If you have "at least seven and not more than ten" you will always be able to maintain a balance between members of the Public Service and outsiders. Furthermore, it will solve the problem in clause 7(2) where three members of the board constitute a quorum, in that you may be able to have an outsider and a member of the Public Service.

Hon. Mr. Pepin: If you say "at least seven", you are telling me to appoint at least seven members. If I do not need seven and five or three are able to do the job, you are suggesting in effect that I should spend money unnecessarily, which I am sure is not your intention.

Senator Flynn: If they are paid so much per day that they work, the problem does not arise.

Hon. Mr. Pepin: I would have to appoint someone and then say to him, "I am sorry, we do not need you; stay at home."! I would suggest that honourable senators leave me the flexibility of having seven, five or three. I would also suggest that the amendment I have proposed takes care of the Committee's main preoccupation, which is to have a better "mix" between officials and outsiders.

The Chairman: Yes, I think it does; except that I should like to have some assurance in the bill that vacancies on the board will be filled with reasonable despatch.

Senator Walker: A minister might wish to control the thinking of the board, as to what province they should give it to and what amount.

Hon. Mr. Pepin: I think the honourable senator is unnecessarily cautious. In such a situation there would be all kinds of things happening. There would be questions in the house and there would be newspaper men reporting any abnormality. And if I tried to control the thinking of the board, the members would resign.

One day it was suggested that I was exercising an influence on Mr. Duffett of Statistics Canada. He said openly that if a minister ever did what someone had suggested I was doing, he would resign. I suggest to honourable senators that this applies also to the board.

Senator Carter: The minister said that he might want seven or at times only five. Will appointments be made for special problems, and what will he do if only five are needed?

Hon. Mr. Pepin: Let us bear in mind what Senator Forsey said on the first day, that this is permanent legislation, but is temporarily applied to a temporary situation, namely, the US surcharge. Therefore it would not be a permanent board attached to permanent legislation. It will be a temporary board attached to the temporary application of this bill.

Senator Flynn: You mentioned the statement made by Senator Forsey, but he was contradicted by the Leader of the Government yesterday. I put the question to the Leader of the Government and he said that you could continue with this legislation after the present fiscal year and after you have exhausted the $80 million by different methods. The Leader of the Government in the Senate stated it would require an amendment to this legislation in order to continue afterwards.

Hon. Mr. Pepin: Yes, he is right.

Senator Flynn: Who is right?

Hon. Mr. Pepin: Whoever said the right thing with respect to the provision of further money after the duration of the occasion of the application of this billeïm In order to have it continue beyond the present year I would have to return to Parliament to get further money. I could do that in two ways; by way of supplementary Estimates or alternatively by an amendment to the bill. I suggest that I would take the way of supplementary Estimates.

Senator Flynn: You are in contradiction with the Leader of the Government.

Hon. Mr. Pepin: No, because in both cases I would return to Parliament.

Senator Flynn: You would come back to Parliament by way of supplementary Estimates?

Hon. Mr. Pepin: It is legal.

Senator Flynn: It seems very curious anyway, as far as this is concerned, that you would leave sections 4 and 5 as they are and by way of an item in the Estimates continue this legislation. These sections have to be read with the rest of the bill, and it seems to me that the limit on the amount and the period of application of the bill . . .

Hon. Mr. Pepin: One does not know what the periods or amounts are going to be. That is the point of departure.

Senator Flynn: I have no objection to your purpose, but I do say that it is badly expressed. If you had said in section 6, for instance, that after the expiration of the present fiscal year the amount required to continue this legislation will be appropriated each year, if that was the case, we would know that this would be the method, but as it is presented now it looks as if you are hopeful that you would not need this legislation after April 30.

Hon. Mr. Pepin: That is it.

Senator Flynn: Well, all right, but do not play on both sides.

Hon. Mr. Pepin: I admit to that. I could have said in the bill that moneys for the implementation of this bill will be provided for by supplementary Estimates.

I think this is a moment of great importance in Canada's history and we were trying to ask Parliament to do as much in these circumstances as could be done by way of Parliamentary action, and this is why, perhaps wrongly, we put the $80 million provision in the bill. It might have been cleaner to do it the other way.

The Chairman: Senator Flynn, notwithstanding the fact that the minister has said he could do it by way of supplementary Estimates, I do not think he can in this bill, the way it is drawn, because there is a limit of $80 million. That is statutory.

Senator Flynn: That is my way of thinking also.

Hon. Mr. Pepin: If I need more money I have to go to Parliament, but I can go to Parliament in two ways: either by asking for an amendment to the bill; or by asking for further funds by way of supplementary Estimates.

The Chairman: I think you can only go one way, Mr. Minister, and that is by way of an amendment to the bill.

Hon. Mr. Pepin: Well, let us hope we do not have to go at all!

Senator Flynn: In any event, you can resolve your difference of opinion with the Leader of the Government in the Senate because he assured us yesterday that it would be through the normal channels of legislation.

The Chairman: That can be a private exercise between the two of them.

Senator Flynn: Yes.

The Chairman: What is the objection, Mr. Minister, to providing for expedition in the filling of vacancies?

Hon. Mr. Pepin: I would suggest that this is taken for granted. This applies to all boards. Is there a clause in the National Energy Board Act saying that the Government should act rapidly in the appointment of members to the board? I suggest this is part of the democratic process.

The Chairman In that event, Mr. Minister, the British North America Act provides for 102 senators. We are short 20 now.

Hon. Mr. Pepin: Let us amend the Senate Act, then! I am just saying it is always difficult to put in *a* bill something which should be in *all* bills. If it makes sense in one bill it makes sense to put it in all bills. I suggest if it is not in other bills it should not be in this one. Perhaps my logic is too Cartesian.

The Chairman: I do not think the logic holds together, Mr. Minister, to be quite frank. What you are saying is, "trust me as minister". We have to look beyond that.

Senator Walker: You may be promoted and then we may have some minister in whom we do not have the same confidence.

Hon. Mr. Pepin: Anywhere I go from here will not be a promotion!

The Chairman: How does the committee feel about the minister's proposal? I think it satisfies the chief concern which we had.

Senator Molson: Mr. Chairman, might I ask a question? Last night there was some talk about panels of the board. This does not cure that at all.

The Chairman: There is another amendment to cover that.

Senator Flynn: That is section 7(2).

The Chairman: Yes. Is the form of the amendment proposed by the minister acceptable in relation to subsection 2 of section 6 of the bill? Is that agreed?

Hon. Senators: Agreed.

The Chairman: What about the next one, Mr. Minister, with relation to clause 7?

Hon. Mr. Pepin: The next one has to do with meetings and quorum. The main preoccupation yesterday was that the chairman, when he is not presiding over the board or over a panel of the board, should appoint a presiding officer. That was the main preoccupation of the committee last night. At that time I said that this was again taken for granted, but since then I have been informed that such a clause is in the Tariff Board Act, so I cannot do the same pirouetteing as I was doing a moment ago! I am willing to give you the same thing as is in the Tariff Board Act, and that shall become section 7(3). It shall read:

> The Chairman shall preside at any sittings of the Board at which he is present and shall designate one of the other members to preside at any sittings of the Board at which he is not present.

That would apply to sittings of the full board or a panel.

The Chairman: That will be subsection (3) of section 7?

Hon. Mr. Pepin: Yes.

Senator Molson: Where does it give authority to call a meeting of a panel of the board? How does it call less than the board? Section 7(1) states:

> The Board shall meet at such times and conduct its proceedings in such manner as may seem to it most convenient for the speedy despatch of business.

Does that give authority to call part of the board?

Hon. Mr. Pepin: There is no reference in the bill to panels. We get this indirectly by saying that the quorum will be at least three. In other words, if the quorum is at least three and if there are seven members, then, you can have two panels sitting.

Senator Flynn: It would be by establishing rules of practice.

Senator Beaubien: It would be at the discretion of the chairman.

Senator Molson: You could have one panel of three sitting?

Senator Flynn: Yes.

Senator Molson: He should have authority to call less than a board, then. How does he call a meeting of a panel?

Hon. Mr. Pepin: He could have a meeting of the board with a quorum of three.

Senator Molson: How does he designate who the three members are?

Hon. Mr. Pepin: The chairman has to be there himself and he will preside over the meeting, but if he is not present he will have to appoint one of the other members to preside over the meeting.

The Chairman: Section 7(1) states:

> The Board shall meet at such times and conduct its proceedings in such a manner as may seem to it most convenient for the speedy despatch of business.

It should also be provided there that the board may meet in panels.

Senator Flynn: It would be much more clear to me.

The Chairman: Suppose you said, "The Board shall meet as the whole Board or in panels".

Hon. Mr. Pepin: I am in a very conciliatory mood this morning. I want this bill to go through as rapidly as possible, so I will accept whatever you say. We can add: "at any sittings of the Board, in whole or in panels, at which he is not present". I think that will cover it.

The Chairman: No. In subsection 1 you need the authority; that is: "the Board shall meet as the whole Board or in panels at such times and conduct its proceedings in such manner as may seem to it most convenient". That would appear to cure the problem.

Senator Flynn: You would need a consequential amendment to subsection 2 to say that three members constitute a quorum of the board or of a panel.

Hon. Mr. Pepin: You are just explicitating.

Senator Flynn: It is obvious the minister is not a lawyer.

Hon. Mr. Pepin: He is a lawyer but a non-practising one.

Senator Flynn: I did not know that. I knew you had been in the press.

The Chairman: First of all, is the proposed amendment to add subsection 3 acceptable?

Hon. Senators: Agreed.

Senator Flynn: "Three members shall constitute a quorum of the board or of a panel".

The Chairman: That would be the addition in subsection 2. Then in subsection 1 it should say: "The Board shall meet as a whole Board or in panels at such times" etc. We add those words. Is that agreeable to the committee?

Hon. Senators: Agreed.

Senator Flynn: There is one question left that was raised by Senator Molson.

Hon. Mr. Pepin: I have to make a correction to what I said to Senator Flynn a moment ago. I am not a lawyer. I have a diploma in law. Apparently there is a difference, and I want to correct myself at the earliest opportunity!

Senator Flynn: A licence in law.

The Chairman: What is the other point.

Senator Flynn: The point is that when you have a panel of three members, the rule being that you should never have only members of the Public Service, you should provide that at least one member of the panel is an outsider.

Senator Beaubien: We have dealt with that with the two-thirds, have we not?

Senator Flynn: No.

The Chairman: The bill in its present form provides that the chairman must be an outsider, so that as long as there is to be a meeting of the whole board or of a panel at which he is present the chairman must preside. If there

are two panels meeting he cannot preside at both, so we require in the amendment the minister submitted that the chairman shall be a member of the board designated by him. All we have to do is to add a word or so to say "an outside member of the board".

Senator Flynn: In the appointment of the deputy chairman.

The Chairman: That is right.

Senator Flynn: You have to do it just the same.

The Chairman: You add "who is not a member of the Public Service".

Senator Flynn: That is right.

Hon. Mr. Pepin: You are complicating matters.

The Chairman: No, we are making it easier for you.

Senator Molson: In effect, Mr. Chairman, you are saying that a panel of this board composed solely of civil servants may not meet?

The Chairman: That is right.

Hon. Mr. Pepin: That is what you are saying. I suggest that the presence of three members from the outside will have a permeating influence on the way the board, either as a board or as a panel, will operate. I suggest you should leave the board the possibility of making decisions exceptionally with only officials there. I am quite sure that if officials take a different philosophical line than the outsiders, this will very easily come out and will be reconciled.

The Chairman: If we did that the trouble would be that we would be defeating the purpose of the amendment we originally proposed, which was to ensure a proper mix. If you can have a panel composed of three members of the Public Service and operate, then we have defeated our purpose.

Hon. Mr. Pepin: I suggest this is not entirely true, with respect, Mr. Chairman, as they say at these meetings.

The Chairman: And in court.

Hon. Mr. Pepin: I suggest that the presence of outsiders on the board will help develop what I call the philosophy of the board. I suggest that the philosophy as determined by the board with the presence of outsiders will be implemented even if occasionally there are no outsiders on a panel to make up the quorum.

Senator Molson: Would not clause 8, which establishes the responsibility of the board to administer the grants and so on, perhaps mean that even though a panel was composed of civil servants, in fact the board will administer the provisions of the act, and therefore the whole board, composed of outsiders and members of the civil service, will be taking the action, even though the consideration was given by a panel perhaps composed entirely of civil servants.

The Chairman: I would expect—and I think there are lots of precedents for it—that where there is a board and the board sitting in panels the regulations might well provide that where a panel sits it reports to the board. What would you think of that, Mr. Minister?

Hon. Mr. Pepin: That is a good suggestion.

The Chairman: They could do it by regulation.

Senator Molson: As far as I am concerned, that would sound reasonable.

The Chairman: It is the board that approves the grant, and therefore while the panel sits and makes decisions, it reports to the board. It is like an executive committee of a board of directors; they report their conclusions to the board and the board either accepts them or does not. I think that is a matter that can be dealt with by regulation.

Hon. Mr. Pepin: If that were in the regulations you would not need it in the legislation.

The Chairman: No, you would not need to touch that.

Hon. Mr. Pepin: Mr. Drahotsky brings to my attention that the difficulty is that there is no legal status for "panels."

Senator Carter: There will be if we have the amendment.

The Chairman: The amendment we are proposing would provide for panels, but the panels can hear and make recommendations; it is the board that must make the decision of approving a grant.

Senator Burchill: They have to approve what the panel decides.

The Chairman: That is right.

Senator Lang: If you call the panels committees you get around it.

The Chairman: Yes, you could call them committees.

Hon. Mr. Pepin: How would the amendments read?

The Chairman: Would you go through them, Mr. Hopkins?

Mr. E. Russel Hopkins, Law Clerk and Parliamentary Counsel: It would read:

> The Board shall meet as a whole Board or in panels at such times and conduct its proceedings in such manner as may,

and so on. Then subsection 2:

> Three members of the Board or of a panel . . .

I suppose of the board, so it would read:

> . . . or of a panel of the Board constitute a quorum.

Senator Flynn: My suggestion was that three members shall constitute a quorum of the board or of a panel. I think it is clearer this way, but it is as you wish.

Mr. Hopkins: I think this is the standard Justice drafting.

Senator Flynn: That does not impress me too much.

Mr. Hopkins: The say, "three members of the Board or a panel constitute a quorum". I do not think it could be misunderstood. That would be the end of subsection 2. Subsection 3 would read:

> The Chairman shall preside at any sittings of the Board at which he is present.

I think it should be:

> . . . At any sittings of the Board or of a panel of the Board at which he is present, and shall designate one of the other members to preside at any sittings of the Board or of a panel of the Board at which he is not present.

The Chairman: There is one question there. In order to ensure that there is at least one outsider present at a panel meeting, I think the chairman of the panel that may be appointed should be limited to an outside member of the board.

Hon. Mr. Pepin: I will resist that, if you will allow me. I am very eager to accommodate, but I will resist that one, because it may very well be that circumstances do not permit the coming to Ottawa of three outsiders when an urgent decision has to be made, and consequently I want to keep that flexibility, of having a quorum made up of three officials.

Senator Flynn: That would not be too bad if we were sure that you cannot continue with this legislation beyond April 30 next year, and that you will have to come back to Parliament, because probably you will at that time be able to prepare other amendments. It is quite obvious that this legislation has been prepared in a hurry, which in the circumstances is understandable.

Hon. Mr. Pepin: I do not think that time should be a criterion there. I have seen legislation that was prepared over a long period of time, that was faulty also.

Senator Flynn: There are contradictions in the bill, which are not important, it may be, at this time; but if you have to come back to us in about five or six months . . .

Hon. Mr. Pepin: Really, I have no intention of doing that. The bill, as Senator Forsey has said, is a permanent bill. The regulations will have to cover a particular situation justifying the invocation of the bill.

The Chairman: I want to point out to you, Mr. Minister, that if we accede to what you have said, and if you have three public servants constituting the panel, because you want to do something quickly, you still must have a meeting of the board in order that you may get the direction of the board as to the grant.

Hon. Mr. Pepin: I am quite eager to suggest to the board that they operate in the way you see fit, which is that the decision made in the panels are to be subject to ratification by the full board. I am quite willing to suggest to the board that because it would be according to the spirit of the bill; but I am not too keen to tie myself to the board to the obligation of having one outsider member on each panel when a panel is formed. I think you should leave a bit of flexibility there.

The Chairman: All right. We are trying to do so. Section 8 gives the authority to administer a grant to the board. The question then is, what is the authority of the panel? The panel can conduct hearings and I am sure the regulations will provide as to what the panel can do. But the panel cannot administer the grants. It could make recommendations, but the board will have to say it adopts what the panel recommends.

Hon. Mr. Pepin: In some ways the panel, if it meets the quorum requirement, operates as the board, in some circumstances.

Senator Molson: Surely there is no reason why a panel should operate as the board for more than a hearing or an investigation? Surely a panel of the board should not administer, for say 60 days or 90 days, the provisions of this bill?

Hon. Mr. Pepin: The purpose of the panel is that there might be a lot of work, especially in the beginning.

The Chairman: Many hearings.

Hon. Mr. Pepin: Hearings, meetings, for analysis, for discussion of a case. That is the reason for the panel. I take as very logical and very valid the observations that you have made on the usefulness of referring the recommendation or decision of the panel to the full board. I will recommend accordingly.

The Chairman: I do not think we need to amend section 8, because section 8 gives the authority to the board to administer the grants. That remains. We have not given the panel the authority to administer the grants.

Senator Flynn: That is right.

The Chairman: I think the regulations, Mr. Minister, should spell out the functions of the panel. I am trying to help you on that.

Hon. Mr. Pepin: I recognize that.

The Chairman: Because that will involve an amendment of the bill. Have we got the question of the panel covered well enough there, do you think?

Hon. Mr. Pepin: I imagine it is too well covered.

Senator Carter: Must the panel consist of three persons, or can the panel consist of less than three?

Mr. Hopkins: Three members of the board or of the panel.

The Chairman: Section 7, as amended, says that the board shall meet as the whole board or in panels at such times, and so on. If the board meets as a panel, you may be getting yourself in a position where it is the board, even as a panel of the board.

Mr. Hopkins: I would agree with the minister.

The Chairman: Yes. Then we have not accomplished what Senator Molson was talking about.

Hon. Mr. Pepin: Senator Molson presented it to me as a suggestion I should make to the board, in drafting its own rules and procedures.

Senator Molson: Surely the board can never get away from the responsibility of carrying out what is defined in the act. It can have panels, it can do what it likes, but in the end surely the board is responsible, and that is all the members of the board. It is not some of them, is that not right?

Hon. Mr. Pepin: Let us try to anticipate on the unpredictable. If the board has the practice, let us say hypothetically, of operating as panels made up only of civil servants, I would suggest that the chairman of the board, an outsider, would resent that very much; and he has all the capacity to prevent it. The chairman of the board, I suggest, will allow a meeting of a panel made exclusively of officials, only in extraordinary circumstances. He, being an outsider, will not want the responsibilities of outsiders on the board to be eroded by the development of a practice of panels meeting including only officials.

The Chairman: Here is the rationalization of it, Mr. Minister. It strikes me like this. The board is the top. What we say here in the amendment is that the board shall meet as a whole board or in panels. That is fine. That is providing authority. But who determines when they meet in a panel? It will be the board that will determine that. And when the board determines that they are meeting in panel, the board will provide the procedures, and your regulations will deal with that. I think we have it covered.

Hon. Mr. Pepin: I am being very frank, I am not sure if the regulations will cover that part of it; but the board has the right to select its own modus operandi.

The Chairman: Each time.

Senator Molson: Mr. Chairman, at the end of the year, the board will make a report to the minister. At that stage you are not going to get a report from a panel. You will get a report from the board. Therefore, what I am saying is that the board is responsible for all that has happened during the year, whether it did it in panel or by the whole board.

Hon. Mr. Pepin: That is so.

The Chairman: Is what we have done satisfactory?

Senator Flynn: Yes.

Hon. Mr. Pepin: You have explicitated really what was in our minds, what would have been done, anyway.

The Chairman: We have not tortured the bill beyond recognition. Are these amendments agreed to?

Hon. Senators: Agreed.

Hon. Mr. Pepin: Mr. Chairman, if I may, I have another amendment to suggest to you. It has to do with the reporting under clause 21 of the bill. Last evening the view was expressed that reporting once every year was not good enough. The same suggestion was made in the house. I stood up in the house and put my hand on the invisible bible and said I would report on a quarterly basis. Because of circumstances there was no time to go into it, I was unable to present it as an amendment, since the procedure did not allow me to do that. You will remember that we were at the report stage.

Therefore, if you want to help me in getting your two amendments through the house, where members of the house may very well say that I was not flexible enough to accept an amendment to clause 21 but flexible enough to accept amendments to clauses 6 and 7—they may ask why I did not accept their amendment!—I am suggesting that you explicit the suggestion made last evening and amend clause 21 so that in place of the words "fiscal year", the bill would say "annual quarter", to put reporting on a quarterly basis. The Department of Justice recommends the word "annual quarter", which is synonymous with three months.

The Chairman: We have to strike out "fiscal year". It occurs twice.

Senator Beaubien: If in March you get the report on the March 31, it does not give much time.

Senator Flynn: The idea would be to make the first report at the end of the calendar year. It could be the quarter terminating on December 31, 1971.

Hon. Mr. Pepin: Mr. Chairman, with respect to the previous amendment on the subject of panels, because it is likely to cause legal difficulties my adviser is checking with the Department of Justice. He should be back in a moment or two.

The Chairman: Last night another question was raised which the minister answered immediately but was asked to reflect upon. That point is that where the board makes a decision (*a*) that it has not the authority to deal with the matter, or (*b*) that the board is against granting any benefit or relief, there should be a right in the person affected to go to the minister, as of right, for a review.

Senator Flynn: If it is beyond the powers of the board I suppose the Federal Court would have jurisdiction to annul the decision.

The Chairman: If the board exceeds its jurisdiction, of course you can go to the court. In fact, you can leave that phase of it and deal only with the phase where the applicant is aggrieved by a decision of the board, in which case he would have the right to go to the minister for a review.

Senator Lang: What is a review?

The Chairman: The minister did not like the word "appeal" and I was inclined to agree with him.

Senator Flynn: Even if the minister makes a review, he cannot impose a new decision on the board.

Hon. Mr. Pepin: Right. The minister can only ask for a review. I wish to emphasize that point.

Senator Flynn: He can review the case, but he would have to ask the board to change its mind. The board would not be obliged to do so.

Hon. Mr. Pepin: That is my understanding also.

Senator Flynn: We do not need to legislate on that score. We might as well leave it as it is. Anybody can appeal to the minister.

The Chairman: I raised the point because I was asked to last night, but my own view is that the minister, in the position he occupies now under the bill, can at any time ask the board to be kind enough to review a decision. But the board is the authority.

Senator Flynn: Otherwise we would have to establish a mechanism to enable the minister to change a decision of the board.

Hon. Mr. Pepin: If you are looking for justification of the approach, which we seem to agree on, it is clause 8(1), "subject to the regulations and the direction of the Minister". Presumably the direction of the minister would include the right to ask the board to review its decision on a case in the light of circumstances, events and facts brought to the attention of the minister.

The Chairman: We have raised the subject as we said we would. The feeling of the committee is that it is not practicable and is unnecessary in the circumstances.

Senator Molson: On the question of a split board, what does the term "panel" mean? Do we know what a panel is? Is it defined? We have had committees and subcommittees, but we have not had panels before, to my knowledge.

Hon. Mr. Pepin: That was Mr. Drahotsky's concern.

The Chairman: When referring to a board it might be more appropriate to use the word "committee" — a committee of the board.

Hon. Mr. Pepin: My first information was that this does not have to be covered owing to the fact that it is the normal practice of boards, for example, the National Energy Board and the Tariff Board, to sit in committee, but when the decision is made it is made by the board. The board cannot say that the decision was made by a committee and consequently the board has not taken a decision. If the board does not take it, there is no decision of the board, or there is a contrary decision of the board.

Senator Benidickson: Mr. Chairman, the Transport Board sometimes sends out a single representative and when he comes back he gets the approval of his colleagues.

Senator Flynn: The Appeal Court of Quebec sits with two panels in Montreal at one time.

Hon. Mr. Pepin: That is what is intended here.

The Chairman: Then we had better stay with the word "panel". What have you to report, Mr. Drahotsky?

Mr. Drahotsky: I have tried to clarify these points with the Department of Justice. I am told that the term "panel" has no legal meaning, unless so defined in one way or another. I have also been reminded that this question arose on a number of occasions when the bill was being considered in cabinet committees. The consensus reached, including the agreement reached in the Cabinet Committee on Legislation, was that clause 7 should be taken in conjunction with clause 9, empowering the board to make such rules as may be necessary for the conduct of its meetings, the management of its affairs and the performance of its duties and functions, and that those two clauses do provide adequate authority to the board to operate on a two-panel basis, and to organize its activities and its deliberations in any way it would consider most expeditious. Thank you, Mr. Chairman.

Senator Beaubien: Mr. Chairman, the Companies Act lays down that notice has to be given to directors. That means all directors. All directors are invited to meetings. If that procedure were followed here there would be no real problem. If all directors are told that the meeting is going to take place and are advised in time, then they are going to turn up.

Senator Flynn: But if everybody wants to sit on the same panel, what will happen then?

Hon. Mr. Pepin: They will be directed by the chairman which panel they are to sit on, and I would suggest that the chairman would try to get in his panels the same kind of mix he gets on the board. That stands to reason.

Senator Molson: According to section 9 it sounds to me as if the rules that the board operates under with respect to panels, in other words, how the panels are made up and how they are called to meetings and things of that sort, would have to be set out in the board's own rules.

The Chairman: Senator Molson, we only got on to this question of panels because the minister introduced the subject by saying he would want the board to sit in panels, and we were trying to find some way whereby he could have authority to do that. If he does not want that, but feels he has enough authority under section 9, then that becomes his job. I think that under that section, the board can make any rules it wants to make. The board can simply say, "You, you and you shall act as a section of the board to deal with this matter." But then that section must go back and report to the board.

Hon. Mr. Pepin: I suggested that very strongly at the time.

Senator Lang: I should like to move that the bill be reported without amendment, Mr. Chairman.

Mr. Chairman: But we have agreed to some amendments.

Is it the wish of the committee that in the amendments we delete all reference to panels?

Senator Flynn: I am very happy the Minister has found the Senate useful in proposing the amendment he had no time to push through in the House of Commons.

Hon. Mr. Pepin: I think that the discussion has been helpful to me in the sense that I will suggest to the Chairman when I meet him after he is appointed that he should try to develop in the panels when they meet the same kind of mix that he has in the board itself. I will suggest that, but I did not want him to be tied to the obligation of doing that in exceptional cases.

The Chairman: Shall I report the bill as amended?

Senator Benidickson: What amendment was agreed on?

The Chairman: The amendments we talked about last evening to section 6, section 7 and section 21. In section 21 we are changing the fiscal year to each annual quarter.

Hon. Mr. Pepin: And in section 7 a new paragraph 3 has been added.

The Chairman: I will read it for you.

Senator Benidickson: Has the committee agreed to Senator Aird's suggestion that the words "at least" should be included in section 6 sub-section 1?

The Chairman: No, but subsection 2 has been amended. The Minister has furnished us with a form of amendment which would read:

> Not more than two-thirds of the members of the Board at any time may be members of the Public Service within the meaning of the Public Service Employment Act, but a vacancy occurring in the membership of the Board that has the effect of temporarily reducing the number of members of the Board who are not members of the Public Service below one-third of the members of the Board does not invalidate the constitution of the Board or impair the right of the members to act if the number of members is not less than a quorum.

Believe me, it does make sense.

Senator Benidickson: It is fairly easy for it to follow the principle in the original bill.

The Chairman: Except if the board of directors decide that the board is going to sit in sections, for instance, and they designate three members who are public servants, whatever decisions or recommendations they are going to make, it will still be the board itself which must afterwards administer the grant. We have not changed that. Is that clear?

Hon. Mr. Pepin: I agree, and I thank the committee for a very good hearing.

The Chairman: We will struggle to report the bill this afternoon, and we can say that the amendments made have been made with the consent and approval of the minister.

We will adjourn now until 3 o'clock this afternoon, when we will continue our hearing in connection with the private bill to establish the United Bank.

The committee adjourned.

APPENDIX "A"

Statement of Minister of Agriculture,
October 1, 1971.

Hon. H. A. Olson (Minister of Agriculture): Mr. Speaker, I want to make a brief statement providing further information on agricultural assistance programs designed to cover unprocessed agricultural products which will not be eligible for assistance under Bill C-262, the Employment Support Act. You will recall that I gave notice of this assistance when I spoke on second reading of Bill C-262 on September 7, 1971.

I can advise that the Agricultural Stabilization Board and the Agricultural Products Board have been authorized to come forward with individual commodity programs designed to help producers adversely affected by the surtax. The programs will take any one of several forms, namely, purchase of the product, deficiency payments or payment to distributors for the benefit of producers. In this latter connection distributors to be eligible must have been exporters of the unprocessed product to the United States in the base period, must demonstrate that the price paid to farmers for raw products was maintained at a level consistent with that which would have been expected in the absence of surtax, that distribution volume and employment were maintained. I say the latter because employment in the agricultural distributing industry is important as well as in the agricultural processing industry.

As with processed products there will be no requirement that exports to the United States be maintained.

I am issuing a press release today inviting applications from the agricultural industry both from producer groups and distributors. Applicants are asked to provide basic data relative to the criteria and on the impact of the surtax on their operations to supplement the information already accumulated by the department.

In conclusion, I want to say that I am very conscious of the need to put these programs in place promptly and consistent with the need of those affected and the international situation.

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THIRD SESSION—TWENTY-EIGHTH PARLIAMENT

1970-71

THE SENATE OF CANADA

PROCEEDINGS

OF THE

STANDING SENATE COMMITTEE ON

BANKING, TRADE AND COMMERCE

The Honourable SALTER A. HAYDEN, *Chairman*

No. 39

THURSDAY, OCTOBER 7, 1971

Third Proceedings on:

"Summary of 1971 Tax Reform Legislation"

(Witnesses—See Minutes of Proceedings)

THE STANDING SENATE COMMITTEE ON BANKING, TRADE AND COMMERCE

The Honourable Salter A. Hayden, *Chairman*

The Honourable Senators,

Aird	Grosart
Beaubien	Haig
Benidickson	Hayden
Blois	Hays
Burchill	Isnor
Carter	Lang
Choquette	Macnaughton
Connolly (*Ottawa West*)	Molson
Cook	Smith
Croll	Sullivan
Desruisseaux	Walker
Everett	Welch
Gélinas	White
Giguère	Willis—(28)

Ex officio members: Flynn and Martin

(Quorum 7)

Order of Reference

Extract from the Minutes of the Proceedings of the Senate, September 14, 1971:

"With leave of the Senate,

The Honourable Senator Hayden moved, seconded by the Honourable Senator Denis, P.C.:

That the Standing Senate Committee on Banking, Trade and Commerce be authorized to examine and consider the Summary of 1971 Tax Reform Legislation, tabled this day, and any bills based on the Budget Resolutions in advance of the said bills coming before the Senate, and any other matters relating thereto; and

That the Committee have power to engage the services of such counsel, staff and technical advisers as may be necessary for the purpose of the said examination.

After debate, and—

The question being put on the motion, it was—

Resolved in the affirmative."

Robert Fortier,
Clerk of the Senate.

24260—1½

Minutes of Proceedings

Thursday, October 7, 1971.

(46)

Pursuant to adjournment and notice the Standing Senate Committee on Banking, Trade and Commerce met this day at 9.30 a.m. to further consider:

"Summary of 1971 Tax Reform Legislation".

Present: The Honourable Senators Hayden (*Chairman*), Aird, Beaubien, Benidickson, Burchill, Carter, Connolly (*Ottawa West*), Cook, Desruisseaux, Flynn, Gélinas, Giguère, Haig, Hays, Isnor, Lang, Molson, Smith, Sullivan, Walker and Welch. (21).

Present, but not of the Committee: The Honourable Senator Heath.

In attendance: The Honourable Lazarus Phillips, Chief Counsel; Mr. C. Albert Poissant, C.A., Tax Consultant.

WITNESSES:

Mr. Arthur A.R. Scace, Partner,
Law Firm of McCarthy and McCarthy.

Mr. Stephen C. Smith, Partner,
Law Firm of McCarthy and McCarthy.

At 12.30 p.m. the Committee adjourned to the call of the Chairman.

ATTEST:

Frank A. Jackson,
Clerk of the Committee.

The Standing Senate Committee on Banking, Trade and Commerce

Evidence

Ottawa, Thursday, October 7, 1971

The Standing Senate Committee on Banking, Trade and Commerce met this day at 9.30 a.m. to give consideration to the Summary of 1971 Tax Reform Legislation, and any bills based on the Budget Resolutions in advance of the said bills coming before the Senate, and any other matters relating thereto.

Hon. Salter A. Hayden (*Chairman*) in the Chair.

The Chairman: With respect to the order we intend to follow this morning, we will first take general matters relating to estates, real estate and corporate acquisitions, and Mr. Scace is going to deal with that. Following that we are going to deal with international taxation, and Mr. Smith will handle that.

You will recall that yesterday we had a fairly extensive discussion on the question of multi-national and international income, and over the next three weeks we shall be having several briefs on that aspect. Therefore, it will be important this morning to get as good a grounding in this as we can.

Mr. Scace, would you care to take over now?

Mr. Arthur R. A. Scace, Partner in the Law Firm of McCarthy & McCarthy: Thank you, Mr. Chairman. In the programs which we have given we have parcelled out estate planning or matters relating to estates as a separate item, and last week we touched on a number of things which are important in that particular area so that to the extent we have already done that I think I will gloss over it unless you would like to go back and delve into it in somewhat greater detail.

The Chairman: You mean we should have a refresher course this morning.

Mr. Scace: If you like.

Senator Benidickson: Some of us need it.

Mr. Scace: When we did capital gains we started off with a summary. Perhaps we might do the same thing this morning. The basic changes, so far as estates and death duties are concerned, are as follows: First, estate and gift tax are to be abolished, and we will have more to say about that as it is clearly the most important aspect of this area. Second, with the exception that in the case of distributions to a spouse or to a qualifying trust in favour of a spouse, there is a deemed realization of all capital assets on death and when a gift is made, and this is the substitution for the gift tax and the estate tax. Third, the attribution rules are altered in order to take account of the imposition of the capital gains tax. Fourth, as we mentioned last time, there is a deemed realization when you cease to be a resident of Canada. In other words, when you emigrate from Canada there is a deemed realization at fair market value. There are, of course, certain exclusions from that and it will not cover taxable Canadian property. Finally, and I think this is an area where you may be receiving a number of briefs, the law concerning the taxation of trusts is now much more extensive and much more complicated, and a number of people in the trust field think that it is possibly quite inadequate.

If I may, I will go through these items. First there is the abolition of estate tax. The provision abolishing it is found in Part II of Bill C-259, and it says that the Estate Tax Act does not apply in the case of the death of any person whose death will have occurred after 1971. So if you can make it to January 1, 1972, there will be no estate tax.

Senator Molson: If we pass the bill.

Mr. Scace: In its place we get a deemed realization on death, as I said. You find that provision in section 70(5) of the bill.

As a review of what we looked at last time, there are two aspects of the deemed realization. First, if you are dealing with non-depreciable capital property, the deemed realization is at fair market value. Similarly, the beneficiary acquires at fair market value. Second, if you are dealing with depreciable capital property, you have the midway point rule. In the legislation the deemed realization price, or the deemed disposition price, is undepreciated capital cost plus one-half of the difference between fair market value and undepreciated capital cost. Similarly, you get an acquisition at that same price.

Senator Connolly: Will you say that again?

Mr. Scace: Yes, sir. In the case of depreciable capital property, it is undepreciated capital cost plus one-half of fair market value minus undepreciated capital cost.

Senator Connolly: It is the old story, isn't it, adding it in and then subtracting it?

Mr. Scace: Well, if you had an asset which had cost $100 and an undepreciated capital cost of $80, and on death the fair market value was $200, your calculation would be $80 plus one-half of $200 minus $80 which is $120, so then it would be $80 plus $60 which is $140.

I think we had examples of this calculation last week, but what you would get here is recapture between undepreciated capital cost and original cost, so there would be recapture between $80 and $100, and between the $100 and the deemed realization price of $140, that would be a capital gain and applying your normal rule, one-half of that would be a taxable capital gain and you would include it in your income.

The Chairman: So that $20 would go into income?

Mr. Scace: Twenty dollars would be the taxable capital gain, that is right.

The Chairman: And $20 would go into income by virtue of recapture at full income rates.

Mr. Scace: At full income rates, that is right.

Hon. Mr. Connolly: Just to make it crystal-clear, that undepreciated asset could for example be a share of stock or a bond that had been purchased for $100 and then dropped to $80.

Mr. Scace: No, sir. Here we are talking about depreciable capital property, that is property upon which you are entitled to take capital cost allowance. In the case you are talking about of non-depreciable capital property, you do not have to go through this calculation, there is a deemed realization at fair market value.

Senator Connolly: That makes it abundantly clear.

Mr. Scace: So you would not have this item here of undepreciated capital cost and the deemed realization would take place at $200 if this were not depreciable capital property and that would be the acquisition price, and in that case there would be a $100 capital gain and a $50 taxable capital gain.

Senator Lang: Mr. Scace, taking the fair market value less the undepreciated capital cost, does the person acquiring the asset have to take into account the undepreciated capital cost?

Mr. Scace: No, sir. There is a different rule where you have that situation, but the formula is much the same. Where your fair market value is less than undepreciated capital cost, the rule is fair market value plus one-half undepreciated cost minus fair market value. They just switched it around. Let me just show you how that would look. In that case you have an asset with a cost of $100, an undepreciated capital cost of $80 and a fair market value on the day of death of $50, so you would have $50 plus one-half of undepreciated capital cost of $80, minus fair market value so you would end up with $50 plus $15 which would equal $65.

Senator Lang: I do not see the equity in that. Do you?

Mr. Scace: That may be a common complaint, senator.

Senator Beaubien: If a man were not feeling very well and he had some property, it would be a great thing for him to get out of it before valuation day and leave nothing but cash.

Mr. Scace: It would be a good idea. I think the rationale to this—if we complicate it just a little more—is that under the present law if you hold a depreciable capital asset, then on death if the asset passes by will, there is no recapture and the donee acquires a fair market value. Now because of that treatment, I think they decided that somehow they had to make a compromise which was somewhat less than the rigour of a fair market value realization, and for that reason you get the midway point rule, I think, which is merely a compromise.

Now this does create a problem, and I think we mentioned this last week too. As I said, if you have a depreciable asset now and $100 is the cost and $80 is the undepreciated capital cost, when you die and leave that asset by will, then the fair market value is $200. There is no recapture on your death of this $20 in capital cost allowance that has been taken—that is the difference between which the beneficiary acquires, $200, which is fair market value, and that becomes his base for capital cost purposes. With these new rules you can get, as I have shown, recapture and that recapture will be retroactive. As I said last time there are methods of avoiding that retroactive recapture, but it still requires reorganization of your affairs.

Senator Burchill: How do you get at the undepreciated capital cost? You know the capital cost but how do you get at the undepreciated capital cost?

Mr. Scace: The undepreciated capital cost is a book figure or an historical figure. Say you bought an apartment building for $100, you are entitled to take capital cost allowance on that apartment building at 5 per cent. So in year number 1 with 5 per cent of $100 being $5, the undepreciated capital cost would be $95.

Senator Burchill: You would have to figure out all that?

Mr. Scace: Yes, but you would know it because you would have been taking it every year. That would be no problem.

Senator Connolly: So that $80 in that example is what would be left after you have taken your depreciation?

Mr. Scace: That is right.

Senator Burchill: But what about an art collection?

Mr. Scace: An art collection would not be depreciable property. To be entitled to capital cost allowance, the property must be purchased for the purpose of producing income. I suppose it might be possible to acquire a piece of art for that purpose, but I think that in most situations it is unlikely.

Now if we can give you a comparison of the rates of tax between the Estate Tax Act as it was and what we will get under Bill C-259 with the deemed realization on death. Under the Estate Tax Act the rates started at 15 per cent on the estate sum if it exceeded $20,000, and it went up to a top rate of 50 per cent where the estate exceeded $300,000.

For Ontario purposes—and my calculations have been based on Ontario—because you had a 50 per cent provincial credit to give account to the Ontario succession duty, you could view the Estate Tax Act rate as being halved, so the top rate—for an Ontario estate at least—would have been 25 per cent under the Estate Tax Act. Now you turn to Bill C-259 and with the combined federal and provincial rates of tax, the top marginal rate is approximately 61.1 per cent. Now with the deemed realization on death, you are only taxing capital gains and therefore you may view that top rate as being halved, because there is only half recognition of a gain and therefore the top rate on death would be 30.55 per cent of one-half of 61.1 per cent. So if you stop there it appears that the maximum rate has gone up by approximately 5½ per cent, but it is based on the capital gains which have accrued but which have not been realized. Theoretically, the tax base under the bill must be

considerably smaller than the tax base under the Estate Tax Act. The only situation in which the base might be the same would be where you started off with no assets, or your whole assets had been invested and you never realized a gain. So you are starting from zero and upon death, in effect, all of your assets would represent unrealized capital gains. The other possibility, which is equally unlikely, is that if the tax base on property received by bequest or gifts prior to 1972 is nil, that is, if all of your property had been inherited or received by gifts prior to 1972, your whole estate might be subject to deemed realization on death.

Senator Hays: Would not all farms be in this situation where a farmer starts with zero and goes through his entire lifetime . . .

Mr. Scace: Many farmers inherit their farms.

Senator Hays: No, starting from zero with the Farm Credit Corporation and a small downpayment and working for 40 years which many farmers do; his whole assets are subject to capital gain. I would suggest that perhaps 90 per cent of the farmers are in this situation.

Mr. Scace: That could be correct, senator. I am not very familiar with farms. He would be entitled to deduct his costs.

Senator Hays: Yes, he would do that on income tax.

The Chairman: His operating costs.

Senator Cook: That would only apply after the valuation date of the farm.

Mr. Scace: Yes.

Senator Hays: And he goes through his entire lifetime and then he dies. He is starting from zero. If you checked the percentage of all farmers, I think you would probably find 90 per cent are in this category.

Senator Beaubien: Mr. Scace, anyone who owns any kind of property today, if no change has occurred between the value at the day of his death and the valuation date, there is no tax.

Mr. Scace: That is right.

Senator Beaubien: It does not matter how you have obtained it. If you should die round the end of January and your property is worth $100,000, and on the valuation date it was worth roughly $100,000, there is no tax.

Mr. Scace: That is right.

The Chairman: It is deemed realization gain. It is attached to the deemed realization and your starting point is as of January 1, 1972.

Senator Hays: Hon. Mr. Phillips said that he did not feel that farms should be subject to the capital gains tax. This is probably what he had in mind. They start from zero and they face this inflation their whole lifetime.

The Chairman: This is what we were saying.

Senator Hays: This would be a good opportunity to back up that statement.

The Chairman: Yes, to reinforce what we have already said. Apparently, they did not hear us the first time.

Senator Beaubien: I think this is a point we ought to stress very heavily. We look at the capital gains tax and we are not very much afraid of it because, after all, we are not going to live that much longer. We are dealing with a change in valuation between some time before the end of the year and whenever a person dies. We are leaving a terrible legacy for the poor people who are starting to earn money now and have to battle through their lives and who turn out to be successful and are able to leave money to their children; and because they are successful they are going to get clobbered by this bill.

The Chairman: Senator Beaubien, "clobbered" is a relative term. As I understood Mr. Scace, the clobbering might consist of a difference in rates, as compared to the estate tax if it continued, of the order of 5½ per cent.

Mr. Scace: That is right.

Senator Beaubien: Except in the case of the inheritance of money where it all has to be paid.

The Chairman: Do you mean by will?

Senator Beaubien: Yes.

Mr. Scace: There is no problem after we get into the system. Once someone inherits something, or receives something by gift after the system starts the acquisition price is fair market value or there is this mid-way point rule in the case of depreciable capital property. However, it starts with a base so I do not think there is a problem.

We have made some calculations, which clearly show that the federal tax cost of dying on most reasonable assumptions will be much less under the new system. There is just some concern during the transition, but you have pinpointed it correctly, that if you are worth $100,000 on December 31 and die on January 1 there is zero tax to the federal Government. If you do that, your beneficiary acquires the property at $100,000 and moves on.

Senator Molson: I thought you said, though, that there was a stage where property acquired by will would attract tax on the whole amount.

Mr. Scace: That is right, senator; I said if we are right with respect to gifted and inherited property acquired prior to 1972 a situation could exist in which the tax base would be almost equal to that under the old Estate Tax Act. In that case, if the rate is 5½ per cent higher, there could be a higher tax.

There are three considerations: one, as I have indicated, we may be wrong in our conclusion; I hope we are. Secondly, the amendments may cure this particular difficulty; we hope they will. Certainly the Department of Finance is aware of it. Thirdly, it is open to anyone to take the fairmarket value election and cure the deficiency.

This is an interesting area, because although we may discuss what the federal Government says it intends to do, the $64,000 question is what the provinces intend to do. That is the real issue.

Senator Cook: This is perhaps just a practical question, but now if someone dies the executor files a return, values

the assets and so on. How will it work practically on his deemed realization? Does that put the onus on the department? Who reports the transfer of the property?

The Chairman: I expect they would check the values as they do now for an estate.

Mr. Scace: You would be required to file an income tax return, as opposed to an estate tax return, senator. Thereby you would have to show what assets you had, what the costs were and what their values were at the date of death.

The Chairman: I expect also, Senator Cook, that the staff presently in National Revenue, in the Estate Tax Section dealing with valuations, etcetera, would simply be transferred to this phase of administration.

Senator Cook: Who files the deemed realization? The legatee, I suppose.

Senator Molson: It will be much simpler to die before valuation day.

Mr. Scace: Senator, I suggest that if you are considering it, you wait until January 1.

We have made calculations, in which we had to adopt a number of assumptions. However, assuming these provisions are implemented on a federal level and assuming, for instance, that Ontario does not change its statute and on the reasonable and fairly realistic assumptions on an estate of $300,000 there is a saving of $32,000 in tax; on an estate of $500 million, there is a saving of $77,000; on an estate of $1 million, there is a saving of $179,000. That illustrates the order of magnitude, assuming the federal Government does what it says and the provinces do not make any change.

The Chairman: Have you assumed some kind of mix in those $300,000, $500,000 and $1 million estates?

Mr. Scace: We have assumed it is all non-depreciable capital assets. The assumptions are quite complicated but, I think, fairly realistic given a normal estate.

Senator Cook: That is assuming no deemed realization, is it not?

Mr. Scace: We are comparing what would happen under the old system and what would happen under the new system, given certain assumptions. These assumptions result in a considerable saving in tax; the federal tax cost of dying is much reduced under the bill and the total tax cost of dying is considerably reduced.

The Chairman: Are you comparing the estate tax and the income tax at deemed realization on the gains?

Mr. Scace: That is right.

Senator Cook: We will pass that section.

The Chairman: I should think everyone would be in favour of that.

Mr. Scace: There is one interesting twist to the deemed realization on death. Clause 70(5) appears to apply only to capital properties, that is non-depreciable capital properties and depreciable capital properties. It does not appear to apply to inventory or trading assets. A common example of an inventory or trading asset would be a piece of land, the profit from the sale of which would be taxed in full. Since it is not included in clause 70(5) it does not appear to be subject to the deemed realization at death. Consequently there could be the anomaly that at death it would be argued that a particular asset is a trading asset and would have been taxed in full on sale, as opposed to the normal asset, where it would be said it is a capital asset and the receiver is entitled to capital gains treatment rather than full inclusion. Again the department is aware of this; I do not know if they will do anything about it.

The Chairman: Are you recommending that everyone seek to develop a trading asset position about the time they discover they are soon to die, or have a pretty good idea they are in the terminal stage?

Mr. Scace: I am not making any recommendation, senator; I think you can draw your own conclusions.

The Chairman: It might be good to have some trading assets though.

Mr. Scace: It would not hurt.

The Chairman: No.

Mr. Scace: As I have said, the abolition of the estate tax and the substitution of the deemed realization on death is really a political question. The reason it came about was that essentially an estate tax is an unpopular tax. The federal Government was collecting it and then in most instances remitting 75 per cent of the amount collected to the provinces.

I do not have the up-to-date figures, but if we said the net return to the federal Government was $100 million per year, we would not be too far out.

So for a relatively small amount of money, the federal Government was taking the blame for what was a very unpopular tax. The Government therefore decided to get out of the field, as it was not worth the candle. Certainly the abolition ran counter to what everybody expected.

If we look at the House of Commons report—and I do not know whether it is wise to bring it up in this forum . . .

The Chairman: Oh, yes.

Mr. Scace: The House of Commons, for instance, said that the estate tax exemption should be increased significantly. There should be no estate tax on estates less than $150,000 and, at the top rate of 50 per cent, should only bite in at $800,000.

I think everybody expected some compromise along those lines, but clearly we were not ready for the abolition.

There is a little story on the subject of abolition. Perhaps the man most surprised by it was a friend of mine, a professor at one of the Toronto law schools, who had the misfortune two or three days before June 18 of completing a definitive manuscript on estate tax. On the night of June 18 he phoned me and said, "Tell me it is not so."; and I had to tell him that unfortunately it was.

Apparently the story has a happy ending. He is a very resourceful man and is now offering a course at the law school in legal history and using the manuscript.

Adressing myself to Senator Beaubien and Senator Molson, this may be a real political issue if it ever comes out. There has been surprisingly little comment on it. If a man who is worth $100 million today should have the misfortune to die, or if his beneficiaries should be so unfortunate, his family would be looking at a federal estate tax of approximately $25 million. If he should die on January 1, that $25 million would be completely obliterated. There would be no tax whatsoever.

If he lives for a period of time into the new system, then some tax will be exigible on one-half of his post 1972 capital gains, but certainly a lot less than $25 million.

Senator Cook: Has Ontario come up in favour of abolition of succession duties?

Mr. Scace: It is hard to know what Ontario is going to do. From reading their publications and budgets over the last two or three years, most readers have interpreted them as meaning that they intended to get out of the field.

It seemed clear, when Mr. McKeough was commenting after June 18, that he was very surprised. I think that Ontario's position now is that they still want to get out of the succession duty field, but they will wait until the capital gains tax on the deemed realization at death gets fully on stream. So it is taking a bite at estates.

Certainly I think it has slowed down their timetable for getting out of the succession duty field.

The Chairman: I think we can assume that if they do, they may follow the lead of the federal authority and find another way. The federal authority has found that deemed realization is a way of producing income. I do not think that if Ontario gets out of the succession duty it means that it is a plus for the taxpayer in the sense that there will not be any tax on dying in Ontario. I think they will find something else for part of it or perhaps all of it, because they have to have money.

Mr. Scace: With Ontario it is not too much of a problem. They already have a succession duty administration. If they want to increase their rates, it is simply a matter of passing a bill. The procedures are there.

I do not think it is too much of a problem with most of the wealthy provinces. But if we take a province like Prince Edward Island, it is impossible to see them imposing a succession duty. The cost of administering it would far outweigh any tax collected. It would merely impose a social tax, and would clearly be a loss leader from a revenue point of view.

Senator Cook: Would you include Newfoundland?

Mr. Scace: I was speaking of the smallest province. I did not want to get into details. Certainly there are some provinces that cannot afford a full-blown succession duty and collection procedure. They might pay for it and undergo the cost, but it would not make any economic sense. It might make some social sense.

Senator Connolly: Mr. Scace said that in the event of death, after the system comes into effect, instead of filing an estate tax return, a special modified income tax return would be filed showing the situation in respect of a decedent's estate on the date of his death and giving the market value of all his assets. I take it that the simple process after that would be for the department to assess a gift tax?

Mr. Scace: They would assess an income tax.

Senator Connolly: Yes, they would assess an income tax. Would it be income deemed to have been realized in the year that he died?

The Chairman: Deemed realization.

Senator Connolly: Assuming that it was a very substantial increase over his normal income, would there be any alleviation?

The Chairman: You mean, could they apply the averaging?

The Honourable Lazarus Phillips, Chief Counsel to the Committee: You have to relate that to the values at valuation date and tie it into the valuation date.

Senator Connolly: I would like Mr. Scace to summarize what he has detailed for us here. Could we direct our attention firstly to this question of a great increase in, a doubling of, the income in the year in which he died?

Mr. Scace: Let us take an example and let us make it one that fits entirely into the new system. Let us assume that in 1973 a man buys an asset for $1 million. That is his cost. He had cash, he buys the asset, and dies in 1980. That is the year of his death. That asset would then be worth $2 million. That is the fair market value.

His gain is $1 million, and his taxable capital gain is $500,000. The tax on that, if we assume a marginal rate of tax of 60 per cent, would be $300,000.

Let us assume that we continued under the old system, and the man died with property worth $2 million. If the federal estate tax on that $2 million was 25 per cent, the estate tax would be $500,000. So he is, in fact, $200,000 better off.

The Chairman: His estate is.

Mr. Scace: Yes, his estate is; his beneficiaries will be. He does not really care any more.

There is a liquidity problem on death, but there always was a liquidity problem on death. You either have to pay the taxes on the assets realized or you purchase insurance to meet the tax cost.

Senator Connolly: So that in the year 1980 there will be a tax of $300,000 to pay?

Mr. Scace: Yes, in 1980.

Senator Connolly: In other words, he has income in that year or a taxable capital in the amount of half a million dollars?

The Chairman: Plus whatever income his estate may have.

Senator Connolly: Plus whatever income he had. This is an enormous increase in income, even for a man in that category, I should think. Is there any alleviation for it under the act?

Senator Lang: He has the same problem under the Estate Tax Act now.

Senator Connolly: I realize that.

Mr. Scace: Mr. Smith and I were just conferring as you were asking the question, senator. We will try to get you an answer. I am not sure whether the general averaging provisions under Section 118, or the ability to purchase an income averaging annuity contract under Section 61 would apply under those circumstances.

Senator Connolly: You have a liquidity problem here and you have to solve it somehow. That is the normal thing; you have that under the present system, but under the new system you still have a tax of $300,000.

Senator Lang: He would have had $500,000 under the old act.

Senator Connolly: I know that, but there is an enormous increase in his income.

The Chairman: Senator Connolly, perhaps Mr. Poissant can make some comments in relation to this.

Mr. C. Albert Poissant, Tax Consultant to the Committee: I think the general averaging provisions apply. If I remember correctly, in the year of death the requirement would be 100 per cent of the previous year's averaging and not 110 per cent. It is 100 per cent in the year of death, so the general averaging provisions would apply. The general averaging provisions apply in certain instances, and one of them is that your income for the year must be at least 110 per cent of the previous year's average, but for the year of death they have removed this requirement of 110 per cent and instead it has to be 100 per cent.

The Chairman: You find that in section 118(3).

Mr. Poissant: Yes.

The Chairman: We have answered your question, Senator Connolly, as best we can.

Senator Connolly: I am very grateful.

Mr. Scace: The problem with the general averaging provision is that we have never done a calculation based on figures of this size. Certainly with more normal income figures the general averaging provision does not produce much of a tax saving. If I had to guess I would think you were only talking about a tax saving of about $20,000. I do not believe it would be a great saving.

The Chairman: The income as a result of death would be the normal income of the person who died up to the date of death, plus the capital gains realized on death. The sum total of those would really have to explode or balloon in order to produce a substantial excess of income for that year in order for the general averaging provisions to apply. In how many estates is that likely to occur? Wherever it does occur it is quite important.

Senator Beaubien: Mr. Chairman, we are not aware of what the provinces are going to do, so that really we are looking at only half of the equation.

Senator Molson: From that point of view anyway.

The Chairman: So far as the provinces are concerned, all we can do is what we did before, and that is state in our report that we seem to be starting at the wrong end and that really some agreement should be reached with the provinces before the legislation can proceed.

Senator Beaubien: The provinces have been getting 75 per cent, have they not, of all of the death duties collected? The provinces that have no estate tax or gift tax will be wanting to get something back.

The Chairman: The revenue that might come from the imposition of succession duties, less the cost of administration, might be reasonably negligible. Those provinces have an economic problem, and I doubt if they are going to solve it by taxation.

Senator Connolly: They probably have to solve it by transferring payments from the federal treasury.

The Chairman: I would think that would be so. However, it is not part of our job at the moment.

Hon. Mr. Phillips: The deemed realization on capital gains could offset succession duties. You are dealing with the poorer provinces and they may never reach the replacement and, in any event, if they do it will take some years. That is why the provinces have already indicated to the federal Government that they feel there should be a postponement of the cancellation of succession duties until the deemed realization on capital gains is in full flight. No one seems to be paying any attention to the payments.

The Chairman: They may get transfer payments in relation to the amount of the deemed realization and the tax thereon. However, that is not a problem we can speculate on at this time. We may decide that we should say something about it as being one of the questions still hovering around, which will be bothersome and for which some solution should be found.

Senator Connolly: Presumably, that kind of thing is going to be dealt with at the federal-provincial meeting or at the ministers of finance meeting.

The Chairman: I am glad you added the word "presumably," because I do not know and I would not want to speculate on what conclusions might be reached.

Senator Cook: If they are worried about the revenue, perhaps it could be done by bringing down the scale year by year. It would only take ten years, if the scale was reduced by 10 per cent a year.

The Chairman: Can we get down to our more immediate problems? Mr. Scace, what is the next area?

Mr. Scace: The next area is gift tax and gifts. Rule 14 of the Income Tax Application Rules apparently abolishes gift tax. It states that Part IV of the former Income Tax Act is continued in force but does not apply in respect of gifts made after 1971. Reading that alone it is clear that gift taxes will apparently be abolished.

Senator Connolly: What page are you reading from?

Mr. Scace: Transitional Rule 14 at page 412. Part IV states that the former act is continued in force but does not apply in respect of gifts made after 1971.

I have used the word "apparently" because if you turn to page 384 and particularly Section 245(2), that particular section was in the old act as section 137(2) and in addition it had subparagraph (c) which has been deleted.

Senator Connolly: I missed your reference.

Mr. Scace: Page 384, Senator Connolly, Section 245(2). That section used to be Section 137(2) of the existing act, and the only change that has been made is the deletion of subparagraph (c). It is a purely inadvertent technical drafting error by deleting subparagraph (c). If you leave section 245(2) in the way it is now and you make a gift, the amount of the gift must be brought into the income of the beneficiary.

If you care to read it through, it seems reasonably clear that that result would apply. It is not intended. The Department of Finance is aware of the problem and we understand they are going to clear it up. It is essential that that matter be rectified before passage.

The abolition of gift tax in many ways is more significant than the abolition of estate tax. If a man is worth $10 million on January 1, there will be no estate tax, no deemed realization on death, but there will be succession duty when he dies. On the other hand, if there is no gift tax, he can give the whole of his estate away to his intended beneficiaries and, provided that he survives the recapture period, in the various provincial succession duty statutes—in Ontario and Quebec it is five years—all death duties can be entirely avoided.

This raises another interesting matter with respect to the federal Government and the provinces. Clearly, if the provinces are going to stay in the succession duty field in some fashion, they must have a gift tax, in order to preserve the integrity of the succession duty. Otherwise, one could just walk through the succession duty, except in those circumstances where the donor does not survive the recapture period.

It seems to me that at least in the case of Ontario, Quebec and British Columbia, the three succession duty provinces, it would not be an unwise bet that they will bring in a gift tax before January 1, 1972.

Hon. Mr. Phillips: And subsequently they could make it retroactive.

The Chairman: You mean, abolish the five-year period?

Senator Molson: Do not give them ideas!

Mr. Scace: If they abolished the five-year recapture period, that would open it up even further. Without the five-year recapture period, if you did not have it when you die there would be no succession duty, but the recapture period would be a sort of going back to net it in. That would not do it; that would be worse.

The Chairman: Then they should make it ten years?

Mr. Scace: Ten years, or indefinite.

Senator Burchill: If the provinces retained the succession duty and the federal gift tax is done away with, how will that affect it? Then you would be able to give your whole estate away, according to that.

Senator Beaubien: You have to live five years, at least.

The Chairman: The amount might be included in your estate if you did not survive the period that they have provided for. In Ontario, it is five years. But if they made that ten years, they would surely catch more people.

Mr. Scace: One could make the period the whole lifetime.

The Chairman: Yes.

Senator Burchill: Some provinces have their own succession duties. For instance, New Brunswick has.

Mr. Scace: It has none.

Senator Heath: May I ask Mr. Scace about the British Columbia legislation on this? Is it not possible that the British Columbia government have made their gift tax retroactive just recently? I think they tried to do this, if it was for a charitable institution, just to get a bite out of a very large estate that was left, as in the case of a donor to a medical school.

Mr. Scace: It is about a year since I went through the British Columbia succession duty act completely, but I think it was a year or a year and a half ago that they did change their law on charitable bequests on death. It had to be a charity within the province, I think. They restricted the ambit of charitable gifts. Whether that was done deliberately against one particular estate I do not know but certainly there was legislation in that area.

Senator Heath: Was it retroactive?

Mr. Scace: It might have been made retroactive. It could very well have been. I know that was one particular amendment generally that they did bring in.

Senator Heath: I see why our chairman is concerned that we should look at the provincial actions before we move.

Mr. Scace: The provinces are a very important factor in this issue. There is no question about that. It makes planning very difficult. All you can do is assume that the federal Government will go through with it, make your plans on that basis, but keeping a very close eye on the provinces. If, as you suggest, and as Hon. Mr. Phillips suggested, they make their legislation retroactive, you could end up having done something on January 1 and find that, with retroactive provincial legislation, it was either of no effect or it resulted in a position that was completely undesirable from your point of view. I can foresee somebody with a large estate giving a substantial part of it to his children, with the thought that he would avoid all death duties and gift taxes; but if they made it retroactive so that there was a substantial tax bill involved, he never would have done that. I would hope that if they make it retroactive they will at least give you the opportunity of being able to unwind it, but that may be somewhat hopeful.

Continuing on, if gift tax is abolished, there will be a deemed realization at fair market value of all gifts. That is in section 69)1)(*b*) (ii). In that case, there is no distinction between depreciable property and non-depreciable capital property.

In the case of both the deemed realization on the making of a gift and the deemed realization on death, there is an

exemption if the property is transferred to a spouse. The transfer may be either absolute to the spouse or to a qualifying trust for the spouse. In order to qualify, the spouse must be entitled to receive all of the income of the trust that arises before his or her death. No person except the spouse can obtain any of the capital of the trust prior to the spouse's death. In those cases, on death there is a tax-free exemption on the transfer. In the case of non-depreciable capital property, the property goes over at its adjusted cost base. In the case of depreciable capital property, the transfer is at undepreciated capital cost.

On that case, I think we went through a number of examples on the last occasion, as to how it would operate. The reference there is section 70(6) in the case of death and section 73 in the case of gift.

Where you have a gift to a qualifying trust, on the death of the spouse there is a deemed disposition at fair market value. This is very much like the present exemption under section 7(1)(*b*) of the Estate Tax Act, where you get an exemption going in but on the spouse's death there is a realization at fair market value.

The Chairman: Who pays the tax on that deemed realization at the spouse's death?

Mr. Scace: I think it is the spouse's estate.

The Chairman: I would think so, because otherwise it would make a mess of the original estate, would it not?

Mr. Scace: We are really into the same old problem we had with the Estate Tax Act, where very complicated exoneration clauses were required in the will. The same will continue under the new bill.

The next topic is the attribution rules. We have had the attribution rules on the statutes for many years. These you will find in sections 20, 21 and 22 of the present act.

Senator Isnor: Before you go on with that, would you briefly give us the situation in respect to gift taxes at the present time?

Mr. Scace: Yes, sir. The gift tax at the present time is found in Part IV of the Income Tax Act. If you make a gift, unless you fall within certain exemptions, there will be a tax payable. In addition, it is a cumulative calculation so that if you make a $10,000 gift, for example, in year one you pay tax on that, and if you make another $10,000 gift in year two the tax is computed on the $20,000 less the tax on the $10,000 for the prior year. So you are always moving up the rate schedule. The most important exemptions under the present gift tax provisions are that there is an exemption on the transfer to a spouse, either absolutely or by means of a qualifying trust; there is a $2,000 exemption in the case of a gift to an individual or specific kind of trust for an individual; and, in addition, there is a $10,000 gift of an interest in real property where that property is a farm and it is given to a child for farming. Essentially, those are the main aspects of the present gift tax.

The Chairman: Senator Isnor, the effect is that if you are accumulative in your gifting, for instance $5,000 this year, $10,000 next year and $20,000 the year after, then they accumulate them to determine the rate in each year. For example, if you make a gift of $5,000 in the first year the rate is 10 per cent, I believe. If you make a gift of $10,000 the following year, where the rate would normally be, say, 12 per cent, the rate is determined on the basis of adding the $5,000 and $10,000 together, so that you would look at what the rate would be on $15,000, and that is what you would pay on the $10,000 on the next year.

Senator Isnor: How many gifts of $2,000 each can you give at the present time?

Mr. Scace: On the exemption of $2,000 you can make any number of gifts. You could make a $2,000 gift to everybody in this room.

Senator Beaubien: Hear, hear.

Mr. Scace: I would recommend that, senator.

You cannot give two $2,000 gifts to the same person in one year and get the deduction. You would end up by paying tax on $2,000.

Senator Isnor: But there is no limit to the number of $2,000 gifts you can make in a year.

Mr. Scace: That is right.

The Chairman: Keep that in mind, senator.

Mr. Scace: We were just dealing with the attribution rules. Under the present act, if you transfer property to your spouse or to a person under the age of 19 the income on the transferred property is attributed back to the transferor. The income belongs to the transferee, but for the tax purposes the transferor must include that income in his income and pay tax at his rate. That is the present situation. Those rates, looking at straight income, are included in the bill.

In addition, however, there are certain complications which are necessary because of the capital gains tax. The first complication is in relation to a transfer to a spouse and is found in section 74(2). Thereby, if a person transfers property to a spouse after 1971, then any capital gains on the transferred property will be attributed back to the transferor. I stress that it is after 1971. If you transfer property today, although the normal income would be attributed back, capital gains will not be attributed back. They only start picking up the capital gains on transfers after 1971.

The Chairman: You had better start gifting right away, if you want to get the benefit of that.

Mr. Scace: Secondly, for some unknown reason there is no capital gains attribution where a gift is made to a person under the age of 19. All you will get is the normal income attribution. I don't know why that was left out. Perhaps it was left out by mistake, or one possibility is that because tax might be payable on the transfer, whether it was a sale or deemed realization, they don't have to attribute back capital gains on the transferred property. I just do not know. In any event, it is not dissimilar to the situation where the transfer is to a spouse.

The Chairman: Well, it is not a specific exclusion, is it? It is just that they do not cover it.

Mr. Scace: They do not cover it, that is right.

Senator Hays: Suppose a person makes a down payment on a house for a one-year old child. The house belongs to the child. It is amortized over 25 years. It can be rentable and paid out in the 25th year. How is this earning handled in so far as the child is concerned?

The Chairman: You mean the rental income?

Senator Hays: Yes.

The Chairman: It is the father's.

Senator Connolly: It is the donor's.

Senator Beaubien: If the child is not related to the donor . . .

Mr. Scace: It does not matter whether the child is related or not. So long as the person is under 19 years of age no relationship is required.

In the circumstances you indicate, Senator Hays, where there is an absolute transfer to the child there will be attribution. What you would undoubtedly do in that case is transfer to a trust so that if you ever wanted to sell the property you would not have the problem of the child not being able to give title on a conveyance. So you would put it into a trust and there would be attribution again. There are methods of avoiding attribution by using both a trust and a corporation, but that gets somewhat complicated.

Senator Hays: So this has not changed.

Mr. Scace: No, sir.

The Chairman: Senator, I thought you were going to suggest a gift of $2,000 each year from age 1 to age 21.

Senator Benidickson: That would be quite normal.

The Chairman: Yes.

Senator Hays: But the earnings would not build up capital for the child.

The Chairman: The earnings would be the earnings of the donor.

Senator Cook: They would be taxable.

The Chairman: Yes. They would be taxable as the earnings of the donor, although they could go into the account of the donee.

Senator Hays: Well, does inflation change the original capital cost? Would the capital gain also be the responsibility of the donor? If so, suppose the donor dies?

Mr. Scace: No, sir. Under the present statute there is no capital gains tax so there is no problem. As I have just said, with transfers to infants or to persons under the age of 19 there is no attribution of the capital gain. There is only the ordinary income, and we don't know why that is so.

Senator Connolly: But there is attribution for gifts, even the exempted gifts, for people over 19.

Mr. Scace: If the person is over 19 there will be no attribution at all.

Senator Connolly: Of capital gain?

Mr. Scace: Of ordinary income or capital gain. It is only when a person is under 19 that there is attribution. So if you gave it to your one-year old child there would be attribution until the child reached the age of 19, and then the attribution would cease.

Senator Connolly: Just to be clear, Mr. Scace, under the new system, if a gift is made to a child, a son or daughter, who is over the age of 19, the income earned on that gift is not attributable to the donor.

Mr. Scace: You are referring just to a child over 19?

Senator Connolly: Yes.

Mr. Scace: That is right. Under the present act and under the new act there is no attribution over 19.

Senator Connolly: But when the gift is to a spouse there is attribution of income?

Mr. Scace: Right, so long as they remain husband and wife.

Senator Connolly: So if a husband makes a gift to his wife, the income earned on that gift is attributable to the donor and is included in his income indefinitely.

The Chairman: So long as the asset remains in existence.

Senator Connolly: Now, under the new rules, what is the situation?

Mr. Scace: Under the new rules what you have just said remains, plus if a capital gain is made on the property it is attributable to the donor as well.

The Chairman: That is in relation to the spouse?

Mr. Scace: That is right. You are now allowed to split income. You can split assets but not income.

Senator Hays: But there is an exemption of $1,000.

Senator Connolly: You get a lot of people asking about these things, and I suppose there is a heavier onus on a donor under the new system because the donor increases his income by the capital.

The Chairman: By the attribution of the capital gain.

Senator Hays: If you go back to the same example I gave and if you give the child $2,000, and the parent is the custodian and he decides in his wisdom to put a down payment on some real property that he thinks is a good investment, then the earnings of this real property is computed in the donor.

The Chairman: But if the donor sold that property and made a capital gain, the capital gain would not be included.

Senator Hays: If he was under 19.

Mr. Scace: That is the point. They have not attributed capital gains under 19. One thing they also have not done is to allow the attribution of capital losses in the spouse situation, and I think all you can do is query that.

Turning now to trusts, the law on trusts has been made extremely complicated but perhaps not complicated

enough. As I indicated those people working daily in the trust field feel there are a number of matters not covered that should be covered. This becomes extremely complicated and I do not know if you would just like me to pick out the problem areas.

The Chairman: Let us have the general incidence and then the problem areas.

Mr. Scace: All right. The taxation on trusts will remain much the way it is now in that income will come into the trust and be taxed, although if it is payable to a beneficiary there is a deduction to the trust. The same will be true for capital gains. The imposition of the capital gains tax does not complicate that aspect too much. However, one very serious problem relates to what they call the taxation of accumulating income on an *inter vivos* trust. Where you have accumulating income in an *inter vivos* trust, that income will be taxed at the greater of the personal rates of tax or at 50.7 per cent.

Senator Connolly: The personal rates of tax of the beneficiary?

Mr. Scace: Of the personal rates schedule. The trust is considered to be an individual and the personal rates apply to the trust. So the minimum rate of tax is 50.7 per cent and it could go up to 61.1 per cent which is the maximum personal tax rate.

This is a clear penalty on many existing *inter vivos* trusts. They had to try to alleviate the penalty in some fashion, and they state that it will not apply to a trust established before June 18, 1971, if it was resident in Canada on June 18, 1971 and without interruption from there on, but did not carry on in active business and, most important, has not received any property by way of gift since June 18, 1971. This may be a trap for many people because trusts were established under the Gift Tax Legislation so that you could take advantage of the $2,000 exemption and in a gift to an individual where the individual was a minor and you established a qualifying trust under section 112(3) of the Income Tax Act. Many of those trusts provide for accumulating the income with vesting before age 40. They will be exempted so long as no contribution is made to them after June 18, 1971, so people should have stopped making contributions and should not make any more contributions this year or in the future.

Senator Benidickson: But was that not subject in many jurisdictions to the donor living for a certain period of time after the gift to the trust?

Mr. Scace: To avoid estate tax and succession duties, that is right, sir. But this is looking at the income tax consequences of it.

The Chairman: But you said in most trusts to which you referred that to avoid this you should not make more contributions to the trust this year, next year or any succeeding year. But supposing in the period from 1871 down to this year there have been contributions?

Mr. Scace: That is no problem, because contributions will remain as trust assets. The accumulating income on those contributions or the trust corpus will continue to be income of the trust and will be taxable at normal personal rates. It will not be subject to this penalty. Now it is conceivable that the normal rates will get up as high as the penalty tax, but then again they may not. But there is this trap.

Senator Lang: If you make a contribution after June 18, do you destroy the whole trust?

Mr. Scace: That is right. The accumulating income of the trust will then, starting on January 1, 1971, be subject to this minimum 50.7 per cent tax.

Senator Benidickson: So if instead of giving $2,000, or whatever the non-taxable gift may have been over the year, to a minor under the age of 19, you had been giving it to a trust, an individual trust for each child, do you say that from June 18, 1971, there is a danger in continuing to make a similar gift to that turst—that you should give the cash to the individual?

Mr. Scace: That is right. The trust income is accumulating. If the trust income is distributed annually, there is no problem.

Senator Benidickson: That is a real trap. I have not read very much about it in the financial papers.

Mr. Scace: If you read the "raspberry books", the Government's summary, you will find a mention of it, but it is a trap.

The Chairman: Let us move on.

Mr. Scace: There are a number of new definitions in the trust area. You should be receiving many briefs on this. There is a new concept of a "preferred beneficiary". A preferred beneficiary is someone who is closely related to the settlor, the spouse of the settlor, or a grandchild of the settlor. The importance of the preferred beneficiary is that an election may be filed whereby the accumulated income of the trust can be taxed to the beneficiary. You will find it in section 104, subsections 14 and 15. The purpose of this is to avoid high tax rates on accumulating income while in the trust. Unfortunately, the law concerning this election is very inprecise. The total amount upon which an election can be made is defined at great length and, perhaps, inadequately in section 104(15). There are a great many problems involved in this particular area. You should be receiving a special submission, if not from the Canadian Bar Association, then from a certain group of lawyers on that particular topic. It is a problem area.

In relation to the capital gains and trusts, the most important aspect is the 21-year deemed realization on non-depreciable capital assets in a trust. This is a corollary or an adjunct to the deemed realization on death of a spouse where you have a qualifying trust. If the assets are transferred to a qualifying trust for a spouse, upon her death there is a deemed realization at fair market value. If there is a succeeding life interest, or any other trust, there will be a deemed realization every 21 years of the non-depreciable capital assets. I suppose that this is somewhat similar to the five-year re-valuation rule for shares of widely-held Canadian companies which you found in the White Paper; although, it is certainly for a longer period of time. It may not be an unfair provision.

Senator Connolly: And it is a rule against perpetuities.

Mr. Scace: The rule against perpetuities could have an effect here, yes.

The Chairman: What section is that?

Mr. Scace: Section 104, subsections 4 and 5.

Senator Connolly: The only difference between this and the rule against perpetuities is that there is a revaluation.

The Chairman: Let us not get into a discussion on the rule against perpetuities.

Mr. Scace: For the 21-year deemed realization for non-depreciable capital properties at fair market value, and for depreciable capital properties, the calculation is the mid-way point rule, as it is at death. It is the same thing. I think you may have problems of liquidity when this deemed realization occurs. You will also have difficulties where established trusts are already in existence and will extend beyond the period of 21 years after the implementation date. I think that all you can do there is perhaps to wind the trust up, or make an application under the various provincial statutes to vary the trust in order to change the provisions so that this 21-year rule cannot apply.

Hon. Mr. Phillips: I would assume the 21-year rule creates problems for the younger lawyers rather than the older lawyers.

Mr. Scace: I guess that is correct, sir.

The Chairman: Only to the extent that the younger lawyers would have a longer space of time in which to look at the problem.

Mr. Scace: And to look at it again.

Hon. Mr. Phillips: Yes, and to attempt to solve it.

The Chairman: I expect the older ones would still have to look at these problems.

Mr. Scace: There are also very complicated rules in relation to the beneficiary of the trust. There are two new terms brought into the bill—one is income beneficiary, the other capital beneficiary. There are very detailed provisions for determining the costs of the various interests. In the case of capital beneficiary, you have to determine the capital gain if the capital interest is sold.

However, those are the most serious problem areas in relation to trusts. The law concerning deceased persons is more or less the same as it was under the current act with one interesting addition, allowable capital losses—that is, one-half of a capital loss—may be deducted in full against any other income in the year of death. Therefore, if there are substantial capital losses in the year of death on the deemed realization they can be adjusted against any other income, as provided in section 71. In addition, net capital losses may be deducted against any other income in the year of death and the immediately preceding year, as provided in section 111(2).

The Chairman: That means that capital losses which it was not possible to take care of otherwise cannot be accumulated.

Mr. Scace: If there were enormous capital loss, or a net capital loss position, it is conceivable that the income in the year of death or the immediately preceding year would not be sufficient. However, it is hard to know; we have not seen this in practice. I think that in most circumstances the net capital loss position would probably be eradicated at death. It may not, but I would hope that if an inequity does result and it appears that this is not the case, the application of these rules will be liberalized, and perhaps extended for some years.

The Chairman: What are you thinking of when you say "liberalized"?

Mr. Scace: In particular that the net capital losses could be deducted against other income, not only in the year of death and the immediately preceding year, but possibly in the preceding five years. There could be a provision to allow the total to be adjusted against other income.

Senator Connolly: Before they finally put your file away.

Mr. Scace: That is right. Mr. Smith last Wednesday discussed registered retirement savings plan.

If you have any particular interest in tax havens I think generally it can be said that they will not be as useful under the new system. If the tax cost of dying is reduced there will not be as much advantage in moving to a tax haven. Section 48, which is the departure tax imposes a penalty for moving to a tax haven. Therefore, depending on the amount of accrued gains, you may decide not to move. However, right now may be a very propitious time to move, or early in the new system, before capital gains have started to accrue.

In relation to insurance, this is all in the estates area, as we mentioned last week, insurance is not subject to capital gains tax. Therefore it is now probably a more interesting investment vehicle. However, if the tax cost of dying is reduced there is probably less need for insurance to cover Senator Connolly's problem of liquidity when the tax is due on death. So these aspects apply both ways.

There is also a problem in relation to key-man insurance. Under the present statute, if a corporation has taken out key-man insurance it goes into capital and can be withdrawn from the corporation tax-free, provided that the undistributed income in the company has been first taken out. However, under the new bill it appears that the only way to take out the proceeds of key-man insurance is by way of taxable dividend. Therefore this is a disadvantage under the new bill, as opposed to the old act. The department is aware of it; we do not know whether they plan to do anything about it.

The Chairman: By "taxable dividend", do you mean that the whole amount would be income?

Mr. Scace: Income to the shareholder, as opposed to its now being a tax-free receipt.

The Chairman: Income to the person receiving, not to the company?

Mr. Scace: No, not to the company. It merely relates to getting the money out of the company.

Estate freezing will continue to exist under the new law. However, it will be freezing against provincial succession

duty, if any, plus the tax on capital gains accrued on the assets rather than against federal estate tax. It will be an attempt to avoid the capital appreciation and deemed realization on death. Freezing will be less attractive under the new bill, since the very act of freezing will trigger the capital gains tax to the extent there is any appreciation. The assets must be transferred at fair market value and if that value exceeds the cost there will be a capital gain tax, whereas now they can be transferred without fear of capital gains tax.

Hon. Mr. Phillips: Mr. Scace, this may not be relevant for the committee with respect to this bill as such, but very relevant in relation to its overall duties.

Are you aware of any studies with respect to the issue of the very point you have discussed—that is the consequences of individuals or corporations building up cash positions, rather than buying equity or securities in Canadian companies and thereby stopping investment by Canadians in Canada, which would bring about the suffocation of our economy or an invitation to outside capital?

You are touching on a very crucial point. When people invest in securities at large in Canada, they are facing deemed realization on death. If they put investment in money as such, there is simply no further increase; money is money, whatever its purchasing power.

The Chairman: Or if they put it in bonds.

Hon. Mr. Phillips: Yes; money being money and bonds being equivalent to money. That is one thing.

By buying into the equity of the company this problem is invited, thereby stifling the economy and inviting foreign capital.

I am only putting the question to have it on the record to indicate the seriousness of the point, and as an indication that this committee may well wish to consider that whole question in relation to certain bills, when it becomes the subject of legitimate study.

Senator Beaubien: Putting it into equities would only attract cash, if it were capital gain.

Hon. Mr. Phillips: Exactly.

Senator Beaubien: So the money is not taxed if there is no capital gain.

The Chairman: If it is kept in money it is guarded against the capital gains problem. If it is in bonds it is substantially guarded against the capital gains problem. If it is put into equities the same guard is not up.

Senator Beaubien: Maybe I am a little stupid, but supposing I have half a million dollars and keep it in cash, there is no capital gain. If I put the half-million dollars in stock and it increase to $600,000, there is a capital gain on $100,000. However, I am still better off than if I had the cash. The $500,000 is worth $600,000; sure, there is capital gains tax on $100,000, but if I keep it in cash, when I die it is worth half a million.

Hon. Mr. Phillips: But you are taking the risk on your half a million dollars, and you do not know if you will have the capital gain. You relate your ultimate tax consequences on death; whereas, if you put it in equity stocks, you do not know where you are going. You take a risk, and you are deliberately, through deemed realization, bringing about a situation where you are cooling off equity investment by Canadians.

The Chairman: Senator Beaubien, all that you are illustrating is that, depending upon the amounts available, you may have a substantial problem or you may have a problem that you relate to keeping the cash even after paying taxes, so that it would still leave you a little more money.

I think Senator Phillips was talking about an investment company which had accumulated cash and put it into equities or gains in volume in the course of ordinary operation. With regard to the $500,000 that you are talking about and limiting the capital gains to $100,000, if you put it into securities, shares, and have a capital gain on death of $100,000, then obviously, even by paying tax on the capital gain, you would have more money than if you just kept the cash.

Senator Cook: Is not the only answer to Senator Phillips' problem that of no capital gains?

Hon. Mr. Phillips: Either no capital gains or no capital gains other than on a true realization by disposition at arm's length, other than relationship to trusts, where legitimately the question of perpetuity of rule should apply within reason.

In our Senate report on the White Paper we took the fundamental position that there should be no tax other than on actual realization. We succeeded up to a point. We are now talking about deemed realization.

Senator Beaubien: Deemed on death.

Hon. Mr. Phillips: Yes. We succeeded up to a point. I am making the point before this very important committee that on this very crucial issue we are inviting a situation in Canada where we are deliberately discouraging equity investment and at the same time are inviting foreign capital to penetrate further.

Senator Cook: Does not that situation apply to any country that has capital gains?

Hon. Mr. Phillips: I think I would prefer not to go into that today. It is important enough to record the point.

Mr. Stephen C. Smith, Partner in the Law Firm of McCarthy & McCarthy: What Senator Cook is saying, I think, is that if at the present time you make a capital gain in an equity investment you pay zero tax. If you receive interest income you pay tax at full personal rates.

The tax bill changes that. Instead of being zero tax, your capital gain is at half tax. The incentive has gone from being the whole of the tax to being only half of the tax.

Senator Hays: If interest rates are high, you more or less have to put it into a 9 per cent bond, because you will be paying 46 per cent profit . . .

Hon. Mr. Phillips: Or sit on the bank deposit.

Mr. Scace: That more or less closes the general area of estates. There are many problems facing the legal community, but I think that many of them are soluble.

The Chairman: The second item is international taxation. Mr. Stephen Smith will develop that.

Mr. Smith: Mr. Chairman, in the subject of international taxation, there are really two quite separate topics. On the one hand you have taxation of Canadian residents on their incomes derived from foreign sources, and on the other hand you have taxation by Canada of people who do not reside here. Those are two different topics.

I must apologize if my outline is a little sketchy. I will try to avoid becoming mired in some of the drafting complexities, and will give you what I think is the general effect of it, rather than becoming too involved in the detailed provisions.

The best place to start is probably the Government's summary—this red book—which accomplished the summarizing of it in three pages. It took CCH 56 pages to deal with it in their detailed analysis; so honourable senators will see the difference between a summary treatment and a detailed one.

In broad outline, the main features of the system remain the same, although some details have been changed. Canadian residents will still be taxed on their world incomes. There is no change in that as a basic principle. Non-residents will still be taxed on their income from business and employment in Canada, and Canada will continue to impose a withholding tax on various kinds of payments to non-residents, the most notable of which are dividends, interest, royalties, and payments of that sort.

The red book summarizes the mainchanges. As you know, under the present act you have a credit—I am now talking about the foreign income of Canadian residents—for taxes that you pay to a foreign country when you receive income from that country in Canada. There have been some modifications to that credit which improve it for Canadian residents. Firstly, foreign taxes that are paid on business income, which are in excess of the available credit in any year, because of disparities in the rates between countries, will be availble to be carried forward for up to five years, and deducted later from business income from that country. That is a change in the direction improved equity for the Canadian taxpayer.

The second main change is that after 1975 the foreign tax credit on investment income of individuals will be limited to 15 per cent. If any country should impose a greater withholding tax—that is, on a payment out of their country to a resident in Canada—that excess will be treated as a deductible expense to the Canadian investor, which is not such generous treatment as giving him the full credit.

The third major change is that under the present foreign tax credit, the credit is for taxes paid to a foreign sovereign country. For example, in the case of the United States it is for taxes paid to the US federal Government. No credit is given for state taxes. If you pay an income tax to New York State, the present credit does not pick that up.

The new legislation gives credit for such taxes. It will be recognized either as a deductible expense or as income tax subject to the credit, depending on their treatment in the foreign country.

For example, the United States allows state taxes as a deductible expense to its residents and such taxes will get the same treatment here.

Those are the main changes in the foreign tax credit. I will come back to them later.

The next major area for Canadian residents involves a concept which the summary deals with under the heading "Foreign Affiliate".

As honourable senators probably know, under section 28 of our present act, Canadian residents have for many years been able to get a deduction for dividends received from a foreign company, when they own more than 25 per cent of the voting shares. That would enable someone in Canada to set up a company abroad and earn either investment income or active businesss income abroad, perhaps pay no tax on it abroad in the foreign subsidiary and bring it home, claim a deduction for the full amount of the dividend and pay no tax. The Government obviously feels that that is unfair. It would enable someone who happened to be able to do that to pay no tax whereas another Canadian resident who earned the same type of income in Canada would be subject to the full rates of tax. The way the Government got at that in the bill was to introduce the concept of a foreign affiliate. A foreign affiliate's income, to the extent that it is investment income, is going to be attributed to the Canadian shreholders and be taxed to them. There are other changes with respect to active business income.

A foreign affiliate will be defined as a company that is controlled by a Canadian taxpayer either by himself or together with a related group of people, or one where a Canadian taxpayer owns 25 per cent of the voting shares or 50 per cent of any particular class of shares; also, where a Canadian taxpayer owns 10 per cent of the voting shares, he may elect to have it treated as his foreign affiliate.

Senator Molson: Would you repeat that, please?

Mr. Smith: If a Canadian taxpayer owns 10 per cent of the voting interest he may, if he wishes, elect to have it treated as his foreign affiliate; it is not automatic.

Senator Molson: That is a change from the 25 per cent.

Mr. Smith: Yes. There are several changes.

Senator Molson: That is a decided change.

Mr. Smith: Yes, that is right. Under the new legislation dividends received by a Canadian corporation from a foreign affiliate will be exempt from tax if they are paid out of profits earned before 1976. The point of that is to give Canada a chance to renogotiate its foreign tax treaties; that is the purpose for the five-year period of exemption.

Senator Gélinas: Would you mind repeating that, please?

Mr. Smith: Any dividends received before 1976 will be exempt from tax provided that they are paid out of profits of the foreign affiliate which it earned prior to 1976. That is a transitional period in order to give the new tax treaty system a chance to be built up.

After the transitional period, dividends will also be exempt if they come out of a country with which Canada has a tax treaty. Where they do not come out of a tax treaty country, then they will be exempt from taxation to the extent of the level of tax they bore abroad.

Another matter is the problem of tax sharing.

Hon. Mr. Phillips: Mr. Chairman, may I put a question to Mr. Smith?

Do you not find that treatment rather strange under two headings? For example, compare it with a dividend income received by a Canadian corporation from another Canadian corporation. If the receipient corporation is a private corporation it is subject to a 33⅓ per cent payment immediately as against the receipt of income from an affiliate where you have five years without being subject to any tax whatsoever before you are obliged to distribute.

Mr. Smith: Yes. I will come back to that.

Hon. Mr. Phillips: And do we not find a further extraordinary situation with respect to the taxable income under heading 2—that is, when a Canadian company in due course gets a dividend from an affiliate in a treaty country the recipient company is free of tax whereas in Canada the recipient company of a dividend from another Canadian company is subject to an automatic tax of 33⅓ per cent provided it is a private company? Am I right in my comparison, and do you not find it strange?

Mr. Smith: There are a number of extraordinary results and they come, I think, from the direction in which the Government started. I will work through the details in a moment.

Hon. Mr. Phillips: I apologize; I may have interrupted.

Mr. Smith: There is also a transitional period designed to give relief where a Canadian investor has gone into a developing country on the basis of getting tax concessions from that foreign country; that foreign country, in other words, is not levying any tax. The transitional rule which will be enacted by regulation at a later date will enable dividends from such a project to be brought back tax-free as they would now, provided that they are in respect of projects which one fully committed before the end of 1975.

Senator Connolly: We had this yesterday, Mr. Chairman, from the Chamber of Commerce delegation, as I recall.

Mr. Smith: I will just run through the other changes in outline fashion and I will come back to them.

Foreign business corporations, as you know, are being phased out over five years. The general rate of withholding tax is going to remain at 15 per cent until the end of 1975 and then it will increase to 25 per cent unless it is reduced by treaty. The existing exemptions from withholding tax on Government bonds are continued where they were issued before 1976, and also the exemption on interest payable to certain foreign charitable organizations that register will continue, generally speaking.

The idea that a degree of Canadian ownership will reduce non-resident withholding tax is preserved, and it gets reduced by 5 per cent from what the withholding tax would otherwise be. In other words, if you have a withholding tax of 15 per cent it becomes 10 per cent, and if you have a withholding tax of 25 per cent because there is no treaty, it becomes 20 per cent.

Senator Connolly: What are those circumstances again? There is a 25 per cent withholding tax on dividends paid into a country with which we have no treaty?

Mr. Smith: That is correct.

Senator Connolly: And you say there is an automatic reduction by 5 per cent?

Mr. Smith: Yes, where you have a degree of Canadian ownership in the company paying the dividend. That was brought in by Mr. Gordon, the former Finance Minister, in 1963. You had to have at least a 25 per cent Canadian equity interest in the corporation. That was the time that several United States companies went public in Canada and sold 25 per cent of the stock to the Canadian public and hence had their withholding tax rate reduced from 15 per cent to 10 per cent.

Senator Connolly: It is reduced from 15 per cent to 10 per cent?

Mr. Smith: Yes. If the withholding tax, because there is no treaty, is 25 per cent it will be reduced to 20 per cent, but otherwise it will continue to be a reduction from 15 per cent to 10 per cent.

Senator Connolly: This is to increase Canadian ownership?

Mr. Smith: It increases Canadian ownership in the foreign-controlled company.

Senator Connolly: Yes, in the Canadian company paying the dividends.

Mr. Smith: That is right, the Canadian company paying the dividend. The dividend is being paid to the non-resident from the Canadian company. It is a Canadian company as well as having a Canadian ownership interest. Certain pensions will be subject to withholding tax that have not been subject up to now. There is some revision in the branch tax, to have it follow the treaty rate. There is a provision called the thin capitalization rules, to prevent a Canadian corporation which is foreign-owned from reducing its taxable income in Canada by the payment of foreign interest charges to its foreign parent. The rule there is that, to the extent that the interest is paid on debt which exceeds three times the share equity of the non-resident, the interest will be proportionately disallowed as an expense to the Canadian corporation.

The Chairman: It will be treated as a dividend.

Mr. Smith: That is right. The final change—going through it in a summary way—is that non-resident owned investment corporations will now be subject to tax at 25 per cent, starting in 1976 and the income of the NRO would include capital gains to the same extent as if the NRO were a non-resident person. That is, just certain types of capital gains. The tax on those capital gains will be refunded when dividends are paid out to the non-resident shareholder. There is also a requirement that the NRO'S must be 100 per cent owned by non-residents.

If I may go back and look at some of the details, the most difficult concept is the foreign affiliate. As I said, there is a multiple definition of a foreign affiliate. You find it in section 95(1)(*b*). Basically, you have three ways in which a company can be a foreign affiliate of a Canadian taxpayer. Where the Canadian taxpayer controls it directly, or through a group of people who are related to him, then the foreign company becomes his foreign affiliate.

Where he has at least a 25 per cent voting percentage, which is a defined term in section 95, or if he elects, where he has a 10 per cent voting percentage, it becomes his foreign affiliate. Similarly where the taxpayer and other non-armslength residents have a 50 per cent "equity percentage", which is again a defined term, the company becomes his foreign affiliate.

"Voting percentage", as it implies, merely looks at the number of votes that are available. If you control something through a chain of companies, it will look down through the chain. For example, if you own half of the subsidiary and that subsidiary owns half of another company, you follow those percentages down and finally you have got 25 per cent at the bottom.

Senator Molson: May I ask what the object of subsection 4 is there, the election of 10 per cent?

Mr. Smith: I think that is to give someone an option of having it treated as a foreign affiliate, where that turns out to be more advantageous to him.

Senator Molson: Is it possible it would not be more advantageous than his getting the dividends without tax?

Mr. Smith: It depends on the nature of the foreign affiliate's income. I will get to that. There are some places where it is difficult to pick up the foreign tax credit for the foreign withholding tax, and you might want to have it treated as a foreign affiliate for that purpose.

Hon. Mr. Phillips: May I interrupt Mr. Smith, through the chair? And for the first five years, Senator Molson, exempt. As long as you distribute at the end of the five year period, it cannot be touched on.

Mr. Smith: The "equity percentage", which is defined in section 95(4), looks at the percentage you have of any particular class of shares you have in the foreign affiliate. It takes the portion you have of the class, of each class, and you take the highest percentage. The effect of it is that you may find, in a foreign affiliate where there are a number of different classes of shares and a number of different Canadian residents, holding different classes of shares in varying proportions, they may each end up with a participating percentage which is greater than 100, all told, when added up.

Many honourable senators have the Commerce Clearing House (CCH) analysis of the bill. You will find an example of that at page 225, where they worked out a complicated example and end up with that result.

The result of that is that you could find more than 100 per cent of the foreign affiliates' income had been attributed to various Canadian taxpayers, which is an extraordinary result. It can hardly be intended, unless it is intended merely as a deterrent to using foreign affiliates at all—which could hardly be the government's intention. One has to think that it is probably just a drafting error and that the section would have to be re-worded.

It should also be noted that not only can a corporation be a foreign affiliate; a foreign trust can be a foreign affiliate, too. The obvious intention of that rule is to prevent Canadian taxpayers using a foreign trust as a convenient place to put foreign investment income and avoid Canadian taxes. So such trusts are treated as a foreign affiliate corporation, and you look at the beneficiary's interest. It can either be an income interest or a capital interest. Again, you can find that, where you have a life tenant and a remainder man, they are each deemed to have 100 per cent of the foreign affiliate—which again produces an anomalous result.

Senator Connolly: You will look for an amendment, presumably?

Mr. Smith: Yes. Getting away from the definition, and looking at the result of the definition, once you have a foreign affiliate, the Canadian shareholder must include in his income his equity percentage of all the foreign corporation's passive income. That is basically income of an investment nature or income that could not be characterized as an active business. That income is included in the Canadian shareholder's income, regardless of whether or not it has been distributed. It is deemed to have been distributed to him.

There is a notch provision, or, rather, there is a deduction of $500, so that people who have small amounts of income from such companies will not be bothered with the complexities of it. When I referred to "passive income," that is a short form for "foreign accrual property income" and it is defined in section 95(1)(*a*). As I said, basically it is the net income from investments in property other than active businesses, and net capital gains except on property used in the active business.

There is no definition of "active business" in the bill, but there is a fair amount of jurisprudence in Canada now under the personal corporation sections as to what is an active business, so presumably that will be of some help.

Now, you get a deduction for the underlying foreign income taxes. That is given under section 113(3).

The Chairman: So there would be no benefit of having a foreign affiliate in a tax-free country.

Mr. Smith: No. That is right as it regards passive income, and it is even worse than that. To get the foreign tax credit, when you later pay out a dividend from the foreign affiliate, if the dividend is paid out in the same year as the passive income was attributed, you get the credit. If it is paid in a later year it appears that you do not. The result would be that the total taxes, both foreign and Canadian, that are paid are greater than if you had merely received that foreign investment income directly as an individual instead of through your foreign affiliate.

That is really a problem of timing, but it will be quite serious where you do not control the foreign affiliate, but it is controlled by people who are not Canadian residents and who do not care when the dividend is paid. It could prove expensive for you.

The Chairman: The foreign tax credit is only available to the Canadian shareholder in relation to the earnings of the particular year, which may be paid out, or, if they are not paid out, if they are held, it would still be his income for that year.

Mr. Smith: Right.

Senator Molson: Without tax credit.

The Chairman: Yes. He would have a tax credit. As I understand it, if you pay out in the year in which the earnings are made, you would get a tax credit.

Mr. Smith: Yes.

The Chairman: But if they are not paid out in that year, then the Canadian shareholder is taxed as though he had received the income less the tax credit.

Mr. Smith: Right.

Senator Molson: There is no tax credit.

Mr. Smith: No, it is just included in his income.

Senator Connolly: Not less the tax credit!

The Chairman: It is an off-set of the tax credit.

Senator Connolly: The tax credit is not going to be available to him until the year in which the tax is paid.

The Chairman: I am talking about the tax this foreign affiliate would pay on its earnings in that foreign jurisdiction. If it pays out those earnings in the year in which they are made the Canadian recipient would be entitled to a tax credit, but the position I am citing is that, if they are not paid out in that year, nevertheless, the percentage of earnings of that company related to the shareholding of the Canadian shareholder would be deemed to have been received by him. Now, what happens to the tax credit then that represents taxes paid by the foreign affiliate? Is the credit still available, even if the dividend is not received in that year?

Mr. Smith: No, it really is not. You have to get it in the same year in order to pick it up.

Senator Connolly: You cannot get the credit, I suppose, until you know how much the tax is.

The Chairman: But what I am pointing out is that, if the foreign affiliate has earnings in a year, it pays taxes. I assume that the earnings then that are attributed to the Canadian shareholder in that year, if no dividends are paid, would be a percentage of the net earnings after taxes in the foreign jurisdiction.

Mr. Smith: Perhaps it might help if I gave you an example. Suppose you have a foreign affiliate that earns $100 from investments. Suppose in the foreign country there is a 25 per cent tax on that investment income earned by the foreign affiliate taxed to the foreing affiliate so that you have $25 coming off. That leaves $75. You pay that $75 as a dividend to the Canadian shareholder. Suppose there is a withholding tax of 15 per cent, which would be roughly $11, which would leave the Canadian shareholder roughly $64. Now that is the cash that he has. Under the foreign affiliate rules you have again the $100 income earned by the foreign affiliate, and under section 113(3)(*a*) you take off the $25 tax that the foreign affiliate pays, and again you have the $75 available as a dividend. Now, section 90(2) says that you have a dividend, when paid out of that $75, which has already been included in your income so we will not tax you on that. We will give you zero tax.

The Chairman: If we stop right there, what you are saying is that, since the Canadian shareholder is taxed on the amount still in the hands of the foreign affiliate, then when it is actually paid out to him there is no tax.

Mr. Smith: Yes, that is right.

The Chairman: Are there any questions on that point?

Senator Carter: Does that mean he gets the $75 dividend instead of the $64 as in the previous example, because there is zero tax as against $11 tax?

The Chairman: No. The foreign country may have a withholding tax as well. Therefore, whatever is paid out in dividends, when it reaches the Canadian shareholder, is less by the amount of the withholding tax. If it is paid out in the year in which the earnings are made, the tax credit provision applies.

Senator Lang: Mr. Chairman, in that example if the tax on $64 in Canada was 15 per cent, or equivalent to $11, then there would be zero tax. In other words, if the Canadian tax on the $64 was $11, then there would be zero Canadian tax. Is that right?

The Chairman: In Canada, no.

Senator Molson: What about the refund of the withholding tax?

Mr. Smith: I think perhaps I misled you in the first place. The foreign income of the affiliate which is attributable to the taxpayer, the $75, is already taxed at the shareholder's marginal rate in Canada.

Senator Connolly: Whether he gets it or not, the year in which it is earned abroad he pays tax on it at his own marginal rate.

Mr. Smith: That is right.

Senator Connolly: And he gets no credit for that $25 foreign tax paid?

Mr. Smith: He gets that; it is the foreign withholding tax for which he does not get credit at that point.

Senator Connolly: He gets credit for the $25 foreign tax paid?

Mr. Smith: Yes, he does. The underlying foreign tax is in the foreign affiliate. It is the foreign affiliate's after-tax income that is being attributed to him. Say his marginal rate is 50 per cent, then he would pay half of that $75.

Senator Cook: From what you say he pays the marginal rate on the $75 whether he gets it or not, but when he does get it, he does not pay any more tax.

Mr. Smith: That is right, but neither does he get the credit for the foreign withholding tax—the $11 that I had in that example—unless that is paid in the same year. But if he has different years, he does not pick it up.

Senator Connolly: You are saying there is a trap here and there is an anomaly here.

Mr. Smith: Yes, there is a timing problem.

Senator Connolly: But the amendments should pick this up.

Mr. Smith: Yes. The trouble is that the more you try to do with these foreign affiliate rules, the more complex they become, and they are as complex as they are because they are trying to look through a chain of foreign companies and tax the money here to the same extent that they would be taxed had the money been earned here. But it is more easily said than done.

The Chairman: The way the government proceeds now in relation to these situations where you have passive income in the hands of a foreign affiliate is that they have been taxing the Canadian owner on the basis that there is an agency relationship, and that the foreign affiliate is an agent of the Canadian company, and therefore they have been attributing all the income of the foreign affiliate to the Canadian company and have been making reassessments on that basis.

Hon. Mr. Phillips: We are back to the question that when you play around with deemed-to-be-income and deemed-to-be-realization, we become involved in all kinds of complexities.

Senator Connolly: But in the case that you, Mr. Chairman, and honourable Mr. Phillips have been discussing, the Canadian taxpayer gets credit, does he not, for the foreign tax paid?

Mr. Smith: By the foreign affiliate.

The Chairman: He gets that because it is only the net that is attributed to his income. The net is whatever the income is less the tax paid in the foreign jurisdiction.

Mr. Scace: Mr. Chairman, one of the interesting points here—apart from the mechanics of how this is done—is the intention of the legislation and the intention of assessments which are currently being issued, and the whole philosophy appears to become completely contrary to the US philosophy in their DISC Program—Domestic International Sales Companies—and that bill is currently, I understand, before the US Congress. It is strange to me and to many of us—and the Chairman and honourable Mr. Phillips and I have discussed this—that Canada should be going one way when our major trading partner appears to be going the other way.

The Chairman: Under the DISC Program in the United States it was turned down a year ago by Congress, but I understand it is coming up again and the implications are that it may succeed this time. Therefore domestic companies operating outside the United States and generating income get a tax reduction on that income in their domestic returns.

Hon. Mr. Phillips: I should like to remind you, Mr. Chairman, and all honourable senators that we went into this whole thing in our examination of the White Paper and we brought up the tax expert who had previously been the head, I think, of the Internal Revenue in the United States to explain the handling of this so-called offshore and permissive income and the abandonment by the United States of the originally proposed rigourous rules and the treatment presently given to which Mr. Scace refers. We went to the trouble of explaining all that in the proceedings of this committee and now it has been ignored.

Senator Cook: Is the only reason that a taxpayer would not get credit for the withholding tax in a subsequent year because it would be administratively difficult?

Mr. Smith: It is just the way the bill is drafted. It gives it to him in the same year as a part of the foreign tax. But if it is in a subsequent year, it just says the dividend is tax free but meanwhile he has paid the foreign withholding tax which is lost.

The Chairman: If you look at it broadly and if you need any simplification, surely if they need any statutory support for the present method they are following, that is that they establish what they regard as an agency relationship, and you do not like it, then you can make a contest in court, and it would appear that in a lot of the cases of passive income in a foreign affiliate, it might very well be concluded as a matter of law that this is an agency. If you look at how the operations are carried on, it may well be that in many of them the Canadian company really operates the foreign affiliate and all the management and direction and everything else comes from Canada. It might in those circumstances be regarded as an agent. Presently the department is assessing the income or the earnings of that agency as being the earnings of the Canadian company which has established this and which is giving all the management and direction to the operation. Some of them may even just have a bookkeeper or a trust company office or something like that. So they do not need this legislation in order to deal with that situation. This is what we said in our report on the White Paper. We said that there is ample provision in the present law to deal with that kind of situation.

Senator Cook: I may be somewhat slow but how does that justify not giving credit for the withholding tax paid in other years?

The Chairman: It does not justify it.

Mr. Smith: I think that is just an anomaly in the legislation which might be corrected.

Senator Connolly: May I ask a question in connection with the DISC Program? In the example the net income to the Canadian would be $64.

Mr. Smith: Unless he gets credit for the $11 by getting the dividend in the same year.

Senator Connolly: Perhaps I am under a misapprehension, but let me do it my way and then you can correct me.

Let us assume that the net income is $64 to the Canadian parent. Under this program would that $64 be reduced by $25 plus $11, and his net income reduced by $36?

The Chairman: I do not know whether you can use those figures or not. The idea is that income that comes in from the off-shore operations is subjected to a lower rate of taxes in the United States than domestic income of the same company.

Mr. Scace: Could I illustrate this?

The Chairman: Yes, certainly.

Mr. Scace: Let us take as an example a Canadian company that manufactures pencils, and it has a cost per pencil

of $1, and a selling price of $2. You have a profit of $1 and, let us assume a 50 per cent tax, of 50 cents. So you have a net per pencil of 50 cents. What a number of Canadian companies have been doing is to set up an international sales company in a tax haven country. You have a Canadian parent company and an affiliate in a tax-haven country. They would still manufacture the pencil here for $1. It would be transferred to that tax-haven country, let us say, at $1.20 or whatever would be a fair market value at that level of commerce. You have a profit of 20 cents in Canada plus a 10-cent tax. The international sales company in the tax haven country would sell the pencil on the foreign market at the prevailing price in that market. It has a $1.20 tax cost, a $2 selling price, which is the same as the selling price in Canada, and an 80-cent profit. Now, under the presnt situation, that 80-cent profit can be paid back as a dividend tax-free. The net profit in this case to the Canadian company is 80 cents plus 10 cents, or 90 cents as opposed to having the whole operation in Canada where the net profit would be 50 cents. As the Chairman has stated, the Department of National Revenue is endeavouring to assess this, although I do not think we have had one litigated to this date.

The Chairman: They are in the process now.

Mr. Scace: Yes, there may be an agency relationship here and that may be the net result. There are two ways of looking at this. It reduces the Canadian tax, and there is more after tax brought into the Canadian company. The reduced taxes may permit the foreign affiliate company to sell at a lower rate and more competitively on the foreign market. If that is the achieved result, then this is very useful.

What Mr. Smith has been talking about is that this 80 cent income from the foreign affiliate company in the tax haven country will be distributed when earned in the tax haven country; and you will eventually get it back subject to the technicalities which you find in this type of situation. So, while we were more competitive in the foreign market under the present system, we will be less competitive under the new system.

We do not know what the United States law will be in the future. I understand it is even better than the particular situation we are talking about because you do not have to set up a non-resident company. You merely set up another U.S. company and this company handles your foreign sales. You get reduced taxes on the foreign sales. So you achieve the same, if not better, results without these complexities. To the extent that this makes a United States company more competitive on the foreign market, we are at a disadvantage either with the assessments that are being issued now, or with having to set up a foreign affiliate company.

Senator Connolly: Certainly we should draw this very clearly to the attention of the officials in the Department of Finance.

Mr. Scace: The problem is, senator, this may also be an illegitimate device. Companies established in tax haven countries have been used merely as holding companies for assets which would otherwise be situated in Canada. All they are trying to do is to reduce Canadian taxes. The difficulty is to provide something that would permit a legitimate sales organization to exist where it would be better off in a foreign market. That is a very tough thing to do.

Mr. Smith: The tax bill attempts to be neutral as to source of income, whether it is Canadian or foreign, whether earned in a tax haven or in a high tax jurisdiction. The answer of the Department of Finance would probably be that if the Government considers an export subsidy program is required it would design something that did just that, without all the side ramifications such as those involving portfolio investors.

It could be said that the present system is broad-brush and inefficient in that it provides subsidies for exporters to foreign markets, but also in other cases, where it is not desired to subsidize.

The Chairman: The answer is that the difference between those two cases should be recognized. We dealt with this in our report on the White Paper, at page 76, paragraph 7.

Senator Connolly: Would you read it.

The Chairman: Yes. It states:

> Your Committee rejects in their entirety paragraphs 6.20 and 6.21 of the White Paper and concludes that the introduction of equivalent provisions to Subpart F of the United States Internal Revenue Code would be a grave error.

This was the old U.S. legislation. We are not referring to the DISC program.

> . . . The Committee has concluded on the basis of the briefs presented to it that Subpart F has proven to be an inordinately complicated and inefficient tool in the United States, and that current legislation is being directed to substantially reduce or eliminate many of its effects.

This is the DISC program.

> . . . The Committee recommends that rather than the enactment of new legislation to control so-called tax avoidance on passive income (which the Committee is convinced can be controlled under the present legislation by stricter administration) legislation be introduced, such as that now contemplated by the United States for Domestic International Sales corporations, . . .

That is the DISC.

> . . . in order to aid Canadian exporters to compete adequately with their counterparts in foreign countries.

The trouble is that under the method of dealing with it a bigger stick has been used, or a wider sweep is being made. I illustrated to you some of the cases they are aiming at. For instance, a Canadian company might establish a foreign affiliate, in which it invests. That affiliate might be operating in a jurisdiction where there is no tax. In that case a tax-free dividend would be received by the Canadian company from the foreign affiliate in respect of that investment income. That is termed passive income. This, undoubtedly, is the type of situation that may have spurred the proposed changes in the law. However, it does not distinguish between the deserving—shall I put it that way?—and the undeserving.

We consider this to be an error and thought that these situations could be dealt with within the limits of the present law and its actual administration, which is carried on by the department.

Mr. Smith: A distinction must be made between the two cases. Under this bill, income from the foreign affiliate which is of the general character of investment income becomes attributed automatically to the Canadian resident, whether or not it is distributed. Where it is active business income it is not attributed, but when it is paid out as dividends the foreign tax credit provisions in effect tax it to the extent that it has not borne tax abroad. It has to be raised to the level of the Canadian tax. That is the obstruction to the foreign sales subsidiary. It is that taxing it in Canada on the payment of the dividend to the extent that it has not been taxed abroad. Of course, there is not too much scope for just accumulating it abroad, because if there is no business in which to invest it it would have to be invested in portfolio investments, producing passive income which would be attributed.

The distinction is between an export subsidy arrangement and a taxing statute which ignores that and attempts to treat all Canadian resident taxpayers in the same way, regardless of the source of their income.

The Chairman: The net result of this may be that the so-called tax havens abroad, such as Nassau in the Bahamas and others where there is no income tax, which are looking for income, might very well now introduce income taxes because if the operation earns income there and pays taxes here, it will receive a credit.

The only difference is that if the tax imposed in the tax haven is lower than the Canadian rate, the credit will be only what is paid there. In those circumstances the income would be subjected to the excess, being the difference between the foreign rate and the Canadian rate.

Senator Desruisseaux: We would then be at a disadvantage with the American companies operating offshore.

The Chairman: This is your competitor in the foreign market. It certainly looks this year, according to the assessments which have been made, that some steps will be taken to increase the efficiency, operations and earning power of domestic companies operating entirely outside the United States. It is planned to assist them in their selling. The income derived from these operations will be subject to a lower rate of tax than will their domestic income. How are we to meet that competitively? One way would be to do likewise; another would be by way of an export subsidy, which is a long and involved process and may create problems in the foreign jurisdictions.

Senator Molson: Is there not also a complication with respect to GATT?

The Chairman: Yes.

Senator Molson: So that it enters other fields, so to speak?

Mr. Smith: Nothing need be done before the end of 1975. This transitional period, in essence, preserves the present treatment. Therefore nothing disastrous will happen in 1972 and there will be three years to see what happens to Canadian exports.

The Chairman: You know the difficulties in removing it once it is in the statute. This is the time to sound the alarm.

Mr. Smith: Mr. Scace reminds me that my remarks assume that the activities of the foreign sales company produce "active business income". Maybe there is room for debate as to whether they are in fact active business income.

Hon. Mr. Phillips: I would like to make one point to the senators: it is with respect to the section we handled on foreign source. We insisted that the department had authority under various sections of the Income Tax Act, which we quoted chapter and verse at page 75 of our report, to institute proceedings against offshore companies where the issue involved tax avoidance or tax minimization. We pointed out that we had heard of a number of companies who were obliged to form corporations in foreign jurisdictions because of the law of that particular country.

All these sections having been quoted, we believe that this committee has convinced at least the Department of National Revenue that it has the autority, because it has in fact instituted proceedings by way of assessment against a substantial number of Canadian companies which have offshore companies. The presumption is that the assessments would not have been issued without the support of the legal section that there was authority so to do, which is the very position that we took in our report in chapter 6 on taxing international income.

Mr. Smith: The whole field of foreign affiliates is very complex. Perhaps, by way of relief, I could turn to another topic and look at Canadian income of non-residents. There have been some minor changes in the definition of non-residents in the sense that there is an expansion of the deemed residence rule to include any corporation incorporated in Canada which becomes resident or carries on business in Canada at any time after 1971.

There is a big change in the income that is taxed to a non-resident in that certain capital gains are pulled into the tax base.

The key there is whether the taxable capital gains are in respect of what the act terms "taxable Canadian property". That is defined in section 115(1)(*b*). Basically it is real estate situate in Canada, capital property used in a business in Canada carried on by the non-resident, shares or interests in Canada private companies, shares in a public Canadian company if the non-resident, within a five-year period, owned 25 per cent of the shares in any class, an interest in certain Canadian partnerships, and an interest of 25 per cent in certain mutual fund trusts.

The big exception, obviously, is shares of public Canadian companies where there is less than 25 per cent interest in a class. The reason for that is one could not police it.

Obviously they have included in the tax base those kinds of property where they think they can make a capital gains tax on a non-resident stick.

I have already pointed out the change in the withholding tax rates. There are really two topics that are of greater importance than the others. One is the thin capitalization rule which I mentioned a little while ago, where the ratio of non-resident equity to debt exceeds one to three—that

is, the debt cannot be more than three times the equity. The equity is the capital plus the surplus that the non-resident has an interest in.

It is designed to prevent an artificial or unwarranted reduction in the income of the Canadian subsidiary of a foreign parent. It would be easy to capitalize your Canadian subsidiary so that no income is earned in Canada by that subsidiary, merely by putting in all of the capital required by way of debt, charging a high rate of interest on it, and hence wiping out the subsidiary's profit.

The thin capitalization rules are intended to obtain for Canada a fair share of the income generated by the subsidiary.

The other topic that I wish to mention is the non-resident-owned investment corporation. In the past they have been used largely by foreign investors who wished to have some presence in Canada and yet did not wish to pay a tax penalty for having some presence here.

For example, if a European manufacturer wishes to set up a joint venture in Canada to exploit some natural resource, it requires some debt capital. He could merely buy the bonds from a Canadian company and would suffer a 15 per cent withholding tax on interest payments to him.

The non-resident-owned investment corporation concept allows him to put those bonds in a Canadian company which is taxed at 15 per cent, the same as the withholding rate, and, when the dividend is paid out. to get the interest out of the Canadian NRO and back to his country. There is no further tax, no withholding tax, at that point.

The changes affecting the non-resident-owned investment corporation are contained in section 133. We should also look at section 59 of the transitional rules.

The rate for NROs will remain at 15 per cent until 1976. There is a minor change in the qualification. It used to be that 95 per cent of the shares had to be owned by non-residents. Now it will be 100 per cent. However, that is not really of any consequence.

One change is that in future, in order to comply, the NRO must always have been an NRO. Under the new system you will not be able to take an existing Canadian company and change it into an NRO merely by selling shares to a non-resident and having that company lapse. It must be incorporated and start out business by electing as an NRO. You can create an NRO if you amalgamate a group of companies, but only if each of the amalgamated companies is an NRO.

The big change is that the NRO will have to include in its income capital gains on taxable Canadian property. Those will be taxed initially at a rate of 25 per cent, with a refund when the money is paid out later as a dividend. However, only one half of the tax is refunded and the shareholder will pay withholding tax on the balance.

The changes are significant enough to have scared off many non-residents who own NROs. In our own practice many European investors having NROs have already made plans to move them out of the country. It is not so much the rules themselves, as the fact that they fear it is the first step to taxing them in full on their capital gains.

Portfolio investors worldwide who are investing not to control or exploit natural resources but merely to get a return on their money are easily stampeded, and that stampede seems to have started.

The Chairman: It does represent a loss of revenue to Canada.

Mr. Smith: I am not sure to what extent the changes may have been motivated by a feeling in some other countries that the NRO was an avenue for tax avoidance by, say, a UK or European resident. It may be that Canada felt that it had to cut down the advantage. But it does seem to be slightly less generous treatment and possibly enough to discourage the use of NROs by that kind of portfolio investor.

That is a very rough and brief treatment of some of the highlights of the treatment of non-resident Canadians with respect to their foreign companies.

Are there any questions on that?

Senator Lang: Mr. Smith, could you compare the treatment of non-residents by Canada with, say, the United Kingdom's treatment of non-residents and the United States' treatment of non-residents?

Mr. Smith: I believe the United States has treated non-residents less generously than we have for quite some time. I am not sure what the treatment is in the United Kingdom. I do not think the NRO concept, for example, is paralleled in other high tax jurisdictions. It has been a vehicle of convenience for foreign investors where Canada was not losing anything, but it enabled the foreign investor to exploit Canada's tax treaties in a way that perhaps the country in which he is ultimately investing may not have intended. Once you had an NRO in Canada then it was a Canadian taxpayer and entitled to the benefit of our treaties. It did not hurt us but it may have been resented by some of our trading partners.

The Chairman: Foreign investment in Canada might not otherwise have come in. It did attract substantial foreign investments in Canada.

Senator Lang: Does the United Kingdom or the United States attempt to tax Canadians on capital gains made in their respective countries?

Mr. Smith: All these provisions are subject to treaties, but in the case of an NRO . . .

Senator Lang: Apart from NROs altogether, it seems to me to be a highly artificial operation to attempt to tax capital gains on a non-resident person. Is there reciprocal legislation in the United States?

Mr. Smith: Most of our treaties contain a provision that capital gains will only be taxed in the country in which the taxpayer is resident. For example, the Canada-United States tax treaty states that it is the right of the United States to tax a United States taxpayer who is earning capital gains in Canada, and, similarly, a Canadian taxpayer earning capital gains in the United States pays his tax in Canada.

Taxing a resident of the United States on his Canadian property is required in this bill, so it would require an

amendment to that treaty. I cannot imagine why the United States would agree to such an amendment, but that may not be what the Government is concerned about. They may be trying to tax the non-resident who is sitting off in a tax haven some place.

The Chairman: Before we adjourn I would like to put a reference on the record. We deal with this question in our report. You will find it at page 60, paragraph 16. I will not read it because I presume that every senator is familiar with it.

The only subject matter we have not dealt with is the resource industries. I think that is something which we can postpone consideration on until we get closer to the date when there will be some submissions.

Senator Burchill: Or until we get the amendments.

The Chairman: We do not know what the amendments may be. I do not feel that the amendments in relation to the mining industry will vary the thrust of the bill to any extent. I think the aspects that the mining companies operating internationally are concerned with are the ones having to do with the earnings that they make there and how they will be treated if they bring them home. I know that is the thrust of Alcan who are coming in towards the end of October. Their main concern is the impact on their income available in Canada after the taxation bite under this bill has taken place; that is a substantial matter for them. The Massey-Ferguson Company will also be making submissions and I am satisfied that that will be the thrust of their submissions. These companies are faced with a situation where they may, in many of these foreign jurisdictions, have companies that are national, so it hardly relates to the business of deliberately setting up a business for certain tax purposes.

I would like to express our appreciation to both Mr. Scace and Mr. Smith for what they have done.

Hon. Senators: Hear, hear.

The Chairman: We have sittings for next Wednesday and Thursday. On Wednesday of next week we will have the Canadian Federation of Agriculture and the Canadian Construction Association. On Thursday of next week we will have the National Association of Canadian Credit Unions, the Co-operative Union of Canada and the All State Insurance Company of Canada.

We may increase the number for next Wednesday because we have only two down. When we dealt with the White Paper we were able to do six and sometimes eight in a day; we ran from 9 o'clock until 5 or 5:30. I see no reason yet for sitting at 9 o'clock—but, we may!

Senator Cook: A number of them will have points that are repetitions, will they not?

The Chairman: Yes. What I find is that if you have the other people sitting here during the submissions by the first people, then, they will find that most of the points in their representations are covered in the earlier ones and, as a result, they do not take very long with their submissions.

We are preparing studies. We still have not given up hope that we will get the proposed amendments earlier than having to wait until the section-by-section consideration in the committee of the whole. If we do not receive them in good time it may imperil the coming into force date of the bill. We are not going to be stampeded into dealing with a tremendous number of things that are dumped in our laps. If we do not get them in advance the purpose of setting up this committee at this time will have been defeated. The purpose of having the committee sit at this time was to expedite the consideration, so that we could meet the effective date of the bill. I believe the committee's feeling is that it is not going to be stampeded into rushing through a bill such as this.

Senator Cook: I agree. In any event, they will make it retroactive.

The Chairman: We will now adjourn until next Wednesday morning at 9.30.

The committee adjourned.

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THIRD SESSION—TWENTY-EIGHTH PARLIAMENT

1970-71

THE SENATE OF CANADA

PROCEEDINGS

OF THE

STANDING SENATE COMMITTEE ON

Banking, Trade and Commerce

The Honourable SALTER A. HAYDEN, *Chairman*

No. 40

WEDNESDAY, OCTOBER 13, 1971

Fourth Proceedings on:

"Summary of 1971 Tax Reform Legislation"

(Witnesses:—See Minutes of Proceedings)

THE STANDING SENATE COMMITTEE ON BANKING, TRADE AND COMMERCE

The Honourable Salter A. Hayden, *Chairman*

The Honourable Senators,

Aird	Grosart
Beaubien	Haig
Benidickson	Hayden
Blois	Hays
Burchill	Isnor
Carter	Lang
Choquette	Macnaughton
Connolly (*Ottawa West*)	Molson
Cook	Smith
Croll	Sullivan
Desruisseaux	Walker
Everett	Welch
Gélinas	White
Giguère	Willis—(28)

Ex officio members: Flynn and Martin

(Quorum 7)

Order of Reference

Extract from the Minutes of the Proceedings of the Senate, September 14, 1971:

"With leave of the Senate,

The Honourable Senator Hayden moved, seconded by the Honourable Senator Denis, P.C.:

That the Standing Senate Committee on Banking, Trade and Commerce be authorized to examine and consider the Summary of 1971 Tax Reform Legislation, tabled this day, and any bills based on the Budget Resolutions in advance of the said bills coming before the Senate, and any other matters relating thereto; and

That the Committee have power to engage the services of such counsel, staff and technical advisers as many be necessary for the purpose of the said examination.

After debate, and—

The question being put on the motion, it was—

Resolved in the affirmative."

Robert Fortier,
Clerk of the Senate.

24262—1½

Minutes of Proceedings

Wednesday, October 13, 1971
(47)

Pursuant to adjournment and notice the Standing Senate Committee on Banking, Trade and Commerce met this day at 9.30 a.m. to further consider:

"Summary of 1971 Tax Reform Legislation"

Present: The Honourable Senators Hayden (*Chairman*), Beaubien, Benidickson, Blois, Burchill, Carter, Connolly (*Ottawa West*), Cook, Desruisseaux, Flynn, Haig, Isnor, Lang, Macnaughton, Molson, Walker and Welch. (17)

In attendance: The Honourable Lazarus Phillips, Chief Counsel; Mr. C. Albert Poissant, C.A., Tax Consultent.

WITNESSES:

Canadian Federation of Agriculture:

Mr. Charles Munro, President.
Mr. David Kirk, Executive Secretary.

At 11.40 a.m. the witnesses were excused and the Committee proceeded to the consideration of Returns, Assessments and Appeals, as prepared by Mr. Poissant.

At 12.15 p.m. the Committee adjourned.

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(48)

At 2.15 p.m. the Committee resumed.

Present: The Honourable Senators Hayden (*Chairman*), Beaubien, Blois, Burchill, Carter, Connolly (*Ottawa West*), Cook, Croll, Desruisseaux, Haig, Isnor, Lang, Macnaughton, Molson and Welch. (15)

In attendance: The Honourable Lazarus Phillips, Chief Counsel; Mr. C. Albert Poissant, C.A., Tax Consultant.

WITNESSES:

Canadian Construction Association:

Mr. Robert C. T. Stewart, P. Eng., President,
and President, Cameron Contracting Limited.
Mr. S. D. C. Chutter, General Manager.
Mr. K. V. Sandford, Taxation Officer.

At 3.40 p.m. the Committee adjourned until Thursday, October 14, 1971, at 9.30 a.m.

ATTEST:

Frank A. Jackson,
Clerk of the Committee.

The Standing Senate Committee on Banking, Trade and Commerce

Evidence

Ottawa, Wednesday, October 13, 1971

The Standing Senate Committee on Banking, Trade and Commerce met this day at 9.30 a.m. to give consideration to the Summary of 1971 Tax Reform Legislation, and any bills based on the Budget Resolutions in advance of the said bills coming before the Senate, and any other matters relating thereto.

Hon. Salter A. Hayden (*Chairman*) in the Chair.

The Chairman: Honourable senators, our program for today is as follows: we shall hear the Canadian Federation of Agriculture this morning, and if there is any time left over, Mr. Poissant is going to make a short presentation on some points. Then this afternoon at 2.15 we shall hear from the Canadian Construction Association.

We have with us, representing the Canadian Federation of Agriculture: Mr. Charles Munro, President; and Mr. David Kirk, Executive Secretary.

Mr. Charles Munro, President, Canadian Federation of Agriculture: Mr. Chairman and honourable senators, the Canadian Federation of Agriculture has been concerned on a number of points in the tax reform proposals as proposed by the Minister of Finance, although in general terms we found many of his proposals acceptable. However, in reviewing the legislation we did make a final submission to the minister on August 30, and I assume that you have received copies of the submission that we made. I do not know whether you desire us to read that submission or not.

The Chairman: Well, it is not very long and I think you will want to be sure of covering all the points raised, so perhaps it would be better for you to read it.

Mr. Munro: The only other alternative would be to take the brief and go through it point by point. I would accept your judgment on the matter, but certainly, when dealing with a document as massive as the tax legislation I do not think that we can really summarize it adequately, and in fact I think it is summarized fairly precisely in the document.

This submission consists of three parts, the first one dealing with farm business taxation.

May we make the following representations for changes or clarification in the tax proposals as contained in Bill C-259:

The Family Farm Corporation. One general point we would like to make is that all provisions applicable to farmers as individuals should in principle be applicable to family-held farming corporations. We suggest there be some general provision in the law providing for this. This requires definition of what a family farm corporation is. We would suggest perhaps that 80 per cent of all shares require to be held by members of the family, and 80 per cent of the income to the corporation be from the farming operation. This can be important in many connections.

Transfer of a Farm within a Family, whether by Sale or Inheritance, without Realization of Capital Gains. There is, as we understand it, absolutely no provision for farms to be transferred within a family, except to a spouse, whether by sale or inheritance, without immediate realization of capital gains. This would be true of the sale or transfer of a farm to a son, or inheritance by the son of the farmer. We have been informed that this problem can be avoided in many cases by good estate planning through incorporation of the farm, and this may well be so. Even in such a case the death of the son, the holder of common shares in an incorporation, prior to that of the father, could result in realization of taxable capital gains while the father was still in active charge of the running of the farm, creating severe financial problems.

Senator Beaubien: Mr. Chairman, may I ask a question of the witness?

The Chairman: Certainly.

Senator Beaubien: Mr. Munro, why would a man who owns a farm and desires to turn it over to his son not have to pay tax, while the man who owns a small business and turns it over to his son or desires to leave it to his family would? What is the difference here? Surely, if you own a business and want to leave it to your son, that is a good idea. Why would one get off tax free in this situation and the other person have to pay tax?

Mr. Munro: We are not suggesting that.

Senator Beaubien: You are suggesting there would be no capital gains, or no tax if it is turned over to his son.

Mr. David Kirk, Secretary, Canadian Federation of Agriculture: The incorporation arrangements we are referring to, as we understand it, are available in any situation for general incorporation. These are not special farm provisions. These are forms of incorporation, as I understand the general principle, where the owner of the farm, or the owner of the small business can incorporate that business, and the owner of the farm or of the small corporation would, in fact, take his equity in the form of voting preference shares. The capital gain would accrue to the common shares which would be held by the son. In that way, when the father disposes of his assets, there would be no capital gain on those assets. We are informed that this is common practice in business; and we are not referring to special farm provisions.

Senator Beaubien: Is there a provision where you can turn over the shares of your business to your son without any tax?

The Chairman: Mr. Poissant.

Mr. C. Albert Poissant, Tax Consultant to the Committee: Are you suggesting that if a farm was held by the family farm corporation it would not attract tax? The shares given to the son at the time of the death of the father would attract capital gains tax, as Senator Beaubien has suggested, and the shares that were given to the son, in the place of the farm or in the place of the grocery store, do attract tax.

Mr. Kirk: I am not a corporation tax expert, but the information that we received from a very competent gentleman whom we consulted with and who has been involved in estate planning for farms and other businesses is that if a farmer or a grocery store owner owns a business and he wants his son to go into business with him, he can incorporate that business and he can issue shares which the son would hold which, initially, would have little or no value because he would have issued the full equity value in that business and that will be represented by fixed value preference shares which would also be voting shares. Therefore, the equity holding of the farmer or the businessman would, in fact, not appreciate in value because they are fixed value shares and the capital gains will not be realized until, of course, the common shares are sold. I am not sure how this would work at the time the son would wish to hand it down to his son. I am informed that it can be done, but I do not know how.

Senator Beaubien: Mr. Chairman, may I ask Mr. Poissant if there is anything that would prohibit a farmer incorporating, just as a small businessman can incorporate?

Mr. Kirk: There are possible disadvantages in the farming corporation. One disadvantage is that it is a complicated and difficult procedure with obligations that many farmers do not want to undertake. They do not want to run a corporation. The second point is the problem that can be created even if you have incorporation in terms of the capital gains tax prior to the death of the father; and the third problem, of course, is that the equity of the father is, in fact, fixed. This limits, under certain conditions, obviously, the retirement position of the father.

Senator Connolly: How does the father's interest become fixed? Is he taking a debt security?

Mr. Kirk: He takes preferred shares.

Senator Connolly: Well, they could vary.

Mr. Poissant: They would not normally vary unless they are redeemable at a premium. In this case, the common shares would vary, but very little, because the bulk of the assets transferred to the corporation were given by way of preferred shares to the father. It is true in such a case that at the time of death of the father there would be no realization because the common shares are held by the son.

Senator Connolly: They are held by the son.

Mr. Poissant: Yes.

Senator Cook: Mr. Chairman, is this the point that Senator Beaubien is making, that in the case of the small businessman who, in fact, does carry out this procedure and does take the preference shares and gives the common shares to his son, and in the other case where you have the farmer who does exactly the same thing, he incorporates the farm and takes the preference shares and gives the common shares to his son—are you suggesting that in both cases if the son should die before the father, that is the son of the small businessman or the son of the farmer, there should be any difference in the treatment of the two sons respectively?

Senator Beaubien: I wonder if there is any difference.

Mr. Kirk: When we said there was no difference, we meant that this incorporation provision is a generally prevailing position. Our position is that a transfer, without incorporation, without realization of capital gains, in a family should be permitted. That has been our position throughout. We feel that it should be permitted in the case of farms for reasons which we feel are sound for the maintenance of the family farm. If a case can be made for a small grocery store owner, fine. We are making a case for the farms.

The Chairman: Let us assume that the father decides that he is going to incorporate and he turns his farming assets into this company and takes the preferred shares. Let us also assume that the son buys the common shares. At that time, I would assume the farming assets would go into the company at their fair market value. The equity would be represented by the common shares; but the equity is something that would have to develop at that stage. There would have to be incremental increases. But at the moment, I would say, the value of the common shares that the son would buy and own outright would be very nominal. The son would really be getting in on the ground floor of the operation, if there is any increase in value. As the father's shares are redeemed, of course, there would be more opportunity for that value to develop.

Senator Connolly: I think that this is a wonderful example. Would you follow it right through? In the event that the preferred shares are redeemed, and thereby increase the value of the common shares, until the preferred shares have been completely redeemed—what does the witness have to say in regard to this situation?

The Chairman: The son owns and controls the company?

Senator Connolly: Yes, but I am thinking of the capital gains.

Mr. Kirk: No, the son would simply have to find the money to buy these shares or receive them as a gift. I am talking about the preferred shares. There would be no capital gain on the preferred shares.

Senator Connolly: No, I would like to stick to the Chairman's example. The preferred shares have now been redeemed and the common shares are owned by the son. In other words, he owns the farm and the company. What is the capital gains situation which the son would face regarding those shares?

The Chairman: On disposal?

Senator Connolly: Yes, that is what we are concerned about.

Mr. Kirk: That is right. No, we are not concerned about the avoidance of the payment of capital gains tax should the farm go outside of the family. We are not concerned about the permanent avoidance of the capital gains tax. We are concerned about the realization of capital gains during the operation of the farm while it is within the family and the maintaining of the farming business as an on-going business without being completely disrupted by this transaction.

Mr. Munro: And the maintaining of farming as an on-going business, without being completely disrupted in the transaction.

Senator Cook: Capital gains on death?

Mr. Munro: No, capital gains on the business passed out of the family into other hands.

Senator Cook: You are not objecting to that?

Mr. Munro: No.

Senator Cook: You are objecting to capital gains on death in the family?

Mr. Munro: Yes, we want a deferral.

Senator Connolly: After the shares are regained, the son is in the same position as was his father when he incorporated. Therefore, in fact, he owns the farm. Do you want to carry it another generation and issue preferred shares to him?

Mr. Munro: I am personally a major shareholder in an incorporated farm. I understand from my legal counsel that this can go on for generations if the family wishes to continue farming.

Senator Connolly: The company can continue; it has an indefinite life. What is the situation when the preferred shares have all been paid off and the farmer, who now owns all the common shares, wishes his son to take over? The grandson would then be involved.

Senator Cook: He just sells to another company.

Senator Connolly: That is precisely what I wish to hear from the witnesses; another company must be incorporated which would repeat the exercise originated by the farmer.

Senator Beaubien: Is a farmer now in any way at a comparative disadvantage to a grocer if he incorporates?

Mr. Munro: No; not as against the grocer.

Senator Beaubien: Then you are against this new tax; do you think the farmer should have a special deal?

Mr. Munro: We have not adked for a special deal; we have only asked that Canadian farmers can retain the equity, for the various reasons set out in this brief. We ask that they be allowed to continue, not that they should have any different position from that of a grocer. We are arguing our position and have not taken up the cry on behalf of the grocer; we think he should look after himself.

Senator Cook: Can you advance any reasons why your position is different, or should receive consideration over that given the small family business? I just wish to be helpful. You say that the small family business can look after itself, which is true enough; I am not asking you to argue their case. However, what is the philosophy behind the contention that you in fact should escape and they possibly pay, as the situation now prevails?

Mr. Kirk: There are two aspects: the philosophy, about which farmers feel rather strongly is, first of all that there is a very strong case on social in addition to economic grounds for making it possible for families to continue farming their land. We do not make any apologies for that case.

The second point is that with the typically low returns and very high rate of technological development involving continually increasing capital requirements it can be extremely disruptive to the farm business if capital gains must be realized by the family and withdrawn from the farm. It means that they must dispose of farm assets or incur a large debt load.

Were a similar type of case to be made in a city context we consider it would be the responsibility of those involved to make the case. We make it on grounds of the nature of farming and the desirability, socially in addition to economically, of a stable farming structure. This structure is unstable enough as it is and we do not wish to increase its present instability.

Senator Cook: Capital gains tax is not much of a hardship in cases of farms and farm equipment which do not increase much in value, because there is little on which to pay the tax. However, what is your solution to the situation in which a farm passes from father to son and becomes more and more valuable, with more and more equipment? The son may become a millionaire several times over by reason of the increased value of the land and equipment and yet pay no capital gains tax.

Mr. Kirk: He cannot realize that million dollars without paying capital gains on it; that is definite.

Senator Cook: That is true, yes.

Mr. Kirk: The other reply is that exceedingly few people arrive in that position.

Senator Connolly: As I understand the witnesses, they say that there is more to the problem of a family farm than economics. Their argument is that in addition to tax considerations there is the social aspect of the maintenance of the family farm, as opposed to the maintenance of the family business referred to by Senator Beaubien. They state that it is more desirable to maintain a family farm and for social reasons, therefore, the rules for the family farm should not be the same as those for the family business. Is that a reasonable summary of your position?

Mr. Poissant: The point made by the witnesses is really that the incorporated farm presents no problem. At the top of page 2 of their brief it is stated that if by any chance the son were to die before the father, then to a certain extent there is a return to the father and there should be no deemed realization in that case.

The other point flows through normally, because it has already been given some time previously by way of the

common shares. However, it would return to the father if the son were to die first. The witnesses are really asking that the flow back be free of capital gain, which is something new. The first part was solved through the incorporation but now they ask that what was done 10 or five years previously be undone and the farm flow back to the farmer, if he is still active on it, free of deemed realization.

Mr. Kirk: That is part of our request. We also say, in the remainder of page 2 of the brief, that we indeed think that the principle of deferring deemed realization as long as the farm remains in the family should be followed even if there is no incorporation. There will be farmers who simply do not wish, or neglect to incorporate.

The Chairman: We are talking about two things. One is incorporation, what flows from that, and what they would like to have happen there; and then, as I understand it, they are also talking about the situation, "Well, if we do not want or do not like to incorporate, we should have these benefits as individuals." If the benefits are available to the same extent that they are to anybody else if you incorporate a farm, then that is one situation.

What Mr. Kirk seems to be concerned about is that the son may hold the common shares and the father, who has turned the assets into a limited company, may hold the preferred shares. If the son dies, the common shares will represent the ownership of the farm. But the father, if there is any quantity of preference shares still outstanding, has a pretty strong toehold in relation to his financial interest in the farm.

It is felt that if the son dies first, those common shares should be able to go back to the father without attracting any deemed realization.

Unless a lot of the preferred shares have been redeemed, I doubt if in most cases there would be any substantial value attached to the common shares at that time.

They may represent the equity, but equity is a variable thing. It depends what you can get for it after you pay off the preferred shares.

It is hard to make a ruling of that kind, because you are really granting an exemption from capital gains tax.

I am not saying that it is not possible to do so. Parliament can write the law in any way it wishes, but it has to have good grounds for doing so.

Mr. Kirk suggests that the farm is a kind of entity and is an asset in a way that has value to the country more than simply the value of the piece of property. Keeping people on the farms and keeping farms operating leads to a healthy community.

Senator Connolly: And social conditions.

The Chairman: Yes, and social conditions would urge it. Senators may recall that we made a recommendation in our report on the White Paper. On page 59, paragraph 7 we said:

> Your Committee recommends exemption from capital gains tax to the extent of the first $75,000 of aggregate net lifetime gains derived from the sale or exchange by an individual or his spouse (or by a corporation where such individual or spouse, because of statutory provisions, is obliged to operate through corporate ownership) of farms and orchards where the principal occupation of the transferor is farming.

We said you can make lifetime gains up to $75,000 without attracting capital gains tax.

This is a different concept. Firstly, you do not want any limitation. You want the son to have an unqualified right, if he dies, to have the ownership of the farm turned back to the father.

However, that interjects other problems. The son may be married and have a family. If the son makes a will in which he disposes of the property in the interests of his family, we are wasting time here saying that we should give the son the right to turn the property back to the father without attracting capital gains tax.

The son is the only one who can say that.

The Honourable Lazarus Phillips (Chief Counsel to the Committee): Mr. Chairman, generally speaking, the committee took the position that small-type farming was entitled to special consideration.

I personally still hold that view. Those speaking on behalf of the Federation would make a much better case if they took the simple position, without confusing it with corporate structures as against individuals, that so long as a small farm operation—and the definition of a small farm operation would have to be made—were transferred within the family, no matter which blood member of the family, and the operation of the transferred unit was for farming purposes generally, there should be exemptions in respect of the application of the capital gains tax until its disposition outside the family or its transfer.

The Chairman: That would be a deferral.

Hon. Mr. Phillips: Yes. If I may be permitted to express an opinion other than being counsel—

Senator Flynn: How far would you go in relation to the family?

Hon. Mr. Phillips: I would go to direct blood descendants.

Senator Flynn: Or back?

Hon. Mr. Phillips: Yes, or even upstream as distinguished from downstream. I disagree with the simple statement that a small agricultural unit is a special unit related to the vital operation of our system. With respect to Senator Beaubien, I do not agree with his analogy of a small business in relation to a farm. There is a market for a commercial unit, even a small business unit, or the liquidation of an inventory which is liquid or accounts receivable. The circumstances are entirely different.

There is no market for a farm in Saskatchewan in a section of a drought area in terms of some years. I may be speaking out of my depth, because I have no status other than that of a lawyer.

I remind the committee that in our Senate report on the White Paper we accepted the principle that a distinction had to be drawn between persons engaged bona fide in farming and those engaged in commerce.

Regarding the simple principles of postponement, or, as our chairman said, deferral of capital gains, when there is a transfer of a small-type farm within a family, up or down—the reference was made to upstream as well as downstream—as long as it is so used, the capital gains tax should be deferred. That would strike a more responsive chord than the complicated submission we have had thus far.

Senator Cook: And it would cost very little in terms of tax.

Hon. Mr. Phillips: Yes, it would cost very little indeed.

Senator Beaubien: In the case of a small farm, a small operation, what kind of a capital gains tax would we have on an operation where there is no market?

Hon. Mr. Phillips: That is all the more reason for a deferral.

Senator Beaubien: But I do not think that is what the submission refers to.

The Chairman: Well, let us find out. Mr. Munro, you have heard the discussion. Is the presentation that you are making being made on behalf of what we call the small farmer, or is it for farmers generally; that if a farmer has a windfall and his property becomes valuable, he should be able to realize its creation into a real estate subdivision and make a profit, non-taxable as to capital gains?

Mr. Kirk: That is not our submission.

The Chairman: Tell us your viewpoint in relation to our discussion here of small farm businesses.

Mr. Kirk: In the first place, we are not distinguishing between small farms and large farms; that is the first point. However, the first paragraph of our brief notes that it would be useful to define a family farm corporation; this means that it essentially has to be family held and the profits have to be essentially from the farm operation.

I should emphasize, first of all, that we are not asking for exemption from taxes; we are asking for a deferral of taxes. I think that is quite important.

Senator Cook: For how long a period?

The Chairman: You mean until the farm ceases to be a farming operation?

Mr. Kirk: Yes, until it ceases to be a farming operation.

Except for that one point with respect to the son dying first, we are not asking for special recommendations for farmers on an incorporated basis. We just referred to this because we thought it would be in the thinking of you gentlemen and also in the thinking of the Government. We thought it would be in the picture that this option is in fact open; it is open now under the present law and it would be open under the new law to any corporation. What we are asking for is that, incorporated or not, a family farm not have realization for capital gains until it ceases to be a family farm and the assets are sold off. If it is sold for a subdivision, then capital gains are immediately realized under our recommendations. It is not a question of avoiding taxes or exemption from taxes; it is a question of not realizing the capital gain on that land as long as it continues as an integral operating farming unit, because otherwise you would either have to sell off part of it in order to pay the capital gains tax or undertake a debt in order to pay the capital gains tax. That is our point.

Senator Flynn: How does the provision concerning principal residence affect farms? There is no provision specifically designed to cover farms. You would have to use the provision concerning the exemption for principal residence.

Mr. Kirk: We discuss this in some detail later on in the brief.

The Chairman: It is referred to on page 3 of the brief. You are thinking of the fact that the farmer can make an election under section 40(2)(*c*).

The small farmer would benefit by this election whereby he can deduct $1,000 a year for each year that he has occupied the principal residence on the farm, can he not? If he spent a life time there he would be deducting quite a few $1,000, would he not?

Mr. Kirk: Yes, indeed, and we value that provision a great deal.

Senator Flynn: Is the definition of principal residence applicable to the whole farm, or is it only applicable to the main residence and one acre around the main residence?

The Chairman: Yes.

Senator Flynn: They could not benefit, then, by this deduction of $1,000 a year. If it is a farm, they could not deduct $1,000 from the increased value of the land because it only applies to the one acre around the main residence.

The Chairman: Section 40(2)(*c*) states:

> where the taxpayer is an individual, his gain for a taxation year from the disposition of land used in a farming business carried on by him that includes property that was at any time his principal residence is
>
> (i) His gain for the year, otherwise determined, from the disposition of the portion of the land that does not include the property that was his principal residence, plus his gain for the year, if any, determined under paragraph (*b*) from the disposition of the property that was his principal residence, or

Senator Flynn: This means, then, that the provision respecting principal residence would be applicable to the whole farm.

The Chairman: That is right. Section 40(2)(*c*)(ii) states:

> If the taxpayer so elects in prescribed manner in respect of the land, his gain for the year from the disposition of the land including the property that was his principal residence, determined without regard to paragraph (*b*) or subparagraph (i) of this paragraph, minus $1,000 for each year for which the residence was his principal residence and during which he was resident in Canada;

Senator Burchill: Without defining a small farm, Mr. Munro, how many small farms would be incorporated? What size farm ordinarily would be incorporated?

Mr. Munro: That would be difficult to quantify, but I would suggest that there must be a sizeable business within the farm in order to go to the expense of incorporation and the ensuing expense year by year of maintaining books that meet the requirements of the laws of the land. I am not familiar with the provincial laws in other provinces, but certainlyy here in Ontario a farmer would have two sets of laws pursuant to which he would be required to submit his books, and these books have to be kept in a prescribed manner. It does become an expensive operation to incorporate, and it also adds another dimension to the farming operation, and that is the bookkeeping aspect. Generally speaking, farmers in this country—and this is a fact; it is not a criticism or an excuse or anything else—have had little training in bookkeeping, and if you are going to maintain an incorporated farm you have to keep proper books. This means that people either have to be employed to maintain those books or the farmer has to find that type of person within his own organization.

A small farm means different things to different people, but, relatively speaking, if it is a one-man operation or even a father and son operation, in some instances, they will not have the desire nor the amount of money available to go to the extra expense of incorporating. It is expensive to set up an incorporated farm.

Senator Burchill: So when we talk about small farms and incorporated farms we are talking about two different things?

The Chairman: Yes, and with all due respect to Mr. Munro, I think this presentation is intended to be weighted on the side of the individual and not on the side of the corporate farm.

Mr. Munro: That is right.

The Chairman: So we should look at it as the individual. Some of these benefits in the bill are benefits to the individual who is carrying on a farming operation.

Mr. Munro: The major portion of our concern lies with the individual. Incorporated farms in Canada are quite few in number and we suggest will remain that way for some considerable time to come.

Senator Connolly: Is the principal residence deduction available to the farmer who incorporates?

Mr. Kirk: No, and that is one of our complaints.

Mr. Poissant: In other words, they would like this word "individual" to read as well "a family farm corporation" and to extend the same rules applicable—

Mr. Kirk: To a defined family farm operation.

Senator Connolly: Have you suggested any particular section to be changed? You do not have a draft of the amendments you propose, do you?

The Chairman: No, Senator Connolly, although with the information we now have as a result of our study it would not be difficult to determine, firstly, where the changes should be made, and, secondly, settle the language of the changes.

The question is what we wish to do in that regard. I do not think we can answer "yes" or "no". Our review in relation to the treatment of farms is expressed in our report on the White Paper, and I do not suppose that that view has changed. What we have to assess is whether the treatment that is accorded in the bill is fair in the circumstances.

Senator Cook: I was going to come back to what we said in our report, Mr. Chairman.

Assuming that you could not get total blanket exemption, Mr. Munro, what do you think of the $75,000 figure suggested by the Senate as a definition of a small farm which would be exempt? What figure do you suggest it should be? What do you think of $75,000?

Mr. Munro: It sounds interesting. We really have not quantified this within our organization or discussed it at all. I do not think we went in this direction in our discussion.

Senator Connolly: I wonder where we got the $75,000.

The Chairman: We had quite a lot of discussion here with some of the farming groups. There was some criticism because we limited the qualification to, as it were, the principal occupation of the transferor, his farming. We felt it had to be limited in that way.

Hon. Mr. Phillips: May I remind the members of the committee that we were bothered about how to define a small farming operation, so we came to the conclusion that we were better off by asking for an exemption of capital gains to the extent of the first $75,000 of aggregate net lifetime gains. Obviously, lifetime gains are related to an individual rather than a corporation, which clearly is another matter. We just did not seize ourselves of the problem of corporate structures in relation to farming operations. We came to the conclusion that rather than struggle with the definition of a small farming operation as to acreage, yield, moneys received and that sort of thing on an annual basis, or over a five-year or ten-year basis, the simplest approach would be to recommend the exemption from capital gains of a lifetime amount realized by an individual farmer up to $75,000. That is the history behind our recommendation, as I recollect it.

Mr. Kirk: I would observe that we realize you made that recommendation, and we appreciate it very much. We have to say frankly that this brief is drafted in the light of the tax bill; that is to say, we deliberately did not go back to square one; we attempted to make a recommendation that we thought was, as closely as we could make it, within the context of government thinking, on the grounds that you had made the recommendation, for example, and it was not accepted. We tried to make recommendations that we thought might meet with Mr. Benson's definition of "technical" in his offer for further representations; he said he would welcome further technical representations. These are not altogether technical, but we did try to be reasonable from the point of view of the practicabilities of government decision-making, rightly or wrongly.

The Chairman: It may be that what the Government is proposing in this bill is not too far away from what we

recommended. We recommended that there be an exemption for net lifetime gains derived from the sale or exchange of farming property of $75,000. In the bill, the net lifetime gain is limited by the number of years the farmer has used the residence on the farm as his principal residence. If he was there for a lifetime, maybe 40 or 50 years, in all he has accumulated a net lifetime gain of 40 or 50 times $1,000.

Senator Flynn: Plus the original value. Our $75,000 included the original value and the value at the time of the deemed realization, or the realization.

The Chairman: The difference between the two would be the gain.

Senator Flynn: But there was an exemption up to $75,000. To the $1,000 a year you have to add the original value. If at the time of valuation day a farm was worth $50,000, you can add $1,000 a year at the time of the transfer.

Senator Cook: It would be worth over $125,000 before liability.

Senator Flynn: I think the $75,000 was the total value.

The Chairman: No, net aggregate capital gain.

Senator Flynn: Gain?

The Chairman: Yes.

Senator Flynn: That goes much further.

The Chairman: The deduction of the $1,000 is $1,000 a year from the gain.

Senator Flynn: When the property is transferred to the wife, at present there is no estate tax, but would there be a deemed realization when a transfer is made under the new tax bill? Will the estate of the deceased have to pay a capital gains tax on deemed realization when there is a transfer to the wife?

Senator Connolly: You mean on the death of the husband?

Senator Flynn: Yes.

The Chairman: There is nothing I see that takes away from the right of either spouse to make a gift without deemed realization to the other.

Mr. Poissant: These are roll-overs between spouses.

Mr. Kirk: There is no realization on the inheritance by a wife.

Mr. Poissant: That is right, to the wife from the husband, or vice versa.

Senator Flynn: There is no estate tax.

Hon. Mr. Phillips: No deemed realization.

The Chairman: There is no taxable gain.

Mr. Poissant: No deemed realization.

Senator Flynn: Between husband and wife?

The Chairman: No, not in this bill.

Hon. Mr. Phillips: Roll-overs.

Senator Flynn: It follows the same principle as the estate tax?

Hon. Mr. Phillips: Yes.

The Chairman: I was making the point that the provisions in the bill recognize a principle of deduction in relation to gain; they arrive at it in a different way on this $1,000 a year of occupation of the residence as a principal residence. The net result does not produce as many dollars of exemption, because to produce $75,000 the taxpayer would have to have his principal residence on the farm for 75 years. It does go some distance, and I take it that you are certainly not looking a gift-horse in the mouth and saying, "No, we don't want it."

Mr. Kirk: No. Perhaps I might review some of the problems. There are a few problems with that $1,000. Would it be all right to just review those?

The Chairman: Yes, you go ahead.

Mr. Kirk: The first problem is that it does not apply to an incorporated farm. It should be pointed out that if the principal residence is in the incorporation, then the exemption for the residence, which everybody has, is not available to the farmer.

The Chairman: That every individual has.

Mr. Kirk: That every individual has. One would say that you should separate these in the incorporation, but in fact there are a good many provincial laws on land use that make it impossible to separate them in the incorporation, because they do not permit that. You have to keep that unit. They do this for purposes of land use planning. That is a definite disadvantage and it should be corrected, in our view.

The other point is that you get the $1,000 only in the years when you are in principal residence on the farm. For example, a farmer may be in a rather remote position in, say, Saskatchewan. As you know, the small towns are declining there and many farmers find it highly advantageous to buy, often very cheaply, a house in town, because then they can educate their children adequately, and they do not have the same type of isolation. But if he does that, he loses immediately the $1,000 a year. Or, if the son is working the farm and the father retires to the village, perhaps does some of the work but retains the ownership of the farm, then that $1,000 a year is lost for those years. We do not think that that is reasonable, that he has to be actually on the farm in all cases in that way.

Senator Flynn: He would be able to claim exemption from it, too, if you were to correct the situation as suggested, because the residence that he has bought in town will benefit by the exemption.

The Chairman: Under the general law.

Senator Flynn: Yes.

Mr. Kirk: He could not claim both, of course.

Senator Flynn: Then he would have to have an option between the two, in a case like that.

Mr. Kirk: The option is there, in any case, but often these alternate houses in the town are not going to appreciate very much. This is a convenience. The town is not a major centre and it is not going to be a growing centre, in most of these cases.

Senator Flynn: Is the farm more likely to be growing in value, as an asset?

Mr. Kirk: In many cases, in the Prairie Provinces, yes, it would be much more likely, because what we are getting is a surplus of houses.

Senator Flynn: Even if it remains a farm?

Mr. Kirk: Yes, even if it remains a farm.

The Chairman: Yes, it must be a farm used in the farming business.

Mr. Poissant: Mr. Chairman, it would apply now, if the father were in the town and the son were occupying the farm residence. They could both have a principal residence, under the proposed scheme, because the father has a house and the son has a house.

The Chairman: They both have to be owners.

Mr. Poissant: Yes, but it could happen, if they are owners.

Mr. Kirk: The son would have to be an owner.

Mr. Poissant: Except in the corporation.

Senator Flynn: We are worried about the son acquiring a house and dying before the father.

Senator Cook: You are also saying it is sometimes not possible to split the house and the farm, because of the law? Do you not say that?

Mr. Munro: Yes. This is a definite problem.

The Chairman: The principal residence does not necessarily mean that one lives there every day in the year.

Senator Flynn: It is question of fact.

The Chairman: It must be your home base.

Mr. Kirk: Essentially, what we are saying is that the farm should have the $1,000 a year exemption, or the option of principal residence. It is that simple. The residence requirement on the farm should not be so restricted.

Mr. Poissant: What you are asking here really is—and this prompted the question—that there be perpetual roll-overs, if a man can give the farm to his son, and his son to his son, and his son to his son, and there is never a capital gain in the case of the farmer. Furthermore, in the case of the corporation, where 80 per cent of the shares are held by the family and 80 per cent of the income is from farming, we would have to put additional restrictions to the effect that this family corporation should not have anything else—that is, because the shares could again be transferred ad infinitum, in your example here. If 20 per cent of the assets were something else, were shares in Bell Telephone, they would qualify as part of the family farm corporation under this definition.

Senator Flynn: That is what they are asking. I think they want the definition of the farm to apply to a farm that is owned by a corporation. Then this would be an asset of the corporation.

Mr. Poissant: Then the exclusive assets should only be farming, and we should define further that not only 80 per cent of the shares are held by them—

Senator Flynn: All the shares would be exempt.

The Chairman: This is what they are asking, that a family corporation would be a corporation where 80 per cent of the shares were held by the family and where 80 per cent of the income came from a farming operation.

Senator Flynn: It would open the door to abuses.

Mr. Poissant: Yes, unless you define it further, that no other assets but farming land, farm houses and farming equipment are allowed. It would be very restricted.

Senator Cook: And employed in farming.

Mr. Poissant: Yes, employed in farming, and nothing else, no investments. Otherwise this would be a fair and proper channel to get all the capital gains through by this type of corporation. One can see the complication that could arise.

The Chairman: I think we have given this fairly complete consideration. Can we move on to other points that you have?

Mr. Munro: Yes. I would ask Mr. Kirk to pick up the basic herd concept and deal with that.

Mr. Kirk: Yes. I will read this, if I may, as it is a fairly complicated subject. It is on page 4, item 4, basic herd.

In connection with the provisions for termination of a basic herd system as regards increases in basic herds established by 1971, and establishment of basic herds by further farmers after 1971, we feel strongly a serious error of policy is being made here. That is to say, there will be no expansion of basic herds after 1971 establishment now, and the law says there will be no additions to basic herds. Any farmer can establish a basic herd as of January 1, 1971. Then that herd is valued and on disposition of the herd, according to certain rules, the value of the dispositions is compared to the original value, and capital gains is charged on the difference. Presently it is a unit system and it makes no difference what you sell it for, compared to what you bought it for. One cow is one cow and there is no capital gain. We are not quarrelling with that change. We are not quarrelling with the change to actual valuation of the animals sold from the basic herd and charging a capital gain on the appreciation in value. We accept that. What we are quarrelling with is the termination of the basic herd system, and its freezing. We say:

The basic issue is this: there is a real, valid need to have some system by which the farmer can treat this capital investment in livestock as a capital investment. Consider, for example, the problem of the farmer who wishes to take money out of capital to acquire a herd or a major addition to an existing herd. From his standpoint, he now has a

capital asset which cannot be depreciated. His cost of acquisition of the cattle is an expense to him, if he is on a cash basis of accounting, giving him a number of years of severe losses that will not be corrected by the five-year averaging provision. To go on an accrual basis with annual valuation of the herd is often impractical and undesirable. A much better answer is to establish a basic herd.

The same consideration in a less extreme way applies to farmers who wish to build up their herd year by year, reporting the cost of acquisition as income—as they do now—and enlarging their capital base of animals.

If this is not provided for, the farmer builds up a large sum which will be realized as income immediately on dispersal of the herd.

Farming requires increasing capital investment. It has been Canadian public policy for more than two decades to assist farmers in obtaining the capital requisite for a viable farming operation that alone can satisfy the twin objectives of a decent income for the farmer and reasonably-priced food for the consumer. One effect of the basic herd has been to create capital in livestock operations without the necessity of outside money investment: i.e. an ongoing farm business on basic herd is able to show a balance sheet that includes part of the livestock as a capital asset, rather than entirely in inventory. The effect is that the financial strength of the operation is automatically increased. To phase out the basic herd will have the mischievous side effect of weakening the capital structures of thousands of farming operations without producing a significant gain in tax revenues.

We recognize that with the introduction of a capital gains tax the unit system, whereby proceeds from reduction in basic herd are treated as non-taxable, has less validity. However, the recognition of the basic herd as capital has validity, and there is no reason why proceeds of dispersal should not be assessed by treating the gain on disposal over initial cost on valuation day value as a capital gain rather than as ordinary income, and tax levied accordingly on only half of such gain.

The failure to treat this unique capital asset of the farmer, i.e. animals, as a real form of capital, subject to the same rules on taxation of capital gains is, in our view, discriminatory.

There is a special point which should be dealt with in connection with valuation of basic herd on valuation day. This is not of widespread application, but it could be important to some people.

Much valuable breeding stock will be, on valuation day, in fact under test. This applies for example to young bulls whose semen is being used by insemination stations. The breeding results alone will prove the real value of that animal. There should be provision for later determination of valuation day value based on the results of testing out of animals which is in process on valuation day.

In short, on valuation day you do not know what the animals are worth, because the tests are not in.

Senator Connolly: Just on that point, without seeing the specific wording of the section, I should think that the value does not necessarily have to be determined on valuation day. For a number of reasons it may have to be determined a long time after valuation day. For example, if I own a very valuable painting, I may not know precisely what its value is on valuation day, but, if I get in an expert to assess its value two months later, that is the value that will attach to the painting so far as valuation day is concerned. Would that not be true in connection with cattle?

Mr. Kirk: It might be dealt with by regulation, I suppose. On the other hand, if the department said that the value of a breeding animal is the average value as of that day and then it turns out that that is an exceptionally valuable animal, then they would say, no, that that is not it, it is the average value.

Hon. Mr. Phillips: Mr. Chairman, I think the point made with respect to a herd being a capital asset rather than being inventory is a pretty forceful argument. But the question of applying a special rule of determination of value other than valuation day opens up the door to the complete destruction of the whole concept of value and valuation date. Private investors might very well take the position that their inventory is securities. They might take the position that the value of the securities listed on the exchange may have a value greater than that of the "bid and ask" column, because certain discoveries, for example in the natural resources like mining and so on, have not yet been disclosed to the public by management.

In an effort to solve a minor problem which may have validity, you would destroy the whole concept of value on valuation day. I do not think there would be much chance either of that being accepted as a valid argument for all people, or that it would be accepted, even if valid. But with respect to the first point, if I may be permitted to make an observation, I think it has considerable validity.

The Chairman: Well, with respect to paintings, we know that it sometimes takes a considerable period of time before artists acquire such a standing that the value of their paintings goes up. Some entirely fortuitous event may bring about that rise in value. Therefore, the person who has a painting may object to valuation day as being the proper date for valuation because he does not know at that date the fortuitous circumstance which may alter the value of his painting, either by depreciating it or by increasing it. I do not know how you can shift from a date on which, whatever the conditions are, that is the value because that is the value in the marketplace at that date. If there are conditions that still have to be assessed which might affect the value, I do not know how you can give effect to those.

Senator Connolly: Mr. Chairman, with respect to the example of the security tradeable on the exchange, that security has a determinable value as of valuation day, but in the case of the painting, or in the case of the animal, although there is an intrinsic value on valuation day, that value may not be known. Perhaps the knowledge of what that value is on valuation day only comes to you later. In the case of the stock market you have something tangible. Is there not a difference there?

Mr. Poissant: I might say to Mr. Munro and Mr. Kirk, and, therefore, to their association or federation, that the Minister of National Revenue is now publishing approximately

15 pamphlets, one of which will be concerned with valuation day problems. Perhaps I could recommend to them that they should ask for this particular paragraph of their brief to be inserted in that pamphlet, dealing with this problem that the farmers would have, and then there could be a corresponding set of recommendations with respect to the valuation that could be taken into account in this very particular case. I am sure that, although the booklets are in the process of being printed, there would still be time for such an insertion to be made.

Senator Connolly: Mr. Chairman, perhaps through our staff we could ask the tax department to issue a ruling on this and we could cite what was given to us.

The Chairman: In other words, in the valuation of an article you would make a distinction between the article, the value of which is either black or white, and the article in this case, where there are factors preventing you from getting at the basic value until you know about the product or whatever the article might be. It still presents quite a problem.

Senator Connolly: The determining factors not turning up until later is really the problem. Perhaps if we write to the tax department and inform them of this situation they could put out a bulletin that would cover this one issue. That might clear up the problem.

Mr. Kirk: What we are really talking about here is not acquisitions of animals. We are talking about animals that have been bred by farmers, where the results of the farmers' efforts are simply not known. That is all we are talking about. We are not talking about speculative acquisitions.

Senator Cook: There is a paragraph on page 4 which I do not understand:

> The same consideration in a less extreme way applies to farmers who wish to build up their herd year by year, reporting the cost of acquisition as income and enlarging their capital base of animals.

How do they report the cost of acquisition as income? They pay for it. What does that mean?

Mr. Kirk: We are saying that we wish they would be able to do so. But what you have to do now, and as we are recommending for the future, is, if you add an animal to your basic herd, you have to put into income the cost of that animal.

Senator Cook: You mean you pay for it yourself and you put it into your income?

Mr. Kirk: If you are on a cash basis of accounting, then the way it works, generally, is that your expenses are what you pay out and your income is what you take in. And in that process you might pay out the cost, in fact, of raising an animal which you did not sell.

Senator Connolly: Let us say, for example, that you paid $100 for a calf—

Mr. Kirk: And if you kept that calf—

Senator Cook: Let us stick to the $100 first. You mean that you report that $100 as income?

Mr. Kirk: No.

Senator Cook: Well, this is what it says here.

Mr. Kirk: Well, if you had a capital gain as we are recommending, then when you total your year's operation on a cash basis—so much outgo and so much income—you would have a certain income. But if you wanted to take one of the animals you had in your herd and add that animal to your basic herd, then you would have to add the value of that animal to your income, because you would be transferring it to capital in that year. That is what a farmer with a basic herd does now.

Senator Connolly: He is allowed a deduction for capital investment.

Mr. Kirk: No, he has to put the value in as income if he puts the animal in as basic herd.

The Chairman: But then it is on a cash basis. In dollars or the equivalent of dollars, the inventory has a value, and that comes into his assessment of income at that value, but he has a deduction for his expenses on the other side.

Senator Cook: It does not change his expense picture; it only changes his income picture.

The Chairman: Are there any other questions on this business of basic herd? You say that this concept of a basic herd certainly existed in our income tax law for a number of years. Do you say that there are definite advantages to the farmer in that system and that the changes in the law as proposed do not compensate for that benefit?

Mr. Kirk: Well, I do not know about the compensation, but what we are saying is that the capability of building up a capital asset in livestock is eliminated. That means that if you build up a herd, the day you sell it, it comes into income in that year. It is much better to have brought it into income gradually over the years, and the basic herd makes it possible to do that as you build up your herd.

Mr. Munro: With this exception, Mr. Chairman. In order to establish a herd of an ongoing nature that is of any use to you, and you have $10,000 to invest, then you must invest it in one year because you cannot set up a business on a very gradual basis under present systems today. Then you have a $10,000 expenditure, whereas we could put the $10,000 under the system we have as capital, and then in 15 years' time if the equity—only using figures—is then increased to $15,000 in that herd, it also shows as income in that year. But under present conditions he would still have his original $10,000 of capital being considered as $10,000 of capital under the system which we had before.

Senator Cook: But we have that now, surely.

Mr. Munro: Yes, we have it now.

Senator Cook: And we have it in the bill. Will you not have it under the amendment? I mean if you take $10,000 and you invest it in a herd, will you not still have it?

Mr. Munro: No, this is what we are complaining about. We cannot do that any more, and for five years we are going to have a very serious loss position which we cannot recoup under averaging.

Senator Connolly: You say it is to be phased out at December 31, 1971 under the bill?

Mr. Munro: People can have a basic herd if they are now in farming, but there will be no further additions to the basic herd permitted after January 1, and new farmers cannot establish a basic herd. Even though a young man may walk into the Farm Credit Corporation and borrow $40,000 of which he puts $10,000 into establishing a herd, immediately he has for those five years plus all his other starting expenses, a loss position which he can never recoup.

Senator Connolly: I suppose another way of putting it is this; from now on where a man is starting in farming and he establishes a herd, it is like setting up his inventory, and when he sells that inventory the proceeds go into his income for the year in which he sells it.

The Chairman: Well, the proceeds go into income and for his taxable income you deduct the other goods sold.

Mr. Poissant: Mr. Chairman, may I ask this question? When you say that there might be a loss in your example, Mr. Munro, to the farmer starting in operation, you say that loss would not be applicable in the future against farming income for the next five years?

Mr. Munro: Well, in starting a business I expect he is going to go through in the normal way a heavy loss period during which he would not be taxable and with depreciation on machinery and other assets there is some way in which he can depreciate, so that he can pick it up and choose, if necessary, the amount of depreciation he wants to take. But then if there is no depreciation schedule on the $10,000 investment in cattle, and it shows completely as an expenditure, which over the five-year period could very well be the factor that would put him in a loss position—although he may gain two-thirds of the $10,000 in the loss position—he is still going to lose in the averaging position a portion of that loss.

Mr. Poissant: Yes, but if at the end of the year having started with $10,000 he were to take an inventory of his animals, like in any other trade, and that is only the difference between his beginning inventory and the closing inventory, it will be charged to his operation.

Mr. Kirk: We are talking about people on a cash basis of accounting and not on an accrual basis. On an accrual basis it would work differently, of course.

Mr. Poissant: That is, if the farmer should choose to remain on the cash basis.

Mr. Kirk: You see, they are leaving the option for the farmer to go on a cash basis in the law, but they are making it extraordinarily difficult to use it, by not having the basic herd provisions.

Mr. Poissant: You are quite right and under that condition he should go on an accrual basis for the first year until he has caught up the loss and then revert.

Mr. Munro: But I do not think that is possible. As I understand the law once you go on the accrual basis, that is it.

The Chairman: You have to get the permission of the minister. There is no return from accrual as of right. Maybe that is where you should put your finger on it. If, going on an accrual basis, farmers were to begin to carry on business on the January 1, 1972—if the right to do it on an accrual basis is the beneficial way of doing it, that is the way they should start out and perhaps the law should permit them to shift to a cash basis once they have established themselves.

Senator Cook: Consent should not be unreasonably withheld.

Senator Connolly: Is it suggested then that we should consider an amendment to the bill as introduced to bring about the right of the farmer to have this option?

The Chairman: This is what we are discussing. We are not to the stage where we are thinking in terms of what amendments should be made, if any. We are discussing a possible remedy to the position that this brief complains about. This is what we are asking Mr. Kirk and Mr. Munro. If a farmer started out on January 1, 1972 on an accrual basis, and then when it became beneficial for him to change over to a cash basis he would have the option of doing that, would that not deal with the complaint they are making? and I understood him to say "yes".

Mr. Kirk: I do not know. I do not see through the complexities of this clearly enough to give an answer.

Senator Cook: You are not the only one!

Mr. Poissant: Mr. Chairman, that was provided in the old section 85F and it has been carried forward under section 28(1) of the act whereby if you are on an accrual basis you can elect to change over to a cash basis later on. However, once you have elected, that is the end.

Senator Connolly: In other words, it is up to the Federation to alert the farmers to chose the accrual basis.

Mr. Kirk: There is an option right now whereby you can convert to a cash basis?

Mr. Poissant: You have always had that right, under section 85F.

Mr. Kirk: No, but to return to one.

Mr. Poissant: No, when you are on an accrual basis you can switch over to a cash basis.

Mr. Kirk: You cannot?

Mr. Poissant: You can under section 85F. I do not know whether it reads word for word, but I think you can also under section 28(1). I think it is the same thing. It says in section 28(1):

> For the purpose of computing the income of a taxpayer for a taxation year from a farming business, the income from the business for that year may, if the taxpayer so elects, be computed in accordance with a method (hereinafter in this section referred to as the "cash" method) whereby the income therefrom for that year shall be deemed to be an amount equal to
>
> (*a*) the aggregate of all amounts that . . .

and minus any deductions for the year permitted by paragraphs 20(1)(*a*) and (*b*).

That is the depreciation.

Senator Cook: Is your election lost once you have made it?

Mr. Poissant: Section 28(3) reads as follows:

> Where a taxpayer has filed a return of income under this Part for a taxation year wherein his income for that year from a farming business has been computed in accordance with the method authorized by subsection (1), income from the business for a subsequent taxation year shall, subject to the other provisions of this Part, be computed in accordance with that method unless the taxpayer, with the concurrence of the Minister and upon such terms and conditions as are specified by the Minister, adopts some other method.

I am sorry. You can elect to be on a cash basis, and if you want to change from a cash basis to an accrual basis you can do so under section 28(3), but you can make only one change. I would like to correct myself. It does not appear that you can start on an accrual basis and go to a cash basis.

Hon. Mr. Phillips: Even then, you need the consent of the minister.

The Chairman: If Mr. Kirk and Mr. Munro are able to answer the question which I put to them regarding commencement on an accrual basis on January 1, 1972, and then switching to a cash basis, at their option, when it would become beneficial to them, if that deals with the problem, perhaps that is one of the areas of the problem to which we can look.

Senator Cook: They do not have to answer the question now. They can think it over and let us know. They are not bound by anything they would say now.

The Chairman: Yes. Is there anything else, Mr. Munro?

Mr. Munro: I do not think there is anything else under that section. Perhaps Mr. Kirk could give us a review of item 5, Straight Line Depreciation.

Mr. Kirk: As we mention on page 6 under item 5, Straight Line Depreciation, the option now open to farmers to depreciate assets on a straight line basis should be retained, and recovered depreciation be not included in income. This is the present situation.

We believe this is a very reasonable request. The fact is that in farming income is typically low in relation to investment, obsolescence is rapid, inflation of farmers costs continues year after year, and more expensive and sophisticated machinery, equipment and structures have to be constantly introduced into the business. Often of course there will be no recovery of depreciation, but where there is this should be allowed tax-free as a limited but much needed means of easing the problems of replacement and the necessity of incurring a steadily increasing debt load to keep technologically abreast of the business. We do not view this request as a concession, but as a sensible and realistic recognition and adaptation to the very real problems faced by farmers in their rapidly changing, highly competitive, and inherently very risky business.

The summary of the 1971 tax reform legislation, issued by the Minister of Finance with the new bill states:

> Straight-line depreciation will continue to be available for assets acquired before the new system starts. Depreciation will be calculated on the diminishing balance system for assets acquired after December 31, 1971. If the assets depreciated on a straight-line basis are subsequently sold for more than original cost or Valuation Day value, the difference will be a capital gain. As at present there is no recapture of straight-line depreciation.

In the event that the extension of the straight-line system with freedom from tax on recovered depreciation is not retained, we would like to be sure that the provisions of the bill do in fact meet the full intent of this paragraph. This is referring to the paragraph I have just quoted.

By this we mean that farmers must:

1. Be able to maintain a separate bookkeeping on assets acquired up to December 31, 1971, on the present straight-line basis, with assets subsequently purchased separately set up on a diminishing balance basis.

We were not totally clear whether this was a possibility.

2. That capital gains if any, be calculated on the difference between disposition price and original cost or valuation day value whichever is the higher.

There are occasional cases, they are not frequent, where a machine, perhaps because of inflation, is worth more at valuation day than the amount you originally paid for it. That is not a typical case.

We have had difficulty in satisfying ourselves that the bill fully provides for this, and would like it ensured that this is so if, we repeat, the Government does not meet our very sound and reasonable overall request.

Senator Connolly: This may become a subject matter for our consideration based on a comment in the department's bulletin. It is a question of interpretation.

The Chairman: I am not sure, Senator Connolly, in view of the fact that the minister has made a pretty positive statement that based on any assets you presently own and have owned before January 1, 1972, you continue on your straight-line depreciation. But on those subsequently acquired, you are on a diminishing balance basis, which is the usual basis for capital cost allowances now. I would doubt, in the face of that statement, whether you could expect any different regulation to evolve, unless there were pretty strong recommendations made.

Mr. Kirk: We are not questioning the intention of the minister. We could not find those assurances in the bill whereby these two systems could be set up.

Mr. Poissant: It is not in the bill because it is part of the regulations. That is why it is provided in section 20 which refers to the regulations being issued. That is where it should be. Let us hope it will be there.

Mr. Kirk: That deals with the legislative question, which we did not understand.

Mr. Poissant: It is not in the act as such.

Senator Connolly: Unless we see the regulations, we will not know either.

The Chairman: I am sure that when we have the representatives here from the Department of Finance we can specifically ask that question and we are entitled to an answer.

In the event it is indicated that it will be contained in the regulations, I suppose we should insist on an immediate answer for our consideration, suggesting that if we have to wait for the regulations maybe they will have to wait for the bill.

Senator Cook: Or they should indicate on what authority they say it will be contained in the regulations. Such a statement does no mean a thing without authority.

The Chairman: On previous occasions, for instance in connection with the estate tax bill, the departmental officers gave certain interpretations, which the minister undertook would be applied in the department. That is contained in our proceedings of that day.

In the event, for instance, that law courts in their decisions interpret something differently, the minister would be prepared to amend. I agree that there are limitations in enforcing any such undertaking, but I cannot conceive of a minister giving an undertaking and the Government not being prepared to honour it.

Senator Cook: I said that because I thought it would be departmental officials speaking.

The Chairman: The minister should appear with respect to some of these points.

Mr. Kirk: We are not particularly concerned with the technicalities; our main submission is to maintain the present straight-line system.

The Chairman: It gives you a little more annual write-off than the diminishing balance.

Mr. Kirk: That is correct.

The Chairman: After the first year.

Mr. Kirk: It is also a little help in the rather desperate problem of keeping up with capital investment requirements; we would have more tax-free recovery.

The Chairman: There is a big "if" underlying all this: The capital cost allowances do not mean anything unless there is income.

Mr. Kirk: That is correct.

The Chairman: Of course, if you go for a period of time without income you will cease to operate.

Are there any other points on this section, Mr. Kirk or Mr. Munro?

Mr. Munro: No; I think it has been covered from our point of view. I wonder if Mr. Kirk would take us to the next section, on page 8, under the heading "Partial Sale of Farm Land and Re-investment in Farm Business."

Mr. Kirk: Item 6: Another provision that should be made in the bill relates to sale of a part of a farmer's land. As we read the bill it would not be possible—unless under expropriation—for a farmer to sell land and re-invest the proceeds in the same or another farm without realization, and therefore taxation, of capital gains. There are many circumstances when a re-organization of the farm business requires disposal of land and purchase of either other land, or depreciable assets for the farm business. This is particularly important for a farmer who wishes to change to production of another agricultural product, such as a prairie wheat farmer who starts a hog operation. Public policy has in recent years emphasized the necessity of farmers adapting their production to market conditions. The capital gains tax provision now proposed would introduce unnecessary rigidity. There should be no realization of capital gains on such re-investment. This would be a real problem for many farmers, and we request it be taken into account. Not only this, but we would point out that for persons who do not need to invest their capital gains in their own enterprise, the annuity arrangements permit extensive averaging. That is the annuity arrangements in the new bill, which provide up to 15 years of averaging.

The farmer who wishes to re-invest in farming should have a corresponding option, as we have suggested.

There will be many cases where the farmer, on the other hand, will suffer capital losses on disposal of property. If he is faced at that time with new investment in the reorganization of his business, the backward averaging provision may be of little use to him, or unavailable. That is, he may have used them up. We would recommend in such cases that a forward averaging of the capital loss over five years be provided for.

The Chairman: Mr. Poissant, have you any comment with respect to this?

Mr. Poissant: Yes, I have two questions: First of all, you say that a capital loss should be spread over five years. Do you mean to say that it should be spread over any type of income, or only against capital gains in the next five years?

Mr. Kirk: We refer to farming income.

Mr. Poissant: Not only restricted to capital gain in the next five years?

Mr. Kirk: We say that if there is a capital loss presumably one-half of it, if it is in the capital accounting area, could be carried forward over five years, as farm income can be averaged back for five years. However, in the case of a capital loss, where a farmer is re-organizing his business, the availability of that five-year averaging provision may not be there. He may in fact have had very little income during the previous five years, or he may have exercised the averaging option for four or five of the previous five years. He would therefore be faced immediately with a loss, which he should be allowed to apply ahead.

Mr. Poissant: You say the loss should be applied against farming income over the next five years. The brief requests it be applied not only against capital gains, but also farm income.

The Chairman: If there is not sufficient gain, income cannot be encroached on for $1,000 in any year.

Mr. Poissant: Yes, for ever. This is one of the problems that would be faced in drafting the legislation. I refer to the middle of page 8, where it is stated that this is particularly important for a farmer who wishes to change to production of another agricultural product, such as a prairie wheat farmer who starts a hog operation. There would be a difficulty in determining the demarcation line between strictly agricultural and other products. There could be companies or farmers engaged in other than agricultural production. How would the determination of agricultural products be made and any change within that group be allowed to roll over free, which is really what you are asking?

Mr. Munro: Yes.

Mr. Poissant: How should agricultural products be defined? I know of farms in Quebec, for instance, which are farms only in name and are really in the commercial business of raising chickens for barbecues. In your opinion, would that be a change in agricultural products?

Mr. Kirk: Yes; in our lexicon we consider farming chickens for barbecues as agricultural.

Mr. Poissant: Would other by-products remain in the group of agricultural products?

Mr. Kirk: We would not include TV dinners as agricultural products.

Mr. Poissant: Even if they were prepared by the farmer?

Mr. Kirk: Yes, they would not be included in the definition of agricultural products.

Mr. Poissant: That is my point, that there would have to be some definition.

Mr. Kirk: Yes, there would have to be a definition.

The Chairman: Are there any other points that you would like to raise, Mr. Munro or Mr. Kirk? We have already discussed the item on page 9 headed Principal Residence Under Incorporation. We come now to the heading Aggregation of Assets on Valuation.

Mr. Kirk: This is a fairly technical point. It is our understanding that the way the bill now reads, a taxpayer, in setting a valuation-day value on his assets, must adopt, for all his assets as a group, either original cost or valuation-day value, choosing whichever in the aggregate is the higher.

This is clearly not a satisfactory arrangement. The option should be open for each item of property taken individually. We understand too that this latter arrangement is the intent of the Government as a policy matter, and we urge that in amendments brought in the error be carefully corrected. This is an important matter. This matter has come up much more widely than in farm submissions.

Mr. Poissant: You are not referring to the article in the *Times* and *Post*?

Mr. Kirk: I was told by my advisers that it had come up.

Senator Connolly: An item-by-item valuation.

Senator Haig: The taxpayer does not set a valuation-day value. The valuation day is determined by the Government, and he values his assets on that base. He does not set the valuation day.

The Chairman: No, he does not.

Senator Cook: It says "A valuation-day value".

The Chairman: It states, "A taxpayer, in setting a valuation-day value on his assets." Are there any further points, Mr. Munro?

Mr. Munro: Not unless you have any further questions. Perhaps we can now turn to page 10, "Adding of Losses to Capital Cost".

Mr. Kirk: The hobby farmer provisions of the bill state that non-deductible losses may be added to adjusted capital cost up to the amount of taxes and interest on borrowings. Non-deductible losses more generally may be added to the capital cost.

The Chairman: The effect of that may be to have less exposure by the hobby farmer to capital gains.

Mr. Kirk: In business generally they may be added to capital cost. Farmers will often suffer losses which, while deductible, are not in fact deducted because of the way the averaging option works out or because he has suffered severe income difficulties over a period of years. Losses in any taxation year, up to the maximum of taxes and interest on borrowings, should properly be added to the capital cost if they could not otherwise be set against income by the taxpayer.

The Chairman: Do you have any comment to make on that, Mr. Poissant?

Mr. Poissant: Yes. In other words, you have the same treatment as is being offered to hobby farmers. In one year of the five-year carried forward loss, you either add the loss of the year to the cost base or you keep the loss and carry it forward against your other revenue, am I right?

Mr. Kirk: That is right. It could not be both.

Mr. Munro: We come now to item 10, Guidance to the Farmer.

Mr. Kirk: This says that we appreciate the assurance of the minister that he will do his best to explain as clearly as he can what this is all about. We offer our co-operation and would like to be consulted in the preparation of guidance to farmers.

The Chairman: I think, Mr. Kirk, you should request an opportunity for consultation. Item 11 is "Transitional Period of Grace".

Mr. Kirk: We were informed by our advisers that it is often very difficult to take full advantage of new laws right away, that the consequences and problems related thereto do not become evident and clear except over a period of time. We suggest that at least one year should be provided for the farmer to review his position, for which

period the position of the farmer would be pro forma frozen as at valuation day, for the purpose of making arrangements at any time during a further year's period, so that he does not get caught out on the sheer business of having to act quickly.

The Chairman: Any person to whom it applies is caught by it, if he does not alert himself fast enough.

Senator Cook: We all feel that it is too much too soon, not only for farmers but for everybody.

The Chairman: Yes. The period of grace should be added to whatever the time limits are, to equal a certain period of time within which you can assess your position under the new legislation.

Senator Cook: It should be added more gradually to fit into the system.

The Chairman: It is a terrific job. There are over 250 complicated sections. We know, from former witnesses, that it is not easy to obtain answers. It takes a lot of reading and study. We will have a good look at that, Mr. Kirk.

Mr. Munro: We now have a paragraph on pollution. Would you explain that, Mr. Kirk?

Mr. Kirk: We are saying to the minister that we hope he will give special attention to an adequate definition of pollution control equipment covering farm machinery and equipment. I am not familiar with the area of pollution control equipment for farmers.

Mr. Munro: This is a new ball game that we are in. We have a society that is becoming greatly concerned with various facets of the ecology, and farm pollution is one of them. Technology is concentrating on this metter. We do have smells, odours, and so on. New equipment is appearing consistently and is badly needed to minimize both air and water pollution. But this does not add anything to the income of farmers.

We are asking for some special provision here, that the advice of the Department of Agriculture is sought about equipment that should be eligible for tax exemption. We do not know the dimensions of this ourselves, but we can see it coming.

The Chairman: We are not in a position to define specifically what is pollution equipment, unless you are prepared to give us some help.

Mr. Munro: We are asking that the experts within the taxation department check this out very carefully. We ourselves have some trust in the Department of Agriculture, but we have observed in other jurisdictions where the Government divide themselves, and run in different directions for different reasons, they get out of communication with each other.

Senator Cook: In other words, you are suggesting that they define this pollution equipment, that perhaps we should have public hearings on it, that people should advance their views on whether such equipment should be so defined or otherwise?

Mr. Munro: That may be one answer. We do have some trust in those who are working in the field and helping us to develop this equipment, and we think they should have some say.

The Chairman: It is inconceivable that they would not be concerned.

Mr. Munro: Yes. I hope you are right.

Mr. Kirk: It is our hope that equipment or machinery will not simply be identified as pollution control machines. It will be a complex of technology that will result in pollution control, and what we are concerned about is that they do not so narrowly define what is a pollution control machine that many of the machines the farmer needs for pollution control are, in fact, outside the definition.

The Chairman: On page 12 of your presentation, Mr. Munro, you have a paragraph on depreciation. It has been indicated that capital costs allowances are going to be reviewed. What you are suggesting is a simple single rate to be applied to all depreciable farm assets, namely, 40 per cent on a diminishing balance basis, and 20 per cent on a straight line basis.

Mr. Munro: We feel that the rate of allowable depreciation is in need of review, Mr. Chairman. Let us take as an example, and only as an example, the fact that in my part of the country, southern Ontario, we are greatly concerned right now because we have inadequate corn-storage, and yet if we build a corn storage facility we have to depreciate it at the rate of 2½ per cent, which means it will take 40 years to write off, and before half that time has elapsed the piece of equipment will be obsolete, due to changing technology. It is the same with respect to so many things—feed lots and many other items of equipment and particularly with respect to buildings. The write-off period is hopelessly inadequate.

The Chairman: The minister has indicated that the capital cost allowances will be reviewed. I cannot conceive of them being reviewed in a vacuum.

Senator Cook: Unfortunately, Mr. Chairman, he also indicated that they are too generous.

The Chairman: Yes, I believe he did add that with respect to some instances.

Mr. Munro: In taking a feed lot floor, for example, the concrete could be laid twice before the original concrete is depreciated. It is inconceivable that we have to operate in this manner.

The Chairman: Well, we have noted that, Mr. Munro.

Now, you support the co-operatives in their position with respect to this bill. We have not heard from them yet, although thay are coming in.

Mr. Kirk: Mr. Chairman, with respect to the co-operatives, first of all, I should explain that, as many of you probably understand, there is a very large overlapping of membership between the Canadian Federation of Agriculture and the Co-operative Union of Canada. We are supporting their representations. We are not here as expert witnesses on co-operative taxation; we leave that to them. We do,

however, support their representations. We are convinced from what they tell us that the provisions of the bill will, in fact, create extreme difficulties for co-operatives in their traditional and self-generating techniques of financing, for one thing. That is leaving aside the basic principles that the co-operatives do not believe they make profits in the first place. But even leaving aside that fundamental question the change from 3 per cent to 5 per cent as the minimum net cost base increases the taxes, of course, and the new procedures for the definition of employed capital are such that the basic techniques of getting capital from the membership and rotating it out again and getting it from the patrons primarily as a means of providing a business facility for themselves as patrons would have to be changed rather radically, and it would seriously disrupt the co-operative method of operation.

That is what we understand from them, but, as I say, we are not here as expert witnesses on the co-operatives. We have been leaving this job to the Co-operative Union and they are the people who can tell you about it.

Senator Isnor: How can you fully support their representations if you do not fully understand them?

Mr. Kirk: We fully support their recommendations because we have a large overlapping of membership, sir. It is just a division of labour that we have not ourselves made ourselves experts in this area. We did not prepare ourselves for such a presentation.

The Chairman: That closes your presentation, does it?

Mr. Munro: Yes, it does, sir, and we thank you for hearing us and we hope you will give due consideration to what we have put before you. I do not think our list is an extremely lengthy one, but we felt it was pertinent.

The Chairman: Well, you heard the course of the discussion. Thank you.

The Chairman: If the committee would remain for a short time, Mr. Poissant is going to take perhaps 15 or 20 minutes to explain the administrative changes. I believe it will be useful to a better understanding of the question.

Senator Molson: Mr. Chairman, before we switch, could I ask what the situation is with regard to the amendments? A motion was put forward.

The Chairman: Did I not mention that last day?

Senator Molson: You may have. I may have missed it.

The Chairman: There is no reason why the committee should not know. The resolution and the request contained therein went forward to the Minister of Finance. I was speaking to the Minister of Finance last Thursday and he agreed that the committee should have the amendments at as early a date as possible. He suggested that when the motion to go into Committee of the Whole takes place in the other place all the amendments which the Government is proposing to put forward will be tabled at that time and they will become available to us en masse right away.

Senator Molson: They have had second reading now, so presumably that motion, will come forward any minute.

The Chairman: Yes, that is right.

Senator Molson: Do you happen to know, Mr. Chairman, how many amendments have received favourable consideration?

The Chairman: No, I do not. I have heard a wide range starting at, perhaps, one hundred.

Senator Molson: Yes, with an upper limit of two hundred.

The Chairman: I do not know, but there will be some advantage in having them all at once.

Another thing we have to look at is the possibility that the review of this legislation in Committee of the Whole in the other place may proceed at a faster pace than we thought it would.

Senator Walker: The fact that they got through second reading is amazing. How could they possibly do that?

Senator Flynn: They had to go to Committee of the Whole.

The Chairman: In Committee of the Whole, where they are dealing with it section by section, there is bound to be much more debate and a great many more questions and explanations. It is pretty hard to indulge in general-debate, I would say, on a bill of this size and scope. It would be a difficult thing to do, and that may be the reason why they decided that it would be better to get the questions going in the Committee of the Whole. In any event, I am sorry I did not tell you this at the opening.

Hon. Mr. Phillips: If I may just say, Mr. Chairman, that has a direct bearing upon the representations we have just heard. Some of the recommendations submitted by the Canadian Federation of Agriculture may be reflected in some of the amendments.

There was an indication from the Government, to start with, that they proposed to bring in each amendment as they got to the section. This would have made it utterly impossible for this committee to function intelligently. At least we seem to have extracted the commitment that all of the amendments will be brought down at one time, and as soon as they are brought down we can relate the amendments to the representations as we hear them.

Senator Connolly: There may be further amendments made as a result of discussions in Committee of the Whole in the other place.

The Chairman: We cannot control that. I should add that your chairman and some of his experts have been thinking that at some stage we should be considering making certain interim recommendations to the Senate; in other words, we should not go through the whole hearing process before we start thinking about what, if anything, we put forward by way of suggested changes. Some of these subjects can stand by themselves, and when we get representations, as on international income, for instance, if we have any views that we think should be reflected in the legislation and are not, possibly our position is that we should feed that into the stream right away.

Senator Walker: That would be a good idea.

The Chairman: The way to do that, of course, would be to make an interim report to the Senate, because anything we are attempting to feed into the stream must go to the Senate; it is then available for distribution, it would go to the Government for their consideration, and might very well in those circumstances become the subject of debate in Committee of the Whole in the other place. We are alert to that situation, and we will try to do something about it pretty quickly.

Senator Walker: Otherwise it would be too late, if you left it to the end.

The Chairman: Yes, it may in one sense be too late. Remember, at some time or other we will see the actual bill, which after it has had third reading in the other place will come to us and to this committee. In that sense it would not be too late, but you will not be able to give it the same studied consideration as if you were feeding it in at this time. We will try to do it reasonably soon, and "reasonably soon", Mr. Poissant, I would say would be within a week or ten days.

Mr. Poissant: Yes.

The Chairman: At the latest.

Senator Connolly: For the first interim report?

The Chairman: That is right.

Hon. Mr. Phillips: Perhaps I might insert this. I do not know whether you were here at the time we were dealing with this point, Senator Walker. We are not now considering a money bill here, and we are therefore able to deal with the matter on a broader and more flexible basis by making suggestions.

The Chairman: We will move as fast as we can.

Senator Carter: Do I understand you to say that the regulations will be introduced?

The Chairman: No, the proposed amendments that the Government has indicated it will bring forward.

Senator Carter: The whole works, the regulations as well?

The Chairman: No, the regulations are a separate matter. I understood the minister to say that the regulations would be tabled as they became available. Some of them are being worked on now; it is a massive job.

Hon. Mr. Phillips: There is also the problem that you cannot have regulations unless they are related to a definitive section of the law.

The Chairman: But they can be put out in the form of draft regulations.

Hon. Mr. Phillips: It could be done that way.

The Chairman: I would now like to ask Mr. Poissant to make some comments.

Mr. Poissant: Mr. Chairman, honourable senators, I have prepared a few notes, which you now have in front of you. There are a few additional things I would like to say. The notes cover sections 150 to 180 of the bill. I have made notes only on the changes made from the present system; anything that is unchanged is not reflected in these notes.

The first section in which there has been a change is section 152(4), which is the old section 46(4). The Minister of National Revenue has the right to open a file on assessment after four years if there was misrepresentation in the original assessment. He could do that only if there was a misrepresentation. If there was no misrepresentation he was bound by the four-year limit. Words have now been added to this misrepresentation provision:

> —that is attributable to neglect, carelessness or wilful default.

All my remarks will show that the tax reform reflects the judgments given by various courts in tax cases, many of which have been incorporated into the reform.

Hon. Mr. Phillips: Would you advise some of us who are lawyers whether the situation has improved for dishonest taxpayers and resourceful lawyers? If it is mere neglect, unless it comes under the heading of "neglect, carelessness or wilful default", it can still be a serious misrepresentation, and hence the dishonest taxpayer's position is improved.

Mr. Poissant: That is quite right. This is really a legal point.

Hon. Mr. Phillips: This is indicative of fixing so-called loop-holes.

Mr. Poissant: In the case of *Taylor* the judge decided that any misrepresentation includes innocent misrepresentation, even though the act only referred to misrepresentation. Maybe this is one reason why the old section 46(4) has been amended.

In respect of section 152(5) I say that adjustments on re-assessment after four years are restricted to those items in respect of which there has been misrepresentation or fraud. This is very interesting, because hitherto the department opening a file where there was misrepresentation could check every item in that year, and not only confine the study or examination to matters of misrepresentation. Now the file can be opened after four years, but the examination must be restricted to points in the taxation year subject to misrepresentation or fraud.

I make the additional comment that in the case of *Taylor* it was held that the burden of proof lies on the minister in the case of misrepresentation or fraud, whereas throughout the general act the onus of proof is usually on the taxpayer. In *Taylor* the judge decided that in the case of misrepresentation the onus of proof was on the minister.

Again, if the taxpayer waives a notice of the four-year limit he cannot restrict his four-year limitation to one aspect of his dispute with the minister. Once the waiver is signed, he has signed for everything in the four years and the four years are open for all items.

Under sections 161(1) and (2) I refer to the rate of interest. That is new. It will be defined in regulations from then on.

Section 163(1) says:

> —attempts to evade payment of tax payable—

I have underlined the following:

—by failing to file a return of income.

It is a little dangerous to have an attempt to evade tax by failing to file a tax return. They say this is really when the tax was evaded, and the return was not filed; but it could be meant to mean that the failure to file this by itself is an evasion of tax.

The Chairman: That contradicts a lot of legal decisions.

Mr. Poissant: Yes.

The Chairman: Section 132 at present says there must be *mens rea* or a deliberate attempt at dishonesty, to evade tax.

Mr. Poissant: Yes, to evade tax.

Senator Cook: That should be cleaned up, because obviously it is not what is intended.

The Chairman: I take it, Mr. Poissant, you have made notes where we have said that something must be done.

Mr. Poissant: Yes. I think this was already raised in the House of Commons. There is a case on this, which is cited. It is *Legare Foundry,* 64 D.T.C. 696, where Mr. Legare was successful in saying that he had not tried to evade tax. This is why this section, I understand, was changed. He says you do not evade tax unless you are assessed to pay tax and he said he had not been assessed and therefore he had not been evading. Therefore, it is based now on the filing of the return and not on the assessment, when the bill goes through.

In regard to section 163(2), omissions in returns, this is still the same as section 56(2) of the old act. Here, I would like to make a reference that previously there was a section, 56(3), that says that if you are fined under section 56(1) you cannot be fined again under 56(2). But this saving provision now is being removed. I read the *Panko* case, 71 D.T.C. 5255, Supreme Court. Under this July, 1971 decision of the Supreme Court, they could apply together, and if you have not got the saving provision you could be penalized on the first one, penalized on the second one, although admittedly the Finance Department and the minister may say this is not the purpose of the intent of the law.

I have raised some points. Omissions in the return could be just in a letter to the department. If you made an error in a letter to the department, in sending additional information, this could be fined under section 56(2). Because you omitted to send your statement in the first one you could be penalized under 163(1) and if you have not got this other provision I think there could be a danger that you could be penalized under both sections.

Now, section 163(3) is a new one. It says that in respect of penalties, the onus of proof rests with the minister for this section only. This section would contradict current jurisprudence. In the case of *Pashovitz,* 61 D.T.C. 1167, it was held that "the onus falls on a taxpayer appealing an assessment of a penalty under section 56(1)".

I said before that the onus of proof is always on the taxpayer, and so was the penalty under the tax, the onus of proof; and the judge agreed to that, but this they have changed, by this section 163(3), to say that the onus of the proof in the case of any fine or penalty will be on the minister, to prove that the fine is properly charged.

The Chairman: That is a significant change.

Mr. Poissant: Yes.

The Chairman: It is beneficial, too.

Mr. Poissant: It would be, yes.

The Chairman: Let us not do anything about that.

Mr. Poissant: This is to the taxpayer's benefit.

The Chairman: To the taxpayer's benefit, yes.

Mr. Poissant: In regard to section 164(6), I would like to warn honourable senators there about this. I do not know why this section was stuck in there, but I have to go through with it. If you were to read the section in rough language, it comes to this. Where the estate of a deceased taxpayer has suffered capital losses and*or terminal losses in respect of depreciable property, the estate will be deemed to have paid on account of tax payable for its first taxation year an amount equal to the excess of the tax actually payable by the deceased for the taxation year in which he died over the amount that would have been payable were the capital and*or terminal losses deducted from his income.

In other words, they say that if you, by any chance, have a capital loss in the first year after anyone died, you could elect to consider that capital loss to be the capital loss of the deceased, and you recalculate the tax that he would have saved by having himself the capital loss and any additional tax he paid because of that would be deemed to be a part payment of, the estate payment, against the income tax payable by the estate on account of the revenue.

Senator Molson: A capital gain?

Mr. Poissant: Not only capital gains.

Senator Molson: Against income.

Mr. Poissant: If the estate has to pay tax of $50,000—you have to make calculation as to which is the greater benefit. If the benefit is greater to the deceased, you apply that tax against your own tax payable. I do not know why this is there. I should remind you that this section is Returns, Payments and Assessments. That is probably why that section is in there.

On section 165(3), the taxpayer may indicate on his notice of objection that he wishes to appeal directly to the Tax Review Board of the Federal Court. This is rather an important and very good change, I would think. If the taxpayer is sure that on his notice of objection his arguments are put forward, that he has a good valid case, instead of going through the procedure of having the minister to revise the case and confirm the assessment, he may, on his notice of objection, say he wants to appeal directly to the court, that he does not want to go through the proceedings again because it is too long a process, that he wants to clear the matter immediately. If he does this, he must, of course, waive his right of reconsideration. The minister must consent. I do not know what would happen

if the minister refused, because it is permitted under the act. It says that he must consent. Also, the minister is deemed to have confirmed the assessment. In other words, he is deemed automatically to consent, to confirm what assessment he has issued originally.

Hon. Mr. Phillips: In connection with subsection (3), I would say that the taxpayer who is so advised by a lawyer is badly advised. I have noticed through the years that one will sometimes file a notice of objection which has no particular merit and it is accepted by the minister. I have found there were notorious notices of objection which have been disallowed, and sometimes by the law of error you can get a minister to confirm a bad appeal.

Mr. Poissant: That is a very good point. In this way, if there were another decision or another settlement that you knew of, you could say that in a previous case it had been agreed, in a similar case.

Hon. Mr. Phillips: You have the right to go to the tax court, anyhow. Why not gamble on the law of error?

The Chairman: We are not making a recommendation.

Hon. Mr. Phillips: No, it is a personal observation.

Mr. Poissant: I think there was a question of time involved, too. In regard to section 165(7), the taxpayer need not file a notice of objection in respect of a re-assessment or an additional assessment when he has objected to the original assessment. As honourable senators know, you may be assessed in one year; the assessor may have found out that in three or four months he has overlooked some items and may re-assess by an additional assessment for the very same year. In the case of *Abrahams*, 66 D.T.C. 5451, it was decided that once you re-assess for the same year the first assessment is dropped. It is the second one that counts. In the case of *Abrahams*, he had appealed on the first assessment and he finally discovered that when he was re-assessed, all of the proceedings he had to go through in the first appeal were no longer legally in existence, and he had lost his right of appeal because the time had elapsed, the ninety days and the 180 days. Therefore, now, when you are being re-assessed, all you do is, send a letter back to the court, at whatever stage you are, and you say you are adding your complaint or your arguments to whatever reference was made on the first appeal.

Now I come to section 172 and section 180, and these are both the same. In the past the minister could refuse the registration of the pension plan and he could refuse the certificate for a charitable organization and there was no appeal. You could not challenge his decision. That was the end of it. Now, if he refuses the certificate for the charitable organization or refuses to register the pension plan you have ten days within which to appeal to the Federal Court of Appeal.

Incidentally, I find ten days a rather short period in which to appeal. If you are a charitable organization you may happen to be away when the minister sends the notice, and if you only have ten days you may lose your right of appeal. Although the time can be extended by permission of the Court, I think ten days is too short a period.

The Chairman: Maybe it should be 30 days.

Mr. Poissant: At least.

Senator Connolly: Can you tell us whether it is intended to continue the approvals that have already been given to registered pension plans and to recognized charitable organizations? Or does every registered pension plan have to reapply?

Mr. Poissant: That is a question of administrative procedure. Once you are registered, unless your registration is revoked, you are a bonafide organization.

Senator Connolly: Is that provided for in the transitional sections?

Mr. Poissant: That is a good question. I have not seen it but I imagine it is in the regulations.

Hon. Mr. Phillips: I should have thought it would be in the transitional part. Perhaps we could suspend the answer to that question until we have checked into it further.

Senator Connolly: I notice that in certain sections here you refer to the Appeal Division of the Federal Court and in other sections to the Trial Division of the Federal Court. I take it that in every case where there is recourse to the Federal Court it is specified in the act whether it should go to the Appeal Division or to the Trial Division.

Mr. Poissant: Yes.

Senator Connolly: Perhaps you could clarify one point for me, Mr. Poissant. In section 165(3), you refer to the Tax Review Board of the Federal Court. I do not remember the Court having such a division or unit.

Mr. Poissant: You are quite right. There is a typing error there. Perhaps we should make the correction to section 165(3) right now. It should read, "to the Tax Review Board or the Federal Court".

Now, dealing with section 173(1) and section 173(2), if there is a question of law and both parties agree that it should be settled by the Court, if both parties agree in writing they can then go to the Court and get a settlement of that point.

Senator Flynn: They prepare a joint memorandum, do they?

Mr. Poissant: Yes, and submit it to the Federal Court Trial Division. It is decided there instead of having to go through the old procedures.

Senator Flynn: They have that in the Quebec Civil Code now. You can obtain a judgment on a question of law on a joint statement of the facts.

Senator Connolly: Mr. Chairman, is that the equivalent of a stated case?

Senator Flynn: Probably.

The Chairman: Yes.

Mr. Poissant: Under section 173(2), with respect to the time taken for determination, the suspension of time would hold for items under dispute as well as for the question of fact being determined, but the time taken would not count for the purposes of the four-year period,

the time for filing a notice of objection or the time for instituting an appeal. In other words, the suspension of time applies not only to the item under dispute but applies to everything else as well.

Section 174(1) reads as follows:

> Minister *alone* may apply to the Tax Review Board or the Federal Court—Trial Division for determination of a question of law, fact or mixed law and fact *common* to two or more taxpayers.

As an example of that, you would have the situation of the buyer and seller of depreciable and non-depreciable assets, where the buyer would say, "my value is this", and the vendor would say, "my value is that". In such a case the minister may apply to the Tax Review Board or to the Federal Court, Trial Division, and have a value fixed by either the Board or the Court. That value is going to be fixed for both parties now, whereas previously it was necessary to go to court for the one and to go to court for the other, if he was in disagreement in both cases.

Now, in this case what the applicant must do in his application is to set forth the question to be determined, the names of the taxpayers to be bound by the determination and the facts and reasons for the determination. He then must send a copy of that to the taxpayers concerned and to other persons likely to be affected.

Senator Flynn: It is the same as in section 173(1), except that in this case he does it alone.

Mr. Poissant: Yes, once it comes to his attention that the vendor has sold an item which is subject to depreciation and other items which are not subject to depreciation. Now, we see this most often in the case of alimony payments, where the person making the payments claims that they are payments and are, therefore, deductible from the income, whereas the person receiving the payments takes the position that they are not payments but are a capital sum and are, therefore, not subject to be taxed. So now the minister faced with this kind of conflict has the right to submit the case to the Court or to the Board for a determination.

Senator Flynn: Mr. Poissant, you said that a copy must be sent to the taxpayers concerned and other persons likely to be affected. I suppose that if someone thinks he is affected he can intervene, even if he does not receive a copy of the notice. In other words, anybody who has an interest in a case may intervene.

The Chairman: Section 174(3)(*b*) says that the Tax Review Board or the Federal Court may:

> (*b*) if one or more of the taxpayers so named has or have appealed, make such order joining a party or parties to that or those appeals as it considers appropriate.

Senator Flynn: If someone is not advised and not named in the proceedings, he can probably still intervene if he has an interest.

Mr. Poissant: It does not say that. Do you think, Mr. Chairman, that he would have a right to do so?

The Chairman: I doubt it.

Senator Flynn: It is a question of law and the minister is seeking an opinion from the Court. Anybody who may be affected eventually by this decision should be able to intervene.

The Chairman: The question of law is on a set of facts that have arisen in connection with the situation for two or more taxpayers. Those particular taxpayers have to be named.

Senator Flynn: But they say that copies must be sent to the taxpayers concerned and other persons likely to be affected. So I suggest to you that you may miss some of those "likely to be affected" and they should be able to intervene.

Senator Lang: The taxpayers might be corporations and the shareholders might be the ones who are affected.

Senator Walker: It would only be in stated cases.

Mr. Poissant: Let us say there is someone who could be indirectly affected by the decision, and he is not aware of it. But that would not change anything because he is not directly bound by the decision. He could be indirectly affected, but a decision is a decision.

Senator Flynn: I do not know if the court could reverse its stand.

The Chairman: Well, that is a practical matter.

There is something here, Mr. Poissant—at the stage at which the minister applies for the opinion of the court, he has not made an assessment, but yet when you come to section 174(3)(*a*), it says:

> if none of the taxpayers so named has appealed from such an assessment, . . .

But at stage these do not contemplate an assessment.

Mr. Poissant: If he has appealed, then it is too late.

The Chairman: But how could he appeal it? The assessment has not been made.

Mr. Poissant: But a man could have appealed. Let us take the case of an alimony payment, for instance. A taxpayer files a return and he considers that as a deductible alimony payment, and the tax department at the local level refuses to accept it, and he goes through the procedures of appealing it. In the meantime his divorced wife in another remote place did not file a return because she presumed it was not income, and then it was discovered that it was income. Then, I would say under those conditions the appeal has been filed in a proper way and the minister does not have the right to set aside the appeal procedures and say that he is going to appeal directly to the court.

The Chairman: No, that is not the point I am making. The point I am making is that in 174(2) it says at (*c*):

> (*c*) the facts and reasons on which the Minister relies and on which he based or intends to base assessments of tax payable . . .

Senator Carter: But there is no assessment existing at that time.

The Chairman: There may not be any assessment at that time, because the order he wants from the court is an order determining a question of law so that he can make the assessment.

Mr. Poissant: That is right. I also question the phrase "intended assessment". What is that?

The Chairman: I do not know. Is it something you carry around in your head? Do you write a letter of intent?

Mr. Poissant: That is the first time I have ever seen that in the act.

Senator Connolly: But in that case would not the department make the assessment?

The Chairman: But it does not contemplate that. Look at the material that the minister sends to the court. These are the facts and the reasons on which the minister relies and on which he bases or intends to base assessments and he names the persons. So at that stage there has not been an assessment.

Senator Connolly: The only point I want to make is that he might avoid that by making an assessment in a way that is favourable to the department.

The Chairman: I think the language is not good and it is not clear and we should note it.

Mr. Poissant: I remember when I first saw that in the big book I wondered what was an intention to make an assessment.

Now 178(2) is something new in the act in that if the minister appeals a decision of the Tax Review Board—and by the way this seems to be important because this is the only section where there is a reference to the Tax Review Board—even though you were to appeal to the Federal Court Trial Division directly, it would seem it would not be applied in this case because the reference is only to the Tax Review Board. Now do they want to force every taxpayer to go to the Tax Review Board first and then to the Trial Division and then to the Appeal Court and then to the Supreme Court? Anyway, if there is an appeal from that Board the taxpayer will be refunded his reasonable costs—and I do not know what "reasonable costs" means—as long as the tax involved is $2,500 or less.

Senator Flynn: Well, we discussed that, Mr. Chairman, and the idea appears to be that when the minister appeals and the amount is not higher than $2,500, it is not fair to force the taxpayer to follow before the Tax Review Board or the Federal Court, and I suggest that we should take a note that it should apply in both cases.

Mr. Poissant: Do you agree with that, Mr. Chairman?

The Chairman: Yes.

Mr. Poissant: That an appeal to the Federal Court Trial Division should also be permitted.

The Chairman: That is right.

Senator Connolly: I could not hear what Mr. Poissant said.

Mr. Poissant: Senator Flynn suggested, Senator Connolly, that section 178(2) should also refer to an appeal from the Federal Court Trial Division.

Senator Flynn: "To."

Mr. Poissant: "From." You can appeal to the Review Board or you can appeal to the Trial Division directly, and if the minister appeals from that one, you get your refund. If he appeals from the Trial Division, the taxpayer would not get it. So you are in agreement that in both cases it should apply?

Senator Flynn: I was wondering whether there was an appeal to the Federal Court of Appeal in the case where there was only $2,500 involved.

The Chairman: Wherever the minister's action takes the taxpayer in that bracket.

Senator Flynn: In any case there should not be an appeal to the Supreme Court.

The Chairman: That is right. But they could obtain leave, and I think it should cover the whole process.

The Chairman: I agree that it should cover the whole process.

Senator Flynn: Even if they go to the Supreme Court.

Mr. Poissant: Why not?

Senator Connolly: Because it may be related to a question of law not necessarily related to the amount involved in the appeal.

Senator Flynn: And not necessarily related only to the individual involved in the particular case.

Senator Walker: But what if the taxpayer wanted to appeal?

Senator Flynn: Well, that would be at his own risk. The principle is that if he appeals in a case like that, it is because he considers there is a principle involved and an important precedent may be created, and therefore the taxpayer should not be penalized because this appeal is in the public interest. But on the other hand, as far as the taxpayer is concerned, he has only $2,500 at stake, so if he takes the risk of going up, then he must assume the cost.

Senator Connolly: There is always the possibility that if he gets to the Supreme Court of Canada, the court might decide that it was a case where the taxpayer should not have to pay the cost.

The Chairman: Senator Connolly, you mean appeal *in forma pauperis*? That should be quite a hint to the tax collector, if a person is appealing and he says he has no money to pay his costs, that perhaps they had better make a deal with him.

Mr. Poissant: I have another note here that additional assessments, as stated in the present act, have not been defined as yet, although there are many references as to what constitutes additional assessments. Now, under Administration and Enforcement there are only a few comments which most of you are already aware, but I

would like to say that some provisions of the present Income Tax Act are not being reported in the new Income Tax Act, but they are being found in the Federal Court Act and the Tax Review Board where you will find most of the procedures for appeal. Some of them were previously found in the Income Tax Act, and they are not being carried forward. They are to be found in their respective acts.

Senator Connolly: Do you suggest that this is a good change, to shorten the Income Tax Act and to lengthen the acts respecting the Federal Court?

The Chairman: No, my own feeling on the matter would be that the taxing statute is a very important statute and it affects everybody, but there should be one place where you can go and look up what your rights and remedies are. Some people do not consult lawyers. They consult tax experts who are not lawyers and who are not chartered accountants and who are not familiar with the taxation system. They would not know enough to look at the Federal Court Act.

Senator Connolly: Did Mr. Poissant say whether it would appreciably increase the number of sections if it were carried in the Income Tax Act?

Mr. Poissant: I would say so. However, I am not a lawyer. I would like to give the Chairman my views on the matter. I am of the opinion that it should not be in the Income Tax Act. The Chairman has suggested that some taxpayers are not soliciting legal advice. I feel that they should. They are trying to interpret this section and they are taking the wrong interpretation. It does not represent their rights because they have not looked at it properly. I think this is a legal matter. The Federal Court Act is a very lengthy document.

The Chairman: The thought I had in mind was that you should be able to find in the Income Tax Act a reference to the sections that are carried into the Federal Court Act, so you are alerted.

Senator Connolly: It could be done by reference to the incorporating sections.

The Chairman: That is right. But you do not have to incorporate each section. There should be a reference, however. That occurs in a lot of the legislation that comes before us now.

Mr. Poissant: Under the old system there were many pages, and I would say that the Exchequer Court took about five or six pages, and the Tax Appeal Board took five or six pages. But of what interest is it to know that the chairman of the Tax Appeal Board is appointed for ten years and he has to be a lawyer? That was in the Income Tax Act. Perhaps it should be a reference.

The Chairman: A reference to the section, yes.

Mr. Poissant: This will just take a few more seconds. It says that the taxpayer may appeal—I think that the wording there is pretty clear. I would like to refer to section 231(2), and this is new to the act:

> Minister must return documents seized within 120 days unless otherwise authorized by the courts.

This is as a result of court decisions where the taxpayer has his documents seized as in the case of Lafleur and he went to the Supreme Court and was turned down. The Supreme Court decided that he was not entitled to the document because of an inquiry.

Section 231, subsections (2), (6) and (15) are corrective measures which I think are good and proper.

Section 238(2) is rather new, it extends the penalty to a non-resident who has failed to file a prescribed form on disposition of taxable Canadian property. In other words, he will now be fined just as any other Canadian would be. I admit, of course, that there will be a question regarding collection.

The Chairman: Yes.

Mr. Poissant: But that is their problem. Then, at the end of page 5 under Tax Evasion, Tax Avoidance Dividend Stripping and Associated Corporations, they have not been changed. Mr. Scace referred to that the other day regarding tax evasion, tax avoidance dividend stripping and associated corporations. They are the same.

I would like to make one further comment regarding a comment Mr. Scace made the other day that there is no deemed gift under the present tax reform. I feel that this is an enormous error. There is deemed disposition, but there is no deemed gift. I understand they will have to amend the act to that effect. Under section 4 of the Income Tax Act it described a gift and what was deemed to be a gift. But they removed all of section 4 dealing with gifts because there was no longer a gift tax. If there is no gift tax there should at least be a deemed gift tax. I understand that this is going to be inserted in the amendments. Gentlemen, this is all I have to say.

The Chairman: Thank you, Mr. Poissant.

The committee will adjourn until 2.15 p.m., when we will hear the Canadian Construction Association.

The committee adjourned until 2.15 p.m.

Upon resuming at 2.15 p.m.

The Chairman: Honourable senators, we have a quorum. We have one brief to consider this afternoon, that of the Canadian Construction Association. Mr. Robert C. T. Stewart, President of the Association and of Cameron Contracting Limited, is present. Mr. Stewart, do you intend to make an opening presentation?

Mr. R. C. T. Stewart, President, Canadian Construction Association: Yes, Mr. Chairman.

The Chairman: With Mr. Stewart are Mr. Chutter, of Ottawa, General Manager of the Canadian Construction Association, and Mr. Sandford, their Taxation Officer.

Mr. Stewart: Mr. Chairman, honourable senators, we appreciate very much having this opportunity of coming before you, because we appreciate the valuable work that has come from your committee in the past in relation to income tax reform.

To go back in time, since the immediate post-war period the Canadian Construction Association has made numerous submissions to the Government on the need for special recognition in tax law of the construction industry due to the nature of its operations.

Two of the items which have been of particular concern to us have related to the recognition of the problems involved in the assessment of income in construction operations. We have recommended repeatedly that the completed contract method be officially recognized as a fair and equitable means of reporting income. A special brief on this subject was submitted by the Canadian Construction Association in 1949. This was further confirmed in a brief to the Royal Commission on Taxation. It is worth noting that the late Mr. Carter concluded that the estimate of income on construction work in progress was one of the toughest problems he had ever encountered in his professional career. This subject was raised in our brief on the recent White Paper and has been incorporated in our annual briefs to the federal Government.

It might be noted that in the United States this practice has been widely recognized and there American contractors report their income on the completed contract basis for all contracts of over one year's duration. This is more than the Canadian Construction Association is advocating. We suggest that the completed contract method apply to all contracts of two years or less duration.

It is interesting to note, I might say, that when some American companies have come to Canada they have been horrified to discover that here we are required to report income on a more regular basis. Several major contracts with American principals have got themselves into hot water when they have overlooked the fact that on a two- or three-year contract income must be reported annually as the work progresses.

There is one other item of concern to us. We appreciate the provisions that have been made for small business incentive—

Hon. Mr. Phillips: Before you come to that, do you not in practice receive by way of departmental indulgence at this stage the complete contract approach?

Mr. Stewart: I understand that the department does make some allowances when a contract originally contemplated to be completed within two years is slightly delayed due to unusual circumstances. There are special exemptions, provisions or indulgences granted, but it is one of these things that is tolerated in the administration without firm provision for it in law. With the growing complexity of contracts, a two-year contract is not now regarded as a long contract. Some extend for three and four years.

I made reference to the provisions which have been set up for the Small Buiness Incentive. However, it should be noted that this is perhaps less attractive to the construction industry than to other small businesses within the country. I can only say from my own personal experience that the retention of hold-backs over extended periods of time entails a very substantial tie-up of working capital. Whereas the presently proposed $400,000 of taxable earnings eligible for the reduced rate of taxation is a definite assistance to the smaller companies, the net retained earnings of some $300,000 represented by this does not go very far when major equipment holdings, common in many types of construction, are taken into consideration. There is also the fact that cash flows in construction are frequently extended because of the protracted hold-backs which are often introduced. I know of many contracts that call for a year's maintenance guarantee which, in effect, retains a sizable portion of the hold-back for a period of 12 months after all contract work is essentially completed. So we are concerned about this.

If it is not feasible to change this figure—and it must be acknowledged that some figure has to be chosen as an arbitrary cut-off point—another suggestion might be to provide for accelerated write-offs in other categories of equipment common to the construction industry.

There presently exists one category basically related to earth-moving and concreting equipment which is eligible for accelerated write-off. We have suggested that perhaps greater consideration could be given to other categories of equipment where depreciation, obsolescence, and a straight-forward matter of wearing out during the life of the job, makes it not too realistic to capitalize their initial cost.

The present cut-off point, I might say, is $100 for small tools. With the increasing cost of such tools, this is not as appropriate now as it might have been when it was first introduced.

Senator Connolly: Can you mention the other types of equipment that you have in mind?

Mr. Stewart: I am thinking about specialized equipment, such as flexible tracked vehicles used in some of the northern territories. Pile-driving equipment is another type; also certain types of heavy equipment which represent a major capital cost and which either have a limited life or are required for one specific project.

Senator Connolly: Those are the types of equipment that are now excluded from the regulations?

Mr. Stewart: Yes, from class 22.

Senator Connolly: If you wished to have an enlargement of the class, you would have to be more precise about the categories.

Mr. Stewart: This could be developed. We have had discussions within the association on the particular types that might be more appropriate. I can give the committee more specific cases, namely: "flexible tracked vehicles, four-wheel drive pick-up and service vehicles, floats and float tractors for construction equipment, trucks, et cetera, used in quarries or pits, pile-driving equipment, cranes, aggregate placing equipment, portable asphalt mixing plants and cement mixers".

Those are categories that presently are excluded from class 22. Yet it is equipment that is used in conjunction with heavy equipment that currently has a fast write-off.

Equipment, used in the placing of concrete is eligible for the accelerated, or 50 per cent, write-off. Aggregate placing equipment, which could be an identical or similar unit, is not eligible.

You run into problems in the interpretation and administration of this class which provides that to qualify,

the equipment must be designed exclusively for the designated operations.

Senator Burchill: Is not the equipment in that list eligible at the present time?

Mr. Stewart: Not in the accelerated depreciation.

Senator Burchill: What depreciation do they carry?

Mr. Stewart: At the present time 30 per cent. The accelerated rate is 50 per cent. That is in class 22.

The Chairman: What about the wear-out on items that carry the 30 per cent depreciation?

Mr. Stewart: In the first two categories, our feeling is that generally speaking they have a high rate of depreciation because of the nature of the work they are engaged in. Regarding four-wheel drive pick-ups, for instance, we are not suggesting that the ordinary half-ton truck, used on a construction job, should be eligible. However, when you get into a four-wheel drive operation, working perhaps on a pipe line or a major construction site where four-wheel drive is required, the situation is different.

The Chairman: On that basis, since these items would have a more general application or use, it is the particular application or use that gives you the quick wearing out, is that not right?

Mr. Stewart: I do not think that anyone, in practice, would buy a four-wheel drive vehicle unless the conditions under which he proposed to use it were such that he required four-wheel traction. It relates specifically to construction.

I would be the first to admit that there might be an exception. I think it is generally agreed that there is always an exception, where someone might buy a four-wheel drive vehicle to plough snow or do something else, but in the construction industry the bulk of these vehicles are designed for use on a construction site. The floats and float tractors—these are the low-beds that are used to move the loaders and shovels are presently not eligible for the accelerated depreciation.

The Chairman: Would that be the kind of qualification we might put on these items, namely, when used in certain types of operation?

Mr. Stewart: The difficulty there is, how would you relate its use? It might be used 500 times in a year. On 450 occasions it might be used in the moving of class 22, accelerated depreciation, equipment, and the other 50 times it might be used for hauling lumber incidental to its main use.

The Chairman: I am trying to get at a proper classification of these items, when used in the construction industry, that should carry a higher accelerated rate, to say, 50 per cent instead of 30 per cent.

Senator Connolly: Can you police it if you use the words "when used and to the extent used in a particular type of operation"?

Mr. Stewart: Perhaps Mr. Sandford, our taxation officer, can reply to that. He has some past experience of class 22 in discussions with the department. He might be able to offer something regarding the problems involved in defining these categories more specifically.

The Chairman: If you are claiming special treatment—and certainly an accelerated rate of 50 per cent would be special treatment—then you have to identify it with the object that it is related to, and in connection with which you have this quicker wear-out.

Mr. K. V. Sandford, Taxation Officer, Canadian Construction Association: The Committee might perhaps interject the word "primarily or mainly". There is a problem now with class 22, in the words "designed for". A gravel truck might be allowed if it is moving pulpwood, lumber or cordwood, whereas another truck, which perhaps is not designed for this purpose but has been adapted by the construction company, is disallowed. It might be appropriate to take out the words "designed for" and replace them with the words "used primarily for". You would have to add the words "not only moving and placing earth, rock and material, but moving the equipment that does that".

The Chairman: You could drive some rather big trucks through the words "designed for".

Mr. Sandford: There was one road contractor who had an asphalt tank truck. He was moving the liquid asphalt and he was allowed class 22. He expanded his operation to have tank trucks and trailers and had special tractors to move those trailers. The department allowed the trailers, but not the tractors. Their contention was that the tractor was not designed for the purpose of moving asphalt, so they disallowed the tractor portion. This is the type of problem you run into with these words and I think a use criterion would be more to the point.

The Chairman: Use items have been criticized in many respects. I know they have tried increasingly to get away from it in the tariff classifications.

Mr. Sandford: That is right, but the tariff is a one-shot thing as you come across the border, whereas the depreciation class goes on for years, and if it was up to the taxpayer to prove use and primary use by number of hours—50 per cent of the hours, or whatever—then it could conceivably be that one man would have to sell it to someone else who would not qualify. You would have to go back to a different rate, whereas the tariff item applies once and for all.

The Chairman: That is right. It seems to me you would have to work out language that would not be so dependent on the certification of use by the particular person, and it also might relate to the type of equipment used in the construction industry.

Mr. Sandford: Yes, you could relate it to the industry. That would make a good deal of sense.

The Chairman: If you relate it to the industry, if it is a type of equipment used in the construction industry, then, that is the qualification. Is that too broad?

Mr. Sandford: I think that would certainly be an aid to the contractors.

Mr. S. D. C. Chutter, General Manager, Canadian Construction Association: Mr. Chairman, by way of a reference for the committee, in our brief to your committee in April, 1970, Appendix C did develop this whole subject to a fair extent, and some of the items in there might stand as they are. For example, pile-driving equipment is, so far as I am aware, exclusively a construction item. Trucks and other equipment used in quarries and pits, I suppose, have an end use ascribed to them already. Most of these, I think, would have a construction connotation almost exclusively, and I think the appendix went into some detail to point out that with regard to these flexible tracked vehicles and four-wheel drive pickup trucks, a two-year life was about the extent that you could expect this equipment to last in construction. This relates to its actual longevity.

Hon. Mr. Phillips: Mr. Chairman, you are dealing with relief with respect to small businesses here and you have two approaches, as I understand it. The first approach is the low rate of taxation applicable to the first $50,000 of profit, and the other approach is from the point of view of accelerated depreciation for special categories. Have you considered the latter suggestion dealing with accelerated depreciation? It really comes under the body of the statute proper. Have you considered the justification for the first suggestion; that is, that the first $50,000 be subject to the low rate of taxation and that it should apply to that type of small company where it is established that its fixed assets in ratio to its total assets are in excess of 50 per cent, or in excess of a certain percentage, where you have a situation that distinguishes you from the small retail storekeeper moving inventory in and out, and this type of thing, to which I think you refer in your brief. And your justification for special relief is based upon the fact that you have a high fixed asset position in relationship to your total assets position. Would that not be a better way of approaching it rather than attempting, through this committee, to deal with relief by regulation?

Mr. Stewart: I believe the feeling was that there is the high fixed asset situation which exists in many companies, but there is also the matter of the need for working capital which is applicable over an extended period in many cases. It is somewhat different from that encountered by other small businesses. You made reference to a retail operation. Possibly $300,000—I do not know the earnings after taxes of a retail operation—might represent quite a sizeable organization, whereas in the construction industry you might not have an unusually high fixed asset situation but the lack of liquidity due to extended hold-backs could create the same bind as far as the smaller operations are concerned, or it might tend to limit the effectiveness of the operation. This is why we accepted the small business incentive provided for with this $400,000 total taxable earnings and then said that the Government should also recognize the particular situation that results in other cases in our industry.

The Chairman: Mr. Stewart, I do not think that the small business concept in this bill is of any particular help to the construction industry because the construction industry would have to do much of the financing out of its operations, and there is a limit on the accumulative earnings in this bill, C-259, of $400,000. You can only keep that ceiling of $400,000 from being punctured by periodically paying out dividends to keep reducing it. If you start paying out dividends you are paying out the cash you want to use in your business operations.

Mr. Stewart: The point is that with this proposal contained in our brief, the suggestion is that through the provision of accelerated write-off—

The Chairman: Well, I am just addressing myself to the small business concept. Accelerated write-off would give you cash without affecting your accumulation of earnings.

Mr. Stewart: You still have to earn the cash initially to make your investment.

The Chairman: Yes.

Mr. Stewart: Once you get started on this path it facilitates the healthy growth of the business.

The Chairman: So it would appear that for your industry the proper concept would be one that dealt with your situation and the peculiarities of your situation by adequate write-offs.

Have you any comment on that, Mr. Poissant?

Mr. Poissant: This was one of the comments, Mr. Chairman, which I was going to make.

Hon. Mr. Phillips: Mr. Chairman, if I may, this committee, in dealing with the White Paper on Taxation, took the position that in so far as small businesses were concerned accelerated depreciation was not the road to provide the relief. That is at page 82 of our Appendix.

The Chairman: That is for small businesses.

Hon. Mr. Phillips: Yes, for small businesses.

The Chairman: We said the reason for it was they did not have a great quantity of fixed assets to depreciate.

Hon. Mr. Phillips: That is why I am drawing attention to that. You make the statement which is confirmed by our report.

The Chairman: Yes.

Senator Connolly: Is it correct to say, then, Mr. Chairman, that what the witnesses are talking about not only relates to small construction businesses, but that they are also interested in faster write-offs for a company in the construction industry?

The Chairman: Yes.

Senator Connolly: So that the small business is only a certain segment of their interest.

The Chairman: That is right. That is correct, is it not, Mr. Stewart?

Mr. Stewart: That is right. This would apply across the board, but it would have, we feel, particular significance for the smaller developing companies where the development of working capital is slow at the best of times, and any incentive that can be provided here will lead to development of what we consider would be stronger and more effective construction companies.

Senator Connolly: Mr. Chairman, once that $400,000 level is punctured, then you are in that other category.

The Chairman: Yes, in the small business area this would not help very much because once you get up to the $400,000 level the lower corporate rate is gone and you have to pay out dividends to reduce that $400,000 in order to recover that position again.

Senator Connolly: And impair your cash position.

The Chairman: That is correct. Then what they have to do is to turn around and loan the money, take the money out in dividends, pay taxes, and then loan it to the business. The general theory, when we were dealing with small businesses before, was that they were in the peculiar position where they had to generate their own finances. This would appear to be a broad application to the whole construction industry because they do not have the same market availability to finance construction operations. Therefore they have to generate their own finances in whatever ways they are able. Higher write-offs, if you could justify them, would help their situation. I am sorry for taking over, Mr. Stewart.

Mr. Poissant: Mr. Stewart, this additional or accelerated depreciation that you are talking about will still not be sufficient, in my mind, to make up for the reduced $400,000, because that would only be the tax on the additional depreciation which you would be entitled to, or which you would have the benefit of. That is really a very small item in the construction industry. Let us take for granted that this is an acceptable recommendation. In my mind it is not enough to suffice for the need which you have. My question is, what would you suggest to improve this $400,000 limit in your case?

Mr. Stewart: I feel that the immediate answer would be to increase the level to $500,000 or $600,000, something of this nature.

Mr. Poissant: That is, across the board?

Mr. Stewart: Yes. Perhaps, we are being a little naive in our approach, but the Canadian Construction Association has always tried to take the attitude that we should not be unreasonable or unrealistic. Unfortunately, taxes are with us and someone has to pay them to provide revenue. This is the level that has been deemed appropriate, and it is being suggested as an arbitrary figure of $400,000. We have not presumed that we are in a position to say that it should be increased 20 per cent or 50 per cent; but if this applies across the board, the accelerated write-offs on certain categories of equipment would tend to offset some of the disadvantages under which the construction industry is working. It is a case of trying to improve or offset the particular disadvantages relating to the construction industry because of the heavy investment in fixed assets and the difficulties that are experienced in raising working capital. As the chairman has indicated, because of the high risk nature of the industry there are not too many public companies, or very many bonds floated or common stocks issued.

The Chairman: Mr. Stewart, the accelerated write-off would enable the smaller construction company to stay at the lower corporate rate for a longer period by keeping it under the $400,000 of accumulated earnings.

Mr. Stewart: Yes it would; and the accelerated depreciation is also an incentive to all companies, both large and small, to maintain more current equipment. You have probably observed as well as I have the number of new machines that you see in the earth-moving industry, large hydraulic shovels, back-hoes, elevating scrapers, heavy dozers equipped with rippers—all of these are made possible because of the accelerated depreciation provided under class 22. There is greater incentive to turn in obsolete pieces of equipment and get newer ones to produce more effectively. This is one of the things that has enabled this section of the construction industry to maintain its position much more competitively than—

The Chairman: You are not arguing against yourself by saying that class 22 and the 30 per cent write-off has improved the situation in the industry already?

Mr. Stewart: It has improved the situation considerably, I would say. It has improved the effectiveness; and this is reflected in the fact that the industry has been able to hold its costs in the face of rising labour costs. What we are suggesting is an extension of this idea to other categories of equipment which are susceptible to actual accelerated depreciation which should also be recognized.

Mr. Poissant: And you do not lose the benefit that you already have from the small business deduction which you would lose in the future.

Senator Molson: Do not most of the smaller construction firms rent the bulk of their machinery on which they might expect a decided benefit from the accelerated depreciation?

Mr. Stewart: Senator, they are in a mixed position. Yes, there are companies that will be renting. My own company is by no means large and we are in a mixed position. We did purchase a sizable quatity of equipment under the acclerated rate. We have purchased new units this year, and we are also renting equipment this year in this category.

Senator Connolly: And the rent you just charge up as an expense?

Mr. Stewart: Yes, this is a business expense.

Senator Cook: But you pay for the depreciation through your rent; your rent is set?

Mr. Stewart: Yes, it is a fixed monthly rental, and that is a total cost.

Senator Cook: The owner sets the rent, bearing in mind he is going to write off the equipment.

Mr. Stewart: Yes, that is right. There is a balance. It is a matter of foresseeing how much use can be made of a piece of equipment.

Senator Molson: This would be the same situation with most companies. They would be in a mixed position, with partly owned, and partly rented equipment.

Mr. Stewart: Yes, we are in that position right now. We have had a particular piece of machinery on rental for four months, and we have it on a basis where we can make application of certain rentals towards the purchase. But we have to ask ourselves: Is there going to be enough work, and can we gamble on this? But this is a problem that anyone in business faces, balancing the capital investment versus the rental operation.

The Chairman: In summarizing, an accelerated rate on the type of equipment that you have been talking about in the construction industry could possibly help in two ways. It could help those who are small business operators by keeping them under the $400,000 ceiling for a longer period, or for an indefinite period, and they would get the benefit of the lower rate; and generally, for the industry, it would increase their cash flow.

Mr. Stewart: And provide incentive to maintain a more efficient operation.

Senator Cook: You could have a piece of equipment that still has life left in it but, because it is obsolete, you could discard it and get new equipment.

Mr. Stewart: Yes. This has been done in the past where, before the accelerated write-offs under class 22 came into effect, it was shown that the contractors were spending a very sizable amount of money on equipment repairs as opposed to equipment replacement; and with the advent of the accelerated depreciation it became more attractive to buy equipment and take the higher depreciation allowed.

Senator Cook: Plus the fact that you would be using up-to-date equipment instead of obsolete equipment.

Mr. Stewart: Yes.

Senator Isnor: Dealing with Senator Molson's question about the rental of machinery, up to the present time you have been arguing this point with regard to the larger companies, have you not?

Mr. Stewart: I think this applies to all companies, Senator Isnor. The smaller companies rent equipment as well as the larger ones. Perhaps with the lack of working capital some of the smaller companies may be compelled to rent because they cannot afford to buy, not having the cash to purchase fixed assets.

Senator Isnor: But the bigger companies, for which your argument is largely presented, do have the cash available.

Mr. Stewart: I think you will find that this applies right across the board. The benefits will increase, certainly, for the larger companies merely because of the volume of purchases. The larger companies may obtain more dollars out of an expansion of the accelerated write-off position, but this is of less significance to them than it is for a small man attempting to finance his first purchase of a piece of equipment.

The Chairman: Do not forget, Senator Isnor, that the smaller companies which would fit into the small business category, by accelerated depreciation may be able to stay longer under the limitation on accumulated earnings and enjoy the 25 per cent rate of tax, whereas the bigger company would be paying 51 per cent.

Senator Isnor: That does not enter into this question of rental very much.

The Chairman: I am not speaking of rental, which is another aspect entirely. Equipment is rented because it cannot be purchased.

Hon. Mr. Phillips: Mr. Chairman, I would like to press my point. If we were to ask for relief for the construction industry at large, there might be the situation of a construction company having a small portion of its assets in fixed assets, and we would still be asking for an accelerated depreciation simply because it happens to be in the construction business. I believe that would be a good way to have our recommendation refused. If the request for accelerated depreciation were made for the construction industry, not on a functional basis, that is to say not for every company engaged in the construction business but, rather, for companies engaged in the construction business whose capital assets in relationship to their total assets equal or exceed a percentage, there would be a much stronger case.

There could be an extraordinary situation of a construction company functionally that has $100,000-worth of assets, $10,000 in fixed assets and still asks for accelerated depreciation simply because it is in the construction business. If the request were made having regard to the ratio of fixed to total assets, I personally believe there would be a case.

Mr. Sandford: Certain sectors of the construction industry are more capital-intensive than others. The roadbuilding and heavy construction side of it would benefit more from that proposal, whereas a business in the nature of general contracting, not so capital-intensive, would have the same problems with regard to cash flow.

I think your suggestion is that we should produce an alternative that would help all our companies. However, we cannot think of any other than, as Mr. Stewart said, raising the level. However, to tie it to those specifically that have a fixed asset at a certain level might jeopardize some of the other members of our industry who are not in this position.

Hon. Mr. Phillips: You might jeopardize them to the extent that you are not rendering a service to them as members, but you are improving your base.

The Chairman: The accelerated depreciation under discussion is in relation to the equipment and fixed assets of bricks and mortar. Really where they are seeking relief and assistance seems to be in the equipment area.

Hon. Mr. Phillips: I was thinking of fixed assets in relation to the categories we are discussing.

Mr. Poissant: Mr. Phillips is saying that the same companies are now not buying equipment, but just renting. They would have no relief, and they say this only partly solves the problem of the construction industry, if some have no equipment whatsoever. A ratio of heavy equipment to total assets would perhaps be a criterion for a solution.

Senator Molson: I do not often question Mr. Phillips' opinion on matters. However, I have to question him on this because I wonder if stressing the percentage of assets

and fixed assets and equipment would tend to increase unemployment. It seems to me that the construction industry needs relief with regard to some of the settlements that have been made, more than it does in the equipment field. The settlement with the crane operators recently was perhaps a source of some concern to them. However, if we say they must have a high proportion in fixed assets, then presumably this will result in greater mechanization, which will reduce the labour content and therefore increase unemployment.

The Chairman: It might increase the labour content which is required to produce that equipment.

Senator Molson: The heavy equipment, by and large, I think I might say, is mostly not produced in Canada. I am afraid that that is very largely imported. Am I not correct, Mr. Stewart?

Mr. Stewart: There is a high import rate, but there is an increasing percentage produced in Canada.

Senator Molson: It is still very small, is it not?

Mr. Sandford: Perhaps other incentives to the producers would help here, because certainly the labour problems increase the need for mechanization.

The Chairman: Mr. Stewart, would you care to put in summary form what it is that the construction industry is requesting in this area of acceleration and what you hope to achieve?

Mr. Stewart: It is basically set forth in page 5 of our brief. That contains the categories we are discussing and our feeling that the extension of accelerated depreciation to these categories of equipment would be of benefit to the construction industry. It would give a particular advantage to small businesses in construction operations, where the requirements for capital investment and working capital are more pressing than in other phases of business.

I will just mention another item in the current legislation that is of some concern to us. It relates to Joint Ventures; reference is made to it in the brief. Under the new legislation, joint ventures are considered as partnerships, and there are new approaches for the taxing of partnerships.

It presents problems which have not existed in the past, where two or more construction companies may see fit to join forces to undertake a particular project, where financial problems or undue risk associated with the project might be too great for one company.

It has worked effectively. It has been a rather loose and flexible arrangement. From readings that we get on the new legislation, it will tend to restrict, hamper and place additional costs on anyone contemplating future joint venture operations.

Senator Cook: Would the witness mind telling us if the great benefit to the construction industry will also benefit Canada? We are going to do something that will benefit the construction industry. What is in it for us?

Mr. Stewart: I almost wish the honourable senator had given me this question deliberately, because I could launch into a speech on this subject.

In all seriousness, the construction industry is the largest single industry in Canada. It accounts for 18 per cent of our Gross National Product. Everything that the construction industry does affects other Canadians—the local school rate resulting from the cost of building a school, all the utilities, serivces, hydro electric plants, natural gas pipelines, and so on. Anything that the construction industry can do more effectively, or more efficiently, benefits the whole country. This is the situation in a nutshell.

Senator Lang: How many employees are there in the construction industry?

Mr. Stewart: It has been estimated that there are 568,000 on site and over 600,000 in off-site supporting industries such as manufacturing, design, transportation of constructing, materials, and so forth.

The Chairman: That is an important segment.

Mr. Stewart: If the construction industry is not healthy and not working effectively, the whole country suffers.

The Chairman: Mr. Stewart, would you now care to move on to your next point? Have you finished with joint ventures?

Mr. Stewart: We would like to see something that would exclude short-term joint ventures that are undertaken solely for the execution of a single project, as is common in the construction industry.

Senator Connolly: To be excluded from the partnerthip rules?

Mr. Stewart: Yes. As we see it, the partnership rules were designed basically to cover groups of professionals, possibly in the legal or accounting fields, in architectural operations, or something of this nature, and not to cover the joint effort of two or more construction companies to undertake a specific project which cannot be practically undertaken by any one of them.

The Chairman: In the course of our study of this bill we had the assistance of a gentleman who had made a considerable study of it. He expressed the opinion that a joint venture was not defined in the bill and that it was not a partnership.

Mr. Stewart: May I say, as a poor contractor, that I would not for a moment question the rulings or interpretations you have received. I only hope they are right.

This is a case which emphasises a remark that I was going to make, namely that there are many items in the bill that are not clear to many people—people who are far better trained in the subject than I am.

I know that the concern which has been expressed throughout the country has been repeated within our industry. There are all kinds of problems. I do not think the department itself really knows what is involved. They may know what they intend. In view of the amendments that are currently being considered, or are being introduced, and the various problems that are bound to arise in the interpretation and implementation of the legislation, we in the industry have grave doubts as to whether it is practical to consider its implementation on January 1, 1972.

There is a high percentage of small companies in the construction industry. I have attended a couple of tax seminars by so-called experts on the implications of the new legislation. I think that I have, perhaps, an average appreciation of economics, finance, and what-have-you; but I am hopelessly lost, and I know there are a lot of contractors who are no better than I am.

The Chairman: Do not say "hopelessly lost," Mr. Stewart. We may find some way out of the morass, or whatever you want to call it.

Mr. Stewart: The ideas are good, but there are so many complications that will have to be interpreted by the department and explained to all the firms of auditors and corporate accountants.

In the case of major companies this may not be too bad, because they have specialists who are quite competent in this field. However, we have a tremendous number of small companies associated with the construction industry in this country, who have an accountant, so-called, who is not a chartered accountant. He has had no taxation training. To attempt to introduce a new system of bookkeeping, a cost accounting system, and one thing and another, to meet the requirements of the new legislation, appears to us to present all kinds of practical problems.

The Chairman: Mr. Stewart, I should tell you that some of us have come to the conclusion that although there is a good deal of complexity in Bill C-259, there are many things which appear, after repeated readings, to be very beneficial.

Mr. Stewart: I do not think I would argue that point. You say "repeated readings". That is an operation that we are going through now, as I see it.

The Chairman: That is right.

Mr. Stewart: The chairman of our taxation committee could not be here today because his company is currently involved in the re-assessment of its position in view of the implications of the bill, in trying to meet the situation, to cope with it, to fit their operations into it, and everything else.

These are all practical problems. Let us multiply them by the number of companies that are affected. I cite construction because that is the field which we represent. You are all familiar with the number of small operators, from the two- or three-man operation to the 10-, 20- or 50-man operation. How can you expect people of this type to conform to the new legislation practically and effectively? With all due respect, the firm meaning and interpretation of the bill has still to be settled.

The Chairman: Apropos that point, in a publication put out by the Clarkson, Gordon Company entitled *Tomorrow's Taxes*, there is a chapter on partnerships, and a general summary of it, which conforms with your own thinking.

Paragraph I.5 states:

> The proposed legislation does not introduce a definition of a partnership. With the introduction of new rules that are considerably more comprehensive and complex than before, it will become even more important to determine whether a partnership does, in fact exist. This issue will become critical, for example, in determining whether a particular joint endeavour or joint venture constitutes a partnership and as a consequence whether property transferred to or from such a venture will be subject to the new rule that treats such a transfer of property as a sale at fair market value, resulting perhaps in taxable capital cost allowances. In such circumstances it will be highly desirable that competent legal advice be obtained to determine the status of the undertaking, preferably in advance of completing contemplated transactions.

Mr. Stewart: It does present one more possible complication, and the suggestion that competent legal counsel be consulted on the matter is good advice, but if everyone else in the country is trying to obtain the same competent legal counsel for advice on the implications of the tax changes between now and the end of December, there is going to be a bottleneck.

Senator Cook: The problem is further complicated by the fact that the learned counsel will have no jurisprudence to go by. They are starting a new act now.

The Chairman: Well, of course, you would have a starting point on partnerships, I would expect, in the provincial Partnerships Act.

Senator Cook: I hope so.

Senator Connolly: What you say, then, is that for all practical purposes it is going to be virtually impossible to get the new system running by January 1st. Have you any suggestions to offer the committee as to detail assuming that the new system is to be brought into effect at that time?

Mr. Stewart: When the legislation is passed we would like to see some period—I do not know what the magic number is; three months, four months, six months—

The Chairman: Or a year.

Mr. Stewart: Some period of time during which there could be adequate publication of the legislation, the development of any regulations that might relate to it, the explanation of any areas that are not clear, and a general educational period whereby businesses could find out what they are supposed to do and how they are supposed to operate. The sudden introduction of new legislation when the people are not prepared for it—and perhaps they should be prepared for it—and when they are not aware of how they are to conduct their affairs to comply with the new legislation, seems to me to be an invitation to chaos.

The Chairman: Mr. Stewart, are there not some aspects of a joint venture that might distinguish that type of operation from a partnership? You have a joint venture when two construction firms undertake a project which they might feel was too big for either one of them to undertake alone. Now, what are the aspects of that in connection with how they would go about laying down their rules of operation? Neither one loses its separate entity. Is that right?

Mr. Stewart: They both retain their separate entities. They simply agree to work together during the course of a

particular project and there is some agreement as to the assumption of responsibilities and, presumably, shares in the profit or loss.

The Chairman: You can see a real difference between that and a legal partnership or an accounting partnership.

Mr. Stewart: It is our feeling that they represent quite different fields of operation, and this is why the suggestion has been made that there should be a definition. You could probably arrive at words that would cover the situation, but it is basically for a short term specific project as opposed to a continuing operation designed to cover the affairs of the business.

Senator Haig: Mr. Chairman, is it not sometimes called a consortium?

Mr. Stewart: It could be, yes.

Senator Haig: A group of companies get together to handle a specific project and they enter into an agreement as to the work to be done and the sharing of the profits or losses.

Mr. Stewart: It usually applies to, or is particularly appropriate to major engineering projects where the physical size of the work is beyond the capacity of any one company, or where the degree of risk is such that even if one company did have the physical capacity to undertake the work it would necessitate putting all of its capacity on this one job. Under those circumstances you would have two, three, four, or even five companies pooling their resources. This has happened on some of the major dam projects in British Columbia where the scope of the work was beyond the capacity of any one company.

The Chairman: Mr. Stewart, just pursuing that for a moment. In an ordinary business partnership individuals get together and they decide to carry on a business on a continuing basis, and so they form a partnership. But with a joint venture, two or more companies get together and pool their capacities on a specific project. It is not a continuing arrangement; it has a termination date. It seems to me that there are essential differences and they should be able to work out some definition. I agree that it is hopeless to leave this bill without a definition of partnership because the incidence of liability is great.

Senator Lang: In a joint venture, Mr. Chairman, the two contractors at the same time each enter into a contract with the contractee, do they not, whereas in a partnership the persons joined together do not enter into separate agreements with a third party?

The Chairman: Yes, that is right.

Senator Beaubien: Could we arrive at a definition that would suit the situation, then?

The Chairman: It is practicable to work out a definition, but, equally, it is absolutely necessary that there should be one.

Senator Beaubien: What was done, Mr. Stewart, on the Seaway? A number of companies got together—Iroquois Constructors, and so forth. Did they form separate companies, or—

Mr. Stewart: There were a number of separate contracts and also a number of joint ventures.

Senator Beaubien: Did they form partnerships?

Mr. Stewart: It was usually a joint venture, to the best of my knowledge.

You can have the procedure of creating a separate company for a specific project, but there are disadvantages to this in so far as liability for other people is concerned who may have business with that body. With a joint venture the two or more partners in the joint venture have a continuing liability and responsibility, and this is considered to be in the public interest.

Senator Burchill: Mr. Stewart, has the minister been made aware of the points you are raising before us this afternoon?

Mr. Stewart: Through discussions and representations to Mr. Mahoney, his parliamentary secretary.

The Chairman: Are there any other questions?

Mr. Poissant: Mr. Chairman, I am just wondering that once a partnership is defined in the Income Tax Act, would it be agreeable if a joint venture were regarded as a partnership? Or, in the alternative, there could be an election under the Income Tax Act whereby they could elect to be considered to be not subject to the partnership rule and, therefore, be taxed on their share of income of the joint venture. Would that be a satisfactory solution? The partnership rule remains, but if they wished to embark on a partnership arrangement for a specific project where it might be beneficial to them to do so, they could, with the permission of the minister, be taxed on the share of the income from the joint venture and not as a partnership.

Mr. Sandford: I feel that it would be reasonable, as long as it is clear and understood that they have to make an election. Otherwise, they will get caught.

Mr. Poissant: Yes, we do not have to change a rule, and we do not have to define whether it is a joint venture, or if it is a partnership or not. It is merely a case of two people wanting to explore together such new resources, whether it be for this purpose or for that, and we are asking permission to consider this, not as being a partnership for tax purposes, but as our sole business.

Mr. Sandford: If that were a right rather than a benefit decreed by the minister, I think it would be good; and you might have some definition then as to who could make such an election.

Mr. Poissant: In a joint venture, as the Chairman was saying before, in a continuous partnership there is no such provision, but in a joint venture it is one single transaction.

The Chairman: It is a right of election.

Mr. Sandford: Yes, a right of election.

The Chairman: A right of election to take yourself out of whatever may be the benefits in the partnership relationship.

Mr. Cook: You might run into the situation where one would make an election and the other would elect something different.

The Chairman: I do not think they would enter into a joint venture then.

Mr. Sandford: There are problems such as this. If they should happen to get into a partnership, they have to make certain elections in regards to capital cost allowances. One may have a nice profit or a loss that he is carrying forward, and the other may not.

Senator Cook: That could cause a conflict.

Senator Isnor: Mr. Chairman, before we leave this, would you consider the term "equipment", a fixed asset or another term for income tax purposes?

Mr. Stewart: On page 5 of the brief, we identify certain types of equipment which we feel might well be added to the present list of equipment in class 22. These are fixed assets.

The Chairman: You mean they are fixed, of the freehold?

Mr. Stewart: No, they are not fixed, of the freehold. They are moveable, but they are classified for accounting purposes as fixed assets.

The Chairman: Are there any other questions? Have you anything further you want to add?

Mr. Chutter: Mr. Chairman, there was one point with regard to Hon. Mr. Phillips' initial question relating to reporting on the income tax form. He asked whether the Department of National Revenue did not offer certain indulgences in the reporting of income on a completed contract basis; and I think this is one of the main points the Association would like to stress.

So far as I can remember, throughout the whole postwar period, the Department of National Revenue has allowed the contractor, as an administrtive practice, to report on the completed contract method for lump sum contracts up to two years' duration. This has worked well, and is used by approximately half of our members. It has worked well so far as we know for the department. It has been an administrative practice now for 20 years or more. The only problem from our standpoint is that it has no legal status, and in the event of a dispute over assessments, there is no right of appeal because there is no legal basis for this administrative practice. What our interested members would dearly like to see, I feel, in the interest of equity and regularity, is to have this administrative procedure, which has been in existance for a couple of decades or more, and is in the United States law, confirmed by being given legal status in our own Income Tax Act, and extended to stipulated unit price contracts. Right now it is restricted, in practice, to lump sum contracts.

The Chairman: You have attached an appendix to your brief.

Mr. Stewart: Yes, sir.

The Chairman: And this is your concept of the language that you would like to have changed from administrative practice to gain statutory support.

Mr. Chutter: Yes, this was prepared last year before the bill to amend the Income Tax Act came out. Basically, this would be the proposal from the Association as to the possible wording.

The Chairman: The Department of Finance would also be in possession of this wording?

Mr. Chutter: Yes, this was filed not only with your committee, but with the Department of Finance, the Department of National Revenue, the Department of Justice and anybody else who might be interested.

Mr. Poissant: Mr. Chairman, on this very point, the department recognizes the common practice on the completed contract method but yet in your recommendations, Appendix G—and I agree with you by the way, you are asking for the holdback as well, am I correct? You are asking for the complete contract, and are you not asking in 3(*a*) on page 2 of this appendix that the holdback be given as well?

Mr. Sandford: The reason that is in there is because we are anticipating what action the Government might take on this bill, and what we are trying to do is legalize the *Colford* decision if they should come along with some amendment.

Mr. Poissant: I agree with you entirely. I had a case like this in the department. But your brief does not stress that. It merely says the Government recognizes this method of administrative practice. Yet I think, legally speaking, you are entitled to the holdback at the end of any year.

Mr. Sandford: As we understood it, the Bill did not upset this decision. That is the professional advice we obtained.

Mr. Poissant: Is there a recent judgment on that?

Mr. Sandford: The *Colford* decision has not been upset, so that means we still have it to rely upon.

Mr. Poissant: I know. That should be stressed in your brief that you should be entitled to the holdback, because that is what you are asking in your appendix.

The Chairman: Would you please write us a note specifically dealing with that, since the issue has been raised?

Mr. Sandford: Yes, our whole appendix presupposes this situation. We do not ask for what is in the United States law on completed contracts on jobs of two years' duration, but that the final determination on tax be left until the job is completed and all the results are in.

The Chairman: You want this on a completed lump sum basis, and also on a complete unit price. Anything else?

Mr. Sandford: Mr. Chairman, I think that is all.

The Chairman: We have enjoyed your appearance and your representations here today, and for the manner in which you answered the questions.

Mr. Stewart: That is very kind of you, sir. On behalf of the Association, I can only say we have appreciated the opportunity of presenting our case and trying to explain why we are concerned about the bill's implications to construction in Canada.

The Chairman: Thank you very much.

Now gentlemen, before we adjourn, I should tell you what we have for tomorrow. Tomorrow we will meet in Room 356-S at 9.30 a.m. We have three different groups—the National Association of Canadian Credit Unions, the Co-operative Union of Canada, and the Allstate Insurance Company of Canada. And I should point out to you, in case you are making plans for a week ahead, the following week on Wednesday and Thursday, the 20th and the 21st, we have the Canadian Jewish Congress, and Massey-Ferguson Limited. Massey-Ferguson, I take it, will involve international revenues.

Senator Beaubien: And this will be in the afternoon?

The Chairman: No. I am attempting to fit in Alcan Finances also next Wednesday.

Senator Beaubien: They are down for the 27th.

The Chairman: I know, but it would be convenient if we could hear them when we are discussing a similar question, relating to international income, with Massey-Ferguson. In that case we may enlarge to three hearings on Wednesday, October 20.

On Thursday, October 21 we have a very important group, the Canadian Bar Association. Their hearing has been scheduled to start at 9.30 a.m. Later in the day we will hear the Independent Petroleum Association.

We are endavouring to hear some of the important aspects which we discussed when we were "going to school" to learn about the bill.

Senator Beaubien: I will not be here during the morning of the 20th. If Alcan could be set down for the afternoon it would suit me better.

The Chairman: Depending on how long the Canadian Jewish Congress takes—I know the points involved—we might hear both the Congress and Massey-Ferguson on Wednesday morning and schedule Alcan firmly for the afternoon. I think we can safely say Alcan will appear next Wednesday afternoon.

We will adjourn until tomorrow morning at 9.30.

The committee adjourned.

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THIRD SESSION—TWENTY-EIGHTH PARLIAMENT

1970-71

THE SENATE OF CANADA

PROCEEDINGS

OF THE

STANDING SENATE COMMITTEE ON

Banking, Trade and Commerce

The Honourable SALTER A. HAYDEN, *Chairman*

No. 41

THURSDAY, OCTOBER 14, 1971

Fifth Proceedings on:

"Summary of 1971 Tax Legislation"

(Witnesses:—See Minutes of Proceedings)

24264—1

THE STANDING SENATE COMMITTEE ON BANKING, TRADE AND COMMERCE

The Honourable Salter A. Hayden, *Chairman*

The Honourable Senators,

Aird	Grosart
Beaubien	Haig
Benidickson	Hayden
Blois	Hays
Burchill	Isnor
Carter	Lang
Choquette	Macnaughton
Connolly (*Ottawa West*)	Molson
Cook	Smith
Croll	Sullivan
Desruisseaux	Walker
Everett	Welch
Gélinas	White
Giguère	Willis—(28)

Ex officio members: Flynn and Martin
(Quorum 7)

Order of Reference

Extract from the Minutes of the Proceedings of the Senate, September 14, 1971:

"With leave of the Senate,

The Honourable Senator Hayden moved, seconded by the Honourable Senator Denis, P.C.:

That the Standing Senate Committee on Banking Trade and Commerce be authorized to examine and consider the Summary of 1971 Tax Reform Legislation, tabled this day, and any bills based on the Budget Resolutions in advance of the said bills coming before the Senate, and any other matters relating thereto; and

That the Committee have power to engage the services of such counsel, staff and technical advisers as may be necessary for the purpose of the said examination.

After debate, and—

The question being put on the motion, it was—

Resolved in the affirmative."

Robert Fortier,
Clerk of the Senate.

24264—1½

Minutes of Proceedings

Thursday, October 14, 1971.
(49)

Pursuant to adjournment and notice the Standing Senate Committee on Banking, Trade and Commerce met this day at 9:30 a.m. to further examine:

"Summary of 1971 Tax Reform Legislation".

Present: The Honourable Senators Hayden (*Chairman*), Beaubien, Blois, Burchill, Carter, Connolly (*Ottawa West*), Cook, Desruisseaux, Flynn, Gelinas, Isnor, Lang, Macnaughton, Molson, Smith and Walker—(16).

Present, but not of the Committee: The Honourable Senator Bourget—(1).

In attendance: The Honourable Lazarus Phillips, Chief Counsel; Mr. C. Albert Poissant, C.A., Tax Consultant.

WITNESSES:

National Association of Canadian Credit Unions:

Mr. George May, Chairman, Tax Committee and General Manager of the B.C. Central Credit Union, Vancouver;
Mr. Kenneth Weatherley, President of the Ontario Credit Union League and Executive member of NACCU, Ottawa;
Mr. Frederick Graham, Chartered Accountant, Campbell, Sharp, Nash & Field, Vancouver;
Mr. Joseph J. Dierker, Legal Counsel, Francis, Gauley, Dierker & Dahlem, Saskatoon;
Mr. Andre Morin, Director, Research Department, La Federation des Caisses Populaires Desjardins, Levis, Que.;
Mr. Raymond Blais, Director, Technical Services, La Federation des Caisses Populaires Desjardins, Levis, Que.;
Mr. Robert J. Ingram, General Manager, National Association of Canadian Credit Unions, Toronto.

Co-Operative Union of Canada:

Mr. Breen Melvin, President;
Mr. Joe Dierker, Solicitor;
Mr. Martin Legere, President, Le Conseil Canadien de la Cooperation;
Mr. Richard Newberry, Controller, Co-op Federee de Quebec;
Mr. R. H. D. Phillips, Research Director, Saskatchewan Wheat Pool;
Mr. Ed. Chorney, Treasurer, United Co-operatives of Ontario;
Mr. John R. Moore, Treasurer, Maritime Co-operative Services;
Mr. T. Pat Bell, Treasurer, Federated Co-operatives Ltd.;
Mr. G. L. Harrold, President, Alberta Wheat Pool;
Mr. J. A. Dionne, President, Federation des Magasins Co-op.

Allstate Insurance Company of Canada:

Mr. John Atkinson, President & Managing Director;
Mr. Donald J. McRae, Financial Controller;
Mr. Michael G. Welch, Tax Supervisor.

At 12:25 the Committee adjourned to the call of the Chairman.

ATTEST:

Frank A. Jackson,
Clerk of the Committee.

The Standing Senate Committee on Banking, Trade and Commerce

Evidence

Ottawa, Thursday, October 14, 1971

The Standing Senate Committee on Banking, Trade and Commerce met this day at 9.30 a.m. to give consideration to the Summary of 1971 Tax Reform Legislation, and any bills based on the Budget Resolutions in advance of the said bills coming before the Senate, and any other matters relating thereto.

Hon. Salter A. Hayden (*Chairman*) in the Chair.

The Chairman: Honourable senators, this morning we have three groups making submissions: the National Association of Canadian Credit Unions, the Co-operative Union of Canada, and Allstate Insurance Company of Canada.

We have moved to this committee room this morning because some of those making submissions may wish to make them in French. We have the simultaneous translation system working, so that will facilitate the hearing.

The first group is the National Association of Canadian Credit Unions. I have been furnished with a list of the members attending; and they are: Mr. George May, Chairman of the Tax Committee and General Manager of the B.C. Central Credit Union, Vancouver, B.C.; Mr. Kenneth Weatherley, President of the Ontario Credit Union League, and Executive Member of NACCU, Ottawa; Mr. Frederick Graham, a Chartered Accountant with Campbell, Sharp, Nash & Field, of Vancouver; Mr. Joseph J. Dierker, Legal Counsel of Messrs. Francis, Gauley, Dierker & Dahlem, Saskatoon; Mr. Andre Morin, Director, Research Department, La Fédération des Caisses Populaires Desjardins, Levis, Quebec; Mr. Raymond Blais, Director, Technical Services, La Fédédation des Caisses Populaires Desjardins, Levis, Quebec; Mr. Raymond Blais, Director, Technical Services, La Fédération des Caisses Populaires Desjardins, Levis, Quebec; and Mr. Robert J. Ingram, General Manager of the National Association of Canadian Credit Unions, Toronto.

I take it those are the appearances. Who is going to make the first presentation?

Mr. George May, Chairman of the Tax Committee, National Association of Canadian Credit Unions: Mr. Chairman, I shall. Perhaps Mr. Dierker might join me. He is our legal counsel. In addition, from time to time, I would like to call on our technical advisers.

The Chairman: Yes, we do not have room for all of them up here, but they will be available. Do you wish to make an opening statement?

Mr. May: Yes, if I may. I would like to put on record two additional members of our delegation who are important to our submission and will probably make a contribution during our hearing today. Mr. Paul E. Charron, General Manager of La Fédération des Caisses Populaires Desjardins is with us; along with Mr. Ives Lamothe, Technical Services, La Fédération des Caisses Populaires Desjardins.

Mr. Chairman, in introducing our submission to the Senate, may we first express our appreciation for the previous report of the committee regarding our earlier appearance before you. We appreciated your comments to the Government on our position.

We should also at the outset like to take cognizance of the amendments produced in the House of Commons yesterday respecting the tax bill, and particularly our position in relation thereto. As you might expect, we have not had much opportunity to analyze these amendments and their effect on the position of the credit unions.

The Chairman: We are in the same position; we have not had an opportunity to view the amendments, and they will not be available until approximately 10.30 this morning. Therefore we are dependent on the newspaper report, and you will have to tell us whether that agrees with your understanding of the effect of the amendments.

Mr. May: We will endeavour to do that. There are some areas which were not included in the amendments, which we interpret from the newspaper report, mainly, and our attendance in the house to hear some parts of the actual presentation. We would like to comment specifically on these, as they will now constitute the key issues with relation to the position of the credit unions and the tax bill.

There are two basic issues in this area. I would like to comment on the amendments and these two basic issues which were not dealt with specifically in the amendments introduced yesterday and call on our legal counsel, Mr. Joseph Dierker.

Mr. Joseph J. Dierker, Legal Counsel, National Association of Canadian Credit Unions: Mr. Chairman, we have had the opportunity of reviewing briefly the actual wording of the amendments, in addition to seeing the newspaper report. We will do so, as they have been presented in the House of Commons.

A review of the amendments which have now been proposed by the Government reveals two areas of concern to credit unions and caisses populaires. First is the area of permitted business activity of credit unions and

caisses populaires. The initial draft of clause 137 contained a very serious restriction as to the investments a credit union might make. It was allowed basically loans to members or investments in prime government bonds in the sense of Government of Canada and governments of provinces. This has been modified to permit investment in municipal and secondary government bonds. Credit unions and caisses populaires are, however, concerned about the nature of that definition.

Clause 189, in effect, provides for a penalty tax for monies invested in ineligible investments.

Clause 125 provides for a low rate of tax, basically 25 per cent. This, with some modifications, should be available to credit unions. The Government indicates that they will be introducing some proposals to make this more applicable to credit unions. In that regard we do not have the amendments.

However, we are concerned with respect to the definition of the investments that a credit union can make. If a credit union makes investments other than those specifically defined in that section, a reviewing officer acting for the Department of National Revenue could well construe it as being an ineligible investment under clause 189, in respect of which the credit union would have to pay tax.

We find it a little peculiar that credit unions and caisses populaires should be subject to tax, as other financial corporations, but that there should be a specific provision written into the section defining the investments they can make.

Basically we would like to see provision in the act for a credit union or caisse populaire to carry on a full financial business and exercise the investment powers given under its act of incorporation.

Senator Connolly: Are you referring to clause 189(4)(*b*)?

Mr. Dierker: I do not have the act in front of me.

The Chairman: Clause 189(4)(*b*) deals with ineligible investments. Is that the clause?

Mr. Dierker: Yes, clause 189(4)(*b*) refers to property that was not acquired for the purpose of gaining or producing income from an active business. I am concerned that when this is related to the provision in clause 137 which indicates where a credit union may invest its money which, as I say, is now defined to be government bonds and secondary government bonds, it will be interpreted as being the business activity of a credit union and caisse populaire.

The Chairman: Clause 137 also runs into a number of subclauses; to which are you addressing yourself?

Mr. Dierker: Clause 137(6)(*b*). You will note that in the initial draft of Bill C-259 basically the investments could be only in bonds guaranteed either by the Government of Canada or of a province. This has been modified in the amendments brought down yesterday to include municipal bonds and public bonds.

Senator Connolly: Is that amendment made to clause 137(6)(b)(i)(A)?

The Chairman: We have not yet seen the amendments.

Mr. Dierker: The proposed amendment is to clause 137(6)(b)(B).

Senator Connolly: (i)(B)?

Mr. Dierker: That is correct.

Senator Connolly: Which now reads:

> bonds of, or guaranteed by, the Government of Canada or of a province.

And to that has been added municipal and secondary bonds?

Mr. Dierker: That is right.

Senator Connolly: At both levels?

Mr. Dierker: The wording is this:

> or a Canadian municipality or bonds of a municipal or public body performing a function of Government in Canada.

It specifically excludes bonds of corporations, of course, by that definition.

Senator Gelinas: Does that include the bonds regarding hospitals subsidized by the Province of Quebec?

Mr. Dierker: I would say yes, if they are guaranteed by the Province of Quebec.

Senator Gelinas: It is a guarantee through subsidies: they are not fully guaranteed, as in the case of Hydro Quebec.

Senator Beaubien: The interest is guaranteed.

Mr. Dierker: Perhaps Mr. Morin could answer that.

Mr. Andre Morin, Research Department, La Federation des Caisses Populaires Desjardins: I would think so, Senator. This would be granted, but the problem, at the present time, is that the definition of a caisse populaire is being broadened and it is permitted to have more obligation in its definition, but not to the point where one knows what financial activities it could conduct. In our opinion, the main problem is that we have provincial legislation which is already there to restrict the activities of the caisses populaires, the credit unions. And it seems to us that all the financial activities that are permitted under provincial legislation should also be permitted by legislation as a normal activity because, otherwise, all that is going to happen, we are going to start having a lot of red tape concerning a few investments that can be made. I can give you an example: if credit unions exist in a general finance company, it is a corporation and we are . . .

Senator Beaubien: That is a very good thing.

Mr. Morin: I agree. If credit unions could support the Société générale de financement, they should pay a tax,

an additional tax by buying shares in the S.G.F. because that would be regarded as an investment which is not permissible to credit unions. Provincial legislation provides for it, and at that moment we fall into an administrative trap which must, of necessity, be recognized and there is provincial legislation which already provides for the activity which the caisses populaires, the credit unions, can conduct. Federal legislation which overlaps all that should recognize that, credit unions should be recognized as full-fledged financial institutions. It is not because they are private corporations belonging to a large number of individuals that they should be met with tricky legislation and red tape.

Senator Bourget: Well, what you are asking for is that the conflict which might exist between federal and provincial legislation be eliminated?

Mr. Morin: That is right. Such as section 189 as it now stands, and section 137. We already see a source of conflict there, and it should be specified immediately in 137 that a credit union is a full-fledged financial institution and that the investments, the financial activity permitted under the legislation which governs it is a normal activity.

Senator Connolly: Could I ask this question in English, because I am a little more familiar with it? You speak primarily of a conflict between the law of Quebec respecting investments of co-operatives and the proposed federal act. What is the situation with respect to the other provinces? Is there conflict also?

Mr. Dierker: The answer to that question is "yes."

Senator Connolly: Do you have some concrete proposed amendment which would perhaps reconcile the conflict between the laws of all the provinces and the proposed amendments to the federal tax act?

Mr. Dierker: The suggestion that we are making is that credit unions and caisses populaires be permitted to invest their funds in investments permitted under their provincial acts. That covers the matter province by province. There is also a federal act dealing with some of the centrals.

Senator Connolly: What about subsequent amendments to provincial acts? Would you say that for the time being they should be qualified to make amendments to provincial acts? Is that your idea? It could be that provincial legislatures could amend their legislation from time to time and the federal legislation would not be changed.

Mr. Dierker: With regard to credit unions and caisses populaires making an investment, as from time to time provided under their act of incorporation, as long as the federal act provided that it was an eligible asset within the meaning of section 189, there would be no problem.

The Chairman: The effect would be that the provincial legislature would be writing the ticket, and that would be paramount in the selection of investments.

Mr. Dierker: They presently are, in the sense that provincial governments are the incorporating bodies of credit unions, except for the centrals which operate under the Cooperative Credit Associations Act, which is a federal act.

The Chairman: If amendments come in from time to time, how could you expect a provision now that would say that whatever those amendments might be in the future by the provincial authority, you should have the approval of the federal authority to make those investments? Do you not think that they should have some right of supervision?

Senator Beaubien: Supposing a province said that a credit union could buy junior mining stock?

The Honourable Lazarus Phillips, Chief Counsel to the Committee: I think you are asking for something less than you already have in the act. Under section 137(6)(b) you are not restricted to the type of investments covering and including the amendment, because your income need only be derived primarily from and not exclusively from.

Mr. Dierker: I recognize that.

Hon. Mr. Phillips: The word "primarily" could mean, in law, 51 per cent, and you could get the 49 per cent from other sources.

The penalty section, under section 189(4)(b), says:

> "Ineligible investment" of any particular corporation means a property that was not acquired for the purpose of gaining or producing income from an active business of the particular corporation.

Surely, the active business of a credit union or caisse populaire is an active business allowed by law. Therefore you do not fall into the danger of ineligible investments. I would say you would have all the protection you need under sections 137(6)(c), and 189(4)(b). My impression is that if we attempted to give you relief we might end up by narrowing your broad rights.

Mr. Dierker: If only I could be sure that would be the interpretation given by the Department of National Revenue to the matter of active business.

Hon. Mr. Phillips: Perhaps you should see that I am appointed counsel to the Department of National Revenue!

Hon. Mr. Beaubien: At the usual fee, $1 a year?

Mr. Dierker: I take it that we have your assurance that that would be your opinion?

Hon. Mr. Phillips: That would be my opinion, if you had me appointed.

Mr. C. Albert Poissant, the Committee's Adviser on Taxation: I think that the credit unions, where section 894B is concerned, are perhaps interested in knowing that a company which makes a deposit in a credit union —that should not be classified as an investment which is ineligible but one that is eligible. That is the differentiation; not where you are concerned but where all the

other companies are concerned. Is that the interpretation that you want to give it, sir?

Mr. Morin: About section 189, there are two points, two requests that we had made. An initial request was that a credit union be recognized as a financial institution and that any private corporation which temporarily invested funds in a credit union would see its funds invested in a credit union as an eligible investment. You are quite right, this is perhaps the first thing that struck us, that we had to ask for. We confess that when we first presented the matter to the Finance Department, they were somewhat annoyed saying: we are sorry, we forgot. And that amendment has apparently been made, according to the information we have.

The other amendment would be one simply so as not to have any pitfalls concerning the interpretation of section 189 versus 137.

I quite like the interpretation that Mr. Phillips gave: I am not a lawyer, but that pleased me like that. But it seems that one should always be wary of lawyers as a whole.

Mr. Poissant: Unless, as Mr. Phillips suggested a while ago, you have him as a legal adviser in the Revenue Department.

Hon. Mr. Phillips: That would eliminate the whole difficulty.

The Chairman: Would you please carry on, Mr. Dierker?

Mr. Dierker: We are concerned about what we think is a conflict between sections 137 and 189, and I would recommend this matter to the committee for its consideration.

A matter that concerns us greatly is the application of a small business limit to credit unions and caisses populaires. The information presented in the house yesterday was that an amendment was being considered in respect of this, and this part was reported in the newspaper this morning. However, the amendment is not yet available.

The Chairman: What limit are you referring to, the $400,000?

Mr. Dierker: There are two limits. The first is the $50,000 annual limit, and the second is the maximum of $400,000.

The Chairman: Are you addressing yourself to both of those?

Mr. Dierker: It is a combination.

The Chairman: What do you say the $50,000 and the $400,000 should become?

Mr. Dierker: We are suggesting there should be provision written into either section 137, dealing with credit unions, or section 125, which permits a form of deduction for credit unions and caisses populaires which is not presently provided for in corporations.

Senator Beaubien: Deduction of what?

Mr. Dierker: Deduction of income before calculation of the figures. You will appreciate that under provincial legislation and regulations pertaining to credit unions and caisses populaires, money must be placed in reserve by these organizations to provide for their individual solvency.

They are all separate incorporations and are not tied in with the Bank of Canada or anything of that nature.

Once the funds are put in, these reserves become non-divisible and, as such, the credit unions and caisses populaires cannot pass these out.

There is therefore no way that credit unions and caisses populaires can take advantage of the benefit written into section 125 which permits a corporation to continue to have a low rate of tax if it pays dividends, because there is no way it can legally pay dividends from moneys put into reserves.

I suggest that cognizance be taken of this peculiarity and that provision be made to cover it.

The Chairman: In other words, that the $400,000 accumulated earnings would not include reserves?

Senator Beaubien: The reserves would not be considered as earnings?

Mr. Dierker: The reserves would not include the amounts of money that are put into the non-divisable reserve account.

The Chairman: You mean money put in there out of earnings?

Mr. Dierker: That is right. As you appreciate, to a greater extent these moneys are put in out of earnings under compulsory provincial legislation to provide for the solvency of these organizations.

Senator Connolly: Would you tell us something of the history and how these moneys are used? Are they in that reserve account, as you call it, permanently?

Mr. Dierker: Yes. They are put into the organization and they remain in the credit union as long as the credit union exists. If the credit union ceases to exist they will go to some form of charity, generally speaking.

Senator Beaubien: So they really never become earnings?

Mr. Dierker: They are initially earnings of the credit union but they are not capable of allocation.

The Chairman: What use may be made of the reserve account?

Mr. Dierker: These funds can be invested by the credit union and are invested by the credit union in bonds.

Senator Connolly: Allowable securities?

Mr. Dierker: Yes, allowable securities.

The Chairman: But what is the purpose of the reserve?

Mr. Dierker: The purpose of the reserve is to ensure the financial stability of the credit union. These reserves are basically 20 per cent of the income of the credit union per year, on an average.

The Chairman: Yes.

Mr. Dierker: This is speaking in generalities.

Senator Beaubien: You put aside these reserve funds and you invest them. Now, is the revenue earned from those investments considered as income?

Mr. Dierker: Yes, the revenue is income.

Senator Beaubien: It is considered income. There is no problem there.

Senator Molson: Mr. Chairman, what governs the size of these reserves?

Mr. Dierker: In many provinces it is governed by provincial legislation.

Senator Molson: What is it based on?

Mr. Dierker: Generally speaking, it is based on a percentage of the earnings of the credit union. Up to about 20 per cent of your earnings must be put into a reserve fund.

Senator Burchill: Each year?

Mr. Dierker: Each year, yes.

Mr. Frederick Graham, Member, Tax Committee, National Association of Canadian Credit Unions: I believe the limitation, Senator Molson, is carried on by legislation until the amount of the reserve reaches 10 or 5 per cent of the loans outstanding for the shares, as the case might be. In the federal act the amount is 20 per cent of earnings each year until such time as the reserve is equal to 10 per cent of the paid-up capital and deposits, or, in effect, the loans of the organization.

Senator Connolly: What happens after that? Is that amount required to be put in annually?

Mr. Graham: It stops; it does not carry on.

Senator Connolly: Well, I think you had the same idea, Mr. Chairman; that is, if this fund continued to build up at the rate of 20 per cent forever it would amount to an enormous figure.

Senator Beaubien: Mr. Chairman, once the limit as set down by federal law has been reached, is there any problem then?

Mr. Dierker: Once the limit has been reached there is no further allocation to this reserve.

The Chairman: Which limit, the federal limit or the provincial limit?

Mr. Dierker: Whichever limit is applicable.

Senator Beaubien: Do you take your choice?

Mr. Graham: It depends on whether you are registered under the federal act or under the provincial act. The only organizations under the federal act are the central organizations. There are only four or five provincial centrals which are registered under the federal act. Under the federal act you must go up to 10 per cent. Generally speaking, the provincial limit is something less. In other words, a local credit union would reach its plateau, presumably, at an earlier stage than a central organization under the federal act.

Mr. Morin: May I comment on that? I would simply like the Senator to realize that it is quite rare for the Caisses Populaires to reach the famous limit on reserves, and I can tell you that if one looks at the province of Quebec, we are obliged by law to place 10 per cent of our annual operating surplus, or of our annual profits, if you prefer, in the reserves. In practice, for the past 20 years we have been carrying an average of 50 per cent of our operating surplus in the reserves; nevertheless during that time, taking one year with another, our reserves have represented about 4.5 to 4.6 per cent of our assets. This is a percentage of the operating surplus, and when it is low, even a high percentage will not necessarily offset the increase in assets; once again, even if we place much more in these reserves than we are bound to by law, we still have reserves equal to about 4.5 to 4.6 per cent of our assets, and if you compare that with other financial institutions you will all realize as I do that these reserves are not out of line, far from it; the other financial institutions all have slightly higher reserves than we do.

Now if we look at section 125, this provides an incentive to force this private corporation to specify the individual owners of its surplus, and that,—the reasoning behind that as we understand it is to enable us, first of all, to have the business income taxed at the individual rate, and then to avoid the problem of "dividend stripping", which occurs later when funds begin to accumulate in these enterprises and the time comes when the shareholder stops investing in the business, when he needs his money, and he has a problem because of his tax. If you take this type of reasoning and try to apply it to the Caisses Populaires, it does not work, because our Act states that this reserve fund is indivisible, no one is about to pocket it and be faced with a problem of "dividend stripping"; it is a joint fund belonging to the entire group of members, for use in providing the small businesses in their own area with financial stability. Bear in mind, as Mr. Viateur said earlier, that the Caisses Populaires are all responsible for ensuring their own stability since they are completely autonomous, and when I tell you that they hold 4.6 per cent of their assets in reserve, and that the other financial institutions throughout the country have more than that, I mean to say that this 4.6 per cent is not exorbitant; there is no problem of "dividend stripping"; the institution belongs to the community which will keep its money there to make its enterprise more stable. There is nothing which would militate in favour of a provision requiring large amounts in it; on the other hand, however, it ensures the stability of quite an important sector of financial activity in Canada.

The Chairman: Mr. Morin, we have been talking so far about what I will call the statutory reserve required by provincial and federal authorities representing a percentage of the earnings of the year which must be put into that reserve and which has very tight restrictions on the use that might be made of that reserve. Now, what you wanted was to have the amount of those reserves not entered into the calculation of the $400,000 limit for small businesses.

Senator Connolly: Or the low rate of taxation for the first $50,000 of profit.

The Chairman: I thought I understood you to say that some of the credit unions put into their reserve funds something in excess of the statutory amount. Now, are you asking that whatever amount they put into the reserve fund should be deducted in arriving at the accumulation of earnings to represent the $400,000 a year?

Mr. Morin: Yes.

The Chairman: You realize you have no limitation and you could build up a substantial operation and accumulate substantial reserves only part of which would be subject to the provincial and federal dictates as to what use you might make of such reserves.

Mr. Morin: That does happen, but you will realize that credit unions have never been limited as to the amount they can put in the reserve. Our reserves are made gradually, at the same rate as assets; believe me, we do not need an incentive.

We already have the weight of democracy behind us; our members—what they put in the reserves of the group cannot be distributed among themselves, and certainly we have a weight behind us where people say, "give us patronage dividends rather than putting the money in reserves."

The Chairman: Are you saying that whatever amount you put into the reserve in excess of the statutory requirement, provincial and federal, once it gets into the reserve it cannot be distributed other than in the same way that the provincial and federal statutes would permit you to make use of the reserves? Is that what you are saying?

Mr. Morin: I think so, yes.

Mr. Dierker: That is correct.

Mr. Morin: We are speaking of just a calculation of the amount entering into the total business limit concept. We are not speaking of the rate of taxation on this amount. We are speaking of the five per cent on the amount we are placing in our reserves.

Senator Connolly: Perhaps I might act as a devil's advocate here for amoment. If what the witness says were realized, it seems to me that the credit union in question could defeat the purpose of the provisions of the small business limit. In other words, they could put in almost any amount they desired to keep it below the $50,000 annual limit and the $400,000 overall limit. They would seem to be in a position that other taxpayers who might be in the same type of category might not be able to achieve.

Senator Beaubien: They would have an advantage.

Senator Connolly: I think so. I would ask them to deal with that. I am not using a club but I simply say this is the way it looks to me.

The Chairman: Mr. Morin has said that he is not a lawyer and that he is always very careful when talking to lawyers, so maybe we should talk to their lawyer, Mr. Dierker, and see what he has to say.

Senator Cook: Could I ask a question on this point? Is it correct that when you allocate some money to reserve and it has gone once and for all, the members can never get that money? Is that correct?

Mr. Dierker: Yes, that is correct.

Senator Cook: In other words, you have the choice of paying tax on some and retaining some, or paying no tax and allocating it all to reserve?

Mr. Dierker: No, senator, that choice does not exist for credit unions in Canada.

Senator Cook: Not under your proposed amendment?

Mr. Dierker: No. Under the proposed amendment Mr. Morin was speaking about we are bringing to the attention of this committee that a credit union or caisse populaire does not have the ability to reduce this $50,000 and the $400,000 limit in the way a corporation can, because a corporation can by paying dividends get a $4 credit for every $3 of dividends paid out. In the case of a caisse populaire or a credit union, the moneys put into these reserves cannot be distributed. What we are saying is that these reserves are required, that under many provincial legislations there is no choice. Secondly, even if it is not required by provincial legislation, as in the case of Quebec, where reserves in excess of the provincial requirements are put into reserves, this is done under the existing bylaw provisions of the credit union, and to maintain the stability of the caisse populaire. Once these funds are put in there they can no longer be distributed.

Hon. Mr. Phillips: The expression used is "democratic pressure", I think Mr. Morin said.

Senator Carter: If these reserves are not divisible and cannot be distributed, what advantage is there in building up the reserves beyond what is necessary, beyond what the province requires?

Mr. Graham: That, of course, is the practical answer to what Mr. Morin was saying. Why would the members allow the thing to be built up to such a point to defeat income taxes, when in effect they are losing the right to the moneys themselves? There is no purpose in it, in trying to keep excessive reserves over what can be given back to members.

Senator Carter: Let me put it the other way. Would there not be a disadvantage in building up your re-

serves beyond what is necessary if they cannot be distributed?

Mr. Dierker: The credit union or caisse populaire will continue to have to be a viable financial institution in the community, and to maintain that position it will have to be competitive with other financial institutions. Accordingly, it will have to pay a return to its members on deposits competitive with other returns, which will automatically commercially limit the amount of money that could be put into these reserves.

The Chairman: That may be so, but as I understood the request that was being made you wanted the right to deduct reserves in any calculation of the $400,000 limitation, no matter how or in what manner, whether by compulsion or voluntary act of the credit union, those moneys went into the reserves. In other words, you want an amendment so that the only limitation as to what would go in excess of the statutory reserves would be what the company decided it wanted to put in there. Now, that is pretty unlimited. Maybe you would have to work out better language to justify that position.

Mr. Morin: This will depend on the Minister of Finance, Senator Hayden, and it is to ask that the first $50,000 of taxable income of a credit union not be considered in the calculation of the total business limit. This is for the first $50,000, but everything over $50,000 —at that moment, we come back to the same order, we come under the same standards as private corporations. Everything over $50,000 would be included in the calculation of the total business limit, so that our unions will very quickly come under the 50 per cent rate and our central credit unions, perhaps in the first or second year at the latest will enter into the overall calculation of business. But we want to point out to you that the credit unions—that 93 per cent of the credit unions in Quebec have put less than $25,000 in their reserves in 1969. And those are the small credit unions that we are trying to protect; we are trying to protect them so that they can put sums in their reserves without incurring a high rate of taxation in the more or less short term.

The other question, Senator. We have made a comparison with private enterprise and if you would like to see a few figures, we can hand them out to you. The objective is to make everyone realize, with a very concrete example, that the credit union, in practice, is going to pay a little more tax than a private corporation, and is going to be left with less working capital, and especially, is going to be brought more rapidly up to the high rate of 50 per cent.

My second point: we accept them, those are part of the rules of the game in view of our structure.

But the third point, what is being said is that at that point this runs counter to our legal characteristics.

Senator Bourget: What is the amount of the reserve at this time, in dollars?

Mr. Morin: 105 million, Senator, for Quebec, only, for our Federation.

Mr. Paul E. Charron, General Manager, La Federation des Caisses Populaires Desjardins: It should not be forgotten that the legal reserves are obligatory under provincial legislation, this is a minimum. In actual fact, in our by-laws, it is only ten per cent; 30 per cent is what is being asked for. It should not be forgotten that the reserves which are fixed by provincial legislation are minimums. Actually, the credit unions, through mere caution which experience has confirmed, by virtue of by-laws, have to put 30 per cent, by virtue of the by-laws, because the legal requirement is a minimum, and with inflation, when you take into account depreciations in bonds and immoveables. But when we realize that if we examine the figures closely, we have not put too much, nor should it be forgotten, with the taxation that is upcoming, that will not be a further incentive, it will be a lesser incentive. And that is why there should perhaps be a certain compensation by organizing a certain deduction on the 400,000 and by exempting the first 50,000 because there is a relationship between the two; otherwise, at the present time, temporarily, if you leave the legislation as it is, well, the government is going to receive a little more, but I think that by making the change, the credit union will be permitted to fortify itself more quickly and the tax base in "x" years will be greater, and then, the credit union's position will have been strengthened, and the position of the federal government's revenue will have been strengthened. It is a question of administrative prudence, if you like, and that is why we are asking for a deduction and without taking into account that our shares do not increase in value and they are redeemable on request, and our reserves cannot be divided. Therefore, when that is compared to other corporations, a correction must be made; if not, we are in a situation, let us say, I cannot say the word, restricted, which is going to affect, more or less, at least 90 per cent of our credit unions.

The Chairman: What we are trying to do is to understand clearly what it is that you are asking for. Is this it, that the statutory reserves, federal and provincial, be deductible before you arrive at the $400,000 limitation which would qualify for small business; and plus any voluntary reserves that are created by the credit unions; and the amount of those will be a determination by the individual company; and once it goes into that reserve you want it to be deductible, too, before you arrive at the $400,000. Is that right?

Mr. Morin: Our request is to say that the first taxable $50,000, for a credit union, should not be included in the calculation of the total business limit. The problem could be solved in another way which would be acceptable to us also, and that would be to stipulate that all the sums put in the reserves are taxed at 25 per cent, and that would be another advantage, but we will tell you about that right away, we would gain the second time.

The Chairman: Are you saying that the $400,000 limitation is too small? Not if you can make these deductions, but if you cannot, you say it is too small?

Mr. Morin: No, what we are saying is that this section 125 was written with a private corporation in mind and that operates very well with a private corporation in mind. But, take an association like ours into the picture, that is no good, and we have legal characteristics, once again, and we are not talking to you about the social role of credit unions, we are talking about legal characteristics.

The Chairman: You are making one assumption there. You say that for private corporations the $400,000 works beautifully.

Mr. Morin: Yes.

The Chairman: We have had expressions from private corporations where they think it should be $500,000, $600,000, $700,000. So it is easy to speak for the other fellow.

Senator Connolly: Let us say that a credit union has $20,000 that it is required by law to pay into the reserve, and it wants to pay in $30,000. Suppose that extra $10,000 were available to go to the reserve, or to go elsewhere. Where is "elsewhere"? Would it be distributed amongst the members?

First of all, I assume it would be taxed at the rate applicable to credit unions.

Mr. Dierker: First of all, there would be the 25 per cent tax on...

Senator Connolly: On the $10,000?

Mr. Dierker: On the $30,000.

Senator Connolly: All right. Suppose the $10,000 did not go into reserve, how, normally, would you use it? It is taxable.

Mr. Dierker: It would go out to the members of the credit union as interest on deposits.

Senator Connolly: And it would be income in their hands and therefore it would be taxable?

Mr. Morin: Yes, you are right.

Senator Connolly: That is the same position.

The Chairman: Mr. Poissant would like to ask a question.

Mr. Poissant: Mr. Morin, you said a while ago that 93 per cent of the credit unions have paid less than $25,000 into their reserves in 1969. Can you tell us what was the profit, or the net income of those credit unions for 1969, first of all, before their reserve, and secondly, after their reserve?

Mr. Morin: The overall profits of the credit unions were 20 million in 1969.

Mr. Poissant: In short, that is where my question is directed. Is the $50,000 reserve which you are asking for a credit union individually too much in my opinion? For the large credit unions as a whole, in Montreal or Quebec, that is alright. Perhaps $50,000 is appropriate, but I think that for the credit unions as a whole, including the 93 per cent you are speaking about, it is perhaps too much and what happens, when you compare a small enterprise, the credit union, would for all practical purposes be exempted for practically its lifetime. Note that under the new taxation legislation, you will be permitted to now deduct reserves to arrive at your taxable income. Then, the $50,000, you will be legally entitled to deduct the reserves from your accounts, the reserves on your investments, other type of reserves, on notes, which means that the income of credit unions fiscally speaking, is going to decrease now—and are you now speaking, in addition to that reserve which will now be permitted by law, of an additional $50,000 deduction per credit union?

Mr. Morin: No. The first question is 93 per cent of the number of credit unions, and the simple answer is to tell you that it is 75 per cent of the income of the credit unions. Does that answer your question?

Your second question, there is a misunderstanding in this room and that misunderstanding should be rectified. We are not asking that the first 50,000 dollars put into the reserves not be taxable in the hands of the credit union; we agree that credit unions pay their share of the government's expenditures and that they be taxed in the same amount as a private corporation, at the rate of 25 per cent. But what we are saying is that section 125 is constructed for a private corporation and if a private corporation individualizes, for example, with the capital stock method which is offered to it, it can then remain at the low 25 per cent rate almost indefinitely. And there is no mechanism permitting a credit union to remain at that low rate, that is the problem. Note one thing, when we speak of private corporations and when we speak of legal characteristics, that is what it is, and when you have a private corporation, if you force, if you suggest to a private corporation through tax incentives like that, to take its surplus earnings and put them into capital stock, you are taking the surplus funds which are divided among he members, and you are putting them into capital stock which is frozen for the company, which is golden working capital. When you ask credit unions to operate in the same way, you are asking them to take money which is in reserve funds that canont be distributed; therefore, it is our reserve fund that is frozen, and you put it into capital stock which is redeemable on request. It is a move in the wrong direction. Instead of freezing funds and leaving us more working capital, you freeze it. That is why we told you that the mechanism you have provided for a private corporation cannot function for a credit union and for a private corporation. Once again you are going to allow the private corporation to remain several years at the low 25 per cent rate if it individualizes. The purpose of individualizing profits is to prevent the problem of dividend stripping. We do not have it; there is no reason why you wanted to try to force us to go public; on the contrary, the reasons are there to ask the credit unions to build up reserves so that it will be a stable financial institution in the Canadian economy.

Senator Cook: Mr. Chairman, if the amendment proposed by the witness were accepted, would it be limited to the caisses populaires or would it have a wider application? Would it have implications for all taxpayers?

Mr. Dierker: Do you mean would it apply to credit unions as well as to caisses populaires?

Senator Cook: Would the principle involved extend to other forms of co-operative movements?

Mr. Dierker: For the purposes of this discussion let us define co-operative movements as being credit unions and caisses populaires. The principle of non-divisibility of these reserves applies to both caisses populaires and credit unions and only to these institutions. That is the extent of my knowledge, at any rate.

The Chairman: So the amendment would be by way of exception to deal with these two particular types of institutions.

Mr. Dierker: I think the amendment would probably have to be in section 137 where it deals with caisses populaires and credit unions.

Mr. Poissant: If I may ask the witnesses, if the statutory reserve as permitted under provincial law were acceptable as capital for the caisses populaires or the credit unions, and any excess would follow the normal pattern as being part of the $400,000, would that be acceptable? If the answer is no, do I presume that their statutory reserves are not high enough, which then becomes a provincial problem and not an income tax problem?

The Chairman: Mr. Morin, any argument that you make is to support a higher amount in reserve than the statutory reserves, and you say that it is needed.

Mr. Morin: The reserve is needed, yes.

The Chairman: You say you need a higher amount than the statutory provisions would provide, so why should the statutory provisions not be increased?

Mr. Morin: It is a question of the financial stability of the enterprise.

The Chairman: What I am getting at is that you say there are two sources for building up reserves: the statutory requirements, provincial and federal, and also the voluntary contributions which you make out of earnings. You say that that is necessary and is needed to maintain the stability.

Mr. Morin: Yes.

The Chairman: All right, then, why does the provincial authority not recognize that a larger amount of contribution is needed and provide for a larger amount to be contributed to reserves?

Mr. Morin: You would like to see all the provincial legislatures taking the decisions for you.

The Chairman: No. That may be a smart answer, Mr. Morin, but it does not deal with the question at all. If your argument to me was that the statutory plus the voluntary was needed in order to give stability to the credit unions and to the caisses populaires, that would be one thing. Suppose I accepted that, there is still a very obvious answer: if it is needed, apparently the provincial authority does not realize that it is needed because the provincial authority has not increased the statutory amount. So why not have them increase the statutory amount and then we would have no argument here.

Mr. Morin: The other thing I wish to tell you—the reasoning behind it is good—is that there could be provincial legislation which would be the same throughout the ten provinces, which would stipulate that 50 per cent of excess funds be held in reserve. However, when you consider the law governing "Credit Unions" where excess funds are larger, there could be problems for social reasons from one province to another. Now, just considering Quebec province only, the credit unions generally hold more than 50 percent of excess funds in reserve. However, we have to realize that there are already some credit unions that have large reserves and that could justifiably hold only ten percent of their excess funds in reserve, which is sufficient for credit unions that have already built large reserves, while it isn't sufficient for others. Each has to be treated on its own merit. This minimum of ten percent required by law is a healthy thing, and every credit union should adhere to it. However, practical experience has shown once again that for the majority of credit unions in general, more than that is necessary, even though that law is enough for the larger unions that have sufficient reserves.

The Chairman: But, Mr. Morin, you are asking us to agree to and support an amendment where part of the contribution to the reserve out of earnings would be determined by the individual caisses populaires and credit unions themselves. What we are saying is that you could put it on a stronger basis, if the statutory requirements were increased, or that it may well be that the sum total of the reserves, both voluntary and statutory, should bear a fixed ratio to the deposits—because I understand the reserves are intended to give a certain assurance or stability to the depositors; isn't that right?

Mr. Morin: Yes.

The Chairman: So there could exist a percentage relationship; that is, the sum total of the reserves, voluntary or otherwise, could bear a relationship not in excess of a certain percentage to the deposits. You tell us what the percentage should be.

Senator Cook: Without a percentage rate, the witness is asking us to accept the judgment of each individual caisse populaire as against the judgment of the provincial legislatures.

The Chairman: That is right.

Senator Lang: It seems to me that the caisses populaires or credit unions may very well, as a matter of policy,

be public rather than private corporations, because they are deposit-taking institutions. Really in one sense I think that this discussion may be academc, because the minister under section 89(1)(g) may very well decide that any particular caisse populaire is a public corporation and, as a consequence, is not entitled to the low rate of tax on the $400,000.

Mr. Morin: Except that you have to take into account section 125 and Part V.

Mr. Dierker: Section 137(7) says that:

> (7) Notwithstanding any other provision of this Act, a credit union that would, but for this section, be a private corporation shall be deemed not to be a private corporation except for the purposes of section 125 and Part V.

The Chairman: That is the way they make the small business provisions available.

Mr. Dierker: That is correct. That is where it comes from.

Senator Connolly: Mr. Chairman, it seems to me that individual credit unions have an opportunity to keep themselves as small business corporations in two ways rather than in one way. In the case of the ordinary incorporated company, the company can keep itself in the small business area by paying dividends sufficient to bring it within the $400,000 ceiling. Now, the credit union is saying that it had that right, of course, by paying out its dividends, but it is also saying that the amount paid into—no?

Mr. Graham: No, the dividends are deductible before the computation of income.

The Chairman: Just a minute, now. What I think Senator Connolly is getting at is this. If a private or public corporation which is entitled to the benefit of small business finds it is pushing against its ceiling of $400,000, it can pay out dividends to reduce that amount, but the person who receives the dividends finds that it is income in his hands. Now they reduce the $400,000, but the receiver of the dividend is going to pay income tax on what he receives. Now if a credit union wants voluntarily to contribute, in excess of statutory amounts required for reserves, additional amounts will go into reserves without being subject to any tax.

Senator Connolly: No, it will pay the 25 per cent.

Mr. Graham: It will pay more than 25 per cent.

The Chairman: Do we have to back up and start all over? I thought it was said clearly that what you are asking for is that the statutory reserves plus the additional voluntarily contributions to reserves are to be deducted from the sum total of $400,000 in arriving at the ceiling under which you may operate. Now, did you mean that or not?

Mr. Morin: Oui.

The Chairman: All right, so you meant it. And that means that you are asking that the reserves voluntary and statutory be not considered to be earnings.

Mr. Graham: You still have 25 per cent tax plus. It is a tax-paid transfer, senators, and it will amount to 33 per cent tax regardless.

The Chairman: Well, we have a difference in viewpoint there.

Mr. Graham: Even though it is not part of the $400,000, section 125 only rebates half of the tax.

The Chairman: Are you saying that the statutory reserves that are built up will carry no tax?

Mr. Graham: It will pay a 33 per cent tax. The transfer into the statutory reserves is a tax-paid amount going in so that this has the effect of the credit union paying in respect of that amount 33 per cent tax.

Senator Connolly: I think, Mr. Chairman, that the understanding you had originally was the same as the one I had, but perhaps it was developed later. I heard some one say that it was subject to a tax before it went into the reserve. Then, having put it into the reserve, what you ask now is that it should not accumulate to the point where it is going to puncture this $400,000 ceiling.

Senator Cook: Everybody agrees with that, but the only discussion is how much of this reserve should be considered.

Senator Connolly: All right; both the compulsory contribution and the voluntary contribution should be in this category; it should be exempt. Now suppose for the sake of argument that in the provincial legislature the compulsory amount is increased and increased and increased—this may be an exaggerated example, but I am thinking of the situation of the draftsmen of the federal legislation who have to consider getting, I suppose, the same amount of tax from all taxpayers and the provincial government could reduce the amount of tax that could be collected by the federal authorities by increasing the compulsory reserves. The provincial legislature therefore would be in effect defeating the purpose of the federal act, would it not?

Mr. Graham: The people who are going to operate against that, of course, are going to be the members themselves. Once you transfer it to reserves, you put it beyond the reach of these people forever.

Senator Connolly: So it is not available as dividends.

Mr. Graham: It creates its own defence against that. I mean people would be up in arms if the provincial government said you had to put 60 per cent or whatever amount you like.

Senator Connolly: That is a *reductio ab absurdum* on my part. But let us take your other arm. You can stop the small co-op from hitting its head against a $400,000 ceiling by distributing dividends to the members, can you not?

Mr. Graham: No.

Senator Connolly: Why not?

Mr. Graham: There was one amendment proposed yesterday to the effect that the dividends paid on shares shall be considered as an interest payment and deductible in arriving at the amount of taxable income. So once that goes through, when we are speaking of the income of a caisse populaire or a credit union, the only income left is going to be the amount which is not distributed which is the amount that goes into reserve. There is no other income. There is no tax creditable on distribution because it cannot be distributed. It accumulates and we cannot distribute it so there is no defence against the $400,000 ceiling.

Mr. Dierker: The real answer on the payment of dividends, senator, is that you are prohibited from distributing the money put into reserves.

Senator Connolly: I can understand that, but I was not talking about those moneys; I was talking about the distributed money.

Mr. Graham: But the only income once the dividends are deducted are the reserves. So you are now left with the income of the credit union. Remember it is all taxable in the individual's hands, but the corporate position is that the only thing left will be the undistributed amount representing the reserves.

Mr. Dierker: I think, senator, we can back up one step on this. The money that the credit union pays as interest on deposits is a business expense.

Senator Connolly: Would you say that again, please?

Mr. Dierker: The money that a credit union or any other financial institution, including a bank, pays on money on deposit is a business expense. So that at the end of the year after adding together your income and expenses, so far as the credit union is concerned all that will be left will be the moneys undistributed, the moneys to be allocated for your reserves. The point we are making is that these are the moneys that will go into reserves.

The Chairman: Well, Mr. Dierker, Mr. Morin and I have a difference in view. Are you saying that when income earnings are allocated to reserves in the year (and that would be the net amount of income left after all deductible expenses have been taken away) that notwithstanding the fact it goes into statutory reserve it is income subject to tax?

Mr. Dierker: Yes, it will pay a 25 per cent levy.

Senator Beaubien: But you pay a tax before that money is put into reserve? Isn't the only thing you are afraid of that that money will build up and get you out of the class of the $400,000?

The Chairman: I understand what they are saying.

Senator Beaubien: I know you do, sir, but I was trying to get it clear for myself.

The Chairman: I do not follow it all as a matter of interpretation. Now we are not going to argue out the legal interpretations; Mr. Morin does not want to argue with a lawyer. So, as I say, we are not going to argue it out.

We understand your position and the arguments you have given in support of it, and we can verify whether that agrees with what we think is the interpretation in the act and therefore we can deal with your request on that basis. We have said many things here and we have really threshed out the point very completely. I do not think there is any value in saying anything more.

Senator Desruisseaux: Mr. Morin, what is the present increase in the percentage of the reserves over, let's say, the last two years?

Mr. Morin: Our rate of growth is about 12 percent a year.

Senator Desruisseaux: How much?

Mr. Morin: 12 percent.

Senator Desruisseaux: Deposits?

Mr. Morin: Assets also.

Senator Desruisseaux: I am not talking about assets, I'm talking about deposits.

Mr. Morin: Deposits—it varies on the average—about 12 percent. Deposits represent on the average 85 percent of our assets.

Senator Desruisseaux: Could you expound on that briefly?

Mr. Morin: Yes, going back over the last 20 years, the amounts held in reserves simply maintain these reserves and they are approximately equal to 4.5, 4.6 percent of the assets existing at the year end.

Senator Desruisseaux: Thank you.

Senator Burchill: May I ask a question, Mr. Chairman?

The Chairman: Yes, certainly.

Senator Burchill: This reserve which is indivisible, are there any conditions or circumstances whatever in which it could be divided?

Mr. Dierker: Yes, on the liquidation of the Credit Union; and generally then it goes to a charity function.

The Chairman: It is there is a reserve in relation to deposits.

Senator Burchill: Yes, but it cannot be touched.

Mr. Dierker: By the members? That is correct, not unless it is wound up. It never returns to the members.

The Chairman: No, but it may go to the depositors.

Mr. Dierker: This is true.

Senator Connolly: In the event of a bankruptcy, for example.

The Chairman: Yes.

Senator Connolly: What happens in the event of a failure of one...

Senator Beaubien: You can deduct the amount of the failure.

The Chairman: Certainly. Quite obviously, the reserve is to protect the depositors, that is assuming the depositors need protection, and the reserves must be available.

Senator Carter: May I ask a question, Mr. Chairman? Is depositors' insurance available through Caisses Populaires?

Mr. Dierker: Just to members of Caisses Populaires, not to members of the Credit Unions.

The Chairman: Not to the Credit Union members.

Senator Carter: I think the answer is "yes"?

The Chairman: In part.

Mr. Dierker: It is available to members of Caisses Populaires but not to the Credit Union members.

Mr. Morin: Saving accounts only in the credit unions of Quebec.

Senator Carter: That is additional protection for the depositors. Would that not be better, rather than building up the voluntary contributions? Would that not be better?

Mr. Morin: We have not asked for deposit insurance. It protects us presently, and the policy of the credit unions is to try to cover themselves, in conjunction with all credit unions, and we hope we'll never have need of this deposit insurance.

Mr. Poissant: Mr. Morin, to sum up, your request comes down to this: on the first $50,000, the credit union pays 25 percent. For the remainder, once $400,000 has been paid in and accumulated, the normal amount of tax will be paid. Your request makes sense to me, because if we consider the workings of the treasury as a whole, in effect the treasury is going to receive 25 per cent immediately, and looking at the average tax of shareholders of a normal company who receive bonus dividends, I think the average tax would be seen to be less than 25 percent, or nearly 25 percent.

Mr. Morin: The average tax of citizens in Quebec is 15 percent.

Mr. Poissant: At such a time, the Federal Treasury would immediately gain on the first $50,000, 25 percent, and not being subject to dividends, this tax could not be recovered, while the little company that has profits of $50,000 and that pays out dividends of $50,000 to its shareholders, has paid, for argument's sake, $25,000 in tax; it isn't too rational an example, but for the sake of simplication, let's say the shareholders recover this $25,000 of tax, while the first $25,000 in this case paid by the credit union will, for all practical purposes, be lost in the hands of the members. Therefore, the government could receive its tax almost immediately, if I understand it. Is that what you meant?

Mr. Morin: The example is excellent. The credit unions, as things stand at the moment, are to pay from 3 to 5 million dollars in tax, uniquely for credit unions of Quebec. The change produced by the article under discussion does not change the tax payable by the credit unions. What we are questioning is that we are already going to pay a slightly higher tax than the average tax paid by a private corporation, due to the fact that there is no recovery of the tax payable by the enterprise. But, what we are asking for, is to avoid being pushed up in a short period to a ceiling of 50 percent. And while there are means in existence, moreover, to keep private corporations on the low 25 percent rate, there is nothing of this nature for the credit unions. That is what we are asking for.

The Chairman: Mr. Morin, is it not your case when you transfer earnings into a reserve, you say that they lose the character of earnings because you cannot deal with them in the way in which you would ordinarily deal with earnings. And since the accumulation of the $400,000 is supposed to be an accumulation of earnings, then the moment that you put these earnings in a reserve they have lost the character of earnings.

Mr. Morin: I would agree with this.

Mr. Dierker: Precisely.

The Chairman: Now I understand your point.

Hon. Mr. Phillips: May I touch on a point by way of compromise, being a man of peace? I fell that there is a great deal of merit in the point that the distribution to the members comes to the members by way of interest and not by way of dividend in the normal way, even though it is deductible against the credit unions or caisses populaires. I personally feel that there is a great deal of merit to the point that the staturory reserve plus the voluntary reserve be dealt with in the manner in which you have indicated.

However, I think the Chairman has raised this point: Do you not feel that the combination of both should be related to the deposits or to the total assets, that is, constituting some curve on the freeze? That would appear to make sense. If a recommendation were to come from those of us on the committee who are in favour of this, I think that they would feel more comfortable if they had a little guidance on that point in terms of what the ratio should be to deposits in its totality, or in relationship to total assets.

Senator Connolly: Would Mr. Phillips spell that out more clearly with an example?

Hon. Mr. Phillips: Suppose at the end of 1971 you had $1 million on deposit and your statutory reserves plus

the voluntary reserves were $200,000—that is 20 per cent for the protection of $1 million on deposit. Now my question is: Is that too high or to low, if you had $2 million of overall assets and you had $200,000 of statutory plus voluntary reserves? Is the $200,000 in relation to the $2 million of assets too high or too low?

The Chairman: Perhaps this is a question that you would like to think about for a while.

Hon. Mr. Phillips: And give us some guidance on.

Senator Lang: Mr. Chairman, the highest figure for trust companies is 20 times.

The Chairman: We would like to hear your views, as quickly as possible, on Mr. Phillip's proposal, by way of summary.

Senator Beaubien: You are asking for a ceiling?

The Chairman: Yes. We would like to hear from you rather quickly because we are going to be giving consideration to this matter.

Mr. Morin: Excuse me, Senator Phillips, but we are to pay immediately, even if we are given the exemption of $400,000 that we are asking for. We are going to pay our part of the national expenses. And concerning that point, we are convinced that we are not dodging taxation in any way and that the credit unions are to pay a little more than the private corporation in that sense; you should not be too preoccupied with the possibility of a credit union having large reserves; here again, because of the weight of democracy, it is very, very unlikely. In the past when we had no tax to pay on amounts held in reserve, we did not build exceptionally large or exaggerated reserves. I do not see why when subjected to taxes, we should change our policy. The danger is rather that our credit unions may try to avoid holding money in their reserves so as not to pay tax, and that is our own business, but in an inverse sense; there is no danger of building exaggerated reserves.

Senator Beaubien: Mr. Morin, there is no danger of you building exaggerated reserves. There is no use in objecting to a ceiling because that is what you want, you want to have a ceiling.

The Chairman: I did not realize that it would take so many words to say "yes" or "no".

Senator Beaubien: We are not lawyers.

The Chairman: We put a question to you, to which you replied in your own good time. Having regard to our demand for some expedition, the answer we would like is "yes" or "no". If you say "no", we would like to know why you say "no", if that is not asking too much.

Mr. Morin: Yes, Senator, it's acceptable, but it doesn't appear necessary to us.

The Chairman: The brief filed on behalf of the caisses populaires and credit unions contains a statement that the restriction in section 137(6)(b)(I) with reference to carrying on business in one province should be deleted. Could we have, shortly, an answer?

Mr. Dierker: Mr. Chairman, shortly, the appropriate amendment has been proposed.

The Chairman: I really want to know why?

Mr. Dierker: Why the credit unions and caisses populaires feel this way?

The Chairman: No; why should there be a restriction?

Mr. Dierker: I do not know why there should be; there was one in Bill C-259 and we requested its deletion. The amendments which have now been filed satisfy that request.

The Chairman: Then there is the obvious answer, and it is a short one.

Are there any other points in your brief which you wish to discuss at this time?

Mr. May: Mr. Chairman, given the amendments which were introduced yesterday, we have touched on the two very complex areas which remain of much concern to us. I think we really have presented the issues which remain outstanding.

Your suggestion that we should make a further submission in writing to the committee with respect to these two outstanding areas in an endeavour to clarify by example and supplementary wording will be followed through immediately.

The Chairman: Does this conclude your presentation? You have expressed the view that we should pay full attention to the amendments which were tabled yesterday. We have not seen them yet, but we will later today and will certainly look at them with every consideration.

Mr. May: Very good. We appreciate the opportunity to appear and your consideration.

The Chairman: Thank you very much.

The Chairman: We now have the Co-operative Union of Canada. Mr. Melvin, sitting on my immediate right, is the President. Mr. Legere is the President of Le Conseil Canadien de la Cooperation. Mr. Dierker will also take part in the discussion.

Others present from the Co-operative Union are: Mr. Richard Newberry, Controller, Co-op Federee de Quebec; Mr. R. H. D. Phillips, Research Director, Saskatchewan Wheat Pool; Mr. Ed. Chorney, Treasurer, United Co-operatives of Ontario; Mr. John R. Moore, Treasurer, Maritime Co-operative Services; Mr. T. Pat Bell, Treasurer, Federated Co-operatives Ltd.; Mr. G. L. Harrold, President, Alberta Wheat Pool; and Mr. J. A. Dionne, President, Federation des Magasins Co-op.

Mr. Melvin, will you make your opening statement please?

Mr. Breen Melvin, President, Co-operative Union of Canada: Thank you very much, Mr. Chairman and honourable members of the committee. We appreciate very much the opportunity to appear before you this morning. I would like to make two or three brief comments, and then, if I may, sir, ask Mr. Legere if he would care to say a word or two. I should point out that it may not be entirely clear to you that this is a joint presentation of the Co-operative Union of Canada and Le Conseil canadien de la Coopération; and Mr. Legere would like to speak on behalf of his organization.

May I say first of all that the co-operative movement, as represented by those appearing before you and the organizations which they represent, is very greatly concerned at the impact of the provisions concerning co-operatives in Bill C-259 on their successful operation. We are troubled considerably because some provisions appear to require that co-operatives should forsake their particular nature and become oriented toward the return of earnings on investment, rather than the return of savings to members.

Co-operatives have always been user-member organizations and the patronage-dividend method has been employed to return earnings to them. It appears that the proposed amendments would change this emphasis and require that these returns be made on the basis of investment interest.

Secondly, we are quite concerned that the amendments seem to veer away from what we have understood to be the traditional position of Canadian society and of the Government of Canada. That position is that there are three forms of economic enterprise in our society: The public sector; the private sector; and there is the co-operative sector, which is much smaller than the others.

This has been stated on occasion by people in very responsible positions in Government. We have been happy to hear that and have accepted that it was the case. It would appear that the co-operative sector may suffer very greatly. The suggestion might even be taken from the amendments that it has not an important role and really there are only two sectors in the economy as far as business is concerned.

Senator Connolly: What are those two?

Mr. Melvin: The public sector and the private sector.

Senator Connolly: Where would you fit in?

Mr. Melvin: If the amendments are carried forward and become law, it would appear that we would be over into the private sector of the economy without any recognition of the peculiar features of a co-operative business enterprise.

The third point that I should like to make is that upon inquiry from the International Co-operative Alliance, which is the world federation of co-operatives, and is well posted on the activities of co-operatives, we have been advised that although the taxation position of co-operatives in different countries varies somewhat, even considerably, in no other country is a minimum tax base or minimum earnings imputed to co-operatives by law.

This seems to us to be a peculiar and certainly a very different situation. This is one that does not take into consideration the nature of the kind of enterprise in which we are engaged.

Those are the three comments that I wished to make by way of introduction.

The Chairman: Do you say that there is no element of earnings in the operation of a co-operative?

Mr. Melvin: No. I would not go that far.

The Chairman: What happens to the earnings, if there are some?

Mr. Melvin: I would suggest that in the case of a co-operative, the decision of the members of the co-operative, which is made voluntarily, is that earnings would be distributed among them—and they are also the owners—rather than on the basis of investment they have made by way of capital investment or purchase of shares; that it should be distributed to them on the basis of the business they do with the co-operative. In other words, use the patronage dividend device to make this distribution.

The Chairman: Would you not agree that if you are distributing earnings, the person who receives them should be subject to tax?

Mr. Melvin: This applies to the great majority of members of co-operatives, particularly farm marketing or fishery co-operatives. They take these earnings into consideration when determining their own income tax position each year.

The Chairman: Do they take them into consideration at less than the full amount of the earnings that are paid out?

Mr. Melvin: No. The patronage dividend which they receive reduces the cost of their operation and so becomes a part of the calculation of their income for the year.

The Chairman: When you say "part of the calculation", what do you mean?

Mr. Melvin: It becomes involved in the procedure, in the calculation of their income.

The Chairman: Can you give us an illustration?

Mr. Melvin: Perhaps I should ask Mr. Dierker to deal with this matter in more technical terms.

The Chairman: Mr. Dierker, let us take an example. Supposing a co-operative has earnings of, say, $100,000. Would you please follow that through and tell us what happens to it?

Mr. Dierker: If the co-operatives propose that they be able to distribute this as patronage refunds to their members, and if they are so distributed, the $100,000 will be taken into individual income.

The Chairman: Will be taken into individual income?

Mr. Dierker: Yes.

Senator Beaubien: Is there any tax paid on it first?

Mr. Dierker: You mean under the proposal or under this example? If you have $100,000 of earnings at today's date, a co-operative is permitted to pay this out as a patronage refund, subject to the limitation that they cannot pay patronage refunds so as to reduce their income below a figure equal to 3 per cent of capital employed.

Senator Burchill: On what basis is the patronage dividend based? How is it calculated?

Mr. Dierker: The patronage dividend is calculated on the business done by the member with the co-operative.

The Chairman: And he pays tax on his marginal rate.

Senator Burchill: I get a patronage dividend, and I also have to pay taxes. I wondered what the patronage dividend was based on. I could never figure it out.

Mr. Dierker: The patronage dividend is a deduction to the co-operative as an expense, and it will be taken into your personal income.

Senator Beaubien: Supposing I buy a bulldozer at a cost of $60,000. At the end of the year the co-operative makes some money and I get something back. Do I show that as a reduction in the cost of the bulldozer, or do I show it as coming in as income?

Mr. Dierker: You will show it as coming in as taxable income.

The Chairman: Let us take the example of $100,000 of earnings. There is a limitation on the amount of that you can pay out in patronage dividends.

Mr. Dierker: That is correct.

The Chairman: Is or is not the rest of it, in the hands of the co-operative, subject to tax?

Mr. Dierker: If it is kept in the hands of the co-operatives, it is subject to tax at the standard corporate rate. However, a co-operative can distribute this as a patronage refund after it sets aside the minimum capital employed.

The Chairman: What is the character of the patronage refund in the hands of the co-operative and in the hands of the recipient?

Mr. Dierker: In the hands of the co-operative, it is an expense. In the hands of the recipient, it is income.

The Chairman: The whole of the $100,000 would not be subject to any tax in the hands of the co-operative?

Mr. Dierker: Except for the capital employed feature, yes.

The Chairman: With respect to the capital employed feature, the limitation governs the amount that is paid out in patronage dividends?

Mr. Dierker: That is correct.

The Chairman: But to the co-operative, what is its character in the hands of the co-operative the instant before they pay it out? Is it taxable to the co-operative?

Mr. Dierker: Yes, it is. There are no deductions.

Senator Connolly: Taxable at the corporate rate?

Mr. Dierker: Yes.

Senator Connolly: If it is not a small business company. If it does not comply, it pays the 51 per cent or 52 per cent, or whatever it is?

Mr. Dierker: That is correct. As a point of clarification, the presentation being made here today, once we get into it properly, is not on the basis that a co-operative should not pay tax. We are not quarreling about the payment of tax on moneys kept in the hands of the co-operative; nor are we quarreling about the payment of tax on business done with non-members.

The point we are quarreling about is that there should be a capital employed concept put in between a co-operative and the members, limiting the return that can be paid to members.

Basically, what we are saying is that a co-operative is a form of partnership, a large corporate partnership, and that the earnings be in the hands of the members.

The Chairman: Why limit the amount that is being paid by a co-operative to a member if the whole amount in the hands of the member is subject to his marginal rate of income tax, without any credits?

Mr. Dierker: You mean why is this done?

The Chairman: Yes. Put it this way: Why should it be done?

Mr. Dierker: We do not think it should be done. Our position is that it should not be done. Perhaps, Mr. Chairman, I could explain the features of Bill C-259 with respect to capital employed?

The Chairman: Yes.

Mr. Dierker: Under the present proposal a co-operative is restricted in the amount of patronage refund that it can pay to its members on the business done with the members, so that it cannot reduce the income below a figure equalling 5 per cent of capital employed.

To the best of my knowledge, this is the only place where in taxation law we have a tax imposed directly on capital where capital is deemed to produce some money. If you take a corporation as an example, honourable senators, there is no requirement on a corporation to produce some money on its capital; it can distribute it. There is, however, a limit imposed on a co-operative.

A co-operative can do away with this 5 per cent limit if it pays out this 5 per cent by way of interest on shares or on member equity, so called. It is important to realize that this payment must be by way of interest. If the co-operative pays a return to its members on capital by way of dividends it cannot reduce this 5 per cent. If it pays interest, however, on its share capital it can in fact reduce its income down to zero.

It is a most peculiar feature because what the tax provision says is that co-operatives may zero out their taxable income if they do two things: firstly, pay interest on member equity equal to 5 per cent; and, secondly, they can then pay the balance out as patronage refunds.

Senator Connolly: Would you give us an example of that?

Mr. Dierker: Let us take $100,000 . . .

Senator Connolly: Please identify the $100,000. This is earnings of the co-operative for the year?

Mr. Dierker: At the end of the year.

Senator Connolly: All right.

Mr. Dierker: Let us take the figure of $100,000 before any distribution. Now, supposing, for the purposes of this example, that the 5 per cent of capital employed amounted to $20,000; at a 50 per cent rate of taxation your tax would amount to $10,000. That would leave you $80,000 that you could pay out as patronage refund resulting in an expense to the co-operative and income to the members. You can pay tax on this $20,000 that you have as your capital employed feature, and at the rate of 50 per cent that will be $10,000, or if we pay $20,000 out in interest we can simply reduce that down to zero, provided we paid the interest to the members.

Senator Walker: You are going a little fast. Just go back over that again, please.

Mr. Dierker: You can do two things with the $20,000. You can pay tax on it . . .

Senator Connolly: And then is the balance available for distribution?

Mr. Dierker: Well, we will not talk about distribution right now.

You can pay tax on the $20,000 or it can go into a tax-paying reserve, or you can get rid of it by paying interest on your member equity; not by paying dividends, but by paying interest on member equity.

The Chairman: It will then become a deductible expense.

Mr. Dierker: Yes, it will become an expense for the co-operative and income to the member. Now, if you put that $10,000 into your reserve and then pay it out as patronage refunds, there is no tax credit on it. If a corporation paid it out there would be a tax credit, but in the case of a co-operative paying it out as a patronage refund there is no tax credit. If a co-operative pays it into its reserve, that $10,000 would be re-taxed every year on the basis of the capital employed.

Our position is simply this: If the Government permits the reduction of the $20,000 by payment of interest to the members, why will it not let us pay it out as patronage refund and have it taxable in the hands of the members?

The Chairman: It would accomplish the same thing.

Senator Lang: It would avoid double taxation.

Mr. Dierker: It does create some serious problems in the capital employed formula as it is presently drafted.

One of the things that honourable senators should appreciate is that the increased tax load is not 3 to 5 per cent. As I mentioned, there is a present 3 per cent capital employed formula. It is not simply a 3 to 5 per cent increase. The formula has been substantially adjusted.

At the present time the interest that you can deduct, for instance, is the interest on borrowed moneys, other than to banks or credit unions. This is no longer permitted. Basically, there has been an addition to what must be included in capital employed and a reduction in what you can deduct.

The Chairman: Mr. Dierker, if we took your example or your suggestion, that if you do not have this capital formula limiting the amount of the patronage dividend and the whole amount were paid out as a patronage dividend, in the hands of the recipient that would be subject to his marginal rate of tax and the co-operative would pay no tax.

Mr. Dierker: Except for tax on non-member business.

The Chairman: Yes, non-member business and tax on moneys put into tax-paying reserves.

Mr. Dierker: Yes. There is one refinement that I should bring to your attention. Patronage refunds paid on consumer items—groceries, and so forth—are not taxable income under the proposal.

The Chairman: How would it work? Does the member get a credit from the co-operative whereby he can pick up groceries, or how does it work?

Mr. Dierker: In some cases, that is correct. In other cases, however, there is a general allocation to the member which can be re-invested in the co-operative. In some cases it is a cash payment.

The Chairman: In making your calculation of the credit to the member, the calculation in the first instance is made in dollars, is it?

Mr. Dierker: That is right.

The Chairman: And then the other thing is how he uses it.

Mr. Dierker: That is right.

The Chairman: He can use it to buy groceries, and I assume he gets substantial discounts because he is a member.

Mr. Dierker: Not generally, no.

Senator Burchill: Just to go back to the question of how this calculation is made: Patronage refund means it is calculated on the basis of the business you do with the co-operative. You purchase goods from the co-operative and you also sell to the co-operative so you have a two-way street. Now, when you say the business which is done, is that the total of your buying and your selling?

Mr. Dierker: This would be correct, yes. What you would do, senator, is you would categorize . . .

Senator Connolly: Who is "you"?

Mr. Dierker: The co-operative would categorize the various methods of business. You would categorize the purchases; you would categorize the selling, and you could have different refund rates in respect of the different activities.

The Chairman: Members may sell their product or whatever their production may be to the co-operative. Now, do they have a preferred position in selling as opposed to a non-member?

Mr. Dierker: I would think that the answer would have to be "no" to that. There are some provisions whereby some co-operatives in Canada do, under contract, require members to deal with the co-operative and to that extent there could be a preference in the sense of making the facilities of the co-operative available to members as distinct from non-members.

The Chairman: How do you calculate the non-members' business? That must be quite an item of accounting.

Mr. Dierker: It is a detailed item of accounting. All business done with non-members has to be accounted for and, generally speaking, what happens is that you calculate the same percentage of earnings of member business as of non-member business and lump them together. There is no way that you can divide . . .

The Chairman: You have to make the calculations on indirect items?

Mr. Dierker: That is right.

The Chairman: And I take it that those allocations are approved by the Income Tax Department?

Mr. Dierker: They are reviewed annually, anyway.

The Chairman: Well, perhaps "approved" is the wrong word. In other words, if the taxes were paid and the moneys were accepted without disputing the assessment.

Mr. Dierker: That is right.

One of the points that concerns co-operatives greatly is that this proposal will have the effect of substantially reducing the amount of moneys available for patronage refund. As some of you gentlemen may know, co-operatives get their equity capital—their corporate capital—by way of the re-investment of patronage refunds. The moment the patronage refunds are reduced the equity capital, of course, is being reduced. This is a serious consequence of this. The equity capital in a co-operative continues to revolve for the payment of members' equities.

The Chairman: The newspaper this morning, which is the only source we have at the moment of the proposed amendment, recites this, and perhaps you will tell me whether it is reasonably accurate and what you think of it:

> The Government now proposes that patronage dividends could not reduce income after interest to members, below the lesser of: 5 per cent of members' capital employed, or one-third of the income before patronage dividends, but after interest to members.

Is that reasonably accurate?

Mr. Dierker: That is accurate. There was an amendment before the house yesterday to provide that a co-operative has a right to elect the tax base on which it will pay, either the five per cent capital employed or the one-third income.

The Chairman: Is that satisfactory to the co-ops?

Mr. Dierker: No, it is not.

The Chairman: What is there that is not satisfactory? The fact that they use the capital base at all? Is that it?

Hon. Mr. Phillips: Would you appreciate the opportunity of choosing between Scylla and Charybdis, between the rock and the swirling waters? Is that the option given to you?

Mr. Dierker: That basically is the option given to us.

The Chairman: You mean you are going to drown in any event.

Senator Connolly: Have you stopped beating your wife yet?

Mr. Dierker: The one-third income situation is of assistance to co-operatives who are in very serious financial situations. It will help when you are at the door of bankruptcy on a very low income basis. Keep in mind, gentlemen, that we got these late last evening, but the calculations we have been able to make indicate that they are not satisfactory in the general operations of co-operatives.

Senator Connolly: Have you had discussions with officials in the Department of Finance about these points?

Mr. Dierker: Yes, we have.

Senator Connolly: Before these amendments were brought in?

Mr. Dierker: Yes, we did. The proposal the co-operatives made to the Department of Finance and to Mr. Benson was that co-operatives be permitted to deduct all patronage refunds made, and that at the time of the payment of these patronage refunds they pay to the government a withholding tax. One of the problems, as you appreciate, in patronage refunds, is that there has been a suggestion that if co-operatives pay patronage refunds the payment of the tax is delayed. In a corporation you have the payment of tax and then the distribution of dividends, and the ultimate tax

settling is fairly prompt. In the case of the co-operatives the patronage refund will be made and will be taken into income only the year after. We have attempted to answer this by saying that at the time of making the patronage refund the co-operative pay to the government a withholding tax, which would be creditable to members for the payment of tax on these patronage refunds, and get rid of the capital employed formula once and for all.

The Chairman: I notice, too, it is proposed in the amendments to phase out the additional liability created by this formula. What the paper says is:

> Phasing in the new income tax rules in this way will give the credit unions and co-operatives time to adjust to their new taxable status.

The phasing in is that the rebates will be phased in over ten years by collecting one-tenth of the increase in the first year, two-tenths in the second year and so on. What comment have you to make on that? This is really attempting to make the treatment or the medicine more palatable. Or does it?

Mr. Dierker: It certainly is a form of carrot; there is no question about that. That statement is not in legislative form at the present time. We are presuming that it will apply to co-operatives. We have had some indication that it will.

The Chairman: Was this a request you had made in this form?

Mr. Dierker: No, we did not make this request. Our request has always been that the government should get rid of the capital employed formula once and for all and deal with patronage refunds as an expense to the co-operative doing business. Keep in mind that under all the incorporating statutes—and again we are talking about provincial legislation, as we were with the credit unions—co-operatives must allocate to their members the surplus earnings at the end of the year. It raises some horrendous problems when you consider that the Government is suggesting that the co-operatives keep one-third of their income as a form of discretionary income, which may well be in conflict with provincial statutes requiring them to distribute.

The Chairman: I take it these are co-operatives whose chief business is the sale of, say, farming machinery and equipment of all kinds?

Mr. Dierker: Yes, there are.

The Chairman: If you take the two positions, the co-operative position taxwise and that of the person who is not a co-operative but has a general business operation, in a general business operation the corporation would pay income tax on its earnings, and the shareholder receiving dividends would pay income tax at the marginal rate. For the co-operative engaged in the same field, your suggestion is that the only income tax on the co-op would be to the extent that they set aside tax paid reserves, they would have to clear them for tax purposes at regular rates, and so long as the capital formula applies that amount created by that formula would be taxable income. Is that right?

Mr. Dierker: This is what is proposed.

The Chairman: The sum total of those taxes on the co-op would be, I suggest, substantially less than the private individual engaged in that business would pay.

Mr. Dierker: To answer the question whether it is less or not, you have to take into consideration the corporation and its shareholder, and the co-operative and its member or shareholder. A corporation which has in fact paid tax can then pay out a dividend, in respect of which the member will receive a dividend tax credit, so that ultimately we get down to not too far from personal tax rates.

The Chairman: You think the dividend tax credit the shareholder would receive would balance out any advantage the co-op has in operating according to its methods and the lower rate of corporate tax it would be subjected to? That would be a balancing out in the hands of the shareholder.

Mr. Dierker: The rate of tax in the co-operative and in the corporation will be the same. The quantum of tax actually paid may be less after the co-operative has paid out patronage refunds.

Senator Lang: Otherwise co-operatives would incorporate, would they not?

Mr. Dierker: Would incorporate?

Senator Lang: Yes, if your tax was the same or greater than a corporation a co-operative could incorporate.

Mr. Dierker: This is right. Well, co-operatives are corporate bodies.

Senator Lang: But they could incorporate as a normal corporation.

Mr. Dierker: That is right.

The Chairman: If they did they would pay more taxes.

Mr. Dierker: That is not necessarily a correct statement, senator, because the patronage refund provision is available to corporations, though it is primarily adapted for co-operative methods of operation. Any corporation can make volume discounts.

The Chairman: What I am getting at is that the patronage divided really parallels the dividend that a regular corporation might pay to the shareholders, does it not, having regard to the consequences in the hands of the receiver of the dividend?

Mr. Dierker: It certainly parallels it to the extent that it is a flowing out of the earnings into the hands of the individual.

The Chairman: Yes, and it is subject to whatever his marginal rate of tax might be.

Mr. Dierker: That is correct.

Hon. Mr. Phillips: You are midway between the reactionary and the Marxist, is that not it?

Mr. Dierker: That depends on which philosophy book I am reading.

The Chairman: Which one are you reading?

Mr. Dierker: There is one thing, gentlemen, that you should keep in mind when we talk about tax credits. It is that, under this proposal, and even under the amendments to the proposal on the basis of which co-operatives have the right to elect to pay this tax on this one-third of income, if they do elect to pay that taxes and then do elect to distribute this as patronage refund, there is no tax credit to the co-operative for that.

The Chairman: That is right.

Mr. Dierker: And keep in mind that if you pay tax on one-third of your income, that is one-sixth of your income in respect of which there will be no tax credit at all.

The Chairman: There appear to be balancing-out features. When the patronage dividend is in the hands of the receiver, he is not entitled to a dividend tax credit.

Mr. Dierker: We are not concerned with the payment of the patronage refunds that operate as an expense to the co-operative. What we are concerned about is the patronage refunds which could, if paid out of tax paid surplus; and there is no credit given for that. Secondly, if you put that money into reserves and do not pay it out as a patronage refund, you will every year have to pay tax on the money you put into reserve. That is one of the inconsistencies.

Hon. Mr. Phillips: I was interested in the first point raised. Why do we employ this concept of capital employed, as against all other taxing nations dealing with co-operatives who do not? What is the origin of it?

Mr. Dierker: It commenced in 1946.

The Chairman: The McDougall Commission?

Mr. Dierker: No. The McDougall Commission did not recommend it.

The Chairman: It was before them as part of their material.

Mr. Dierker: It came in in the form of legislation after the McDougall Commission had reported.

The Chairman: Yes.

Mr. Dierker: But the McDougall Commission did not recommend a capital employed tax.

Senator Connolly: Why?

Mr. R. H. D. Phillips, Research Director, Saskatchewan Wheat Pool: Mr. Chairman, could I respond to that? My understanding of the history of this, Senator Phillips, is that following the McDougall Commission the recommendation was that co-operatives ought in fact to be able to distribute earnings to members and they would then become taxable in the recipients hands. But somewhere betwixt that recommendation and the legislation which followed, there was introduced the proposition that, notwithstanding, a co-operative, because it is a corporate enterprise, has corporate income, and this was a measure of that corporate income, and my understanding is that the 3 per cent rate which now applies was at that time a reasonable long-term rate, in long-term government bonds.

Senator Lang: That is right.

Mr. R. H. D. Phillips: You will recall that the white paper suggested that the percentage ought to be related to the Government's Treasury bills now.

The Chairman: Yes.

Mr. R. H. D. Phillips: And that the legislation advance is the number of five, which is somewhere midpoint in this and has no more rationale, in my view, than that. That is the history, as I understand it.

The Chairman: I know something about the McDougall Commission, because I was appearing before it on behalf of some people.

Mr. R. H. D. Phillips: I would like, if I may, Mr. Chairman, to respond to the question you had about the recurrence of the patronage dividend from a co-operative to its member, as being similar to a dividend on share capital in an ordinary corporation. This is an illusion, Mr. Chairman, and it is in this respect that the return paid by an ordinary corporation is a return on the basis of the recipient's portion of its ownership. The return in respect to a co-operative is a sharing of the total earnings, in the same way, if I may put it, that a firm of lawyers may share earnings among the partners.

The Chairman: Except that some of them do not share them equally.

Mr. R. H. D. Phillips: They do not in a co-operative, either. They share them on the basis of their participation in the business, and I presume that is how lawyers do it.

The Chairman: The shareholders share in the earnings of the corporation on the basis of the percentage of their holdings.

Mr. R. H. D. Phillips: That is right, but in a co-operative the shareholders have elected not to receive a return on the shares, literally, and this is allowed by law.

The Chairman: Are there any other questions on that point?

Senator Connolly: You say that in a co-operative the participants elect not to take a return on their interest in the co-operative?

Mr. R. H. D. Phillips: In some co-operatives, yes.

Senator Connolly: Surely, the patronage dividend is a return to them?

Senator Burchill: Not on the shares.

Mr. Dierker: Not on the shares. The patronage refund has no relationship to ownership.

The Chairman: If it does not, then everyone would get the same amount?

Mr. Dierker: No. The amount varies in accordance with the business you had done with the co-op.

Senator Connolly: It is based on use, on use of the co-operative.

Mr. Dierker: That is right.

Senator Connolly: The yardstick is variable from year to year, depending upon the amount of business you do with the co-operative.

Mr. Dierker: Exactly.

Senator Connolly: While in the case of a share, if the shareholder does not buy any more shares from one year to another, he gets the same percentage as he always would get in relation to the whole?

Mr. Dierker: That is correct.

Senator Burchill: Mr. Dierker, you indicated that you thought that possibly the change in Bill C-259 was due to the fact that your payments were not made in time. There was a factor of time there, in that your payments were not made until the following year? Did you not say something like that?

Mr. Dierker: I suggested that we proposed to the Government a system whereby co-operatives be permitted to pay out patronage refunds without reference to capital employed. At that time they paid a 10 per cent withholding tax.

Senator Burchill: But why is there that year's delay in sending in your tax? Why is it not possible to send it in in the year of the business?

Mr. Dierker: There is not a year. It is simply that the co-operative declares the patronage refund at the end of the year. It goes into the individual's next tax return. It goes immediately into the individual's next tax return.

Senator Burchill: It goes into the year in which you are operating?

Mr. Dierker: No, it goes into the year in which you receive the patronage refund, which may be the next year. It becomes income when it is made.

The Chairman: What you are really asking us is that we should support an amendment which would remove the capital formula for determining income?

Mr. Dierker: That is correct.

The Chairman: Is that right?

Mr. Dierker: That is exactly it.

The Chairman: Is there anything else? Let us assume that we did that. Whether the Government accepts it or not is another question. When it comes down to an issue as between the two Houses, and they both stand firm, that is another question that will have to be resolved at that time. There are all these interesting possibilities. Is there any other point?

Mr. Dierker: Mr. Chairman, if co-operatives were permitted to deduct patronage refunds without reference to capital employed, the balance of the related problems are automatically eliminated. If it stays in, there are many problems. As I indicated, there is no passing on of credit; you immediately get into the $400,000 limit and we can go through the same type of discussion as we did with the credit unions. You have a mare's nest of problems in connection with capital employed.

The Chairman: Alternatively, you would want us to look at this on the basis that you might not achieve your objective in having the capital formula removed. You might have some second best course that you would want to put forward, is that right? Or, is it all or nothing?

Mr. Dierker: That is a difficult question for me to answer. We would hope that it is all. We would hope that we would get rid of capital employed. However, we have to be practical. If it has not been done away with in the amendments proposed yesterday by Mr. Benson, we would think there are substantial modifications that are required to the capital employed formula.

The Chairman: I will come back to that in a moment. Is there any way in which you could give an estimate as to what the difference in tax revenue would be, to the Government, between using the capital formula and not using it?

Mr. Dierker: I do not know. I do not think we could, because you have to estimate then what co-operatives would do. You have to keep in mind that the bill provides that co-operatives may, in fact, eliminate their taxable income to zero, providing they pay it out in interest. So we then have to guess whether co-operatives will pay interest, and, if so, how much. I do not know that anybody could really make an intelligent guess on that.

The Chairman: It would be practicable to follow that course and pay it out in interest, would it not?

Mr. Dierker: We think it is practical as a corporate move, but it is not what the co-operatives wish to do because they wish to pay out the earnings as a return on patronage and not as a return on capital, and the interest, of course, is a return on capital. Secondly, most co-operatives are incorporated on a share basis. Dividends are not deductible from this, even if they wanted to pay it out.

The Chairman: No, but what you said was that you could reduce your tax in the co-operative down to zero if you paid out your earnings in the patronage dividends.

Mr. Dierker: Right.

Mr. Melvin: The problem there, Mr. Chairman, is that for co-operatives this would amount to a voluntary

abandonment of their essential character. That they are certainly not willing to do.

The Chairman: Well, we are just exploring the possibilities here. Mr. Dierker gave the answer that the co-operative could reduce its tax liabilities to zero by paying out its earnings in patronage dividends. I am just pursuing that. What are the objections to following that course. Would they run out of working capital, or what?

Mr. Dierker: To pay it out as patronage refunds?

The Chairman: Yes.

Mr. Dierker: I think the comment I made was that co-operatives could reduce their taxable income to zero by paying interest on member equity to the extent of 5 per cent on capital employed and then paying the balance out as patronage refunds.

The Chairman: Yes.

Mr. Dierker: If the co-operative could pay out everything as patronage refunds, there would be no problem in the co-operative structure. From the best guesses that we can make, if this is permitted together with something in the order of a 10 per cent withholding tax, we should be very parallel to what the Government has proposed.

Hon. Mr. Phillips: Admittedly certain portions of the patronage dividends are not taxable in the hands of the recipients.

Mr. Dierker: That is right.

Hon. Mr. Phillips: There is a variability there with such things as foods and so on.

Mr. Dierker: That is right.

Hon. Mr. Phillips: Incidentally, is counsel to Seagram suggesting that beverages should be included in the patronage dividend deductions, or is it solely for pure foods and groceries?

The Chairman: Of course, you can always spend your dividends on the acquisition of products.

Hon. Mr. Phillips: I just wanted to know how it works out for patronage dividends.

Mr. Poissant: Mr. Dierker, am I right that you were suggesting that the real problem is a deferral of taxes, because some of the recipients of the patronage dividends would account for that revenue only in the following year although they are allowed to take it as an expense in the previous year. You have 12 months after the year-end to consider the payment of patronage dividends. The ordinary company would pay interest this year, would deduct interest this year and would calculate its income tax in this year, whereas you calculate your income and take into account only the patronage dividends paid in the following 12 months.

Mr. Dierker: That is correct.

Mr. Poissant: So there is a deferral of tax because they permit you to do that. Now you say you compromise this deferral of tax which is the problem, really. So now we are willing to have a withholding tax on the amount paid, and what was the amount of tax you suggested? Was it 10 per cent?

Mr. Dierker: Yes, 10 per cent withholding tax.

Mr. Poissant: And that would be paid in the year in which you take into account the expenses. For example, in year one, even though the patronage dividend has not yet been paid, it will be paid in year two because you withhold the patronage dividend in year one.

Mr. Dierker: We would pay the withholding tax at the time of paying the patronage refunds.

Mr. Poissant: Which is still a year after, though.

Mr. Dierker: No. It should not be.

Mr. Poissant: Well, you have up to 12 months after your year-end to consider patronage dividends as an element of expense in a year.

Mr. Dierker: In an operating co-operative, the patronage refund is paid through immediately. The problem in deferment is not really in the co-operative. The problem in deferment is when the recipient will take it into his personal income and settle the final tax bill.

Mr. Poissant: There are two deferrals involved, I think. There is yours, because you would be allowed to take the expenses in the year after, although they would be taken as the current year's expenses, and then there would be the recipient's, who, it seems to me, would be taxed only in the following year.

Mr. Dierker: These things will of necessity balance themselves out as the co-operative operates. The withholding tax would be a compensation.

Mr. Poissant: At the time of payment. Well, at least some of the deferral would be reduced.

Mr. Dierker: It would be covered up.

Mr. Poissant: It would be covered up, yes, and you are suggesting a 10 per cent withholding tax for that purpose.

Mr. Dierker: We think that would be an adequate level, yes.

Hon. Mr. Phillips: Are the Government records clear on the point that we are the only country using the capital employed method in respect of co-operatives, where co-operatives function?

Mr. Dierker: I believe we have made that statement to the Government. They should be cognizant of it.

The Chairman: Mr. Dierker, if the capital employed formula were removed, then it would be easier for the co-operatives to reduce their tax liabilities to zero as co-operatives, except where they were creating reserves.

Mr. Dierker: That is right, yes.

The Chairman: And with respect to non-member business, which, incidentally, there has been no comment on, is non-member business a significant percentage of the total?

Mr. Dierker: Referring to across Canada the answer would be no. There are some individual co-operatives where the level is higher, but basically co-operative people have always felt that if the co-operative competes in the business market it should be dealt with as a corporation and as such they have no complaint with regard to income on non-member business.

Senator Isnor: The co-operatives do compete in regular business competition, do they not?

Mr. Dierker: In the sense of dealing with its members it is providing services to the members that they would otherwise go to some other place for, yes. To that extent it competes.

Senator Isnor: But dealing with it from the general public point of view, you cater to the public in general, do you not?

Mr. Melvin: The doors are open, sir, to the public, particularly in consumer co-operatives. To the extent that the public comes to the co-operative to make its purchases the co-operative is competing successfully and is quite prepared to pay tax on the earnings from that non-member business.

Senator Isnor: But your records would not show that.

The Chairman: Yes, they do.

Mr. Dierker: Yes. Our records show every dollar's worth of business. It is required that it be totally calculated.

Senator Carter: Do you keep the same accounts for non-members as for members? You distribute dividends in proportion to the amount of business each member has?

Mr. Dierker: Right.

Senator Carter: So you must keep a separate account for each member?

Mr. Dierker: That is correct.

Senator Carter: How do you find out? How do you know?

Mr. Dierker: Well, each member has his own membership number and when he makes a purchase this number is recorded and a computation is made at the end of a period to show the business done by that member with the co-operative. If it is a non-member, it is merely calculated in the total for non-member business.

Senator Burchill: Are you sure that taxes are paid on non-member business?

Mr. Dierker: Oh, yes, tax is paid on non-member business.

The Chairman: If there are no further questions on this point, is there a further point you want to move onto? Do you want to move into the area of modifications in the event that the capital-employed formula is not accepted?

Mr. Dierker: Well, I have already mentioned some of the areas that concern us greatly if the capital-employed formula continues. The first is that if co-operatives have to pay tax on this level and pay out patronage refunds out of this tax-free surplus, there is no credit. That to me seems to be inequitable.

The Chairman: That is in your brief?

Mr. Dierker: That is in our brief. We have also mentioned the fact that tax-paid surplus put into reserves should be annually retaxed. If there is going to be a capital-employed formula, it should be on member-contributed capital in the sense that it is on the moneys made available by the members to the co-operative. If you are going to deem a return on interest to members it should be on the money that they provide. It should not be on tax-paid surpluses which are annually provided. There are such other innocuous things in the capital-employed formula. For instance, if a co-operative revalues its assets for the purposes of security, or something like that, it would appear that this re-evaluation is included in the capital-employed formula and they will have to pay tax on the re-evaluation of their assets. It is a very innocuous package that has been put together. If for instance the co-operative gets a grant such as an area development grant, it goes into capital-employed even though it is not member-contributed capital. These are the things that are objected to.

Senator Isnor: But is it not up to you as to how you show it?

Mr. Dierker: No, it is provided in the statute that we must include that in the assets for capital-employed calculation.

The Chairman: What you are suggesting is that there should be a definition of "capital-employed" for the purposes of these provisions?

Mr. Dierker: Our suggestion is that if there has to be a capital-employed formula, the definition should be very simple and it is member-contributed capital, period.

Hon. Mr. Phillips: Are you therefore saying that if you retain the capital-employed method that patronage dividends should be assimilated to ordinary dividends? If the government retains the capital-employed method, are you saying that one aspect of the relief should be that the patronage dividends in the hands of the recipient should be assimilated like ordinary commercial dividends?

Mr. Dierker: Only those patronage refunds that come out of tax-paid surplus.

The Chairman: But we are not talking about what exists. We are trying to assimilate the position of the person who receives a patronage dividend as opposed to that of the preson who receives an ordinary dividend —in other words a dividend tax credit.

Mr. Dierker: Well, you could not have a dividend tax credit for those patronage refunds that act as an expense for co-operative income, but you should have a dividend tax credit for those patronage refunds that the co-operative pays out of tax-paid surpluses. I also want to reinforce the comment that despite these objections, co-operatives basically object to the concept that their form of capital must have a computed return. That is it in a nutshell.

Senator Walker: It is the change in principle that you object to?

Mr. Dierker: Well, the capital-employed formula as it presently exists, we object to its existing and to its continuing to exists.

The Chairman: Mr. Dierker, I was wondering if making the assumption that the capital-employed formula continues, you could do this sort of thing; could you give us the shortest statement in the world—other than just "yes" or "no"—say, four points as to modifications, without any development.

Mr. Dierker: Would you like to have that in writing?

The Chairman: Yes, and as quickly as we can get it.

Mr. Dierker: Within the next day or two.

Mr. Martin Legere, Chairman, The Canadian Council of Cooperatives: Mr. Chairman, as it is already midday, I will be brief.

First, I ought to thank you very sincerely for the wonderful welcome that you have given me.

We are happy to see that there have been some amendments since yesterday proposed for the bill, however we wish to tell you frankly that we are not satified with the proposed amendments, as I have the impression that the mistake is very simply being moved from place to place. I believe that it has still been forgotten,—and we have to say it again for the hundredth time perhaps— that there is a distinction to be made between a co-operative institution and capitalist institution. I believe that the problem is precisely at this stage where the distinction should be made, and I believe that the law-makers ought to be ready to introduce the amendments we are asking for. Moreover, I believe that the social role of cooperatives should also be considered.

I also believe that, in our country where a just society is preached, that consideration should be given to the fact that cooperatives and credit unions belong in this context. Unfortunately, in Bill C-259, no account has been made of the social fact of the cooperative movements.

Now, honourable Senators, I know your role is precisely to protect society, and we hope that in your recommendations, you will see to it that institutions such as credit unions and cooperatives, which are institutions really close to the people,—we hope you will see to it, and I say it again; that amendments are made to the present bill, and that our recommendations, which have been presented to you, will be put into execution.

Once again, a very sincere thank-you for your kind welcome.

The Chairman: Thank you very much.

The Chairman: Honourable senators, it is 12 o'clock and we have one other submission. I am told that if we proceed now, the principals will take not more than ten minutes. If the hearing should take longer than that it will be because of the length of our questions. I am referring now to the submission from Allstate.

Is it agreeable, Mr. Atkinson, that we proceed now on that basis? We do not want to shorten your discussion in any way if you think you can do a reasonable job in ten minutes, we will start now.

I should say, honourable senators, that we have the representatives of Allstate and they are: Mr. John Atkinson, President and Managing Director, Mr. Donald J. McRae, Financial Controller; and Mr. Michael G. Welch, Tax Supervisor.

As a preliminary question I should like to ask Mr. Atkinson if we can have his assurance that we are "in good hands".

Mr. John Atkinson, President and Managing Director, Allstate Insurance Company of Canada: Yes Mr. Chairman.

The Chairman: Do you wish to make an opening statement?

Mr. Atkinson: Yes. We are in Ottawa, Mr. Chairman and honourable senators, because of the grave concern that we along with our employees, have concerning the effect of the Tax Reform Bill on members of employees' profit-sharing plan. Some provisions of the bill would seem to be punitive and unjust to the employees.

In the brief I refer, of course, to the realization which is deemed to have taken place when the trust delivers to the retiring employee the shares which he has owned beneficially since they were purchased. Also I refer to the taxation of the resulting capital gain as ordinary income rather than as capital gain, thereby doubling the tax— in fact, much more than doubling the tax in most cases, because of the progressive tax rates.

We consider both of these provisions inequitable for reasons which are laid out in the submission before your committee, Mr. Chairman. I would like to emphasize that there is enormous concern and significance to the Canadian employees regarding our employees' profit-sharing plan. It undercuts their effort to provide for themselves in their retirement. This is especially true in the profit-sharing plans which count heavily on investment to achieve a worthwhile and secure retirement.

I would like to make a very brief commentary regarding the employees' profit-sharing plan as compared to the deferred profit-sharing plan. In our company, we have chosen to follow the course of the employees' profit-sharing plan; and 97 per cent of all eligible employees belong to our plan and pay taxes on all elements of income as they continue through their careers with the company. We are taxed on such items as the company's contribution to the plan, dividends from its allocated shares, income from general trust investments, lapsed credits due to those who have withdrawn from the plan before vesting into the plan, and, in the future, on taxable capital gains realized by the trust.

Now, in the deferred plan, the members of those deferred plans do not pay taxes on an incurred income basis. We are not suggesting for a moment that we should receive special benefit as it relates to capital gains under this bill. All we are asking is that the plan, under section 144 does not trigger a capital gains tax.

The Chairman: Then, as I understand it, if section 144 provided for a capital gains tax, your objection would not be the same?

Mr. Atkinson: That is right. We are accepting the principle of the capital gains tax.

The Chairman: The other point which you are objecting to is that a member continues in the plan he has to pay income tax over the entire period of the plan as the plan realizes earnings and as they are attributable to him?

Mr. Atkinson: No, we chose to follow this course right from its inception. What we are saying is that under section 144, the treatment of the employees' profit-sharing plan triggers a capital gains tax, and it is taken into income at that point. We feel that this is a mistake. It is so discriminatory as far as the employees' profit-sharing plan is concerned.

Senator Walker: The shares which you beneficially hold for the employees, do you pay tax on that all the way along?

Mr. Atkinson: Yes, sir.

The Chairman: Yes, you pay income tax on them.

Senator Walker: And when he benefits from it, it is considered *in toto* and he has to pay tax on it.

Mr. Atkinson: One of the great benefits to us was that we paid our taxes as we went along, with the sure feeling that we would not be taxed on it when we took the plan out. Now, we accept this as a continuing principle; but we are deeply concerned about the fact that when the trust delivers the shares to us it triggers an income tax, under this bill, at our personal rates, which is discriminatory.

The Chairman: Is this the sum total of your submission?

Mr. Atkinson: Yes, this is the sum total.

Senator Walker: This must be a mistake.

Mr. Atkinson: Yes, we think it is very discriminatory and we have communicated that to the department, but up until the present, it has not been changed.

The Chairman: It is hard to figure out the reason or logic behind levying the full income tax rate on a capital gain in this circumstance. This is a capital gain that occurs in the same way that all capital gains occur.

Senator Cook: There should be no change in the beneficial ownership because the trust holds the shares for the employees in any event.

The Chairman: That is right.

Senator Walker: And the tax is paid all the way through.

Mr. Donald J. McRae, Financial Controller, Allstate Insurance Company of Canada: I feel there is one other point which we should raise, and that is when the employee retires and is given his shares, under the present legislation, he is going to be taxed at that time without really realizing the sale of those shares; he is going to be taxed right away. Whereas in other types of trust he can get his shares, and he can sell them over a period of time, thus reducing the amount of taxes that we would have to pay. However, under this legislation, as it applies to our fund, he will be taxed as soon as . . .

Senator Isnor: Taxed on what?

Mr. McRae: On the capital gains.

The Chairman: On the capital gains, yes.

Mr. McRae: . . . as soon as those shares are delivered to him from the trust.

Senator Beaubien: Whether he sells or not.

Mr. McRae: Yes.

The Chairman: Then, there are two areas of capital gain, one that occurs during the current operation of the plan . . .

Mr. McRae: And then again when we sell the shares.

The Chairman: Not when you sell the shares, but when they are delivered.

Mr. Atkinson: Yes, when they are delivered, but subsequent to that, when we sell them.

Mr. Michael G. Welch, Tax Supervisor, Allstate Insurance Company of Canada: If the trust realizes a capital gain, it is passed on to the employee in the year in which it is made and he pays tax on it. The point we are making is that his interest in the plan is of a capital nature, and he has paid tax on everything that went in to the trust. When he receives the shares from his capital interest he should be able to receive them as such and only pay a tax when he disposes of them. They have been his, beneficially, from the beginning. And he should pay tax only when he disposes of them.

Then it should be a capital gains tax, although it is applicable to only half the total amount. So it would appear that there are two inequities here that seem hard to understand.

The Chairman: I should point out that under section 52(5), dealing with the cost of property transferred by the trustee under the employees profit sharing plan, it says:

> (5) Where any property has, after 1971, been transferred to a beneficiary by a trustee under an employees profit sharing plan,
>
> (a) subsection (1) does not apply in respect of the property;—

And this is the real stickler:

> (b) the beneficiary shall be deemed to have acquired the property at a cost to him equal to its fair market value at the time of the transfer.

So, there is a deemed realization at that time.

Senator Beaubien: At the time of the transfer, whether he owned it before or not?

The Chairman: Whether he sells it or not.

Mr. Poissant: Mr. Chairman, upon reading section 144, is this the point that you are making, it is deemed to be a cost acquired by the taxpayer; but is there a deemed realization by the trust at that time?

Mr. Welch: That is the second point; then we must consider clause 144(4). First of all it is clause 144(7).

Mr. Poissant: Yes, the exemption for capital gain realized from the trust is clause 144(7), a deemed realization by the trust.

Mr. Welch: That is a point you would also have to take up after considering clause 144(7). That is the definition of disposition of clause 54(c) should be made applicable to clause 144(4). The definition says "shall be this," but goes on that for greater certainty it does not include:

> (v) any transfer of property by virtue of which there is a change in the legal ownership of the property without any change in the beneficial ownership thereof,

That section should be made applicable; it is not at present.

Mr. Poissant: That is for the ordinary trust; there is no change in actual ownership.

Mr. Welch: That is right; in case clause 144(7) were amended and clause 144(4) remained as it is.

Secondly, clause 52(5) should be made to read as does clause 107(2), which applies to all other trusts. That is, it specifically excludes a deemed realization.

Mr. Poissant: Is that a deemed realization in clause 52(5), or a deemed cost to the taxpayer?

Mr. Welch: That has relationship to clause 144(7)(f).

We are saying that everything that cannot be attributable to these things will be taxed as income, and it says

> the portion, if any, of the increase in the value of property transferred to the beneficiary by the trustee that would have been considered to be a capital gain made by the trust in 1971 if the trustee had sold the property on December 31, 1971 for its fair market value at that time,

Mr. Poissant: In other words, we only need the deemed realization by the trust, because it would be in one of the exceptions. You are suggesting that this is ordinary income because it says that it is not in one of the exceptions. It is not a capital gain realized by the trust. Clause 52(5) is a deemed cost to the taxpayer, but we have no reference to a deemed realization. Clause 52(5), I agree, takes the cost based on fair market value, but nowhere do we have a deemed realization at that time; maybe it should be by the trustee.

The Chairman: Clause 52(5) only establishes the value to the taxpayer, which is fair market value at the time of the transfer.

Mr. Poissant: But who realized the gain?

The Chairman: That is a question of whether it is the trust.

Mr. Poissant: It is income, because it is not a deemed realization by the trust.

Mr. Welch: At present the word "disposed" in clause 144 is taken as not being a deemed realization.

The Chairman: But clause 144(4) makes the gain in the trust, or the loss as the case may be, a capital gain or capital loss to the employee.

Mr. Welch: As far as the trust sells my shares and gain is allocated to me as capital gains and I pay tax on it in that year. The tricky part of it is, what is the definition of disposition? When the trust gives me my hundred shares on my retirement, forgetting clause 144(7) and going back to clause 144(4), it provides that in a disposition by the trust. So we must have the security that disposition would not be interpreted in that way.

That is why I suggested that the definition of disposition in clause 54(c) should be made applicable to clause 144(4).

Mr. Poissant: But are you saying that you would not like this to be a deemed disposition by the trust?

Mr. Welch: All we are really asking is that the shares in the trust and any monies in the trust are of a capital nature to the member, and he should be able to receive either the money or the shares without triggering a capital gain. The only way a capital gain is triggered is by a deemed realization which, although it may not use the word "deemed" is the effect of clause 144(7) and it could be the effect of clause 144(4).

Mr. Poissant: Yes, but if we have a deemed realization of a capital gain, we only solve part of the problem. First we should have a roll-over; the cost base of the trust should be the cost base of the taxpayer.

Mr. Welch: Yes.

Mr. Poissant: If there is to be one, it should not be in the hands of the taxpayer but in the hands of the trust. If there is a roll-over there is no deemed realization.

Mr. Welch: One obvious suggestion is that clause 144(7)(f) instead of providing "the portion, if any, of the increase," should just say "the increase of the value of the property transferred" is excluded.

Senator Cook: There does not seem to be any rationale for a deemed realization.

The Chairman: No, it can be dealt with in a practical manner without any assumption of a deemed realization.

Mr. Poissant: Just a roll-over would solve all our problems.

Mr. Welch: Defining "disposition" as in clause 54(c) would cure the problem of clause 144(4). However, clause 144(7) is the less desirable of the two and must be solved first. In other words, clause 144(7)(f), instead of saying "the portion, if any," should read "the increase in the value", because it is clause 144(7) which triggers this tax to start with.

Mr. Poissant: As ordinary income.

Mr. Welch: That is our first request. We do not think that is right. Secondly, if that is changed, we are also worried about clause 144(4), because I cannot find any definition of disposition in the bill which would apply to that. There is a good definition at clause 54(c) which should apply to it but it has to be specifically set forth, because it is in a different section.

Mr. Poissant: In your opinion clause 54(c) would not apply to the employee in the profit-sharing plan?

Mr. Welch: It says that disposition is not a deemed realization.

Mr. Poissant: That is the definition of disposition and there is no restriction.

Mr. Welch: Yes, it defines disposition, but it says for greater certainty does not include any transfer of property, which is property such as our shares, by virtue of which there is a change in the legal ownership without any change in the beneficial ownership.

With that definition included it could not be held that disposed in clause 144 includes handing them over. Our view is that handing them over to the employee is not a disposition and we want it excluded.

Mr. Poissant: In other words clause 54(c) could be amended to make it clear that it does not apply in the case of shares; that is the roll-over.

Mr. Welch: The other point is that other trusts under clause 107(2), which are not necessarily retirement plans at all, are specifically excluded. They specifically do not have a deemed realization. In other words, clause 52(5) should read as does clause 107(2). Section 107(2) applies to other trusts and not a profit-sharing trust. It says quite specifically that when a property is handed over to the beneficiary, he receives it at what they call the cost amount, at the original cost of the property. He is deemed to receive it not at its current market value but rather at its original cost. This is very important.

Mr. Poissant: In other words, an amendment to 54(c) would do the trick; in other words, "to exclude"?

Mr. Welch: Yes. Section 54(c) should be made applicable to section 144(4).

Section 144(7)(f) should be made to read, not "the portion of" but rather "the increase of".

The Chairman: That makes more sense.

Mr. Poissant: Would you give us a draft of that?

Mr. Welch: I did not want to propose a specific amendment.

The Chairman: However, you are being asked to now, and very quickly. We will, of course, give you today and tomorrow in which to do it; but we would expect any amendments by Monday.

Thank you, gentlemen. That concludes today's hearing. The committee will adjourn until next Wednesday morning at 9.30 a.m.

The committee adjourned.

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THIRD SESSION—TWENTY-EIGHTH PARLIAMENT

1970-71

THE SENATE OF CANADA

PROCEEDINGS

OF THE

STANDING SENATE COMMITTEE ON

BANKING, TRADE AND COMMERCE

The Honourable SALTER A. HAYDEN, *Chairman*

No. 42

WEDNESDAY, OCTOBER 20, 1971

Sixth Proceedings on:

"Summary of 1971 Tax Reform Legislation"

(Witnesses—See Minutes of Proceedings)

24266–1

THE STANDING SENATE COMMITTEE ON BANKING, TRADE AND COMMERCE

The Honourable Salter A. Hayden, *Chairman*

The Honourable Senators,

Aird	Grosart
Beaubien	Haig
Benidickson	Hayden
Blois	Hays
Burchill	Isnor
Carter	Lang
Choquette	Macnaughton
Connolly (*Ottawa West*)	Molson
Cook	Smith
Croll	Sullivan
Desruisseaux	Walker
Everett	Welch
Gélinas	White
Giguère	Willis—(28)

Ex officio members: Flynn and Martin

(Quorum 7)

Orders of Reference

Extract from the Minutes of the Proceedings of the Senate, September 14, 1971:

"With leave of the Senate,

The Honourable Senator Hayden moved, seconded by the Honourable Senator Denis, P.C.:

That the Standing Senate Committee on Banking, Trade and Commerce be authorized to examine and consider the Summary of 1971 Tax Reform Legislation, tabled this day, and any bills based on the Budget Resolutions in advance of the said bills coming before the Senate, and any other matters relating thereto; and

That the Committee have power to engage the services of such counsel, staff and technical advisers as may be necessary for the purpose of the said examination.

After debate, and—

The question being put on the motion, it was—

Resolved in the affirmative."

Robert Fortier,

Clerk of the Senate.

24266—1½

Minutes of Proceedings

Wednesday, October 20, 1971.

(50)

Pursuant to adjournment and notice the Standing Senate Committee on Banking, Trade and Commerce met this day at 9:30 a.m. to further consider:

"Summary of 1971 Tax Reform Legislation"

Present: The Honourable Senators Hayden (*Chairman*), Blois, Carter, Connolly (*Ottawa West*), Desruisseaux, Gelinas, Hays, Isnor, Molson, Smith, Walker and Willis—(12).

In attendance: The Honourable Lazarus Phillips, Chief Counsel; Mr. C. Albert Poissant, C.A., Tax Consultant and Mr. Alan Irving, Legal Advisor.

WITNESSES:

Massey-Ferguson:

Mr. Peter N. Breyfogle, Comptroller;
Mr. Roy W. MacLaren, Assistant Vice President, Public Relations;
Mr. H. Arnold Sherman, Assistant Comptroller, Taxation;
Mr. Jahan P. Wleugel, Treasurer.

Canadian Jewish Congress:

Mr. Wolfe Goodman, Q.C.:
Mr. Saul Hayes, Q.C., Executive Vice President;
Mr. Barry Clamen, C.A.:
Mr. J.H. Berger.

At 11:50 a.m. the Committee adjourned.

2:15 p.m.

(51)

At 2:15 p.m. the Committee resumed.

Present: The Honourable Senators Hayden (*Chairman*), Blois, Carter, Connolly (*Ottawa West*), Desruisseaux, Gelinas, Hays, Isnor, Lang, Smith and Willis—(11).

Present, but not of the Committee: The Honourable Senator McDonald—(1).

In attendance: The Honourable Lazarus Phillips, Chief Counsel; Mr. C. Albert Poissant, C.A., Tax Consultant and Mr. Alan Irving, Legal Advisor.

WITNESSES:

Aluminium Company of Canada Limited:

Mr. John G. Lees, Vice President;
Mr. W. J. Reid, Vice President and Treasurer, Aluminum Company of Canada Limited.

At 3:50 p.m. the Committee adjourned until Thursday, October 21, 1971.

ATTEST:

Frank A. Jackson,

Clerk of the Committee.

The Standing Senate Committee on Banking, Trade and Commerce

Evidence

Ottawa, Wednesday, October 20, 1971.

The Standing Senate Committee on Banking, Trade and Commerce met this day at 9.30 a.m. to give consideration to the Summary of 1971 Tax Reform Legislation, and any bills based on the Budget Resolutions in advance of the said bills coming before the Senate, and any other matters relating thereto.

Senator Salter A. Hayden (*Chairman*) in the Chair.

The Chairman: Honourable senators, I call the meeting to order. We have several submissions today, the first being by Massey-Ferguson. Later in the morning we will hear the Canadian Jewish Congress. This afternoon we will deal with Alcan Finances Limited. Following our adjournment this morning we will resume at 2.15.

The appearances on behalf of Massey-Ferguson are: Mr. Peter N. Breyfogle, Comptroller; Mr. Roy W. MacLaren, Assistant to the Vice-President, Public Relations; Mr. H. Arnold Sherman, Assistant Comptroller, Taxation; and Mr. Jahan P. Wleugel, Treasurer.

Do you intend to make an opening statement, Mr. Breyfogle?

Mr. Peter N. Breyfogle, Comptroller, Massey-Ferguson Limited: Yes. Mr. Chairman and honourable senators, I would like to open my comments by saying on behalf of Massey-Ferguson that we are very grateful for this opportunity to discuss with you our views on the Tax Reform Bill.

It has become popular in recent years to play down the value of multi-national corporations to the economies of the countries in which they operate. This is an attitude which I personally consider unreasonable and I thought it might be useful for you if I quoted as an example some facts on Massey-Ferguson in Canada.

—Total assets employed in Canada are $230 million.

—We export from Canada 75 per cent of our production and we export two dollars of goods for every one dollar that we import.

—In Canada we have one of our major engineering centres which is, amongst other things, the centre for our world-wide combine engineering activity.

—Total Canadian employment exceeds 4,000 persons.

—Our world-wide headquarters are located in Canada, providing work not only for the company's own employees, but also requiring such outside services as lawyers, accountants, investment bankers, etc.

—We have more than 60 per cent Canadian shareholders and the dividends our shareholders receive result from operations throughout the world.

These facts demonstrate that Canada plays not only a significant role in Massey-Ferguson's total operations but also that our activities in Canada are important in the Canadian economy.

Since we had the privilege of appearing before you in May, 1970, much has happened to modify the proposals contained in the White Paper on tax reform, however the basic problem still remains. In my comments on that occasion I highlighted the four objectives explicitly recognized in the White Paper

1. The Canadian tax system should not encourage nor discourage foreign investment by Canadians.

2. Canadian companies competing in the foreign market should not be subject to more onerous taxes than their competition (particularly U.S. competition).

3. Canada should promote a climate hospitable to the unrestricted flow of capital across international boundaries.

4. Canadian tax laws should not permit the evasion of Canadian tax through artificial arrangements.

Bearing in mind the economic environment of the past few months and in particular the announcement of Mr. Benson last week, I would suggest that, even more than normally, industry and government share two basic desires—to create jobs for Canadian citizens, to create profit for Canadian shareholders, and in achieving these purposes to create revenue for the Canadian Government.

I said at that time that the White Paper proposals were in fact in basic conflict with the first three of its own objectives, and that the only principle that was given real recognition was the fourth—the anti-avoidance objective. The situation remains basically the same today despite the modifications between the White Paper and the Tax Reform Bill. Indeed, the draft legislation goes even beyond the stated intentions of the Minister of Finance during the presentation of the bill. The result is to increase the tax burden of Canadian companies, and in so doing ensures that the first three objectives which I have just mentioned cannot be achieved.

In the brief we prepared for discussion at this meeting, and in particular in the appendices attached to it, we have gone into some detail on possible alterations to the bill to ameliorate the situation. I do not believe it would be worthwhile for me to repeat these points at this stage, as you have all received the material.

Rather than comment in more detail on the Tax Reform Bill, I would like to preface our discussions with four basic points which, in our view, are more important than any specific technical contribution on the bill which we might make.

1. We have found the bill, as it affects multi-national corporations, to be extremely complex and, quite frankly, a frustrating diversion from the serious business questions

which we face—questions which have been so obviously accelerated by the recent United States' action.

2. The effect of the proposals relating to the taxation of the international income of Canadian-based multi-national corporations will be substantial. The proposals will result in a loss of international competitiveness or the departure of such corporations from Canada. While we cannot believe that this represents the intention of the Canadian Government, one or the other, or both, of these results are only a matter of time, if the proposed changes are enacted.

3. Quite apart from this long-term result and in addition to it, we are convinced that now is the wrong time for Canada to establish its long-term policies in the area of international trade and the multi-national corporation. Each of the major trading companies of the world is now engaged in adopting a stance for negotiations to maintain or expand its trading position. For Canada at this time to drastically impair its own competitiveness in international trade appears to us to be almost an incredible course of action.

4. The international provisions assume and require external treaty negotiations to be workable. This is clearly no time for the opening up of provisions of existing treaties or attempting to work out new treaties with the many countries with whom they are needed if the new approach is not to have the most serious adverse effect on our international competitive position. I doubt if any one of us would like the job of renegotiating the U.S. treaty today.

We question therefore the wisdom of attempting in a hurried manner to advance specific suggestions for technical improvements in the bill. Rather, we recommend simply deferring corporate and international provisions of the bill for at least a year. This delay will permit further study, allow time for the international trade picture to become more clear, and free business to deal with today's business problems without diversion of energy to cope with new tax provisions. These tax provisions will do nothing to improve our ability to contribute to the growth of the Canadian economy directly, or to enhance our ability to compete in the world economy and therefore contribute in the long-term to the attainment of the great potential of Canada.

Senator Isnor: What is the percentage of your export business?

Mr. Breyfogle: Seventy-five per cent of our production in Canada is exported from Canada.

Senator Walker: What about to the United States?

Mr. Breyfogle: Somewhere over 70 per cent of production. In other words, 70 per cent out of the 75 per cent.

The Chairman: Are your exports subject to the United States' surcharge?

Mr. Breyfogle: Most of our exports are not subject to the surcharge. However, they do get caught by the "US only" requirement for the investment tax credit, which is supposed to be reduced from 10 per cent to 7 per cent. That is a direct penalty.

Senator Connolly: Will the DISC program affect you?

Mr. Breyfogle: The DISC program will affect us not only because the US manufacturers of farm machinery will have a substantial financial advantage in exporting to Canada, but also because as a company we have tended to keep the greater part of our north American manufacturing facilities located in Canada rather than in the United States. Therefore we lose. Because of that, we do not have the opportunity that our competition has.

The Chairman: Let us analyse that. I take it that at present your competitors in the United States do export to Canada?

Mr. Breyfogle: Yes, sir.

The Chairman: You expect that in the atmosphere of the DISC it could lead to more exports, is that right?

Mr. Breyfogle: They will have an opportunity of obtaining a substantial benefit from a tax point of view. In 1970 the trade balance against Canada was $113 million in farm machinery. It consisted of $274 million imports by Canada and $160 million exports from Canada to the United States.

Senator Connolly: What is the imbalance?

Mr. Breyfogle: Last year the imbalance was $113 million.

The Chairman: The DISC would work to your disadvantage in the fact that the domestic United States manufacturer and exporter would enjoy a lower corporate tax rate in the United States on that part of his earnings which resulted from foreign operations.

Mr. Breyfogle: Yes.

The Chairman: What is the percentage of discount off the regular corporate rate?

Mr. Breyfogle: I should like to ask Mr. Sherman to answer that question.

Mr. H. Arnold Sherman, Assistant Comptroller, Taxation, Massey-Ferguson Limited: The present proposal is that the DISC company will be able to set up profit in its own books on the total transaction, on what the manufacturer manufactures and sells to the DISC, and the DISC resells to the company located in the foreign country, such as Canada.

They have three options. They can either take 4 per cent of the sales price as their profit, they can take 50 per cent of the total profit of the whole transaction, including the manufacturer's profit, or they can take the normal pricing basis if they feel that it is better for them. But in the third case, it is subject to the usual tax by the United States IRS authorities under section 42.

Senator Connolly: For the record, what does IRS mean?

Mr. Sherman: The Inland Revenue Service of the United States. In either of the first two cases, there is a small additional advantage. They can add some 10 per cent of their export promotion expenses to this profit. They look at the three possibilities and take the one that is most favourable. Profit in the DISC is never taxed until it is distributed to the shareholders of the DISC.

The Chairman: The concept is that you have the manufacturer in the United States who manufactures the equipment. Then you have a domestic sales organization in the United States that will obtain the foreign market and will be the vendor and exporter in that market. Regarding the 4 per cent that you were talking about as one of the options, they could take 4 per cent of the total dollar amount of the sales and bring that into the DISC. I am referring to this exporting organization. It is domestic in form.

Mr. Sherman: DISC means Domestic International Sales Corporation.

The Chairman: They can bring that directly into profit. Is that a tax-paid profit, or is it subject to tax after that?

Mr. Sherman: It is subject to tax when the DISC organization distributes it to its shareholder. The shareholder would normally be the manufacturing company in the United States. This tax can be deferred idefinitely. There is no requirement to make a distribution. It can be loaned to the parent company provided it is invested in export related assets. Export related assets are defined so broadly that effectively the DISC can retain the profit while lending the tax back to its parent company. In other words, there is no need for the tax to be paid for ten years.

The Chairman: Is it included in the definition of the use to be made of this money that it can be used to provide additional equipment to manufacture more exportable products?

Mr. Sherman: Yes.

The Chairman: And that is all without any tax deduction? In other words, this is tax deferral on a grand scale.

Mr. Sherman: Yes.

Senator Connolly: Would your American affiliate qualify under the DISC legislation?

Mr. Sherman: Yes.

Senator Connolly: There are so many questions I would like to ask.

The Chairman: That is a very interesting question, Senator Connolly. Would you like to develop it?

Senator Walker: We would like to know why they would, with the balance of trade the way it is.

The Chairman: Senator Walker, what I was thinking of here was that there are Massey-Ferguson affiliates operating in the United States.

I take it, Mr. Sherman, that the Massey-Ferguson affiliates in the United States manufacture a product which you export to Canada?

Mr. Sherman: Yes.

The Chairman: How much of the imbalance in exports that come to Canada from the United States is contributed to by your operations in the United States?

Senator Walker: That is a good question.

Mr. Sherman: We export to the United States $2 for every $1 we import, and we represent more or less 50 per cent of the farm machinery exported from Canada.

Senator Connolly: How much of the United States export of farm machinery do you represent in your United States companies?

Mr. Sherman: We would represent a little over 10 per cent of the exports from the United States into Canada. The United States exports twice as much into Canada as it imports from Canada. Our picture is exactly the other way around.

The Chairman: So that your American affiliates exporting from the United States to Canada could qualify under the DISC legislation?

Mr. Sherman: Under the DISC legislation we would set up a DISC corporation and receive the benefit for those goods which we manufacture in the United States and which we import into Canada.

The Chairman: Do the United States companies, who export to Canada and who are in competition in the export area, have other advantages by reason of being United States companies—advantages that are not available to you?

Senator Walker: Other than those under the DISC legislation.

Mr. Roy W. MacLaren, Assistant to the Vice-President, Public Relations, Massey-Ferguson Limited: At the present time the United States exporting corporations have been able to defer profit by the use of offshore subsidiaries. Although the United States enacted the sub Part F legislation in 1962, major corporations in the United States do not have any problem getting around those provisions because there are exceptions and alternatives and groupings that permit a U.S. corporation not to be penalized by the existence of this sub Part F legislation.

As of today a Canadian corporation is in the same effective position. Under the present Income Tax Act they do not have to pay income tax on dividends from foreign subsidiaries. There is an equivalent situation to the position of a United States corporation. However, once Bill C-259 is enacted we would not have this possibility to follow.

I do not feel it is clear from Bill C-259 that we would be taxed in Canada on the profits of our DISC if our United States subsidiary had a DISC, because that section of the bill has to be regulated. It seems clear to me that if we did have a DISC we would lose all of the advantage because when it retained the profit the profit would then be taxed in Canada.

The Chairman: Yes, because the profit of the DISC would enable your export company to maintain without tax in the United States, and you would have to bring it into your Canadian income and it would carry the full Canadian rate.

Mr. MacLaren: Yes.

The Honourable Lazarus Phillips, Chief Counsel to the committee: Would you not be subject to this extraordinary situation, that your DISC company in the United States would be an affiliate and if you lend the money to your parent on the deferral you would than have non-business income? You therefore would have foreign accrual property income which would be effectively taxed in Canada under the proposed amendments in this new bill that we are discussing.

Mr. MacLaren: Yes. What I am not clear about is whether we would not also be taxed on the DISC profit as well.

Hon. Mr. Phillips: Except that the indication is that the DISC profit would really result from normal business operations and, presumably, it might come under foreign accrual property income.

Mr. MacLaren: It might not.

Mr. Sherman: There is uncertainty in our reading of this area of the bill.

Hon. Mr. Phillips: But you do have the extraordinary situation where you get the DISC benefit in the United States, whereas automatically you are affected by foreign accrual property income. Incidentally, this would not be in 1976, but in 1973.

The Chairman: Yes.

Hon. Mr. Phillips: When speaking of an extension for a year are you suggesting that the sections of the law as presently drafted should come into effect on January 1, 1974; and when you speak of a deferral of a year with respect to dividends are you suggesting that such dividend income come into effect in 1977, rather than in 1976? I am wondering what you mean by deferral by a year. Could you develop that?

Mr. Sherman: What we are requesting is that consideration be given to deferral of enactment of the bill by a year, rather than the time cut-in of the provisions of the bill being deferred for a year. Our purpose there is to provide more time for deliberation, for calculation of the impact of the bill, and for reviewing some of the difficult areas of the text of the bill in terms of its application to multinational corporations, in particular. We believe that if this year is taken the character of the bill will be quite drastically changed, bearing in mind the trade problems which are facing Canada and many other countries.

Hon. Mr. Phillips: This is a very important point, Mr. Chairman, and honourable senators. Are you asking for the deletion of that section which deals with international income pending further consideration? Mere postponement by a year is the very thing that is presently covered in the draft. It seems to me you are either asking for deletion of that section pending further study or, alternatively, that 1973 should read 1974 and 1976 should read 1977.

Mr. Sherman: We are asking for deletion pending further study.

The Chairman: You appreciate that there are many beneficial things in Bill C-259 and, therefore, your request could not take the form of a request that we suspend the coming-into-force date of the bill.

Mr. Sherman: We are not proposing this for the bill in total, of course, sir.

The Chairman: Only for those sections that particularly affect your operations?

Mr. Sherman: Yes.

Senator Connolly: May I ask this general question? It does not really relate to the technical area you are discussing. You are obviously an important multinational Canadian-owned corporation. Are there many other such corporations in the Canadian economy? We do not want to be legislating here for one particular company, so perhaps you would give us some indication of the scope of this problem in terms of other Canadian-owned multinational corporations.

Mr. Sherman: If I could start by making a general answer to this question, it is this: Our belief is that the world is becoming rapidly more technology-oriented and that industry—national corporations and multinational corporations—will rely on a high degree of technology for the base of their future growth. It seems to us that Canada has two choices for its future development. It can either encourage multinational corporations, because a company operating solely in Canada, bearing in mind the population of Canada, is not large enough to support the technological base that is required to compete with other countries—

Senator Connolly: In some areas.

Mr. Sherman: In more and more areas as the world's history progresses.

Senator Connolly: All right.

Mr. Sherman: The other alternative is to obtain this technology from subsidiaries of multinational corporations based in other countries. We believe the former is the better approach for Canada.

I think Mr. Wleugel can recite you a list of these various companies in the Canadian economy.

Mr. Jahan P. Wleugel, Treasurer, Massey-Ferguson Limited: Such corporations as Alcan, Brascan, some of the brewery companies, International Nickel Company. The Polymer Corporation, which is a Crown corporation, is also a multinational corporation. All these companies are indeed affected by this regulation. I am quite sure there are others that can be mentioned, and that you will know of many other examples. These are the important names.

The Chairman: You did not mention Alcan.

Mr. Wleugel: I am sorry, sir.

Senator Connolly: It was that point that I thought we should have on the record, because in fairness to the witnesses we want to make sure that it is not just their problem; it is the problem of a good many Canadian-owned multinational corporations.

Senator Walker: Are they taking the same attitude in the present situation as you are?

The Chairman: Alcan is; we now have their brief and they will be heard this afternoon. I cannot conceive of any of them not taking that position.

Senator Molson: Did we not have that experience in considering the White Paper?

The Chairman: We did.

Senator Molson: I think the record far enough back would show that we have a great many multi-national companies who are very seriously affected.

The Chairman: All the briefs are still available, so we have quite a record compiled already. I was wondering which one of you would care to tackle this question. Suppose we take your situation operating abroad. You would have a foreign affiliate. Let us take the case where you control that foreign affiliate, and the case where you may have only 49 per cent because of national laws in that country. Let us take those two instances and follow through what happens to the earnings of those companies by reason of Bill C-259. Take the first situation, a foreign affiliate which your company controls, which has earnings. Go ahead and tell us what happens under the bill.

Mr. Wleugel: Could we, for instance, take our Mexican subsidiary? Would you first like one we control, or one where we have only 49 per cent?

The Chairman: These are two instances that I would like to have developed.

Senator Connolly: For the sake of making the record clear, I take it we have finished discussing the DISC problem and are now going on to the more general picture.

The Chairman: The DISC position in the States has adverse effects on Massey-Ferguson, or perhaps we should say adverse aspects. For our purposes now perhaps that is as much as we need.

Senator Connolly: That is right.

The Chairman: Now would you get back to my illustration?

Mr. Breyfogle: Could I perhaps make one more comment on DISC. DISC is one part of a United States program, which will be difficult for other countries to cope with. However, it is only one part of an environment in which a company can do business on a multi-national basis. Perhaps of as much significance as DISC itself is the relationship of DISC to the other opportunities granted by legislation in various countries to do business. We therefore feel that the DISC is very appropriate in relation to our discussions on Bill C-259, because there are things we now have which provide assistance to multi-national corporations, which provide an off-set to the DISC in some way but not as a complete off-set. Bill C-259 takes those away, and this is most important to us.

Senator Connolly: Would you think that a DISC legislation in Canada would be a good thing for the Canadian-owned multi-national corporations?

The Chairman: You mean something like the DISC legislation?

Senator Connolly: Legislation, yes.

Mr. Breyfogle: In theory, yes, it would appear to be a good thing. We are concerned about the cost of such a program in Canada, and therefore whether it is practical, or whether there are alternatives that would maintain Canada's competitive posture without going to the lengths of DISC.

The Chairman: But what you have now in Canada under our tax laws works satisfactorily as an off-set to DISC operations in the States.

Mr. Breyfogle: I would say as a partial off-set to DISC.

The Chairman: You have been able to live with it.

Mr. Breyfogle: There has not yet been a DISC in the States, fortunately.

The Chairman: When you say "partially" what do you mean? If you had DISC in the States and you continued with the present law in relation to your offshore operations and the bringing home of the earnings, to what extent do you mean it would partially off-set it?

Mr. Sherman: There would need to be further relief, I think, to take account of the fact that a Canadian corporation pays its income tax very much more quickly than a United States corporation, so there are different cash flow consequences. DISC is very much a matter of cash flow.

The Chairman: What is the difference in the period for cash flow?

Mr. Sherman: A Canadian corporation begins to pay right at the beginning of its fiscal year. The United States corporation has a delay of several months, and the payments are spaced out more over a longer period. I am sorry I do not have the information in my head, but there is a considerable gap. We did look at the timing, and there is quite a big difference in favour of the United States corporation.

Senator Carter: Do you foresee developments in other countries that might compel the United States to modify their DISC legislation?

The Chairman: What you are asking them to do is look in the crystal ball world wide to see if they can see anything brewing there that might be inclined to compel the United States to abandon or reduce its DISC.

Mr. Breyfogle: I think the history of events since August 14 has demonstrated that the United States economy, with all its problems, is still a very significant economy in world affairs. It is still a very highly self-contained economy, and it can go its own way. The DISC advantages are very material in the United States. On the other hand, the sort of advantage provided by many European countries, for example, through tax rebates and turnover tax that is refunded on exports, does not put them in a very good position to put pressure on the United States Government to remove the DISC.

Mr. Wleugel: I think the DISC has perhaps been driven a little out of proportion as far as being an example of typical tax devices used is concerned, because here in Canada you naturally look very much more closely at what the United States is doing in these areas. For

instance, Germany has for years had the same type of incentives, not more in connection with the matter of setting up a separate corporation, which really the DISC essentially is, but as a simple tax device in their own tax laws, making for what in essence are either accelerated depreciations related to investments abroad or, in essence, actually permissions in write-off against German domestic taxes on investments abroad.

Just to mention one example, the United Kingdom had its Export Corporation Act, which permitted, actually also legalized, a DISC or a tax deferral of even a larger extent that the United States. This was discontinued in 1966-67 essentially because of exchange control regulations in the United Kingdom. On the assumption again there that the basic reasons for having it would still be valid, one could also speculate that if and when the monetary crisis and the imbalance of exchange rates are being settled, the United Kingdom might take their export corporation concept up again. There is a multitude of ways of doing it. The Japanese do it by permitting the companies to have a leverage of one-to-ten, and substantial direct subsidies to exports. I think we should be very careful here in Canada, not necessarily to say—because the U.S. might find the DISC is the ideal solution on the basis of its setup, on the basis on which it operates—that we should necessarily follow just because of that. I think we would have to look very carefully at what is required.

The Chairman: I did not gather that there was any suggestion here that DISC should be adopted in Canada.

Mr. Wleugel: No.

The Chairman: You were starting out by saying that the system we have at this time, in bringing the dividends home without paying any Canadian tax on them, does give some advantage as an offset to Canadian export sales. It permits them to be a little more competitive. We are not saying that DISC would do the job better. Each country evolves its own tools, you may take it, in fiscal policy, in taxation, in tariffs, in incentives, in subsidies, and in an infinite variety of things. But my question has not been answered yet.

Senator Connolly: I am afraid we diverted the witness from your question.

The Chairman: I would like to get back to that now.

Mr. Wleugel: The basic question?

The Chairman: Yes.

Mr. Wleugel: You mentioned you would like two specific examples. We would like to take the example of the U.K. group of companies which is a subsidiary, as far as Massey-Ferguson Limited is concerned. It is a holding company in the U.K., with operating subsidiaries in the U.K. that is one example. We would like, as a second example, to take a Mexican minority controlled subsidiary. It is a simple example and I think it makes the point very clearly.

With your permission, we should like to add a third example, which is actually in specific legislation. For instance, in a country like Brazil, you have specific incentives through taxation to invest portions of your tax money, as you have to, in the northeast of Brazil, as part of the development of that area. All these three groups have very specific problems related to the current bill. With your permission, Mr. Chairman, I would like to ask Mr. Sherman to go through these technically in detail, to follow the route of dividends and other problems in these three typical examples. There is a multitude of others, but I think these will do.

The Chairman: Those three will do. Now, Mr. Sherman.

Mr. Sherman: Mr. Chairman, we start with the U.K., which has a nominal comprehensive tax treaty with Canada, and we must assume that there will be a treaty in effect for the purpose of this discussion. Therefore, under Bill C-259 there will be no Canadian tax on dividends paid by the U.K. to its Canadian parent. However, so far as the foreign accrual property income is concerned, the consequences are not at all clear, either from the bill, which does not have too much on, nor from the Department of Finance press release.

For example, take a group such as ours, of manufacturing companies, trading companies, export, agency companies, where altogether there are probably 30 companies in the U.K. of which perhaps 10 or 12 are active. Of these companies, some would be in a loss position, just from the way things operate, and under the U.K. tax system one company can make good the losses of the other.

We are afraid that if we did that, that payment would become foreign accrual property income. We are not sure what the consequences are, but we are afraid of them.

There are similar problems. For example, if our U.K. engineers were to develop something and another U.K. company wanted to use it, and the company, the third party using it, were to pay a fee, we are fairly certain that that royalty or fee for technical services, or whatever it was, would be part of the foreign accrual property income.

The consequence of any of our U.K. companies having foreign accrual property income is that that income becomes taxable as earned to Massey-Ferguson Limited, whether or not we declare it as dividends, whatever we do, even if we have no intention of bringing it back because the funds are required for U.K. expansion.

There is a further category I did not mention, which is probably more important, that is, intercompany interest. We have a holding company, a Canadian company would make an advance to that company, and then the advances would be used, perhaps, as they are required, by different operating companies. To the extent that interest was charged on those advances within a group of U.K. companies, this would probably be foreign accrual property income and again taxed in Canada as earned. We have to charge interest under U.K. tax rules; if we do, we are taxed in Canada.

Senator Connolly: At present, you would not be taxed, under the existing law.

Mr. Sherman: That is right. That is the U.K. situation.

The Chairman: Just stopping right there, you have a series of subsidiaries in the U.K. and they are subsidiaries of the chief company in Canada. Let us take the inter-relationship there. If one of those companies makes a loss and

another one makes a profit, for Canadian tax purposes you are not entitled to offset.

Mr. Sherman: No.

Senator Connolly: Under the new bill.

The Chairman: Under Bill C-259.

Mr. Sherman: Under Bill C-259, the results of each individual company are of no concern to us, because there is no question of taxation on dividends. It is only the question of foreign accrual property income, which is a new concept.

Senator Connolly: It is a new concept?

Mr. Sherman: To the extent that one company has foreign accrual property income and the other has what one might call a foreign accrual property income loss, we are not permitted to offset them. It is one way taxation.

Senator Connolly: Would it be a temporary, even a partial advantage, if there were such things as foreign accrual property income profit and foreign accrual property income loss?

Mr. Sherman: Yes, this is one of the minor measures that would help. certainly.

Senator Connolly: You would still have the problem of taxing the foreign accrual property, if you had foreign accrual property income, under the new Bill C-259, which you have not under the existing law.

Mr. Sherman: That is right.

The Chairman: Is there any difficulty by reason of the fact that it is conceivable under this bill that something which produces earnings from active business operations might lose that character under Bill C-259 and become in part, or altogether, foreign accrual income property?

Mr. Sherman: We really do not know what the concept of an active business is, and I have not been able to find any lawyer in Canada who could tell me what the concept is. It would be unwise for us to proceed on the basis that some of these things are not applicable, since undoubtedly the Department of National Revenue, when it comes to audit our 1973 return, will atempt to tax us on its viewpoint.

Hon. Mr. Phillips: It is always unwise to depend upon lawyers in doing things in that way.

The Chariman: We are not looking for any rebuttal evidence.

Mr. Sherman: We do operate through one holding company in the U.K. which holds a group of mnay subsidiaries. That is our corporate structure in the U.K.

The Chairman: That holding company is the one which would remit directly to the Canadian company?

Mr. Sherman: Yes.

The Chairman: Then by that route what one would ordinarily thing of as income from active business operations could, under this bill, very well be foreign property accrual.

Mr. Wleugel: Since it is routed through a holding company, I think anybody looking upon the corporate structure in the U.K. would say that it is the only sensible way of setting up the corporate structure financially in the way we run the interactions between the various units. We have a holding company which is obviously and absolutely a corporate arrangement, and the question that arises in our minds is whether we will get stuck with taxes actually, potentially, or possibly on the basis of our normal operating income. The answer is something we do not know.

The Chairman: You are saying that the bill is defective in that it does not define some very essential terms.

Mr. Breyfogle: We consider the bill is defective in that it does not properly define a large number of terms.

Mr. Wleugel: Particularly in the section on international income, which is what we are particularly concerned about.

Hon. Mr. Phillips: I wonder, Mr. Chairman, if you will allow me to suspend the consideration of the two other countries, because this has a direct bearing on what we are now discussing. This Senate committee took the position under the White Paper that we were putting the cart before the horse in dealing with the whole question of international income. We so stated in our report at pages 42 and 43, and on the whole history of taxation of international income we took that position.

In effect, we said, "Put through the treaties first and we will know what our treaty countries are and we will know what are not treaty countries." Then, in dealing with the laws of each treaty country or non-treaty country, a multinational corporation will know the incidences of taxatin within reason.

When I speak of international income I am speaking of that section which deals with international income of Canadian taxpayers, not the reverse—that is, the income of non-residents and income of Canadian sources—and I should like to know whether we would solve the problem for the present with the suggestion that there are three alternatives: One, that we ask for the deletion of the whole section because of the chaotic and confused situation in the modern world. Two, that we ask that 72 read 73, and 76 read 77, so that we have a respite of two years rather than one year. Three— and this is the one that I like best and would like your reactions to in relation to the Chairman's request—that in regard to the income of the Canadian multi-national corporation in respect of any company from a source other than Canada, the application of the present law be suspended until such time as there has been either the completion of a treaty with a country, or a statement by Canada that it is not able to get a treaty. Essentially, the whole section covers what is an affiliate, the treatment of dividends from the affiliate, and, this foreign property accrual income. The determination of what an affiliate will be, of what dividend income treatment will be like, and what foreign property accrual income will be like will depend upon the treaties. This is the delay as covered by the bill in section 72 and moving into section 76. Would not the multi-national corporations be better off in suggesting that the application of this section be suspended until such time as we are dealing either with the treaty country or non-treaty country? In

the interval the whole subject matter could be dealt with by the Government either by way of revising its thinking on the domestic wording of the legislation and the regulations therein, or by determining whether there is a treaty. That is why when you deal with Canada and the U.K. you have one set of rules, whereas with respect to Mexico, which you are going to come to, you have another set of rules, and with respect to an undeveloped country you will have another set of rules.

The Chairman: In that connection, Canada would not be at a disadvantage in dealing with any questions that could be classified as tax avoidance.

Hon. Mr. Phillips: Definitely not. That is right.

The Chairman: That whole field is open. They are administering the present statute on the basis of agency. That is, that where there is a foreign company that is wholly owned by a Canadian company and all the management and direction comes from the Canadian company, in their assessments the Income Tax Department have been assessing the income of that foreign company as income of the Canadian company on the basis of agency. They have been making these assessments. Some of them are under appeal and some of them have been settled. So there is ample scope in the present law to distinguish between what is a genuine, bona fide business operation outside of Canada, and those efforts which this bill attempts to deal with on the basis of passive income by bringing that income directly into the income of the Canadian company. There is not the urgency because a lot of tax revenue might be escaping the tax collector; there would not be that urgency even if the application of these sections were suspended for an extra year beyond what is contemplated in order to get a proper understanding. Of course, every one will have to agree that it is good for Canada to have multi-national operations.

Senator Hays: In that regard, Mr. Chairman, what kind of money are we speaking of?

The Chairman: Do you mean in dollars of tax revenue?

Senator Hays: Yes.

The Chairman: I am not sure we have that figure.

Mr. Sherman: Mr. Chairman, the White Paper referred to a figure of $10 million. There is no reference to that in the 1971 Summary, however.

Senator Hays: How much would that affect Massey-Ferguson?

Mr. Sherman: We do not know what the provisions mean, and consequently we are not able to guess. It is too wide a range.

Mr. Wleugel: It would depend largely on our own level of income all over the world. In a normal year we might have $40 million after tax. After all, if we sell in the order of over a billion dollars a year, it might be in the order of $4 million, $5 million or $6 million. Something like that. That is purely a guess on our own situation.

Senator Connolly: I am sorry, would you mind repeating that?

Mr. Wleugel: If we say that our normal world-wide income is $40 million after tax on a billion-dollar sale, that is probably a reasonably historical number. It is not one that we have achieved lately. On that basis, probably income which would be questionable would, perhaps, be in the order of $4 million, $5 million or $6 million.

Senator Connolly: You might have to pay 50 per cent of the total estimated revenue.

Mr. Wleugel: Again it depends upon many assumptions and it is unclear to us, quite honestly, what the bill really means for us. We know a few areas where the bill definitely means something, but most of them are grey areas where we do not quite see the impact because of the unclear definitions related to developing countries where we operate.

The Chairman: We are going to consider Mexico in a moment, but your U.K. discussion has provoked this thought so far as I am concerned, that supposing Bill C-259, with all these provisions we are talking about, is enacted, then this might force Massey-Ferguson to establish just one operating company in the U.K. and carry on all the other corporate operations as branches of that company. That is just a suggestion. Having done that, you would certainly get a pooling of your losses and profits in the branch operations, because they would all be coming into just the one company. If you did that, what would be the result so far as this bill is concerned?

Mr. Breyfogle: I would like to answer that. The proposal you have made—

The Chairman: Well, it was not a proposal; it was a suggestion.

Mr. Breyfogle: The suggestion you have made would be very difficult technically because of the U.K. capital gains tax, and I believe this is where a country gets into very serious trouble if it tries to extend its own taxation pattern around the world, because it is extending its own taxation pattern into a multitude of different taxation patterns based on totally different concepts and theories of taxation. Some things that are defined as foreign accrual property income in Canada would not be so defined in other countries, because those other countries already have an alternative method of raising their tax revenue. These are alternative taxes which we are paying in doing business in those countries. Hence, the addition of foreign accrual property income, and the proposal that you suggested, and the capital gains that might be inherent in such a reorganization, are direct penalties to the multi-national corporations operating abroad when Canada has the type of legislation proposed.

The Chairman: The making of adjustments that would appear to minimize the impact of this legislation as far as Canada is concerned might create an entirely new group of problems in the other country.

Mr. Breyfogle: If we might come back to the discussion we had on the amount of tax involved, if we were to proceed with the implementation of Bill C-259, I do not believe it is possible for us as a company to put a number on this today. Bearing in mind the ramifications of the tax bill as proposed and also bearing in mind the situation we are in,

we do not have income diverted from Canada as a company. We have taken steps to legally and within the tax laws of the country within which we operate to minimize our tax bill. If this bill is passed, some of these steps will in fact mean tax penalties in Canada, not in the countries in which we operate, and as a result of these we would rearrange these steps. The rearrangement of these steps will not mean more tax revenue for Canada, but it will mean more revenue for those other countries in which we operate.

On the other hand, as Canada gets into this situation and as Bill C-259 begins to affect more and more multi-national companies in their operations—we have had two examples announced recently of companies who have left Canada because of this situation—Canada will lose jobs. Even if the $10 million as outlined in the White Paper of incremental tax revenue comes to Canada, because of the bill—and this is something which we question as to whether it will happen or not—that is, if I may use the vernacular, peanuts in relation to the simple unemployment benefits that Canada may have to pay out due to the loss of jobs. If you then add the social cost of unemployment on top of that, I think there is a very poor cost benefit situation in the enactment of the international provisions in Bill C-259.

We therefore feel that politically there is a sound and valid reason for deferring the international aspects of the bill, and we endorse very strongly the Chairman's statement that within the current bill the government has the ability to ensure that income is not diverted from Canada.

Senator Hays: What would this $4 million tax bill, or the $46 million that you speak of on $1 billion worth of business, do to your company?

Mr. Breyfogle: I would like to reply to that by saying that I do not think it will be that much, and certainly it will not mean that much extra tax paid in Canada. It will make us less competitive. As I mentioned in my opening remarks, I hope it will not make us leave Canada, but it will certainly impose penalties, and as a result it will mean the losing of jobs in Canada and abroad, and it will lose profits to Canadian shareholders which are taxable.

The Chairman: If I might follow that up. Would you just say what are the different operations that are actually carried on in Canada now?

Mr. Breyfogle: In Canada we have the manufacture of combines for the total North American market and for some overseas markets. This is our largest combine plant, and it is one of the largest in the world.

The Chairman: And what is the amount of employment that it gives directly?

Mr. Breyfogle: Our total employment in Canada—and I cannot give you the combine plant by itself at this stage—is 4,200 to 4,300 people. It ranges up and down according to activity levels, and it has been up to 5,000 when the farm economy was more buoyant. We have a foundry here in Canada, and we have very extensive machine shops and press shops. We also do assembly of balers and a very wide range of implements, many of which are exported as well. We have discussed with the Department of Industry, Trade and Commerce other possible options for manufacturing in Canada which are under review. This, of course, will depend upon the outcome of Bill C-259, and also, upon the trade relationships between the United States and Canada.

Mr. C. Albert Poissant, Tax Consultant to the Committee: Mr. Chairman, may I ask the witness a question?

The Chairman: Yes, certainly.

Mr. Poissant: You are recommending in your brief that consolidated income tax returns ought to be allowed. Let us examine the situation in light of your first recommendation that this whole group of sections be deleted. Let us examine this, first, on the basis of foreign affiliates only, and, secondly, on the basis of the combination. I realize you are not making this recommendation; but you are making a recommendation on behalf of the group. Let us examine this in two parts: one for all of the outside countries except Canada, and one for the total group including Canada. Would that be of any benefit to you? I am referring to page 9, item 7, which permits Canadian corporate groups to file consolidated income tax

Mr. Sherman: That refers to Canadian corporate groups; in other words, Canadian companies.

Mr. Poissant: I see; by groups you did not mean all groups?

Mr. Sherman: No, Canadian companies.

Mr. Poissant: I thought the word "groups" meant all of the companies, but it is strictly Canadian companies. Would it be of any help if we could have consolidated tax returns for foreign affiliates?

I see two problems here: First, those countries where they do not levy taxes on foreign affiliate companies and, secondly, where the tax is an indirect taxation rather than a direct taxation. This is a problem because once you have incentive with one country you do not want to give it back to that country because that incentive is the reason you are there in the first place. But could we not have an average tax for total world-wide income, except Canada, which would be nil in the country where you obtain the incentive? Could we not have an average income throughout the world and an average top? Would that not take into account this indirect type of income which the Government is after? Secondly, would that not take into account the incentive that you are being offered in other countries where the tax rate is zero which reduces the average? Thirdly, would this not eliminate the problem that exists in countries where you have losses as well; where you cannot carry the loss against other types of income?

Mr. Sherman: It is similar in concept to the United States Sub-part F and they have made it work by offering several ways out to the big companies. If it were written in the way Bill C-259 has been written, with no ways out, and extended to consolidating it world-wide, my judgment is that it would be unworkable because of the complexities involved. One example of this would be foreign exchange. You can translate the financial statements of these foreign companies using this principle, in seven different ways and come up with seven different results according to the way you want to look at it. I can see difficulties in that one

small area alone. It would mean you would have to have a small book to translate the financial statements.

Mr. Wleugel: And not only that, but there is income being transferred into Canada which is the second part of the bill as it is proposed, as well as your example where there could be taxation of areas of income which were never transferable to Canada in any form because of the exchange, or the regulations, et cetera.

The Chairman: Yes, the concept of this provision as it is stated by the minister was that he wanted to put the companies operating outside of Canada through their foreign affiliates in the same position they would be in if they were operating within Canada. Now, what you say is that this is utterly impossible.

Mr. Sherman: Yes.

The Chairman: They can do it, however, by saying that if you have earnings abroad they are, for tax purposes, earnings of the Canadian company; and if you have not paid full taxes abroad then you pay the difference between what you paid abroad and what the Canadian rate would be here. This would cut right through the problem of foreign exchange—the problem of exchange control and restrictions of transfer of funds. It just ignores all these problems.

Mr. Wleugel: That is correct.

The Chairman: And it is a desert in which they want you to operate.

Senator Molson: It was mentioned that one or two multinational companies have left the country recently or have ceased operations. Would you care to identify those companies?

Mr. Breyfogle: The two companies that have been identified in the press are the Patino Company and the Hunter Douglas Company.

The Chairman: Now, Patino is a mining company and Hunter Douglas is—

Mr. Sherman: It is a manufacturing operation in Canada.

Mr. Breyfogle: They manufacture building materials and architectural products.

Senator Connolly: Are these U.S. owned?

Mr. Breyfogle: No, they are Canadian.

Mr. Sherman: Hunter Douglas is Canadian.

The Chairman: These are Canadian corporate companies regardless of what their ownership might be.

Mr. Wleugel: It was substantially owned in Canada, so I understand from the press reports of the *Globe and Mail.*

The Chairman: This is something which easily can be followed up. Now, can we get on to Mexico because this illustrates something else.

Mr. Sherman: Do you want me to answer the honourable Mr. Phillips' comments about the deferment of the provisions before I go on to the situation in Mexico? Mexico is a country where there will be no treaty.

The Chairman: No; you are operating in Mexico, and you have Bill C-259 in force in Canada.

Mr. Sherman: That is right.

The Chairman: And the interest in your operations in Mexico is a minority interest because of the laws of Mexico? A foreigner may not have a controlling interest there; is that right?

Mr. Sherman: That is right.

The Chairman: I just want to know how that works.

Mr. Sherman: There cannot be a treaty between Canada and Mexico because Mexico has said that they are not interested in entering into tax treaties with any countries. They have no tax treaties. So we would be operating under Bill C-259 without the benefits of a treaty. Profits from the Mexican company, to the extent of 49 per cent, would be distributed as dividends. To the extent that they were distributed, 49 per cent would come to Massey-Ferguson in Toronto. We would receive them subject to tax in Canada with a credit for the corporate income tax in Mexico which is currently on a sliding scale up to a maximum of 42 per cent, along with credits for the withholding tax on the dividends. On the face of it, the combination of the two taxes would mean that Canada would not ask for any additional taxes. However, the Mexican Government has some laws also. They are not tax-sparing, but they are laws to encourage new and necessary industries. Under their law, for instance, they would look at our company in Mexico and indicate that two of our products, two major tractors, are necessary to Mexico. Therefore, they have reached an acceptable degree of Mexican content so the income tax rate will be only 25 per cent. The combination of the 25 per cent Mexican tax rate and the withholding tax would mean that there would be an additional tax paid in Canada on our dividends from Mexico.

The Chairman: The simple answer is that the incentive earning derived in Mexico is taxed away in Canada.

Senator Connolly: It is 50 per cent of it. It goes from 52 per cent down to 48 per cent in time. Is that right, Mr. Chairman?

The Chairman: Yes.

Senator Connolly: Not the whole of it. It would be taxed at Canadian corporate rates.

Mr. Sherman: With a credit for the 25 per cent.

Senator Connolly: That is right.

Mr. Sherman: To turn to the other aspect of foreign accrual income, this does not appear to be affected in any way by the existence of a treaty. In the case of Mexico, we do not control the company, consequently they would be at liberty to invest surplus funds in any manner. We, as a shareholder, presumably would have our representatives participate in any discussions held by the directors as to the course of action. However, to the extent they realize income from these investments, we would be taxed on 49 per cent, whether or not it was distributed to Canada.

The Chairman: Yes, because the earnings in that Mexican company are transposed into Canadian company earnings.

Senator Molson: Even in a minority position?

Senator Hays: Yes, even though you do not receive them.

The Chairman: Yes, a minority position does not make any difference.

Senator Connolly: Would the current exchange rates prevail for valuing the amount of the Canadian taxable income in that case?

Mr. Sherman: This is explained in a press release of the Department of Finance, that it will be provided for by regulation. I do not really understand it, but I do not think they intend to attempt to convert anything until the time of remittance of a dividend.

Just how foreign accrual property income is determined in a case where property is fluctuating widely, I do not know.

Senator Connolly: It would depend on the day the remittance is made.

Mr. Sherman: There is no remittance.

Hon. Mr. Phillips: It is an accrual basis.

Senator Connolly: Of course, that would be a deemed remittance.

The Chairman: Yes.

Senator Hays: What would your board of directors do in the event Bill C-259 were passed? Would this mean you would leave Mexico as a majority shareholder? Would there be any alternative?

Mr. Breyfogle: I do not believe it is proper for us to speculate on what the board of directors would do if the bill is amended. Tax treaties and tax evolution in other countries are also involved. We would have to present individual cases to the board after careful study in order to have a clear picture. At that stage the decision would be made.

Senator Hays: How would Canada treat losses in those countries?

Mr. Sherman: There would be no dividend, therefore no tax. However, in the meantime, if the company earned $50,000 from investments while it lost $500,000 on its operation, we would be taxed in Canada on the $50,000 earned. The half-a-million-dollar loss is forgotten.

The Chairman: That would be passive income.

Mr. Sherman: Yes.

Mr. Breyfogle: Taking that to a logical extreme under circumstances which can develop in complex tax environments where heavy incentives exist, it could well be worth while for a non-controlled company with only a minority interest to so arrange its affairs that it takes what is in fact foreign accrual property income and loses on an operating basis. That may be the best solution for that company in its local and business environment.

Mr. Wleugel: And for the majority shareholders.

Mr. Breyfogle: Yes; this is something we cannot change. Further, with respect to companies where we have only a small investment and virtually the total management goes on day to day or even month to month without participation by Massey-Ferguson, we may not discover the existence of a foreign accrual income. We could be in default because of either record-keeping problems or even a desire by the local management to not totally reveal the situation to us as a small minority shareholder in that company.

The Chairman: Are there any other features of this area you wish to discuss?

Mr. Sherman: The third example, of Brazil, is in a middle category. There is no treaty at the moment but there is some indication that one may be signed before 1976. The corporate tax rate in Brazil is quite low as an incentive to corporations to invest in the large area of north-eastern Brazil and the Amazon region, which are underdeveloped. Our wholly-owned subsidiary there has the opportunity to pay a corporation tax at only 15 per cent, provided the other 15 per cent of the total 30 per cent rate is invested in approved projects. They can be loans or actually investment in shares. In the case of loans, they will pay interest; if it is shares, they will pay dividends, not in cash, but in stock. That is customary in Brazil. However, under Bill C-259 the definition of a dividend includes a stock dividend. This is a change from the present law.

The position with respect to our subsidiary in Brazil is that we would wish to take advantage of this opportunity to invest in the north-east. This helps the Brazilian subsidiary's business, in addition to the public relations value of being able to say we have applied so many thousands of cruzeiro to a well known project. Our name would appear on the list of major corporations involved in these important projects. The badly needed development of these areas is also a social consideration.

The alternative is to pay it to the Government as tax. Given the opportunity, we prefer to make the investment, which may some day yield a return to us.

Because we pay such a low corporate tax rate which, combined with the dividend withholding tax is substantially below the Canadian corporation tax rate, any dividends paid by our Brazilian subsidiary to Canada, in the absence of a treaty, will be fully taxable in Canada, with a credit for some part of the tax paid in Brazil.

We do not know what the position would be in the event a treaty were signed. We are making investments which will yield income between now and 1976. We do not know what the consequences will be in 1976, because we do not know if there will be a treaty, nor what such an instrument would provide with respect to these investments.

I do not know what we ought to do in the light of these possibilities.

The Chairman: Yes, but you do know that incentives gained in any other country that apply in abatement of your tax there will be taxed away from you in Canada under this bill.

Mr. Sherman: Yes, tax-sparing does not apply to this situation.

Mr. Wleugel: In this specific example the income derived from an investment in the north-east can in no circumstances be remitted to Canada. This is part of the Brazilian regulations, so it is not even a temporary exchange problem. It is a permanent part of the legislation in Brazil, that you cannot remit the results of these investments in the northeast to a foreign country. You can remit them to your Brazilian operating company, but you cannot remit them to the Brazilian operating company in Canada.

Mr. Sherman: Whether or not there is a treaty, that income is foreign-controlled income earned in Canada, although it can never be remitted to Canada. We have to take some of our Canadian profit and pay that to the Canadian Government as tax on the Brazilian investment income.

Senator Hays: How do the United States and the United Kingdom treat this sort of investment in their tax laws?

Mr. Sherman: The United States effectively remits a credit by the use of averages. A United States corporation with a world-wide operation is permitted to average its taxes, with the result that it can take its Canadian profit, taxed to 50 per cent plus 15 per cent on withholding tax, and its other high tax areas, and use that profit, and the tax credits that result, to offset the situation in countries like Brazil where there are incentives. As a practical matter it is able to avoid paying tax on these incentives.

Senator Hays: Both the United Kingdom and the United States would receive the benefit.

Mr. Sherman: The United Kingdom has a different method of taxing foreign income. There is no attempt to tax that kind of thing unless there is a dividend, and then there is a complicated underlying tax credit.

Mr. Poissant: Have you seen the recent amendments to Bill C-259?

Mr. Sherman: Yes, I have seen them.

Mr. Poissant: Have they changed the problem that you raise in Appendix VII?

Mr. Sherman: I only received them yesterday. I have not had a chance at this particular point.

Mr. Poissant: One change was made in the case of the exit tax which corrected one point that you had in mind.

The Chairman: We have certainly gone into the core of this problem, and we may have it again this afternoon with some variations as it affects Alcan.

Hon. Mr. Phillips: Have you been in touch with the Finance Department with respect to proposed amendments on international income? And, if so, do you know when such amendments can be expected?

Mr. Sherman: I have been in touch with the Department of Finance. I think their words were that they will take a look at them. That is as far as they go.

The Chairman: How long ago was that?

Mr. Sherman: A couple of months or more.

The Chairman: Then there has been an opportunity to do something, if the will were there to do it?

Mr. Sherman: Mr. Benson, in his speech the other day, said that he was not proposing any amendments to foreign income. He said, "We have already received a number of presentations relating to the passive income provision, and it seems clear that some changes to the law in this area should be made before the provisions take effect. However, we have concluded that it would be premature to introduce changes at this time before all representations have been received and given the study they require."

The Chairman: That would include any representations that we might make.

Mr. Sherman: Presumably.

Mr. Poissant: That makes your position stronger, if they have not yet had a chance to study all the briefs.

The Chairman: If in the course of the next week you have an opportunity to study the amendments and find anything that is relieving, I hope you will let us know.

Mr. Poissant: Mr. Chairman, there is no amendment. I have them all here. There is no amendment except in the case of capital loss raised in their "exit tax". They change the word "disposal" for the words "capital gains".

Mr. Sherman: We are keeping in touch with the Department of Finance.

Hon. Mr. Phillips: You started your presentation by suggesting that the provisions of international income be suspended for a year. We then tried to clarify the situation between suspension for a year and deferment of the section generally, and we introduced the concept of the application of the sections in relation to consummation and non-consummation of treaties.

Leaving aside complete deferment, which may be unrealistic, which do you prefer? Your request is that the applications be suspended for a year, or, alternatively, that the international sections come into play in respect of each country, depending upon the determination or finalization of a treaty or determination that there is no treaty in respect of source of income.

Mr. Breyfogle: If it is not possible to defer introduction of the international section for an additional year, I believe we should combine the three ideas that have come forward during our discussion so far. Firstly, I believe that we should introduce changes in the legislation as outlined on pages 7, 8 and 9 of our brief. Would you like me to read those pages into the record?

The Chairman: No. Let me have a look at them first. We have adopted a different practice from last year. At the last hearing on the White Paper we incorporated the briefs. We found, however, that the account that we received from the Printing Bureau, charging us for their service, was a very substantial one. We therefore decided that we should read the briefs and not necessarily incorporate them as part of the record. It is enough if you refer to the pages. The reference will be in the record, and we can then read the appropriate pages.

Mr. Breyfogle: Perhaps I should read the two pages for the convenience of the committee. I shall commence at the bottom of page 7 of our brief.

Senator Connolly: These are recommendations?

Mr. Breyfogle: Yes:

As an alternative to deferral or withdrawal of the international section of the Bill, the following is a brief summary of minimal amendments which we suggest:

1. Re-define "foreign accrual property income" to restrict it to "diverted income" as was the expressed intent of the Government. Exclude from "foreign accrual property income" income which has not been diverted from Canada.

2. Re-define "foreign affiliates" to include only companies controlled directly or indirectly by a Canadian corporation, as many Canadian companies will neither have nor be able to obtain the necessary information for compliance when a control situation does not exist.

3. Include relieving provisions with respect to foreign accrual property income, to permit deficiencies in one country to offset income in another and to provide loss carry forward and carry back provisions no less favourable than those in effect in Canada for Canadian business income.

The Chairman: Stop right there, please. Mr. Benson made a statement and his idea was, for the purposes of taxation, for foreign affiliates to be treated as if they were operating in Canada. But if they do not give you your loss carry-forward and loss carry-back, they are not doing that.

Mr. Breyfogle: That is correct.

No. 4: Permit foreign tax credits to be averaged, so that credits in high tax jurisdictions can be used to offset liabilities in low tax countries.

No. 5: Permit tax exemptions for foreign subsidiaries involved in corporate reorganizations.

No. 6: Amend the "Exit Tax".

The Chairman: Or departure tax.

Mr. Breyfogle: Yes.

No. 7: Permit Canadian corporate groups to file consolidated income tax returns.

No. 8: Eliminate the tax advantage granted, perhaps inadvertently, to foreign-owned Canadian finance companies.

In addition to those amendments, Mr. Chairman, I believe that, as an alternative to a one-year deferral to the introduction of the legislation on international corporations, we should include both a one-year deferral in the application of these provisions and the proposal suggested by Mr. Phillips that the application be deferred until tax treaties are negotiated with those countries involved.

Hon. Mr. Phillips: On a seriatim basis.

Mr. Breyfogle: Yes. I believe we need the extra year because of the difficulties in tax treaties, and if you do not introduce this extra year's deferral of application, we will perpetuate an additional period of uncertainty of waiting for tax treaties to be negotiated.

The Chairman: We understand what you mean, but if you say the coming into force date of the legislation is deferred until tax treaties are negotiated, that might be a deferral forever. There are some countries who will not negotiate tax treaties.

Mr. Breyfogle: On the basis of knowing that, even if the tax treaties are implemented, for example, on foreign property accrual income, we would have a problem. At least, with the one year's deferral we have another year in which to get our business in order and ensure that we do not penalize the Canadian economy and our Canadian shareholders by not being able to make the decisions which are necessary for the ongoing operation of our businesses.

The Chairman: Are there any other questions? We have had a good run on this and we will have a further run over some of the ground on which we have acquired some knowledge from you. I believe we have the substance of your problem. Thank you very much.

Mr. Breyfogle: Thank you, sir.

The Chairman: Honourable senators, we have one other submission this morning, from the Canadian Jewish Congress.

On the list of appearances we have Mr. Wolfe Goodman and Mr. Saul Hayes.

Mr. Hayes, are you going to make an opening statement?

Mr. Saul Hayes, Q.C., Executive Vice-President, Canadian Jewish Congress: Honourable senators, first I would like to thank you for hearing us. I would like to introduce the members of this delegation and explain why we are here.

To my immediate right is Mr. Wolfe Goodman, of the firm of Goodman and Carr, Barristers and Solicitors, Toronto. To his right is Mr. Harry Berger, Director of the Allied Jewish Community Services and also Director of its Committee on Foundations and Endowments. To his right is Mr. Barry Clamen, an accountant with the Montreal firm of Richter, Usher and Company. I am the Executive Vice-President of the Canadian Jewish Congress.

The Canadian Jewish Congress is an umbrella organization interested in the welfare of the Jewish community and its relationship to its citizens across the country. The head office is in Montreal, and it has offices in a number of cities of Canada.

I would like to introduce the delegation and its view by saying that we are here, perhaps happily, because we have no personal interest. It is not a matter of profits or material aspects. We are here on behalf of that private sector of Canadian life which deals with philanthropy, monetary efforts for the commonweal, and that whole conspectus of activities which the private sector has traditionally in Canada effected for the good of the Canadian community. While we are here, you might say, in the interest of the Jewish community, frankly without any mandate, what we are going to say will presumably be the same things which are being said, or which will be said, by any group of dedicated voluntary members of the community who wish

to advance the interests of charity, philanthropy and welfare. In that respect I say, therefore, we are here not in any personal capacity or on behalf of any given group of dividend receivers or shareholders, but in the common interests of the community at large.

We greatly fear that some of the aspects proposed under this tax legislation will severely crib, cabin and confine the activities of that private sector which I relate to. My accounting friends are more familiar with the details of it.

With your permission, honourable senators, Mr. Goodman will lead off. I assure you in advance that our brief will be short because it is narrowed down to the simple perspectives of the aspects of it which deal with welfare and philanthropy.

The Chairman: Mr. Goodman, perhaps you can tell us how the bill adversely affects the purposes of your organization.

Mr. Wolfe Goodman, Q.C., Canadian Jewish Congress: Yes, Mr. Chairman. The problem is a familiar one to this committee. This committee examined the White Paper on Tax Reform and in the course of its investigation it recognized the problem which would arise if a donor or testator gave property to charity which had substantially appreciated in value while he had held it. Your committee, sir, stated in its review of the White Paper at page 61:

> With respect to gifts of property to museums and other charitable organizations, the Committee wished to retain to the extent possible incentives for the continuation of such gifts, while at the same time, not permitting taxpayers an unfair use of such donations for the purpose of realizing tax benefits not basically contemplated by the taxing statute.

On balance, therefore, your committee came to the conclusion that there should be no capital gains tax imposed on gifts of property to museums, universities or charitable organizations, but that a taxpayer should not be permitted to deduct in the computation of his income a greater amount under section 27(1)(*a*) of the present Income Tax Act than the cost or value at valuation day to him of the asset donated. Your committee, therefore, succinctly examined the problem and characterized it. We merely wish to draw to your attention that the bill has not resolved this problem, but has in some ways aggravated it.

Senator Connolly: For the sake of the record, Mr. Goodman, would you give us an example?

Mr. Goodman: Yes. Imagine that an individual, under his will, leaves to a community camp council his summer property, including surrounding land, which cost him $10,000 in 1972 and which was worth $35,000 at the date of his death in 1980. He will be deemed to have disposed of this property immediately before his death for $35,000 resulting in realization of a capital gain of $25,000, one-half of which, or $12,500 will have to be included in computing his income for the year in which he died.

Senator Connolly: At his marginal rate.

Mr. Goodman: At his marginal rate, yes. The problem may be somewhat more acute in respect of a gift of depreciable property because there the rule is that the property is deemed to be disposed of at the average of its undepreciated capital cost; that is, its depreciated value in non-technical terms, and its fair market value at the date of death. In those circumstances, if the property has appreciated substantially in value during his lifetime over its original cost there will be a liability for recapture of capital cost allowances, which of course are taxed in full as ordinary income, and also a possible liability in respect of a taxable capital gain, which of course is only half of the gain involved.

In the example in the brief, in paragraph (*b*), there is a fully rented factory building, which cost $400,000 in 1972; in 1980 it depreciated to $200,000. Let us suppose a fair market value of $700,000, and bearing in mind the type of inflation that has occurred in the last 20 years, it does not seem impossible to imagine those figures. The donor, the testator, would be deemed to dispose of the property at the average of $200,000 and $700,000; that is, at $450,000. This results not only in recapture of the capital cost allowances of $200,000 taken during his lifetime, which must be brought into income, but also in a taxable capital gain of $25,000.

The provisions in respect of *inter vivos* gifts are slightly different, because there a single rule is applicable to both depreciable and non-depreciable property; that is, it is deemed to be disposed of at its fair market value. Therefore, with an *inter vivos* gift of depreciable property, such as a factory building or office building, or what-have-you, the tax would be considerably more onerous, involving both recapture of capital cost allowances in many circumstances, and also taxable capital gains.

It is not difficult to understand the concern that the Department of Finance and the draftsmen of this bill felt in respect of what they regarded as unjustifiable tax benefits. We would be blinding ourselves to reality not to recognize that in certain circumstances the situation in the United States, for example, does result in what appear to be unjustified tax benefits. For example, an individual gives marketable securities to a charity; they cost him $1,000; they are worth, say, $5,000 at the date of gift; he gets a charitable donation deduction for $5,000 under United States law, but he is not regarded as having realized a taxable capital gain. Presumably the desire of the draftsmen of the bill was to put such an individual in the same position as though he had disposed of these marketable securities first, and then given the remaining cash to the charitable organization. One can well appreciate that in respect of marketable securities this is perhaps a reasonable rule. Unfortunately, as is the situation with the five-year revaluation rule, what might be reasonable in respect of highly marketable securities might be most unreasonable in respect of property which it is not intended to dispose of.

Senator Connolly: In other words, what you are saying is that he makes this gift and has to make an additional payment out, and it will cost him the amount of the capital gains tax to make his gift?

Mr. Goodman: That is correct, sir. When we are talking about the type of gifts to which I have referred, this can be terribly onerous. I was recently involved in a very large gift to Canadian institutions of art worth several millions of dollars. While I cannot speak for the donor, who has

since passed away, I cannot conceive of a gift of that sort being made in 1980 under legislation similar to Bill C-259, where it would result in a substantial cash payment by the donor for the privilege of making this gift.

Senator Connolly: That would apply whether it is done by way of gift or by way of bequest under a will.

Mr. Goodman: Yes, sir. The *inter vivos* gift situation is a little easier to deal with, because we do have a charitable donation deduction during the individual's lifetime.

Hon. Mr. Phillips: In any event, on the question of *inter vivos* gifts, the assumption is that with the elimination of gift taxes at the federal level it ceases to be relevant, does it not, under Bill C-259?

Mr. Goodman: Certainly, gift tax is not the problem any more.

Hon. Mr. Phillips: That is what I wish to point out. It is currently, but from the point of view of dealing with Bill C-259 the real problem is the disposition at death.

Mr. Goodman: Yes, sir.

The Chairman: On the application of the capital gain.

Hon. Mr. Phillips: On the application of the capital gain. Under Bill C-259, the federal Government has indicated that gift taxes will not be applicable any more at the end of 1971. Therefore the real issue we now have to face is not in relation to gifts *inter vivos* but only in relation to gifts on demand.

Mr. Goodman: May I respectfully make a comment on that?

Hon. Mr. Phillips: Yes. I am wondering whether I am right there.

Mr. Goodman: I do not think you are entirely right, sir.

Hon. Mr. Phillips: Let us develop it, then.

Mr. Goodman: As far as both gift tax and estate tax are concerned, specific exemption is provided from the application of both for gifts to charitable institutions. With the elimination of gift taxes and estate taxes at the end of 1971, as contemplated by this bill, our only concern is with the tax on the deemed capital gain, either at death or on the making of an *inter vivos* gift.

The Chairman: At death or on realization, on disposal, "otherwise than".

Mr. Goodman: Yes, if we regard an *inter vivos* gift as a realization, certainly it is a disposal.

Hon. Mr. Phillips: I see your point.

Mr. Goodman: It is deemed to be a realization at fair market value for both depreciable and non-depreciable property.

Hon. Mr. Phillips: In respect of capital gains?

Mr. Goodman: Yes. Under the bill no distinction is made between *inter vivos* or testamentary gifts to charitable institutions, and to any other donations. It is the failure to discriminate between these charitable and non-charitable beneficiaries that is at the root of our difficulty in the present case.

The Chairman: All they have done is to remove the half on gift tax and estate tax, and got another half now on capital gains, which may pick up the slack that they are losing.

Mr. Goodman: Yes, but that is, of course, a more general question on finance and fiscal policy, on which I could not comment. Whereas in the past great care was taken to ensure that charitable giving, both during one's lifetime and at death, was not inhibited by tax laws, no such care has been taken in the new legislation.

Senator Connolly: In other words, if I may give a concrete example, a will is in being today and the testator is still alive, the will provides for, let us say, a fund of $100,000 to be disposed of at his or her death. Under the present law there is no gift tax, because it a testamentary disposition, and because it is a charitable bequest it does not attract any duty, succession duty or estate tax.

Mr. Goodman: That is quite correct.

Senator Connolly: However, if that will were not changed and the testator died after 1972, they the application of the capital gains tax might very well have an affect.

The Chairman: Except that it would not affect dollars if the gift was of so many dollars.

Senator Connolly: No, it would not affect dollars except in the sense that it would decrease the liquidity of the estate, because there would be capital gains tax to be paid by the testator's estate.

The Chairman: Only if he gave assets, depreciable assets or non-depreciated assets, and there is some gain on death as against cost.

Senator Connolly: Yes, precisely. I am assuming that there is a gain at the time of death.

The Chairman: First of all, one must assume that the disposition is in kind and not just dollars.

Senator Connolly: Yes, of course. I agree there. I am talking now about, say, a will which provided that the balance of the corpus of the estate shall go to such-and-such a charity.

The Chairman: If that is in the form of a depreciable asset, then you have this capital gains profit.

Senator Connolly: And the will that is in being today and is not changed until after 1972 might very well mean that there has been an appreciation over cost, resulting in attracting a capital gains tax.

The Chairman: A lot of wills will have to be restudied. They have been restudied a couple of times in the last couple of years because of threatened changes and they will have to be restudied again.

Senator Connolly: From the point of view of these witnesses and the point of view generally of the Canadian community, it seems to me that if the proposed law does

what the witness says, and I have no doubt that it does, then it is going to be extremely difficult for people to make up their minds to make charitable bequests in their bills, because of the danger of capital gains tax. Is that the burden?

Senator Hays: They could give cash.

Senator Connolly: Then they have paid the tax.

The Chairman: I suppose they could even get at you for this. If your will directed that the proceeds on the sale of certain assets be paid to certain charitable organizations, then in arriving at the proceeds of the sale, if there is a gain, the testator's estate has run into a capital gain problem. I do not think he can defeat it just by giving the proceeds of sale of the depreciable asset instead of giving the asset itself.

Mr. Goodman: Not only that; I would question whether it would be desirable.

Senator Connolly: On your point, Mr. Chairman, it goes to the question of liquidity of the estate.

The Chairman: Yes.

Senator Connolly: If people are going to be in doubt about how liquid their estate will be, they will probably, when they come to make their will, take the easy way out and say they cannot take chance on making a charitable donation of the magnitude they originally proposed. Some other device may be adopted. Perhaps some gift will be made, but it will not be the kind that heretofore has been made with full assurance.

The Chairman: It may be that they will have to keep the property that they are giving in the form of non-depreciable property so that at least they will avoid the tax.

Senator Connolly: That is the most difficult thing in the world for a testator to do. How does a testator know what his estate is going to be like ten years hence?

The Chairman: This appears obviously to be interfering with giving for charitable purposes.

Mr. Poissant: Mr. Chairman, would you permit me a question?

The Chairman: Yes.

Mr. Poissant: Mr. Goodman, how could you equate a situation like this, where a donor has $20,000, made up of $10,000 in cash and $10,000 in the value of depreciable assets? He has two gifts to make, one to his daughter and one to a charitable organization. You would say that no doubt he would give to the charitable organization the item which may have recapture depreciation. He does not want to be caught with recapture depreciation. How do you equate a situation like this, where the donor would use the charitable donation to get rid of his capital gain tax and the recaptured depreciation?

Mr. Goodman: I recognize that, where we are talking about property that is intended to be sold by the charity, such as the marketable securities that I gave in a previous example—

The Chairman: Is there not a deemed value in those circumstances?

Mr. Poissant: There is a deemed value now, under Bill C-259.

Mr. Goodman: One can understand the situation in which the legislature, Parliament, says that upon the making of a gift of marketable securities these securities would be deemed to be disposed of at their fair market value. This is designed to prevent the situation arising which arises in the United States where, immediately upon the making of such a gift, the charity that receives it disposes of the shares and realizes the money without payment of any tax liability and the government therefore loses the tax on what otherwise might be taxable as a capital gain.

Senator Connolly: Let us stop there for half a second. Say you observe this, that the gain there goes to the charity.

The Chairman: It may be that is part of the solution of this problem. If you transfer the realized gain, as a benefit to the charity and not as a liability of the deceased and his estate, would that accomplish what you are looking for?

Mr. Goodman: That seems possible, sir, particularly since our primary concern is with that type of property which is not going to be disposed of by the charitable organization that we are speaking of. I give the example of the summer camp and a gift. We would expect that the charitable institution would retain that in perpetuity, or substantially in perpetuity. One could understand, therefore, that if an obligation were imposed upon the charitable institution to pay, upon realization of that asset, the amount of tax which the donor might otherwise have paid on it if he had given it to a non-charitable donee, that might be an acceptable solution.

The Chairman: What you do is twofold: you would impose the capital gain and the incidence of that on the charity; and you would defer the tax until realization.

Senator Hays: Could that not be covered by a clause in the act under exemptions?

The Chairman: Yes.

Senator Hays: And ministerial discretion to exempt?

The Chairman: I would not even have ministerial discretion.

Senator Hays: You get that today in the United Funds. These are all exemptions. You can apply for them.

The Chairman: This would have to be a specific provision, to isolate the capital gain.

Senator Connolly: I think what Senator Hays is talking about is ministerial discretion in determining whether a given organization is charitable.

The Chairman: Yes. I am assuming that, when one is talking about a charitable organization, it is one that is registered.

Senator Connolly: One that is approved.

The Chairman: Yes.

Senator Connolly: I may be wrong about the theory of taxation in respect of charitable organizations. These organizations are non-taxable and non-profit organizations. If they make a capital gain or any other kind of gain, out of a bequest made to them, through good management, because they are charitable I do not think they should be taxed. I may be out of step with current theories of taxation, but I think this is implicit in our law today, is it not?

Mr. Goodman: Yes, it is certainly implicit in our law today.

Senator Hays: Just to a point.

Senator Connolly: What is the point beyond which it is not implicit?

Senator Hays: If you want to give away money today, you pay estate tax on it.

Mr. Goodman: Not if you give it to a charitable organization.

Senator Connolly: Not on charitable gifts. I think it is an absolute provision of the law.

Mr. Hayes: Mr. Chairman, may I intervene? Senator Connolly's point is one that should be pursued. He says he may be out of line on the matter of what the taxation interest is. He is not out of line on the whole concept of what charities are all about. Therefore, where the sector of private giving and the management by voluntary efforts of charities is concerned, it would be a dangerous step even to permit the idea that later, when the charity gives it up, there will be a capital gain which will then be exigible.

Hon. Mr. Phillips: I agree with you 100 per cent. I think that is a dangerous, retrogressive step.

Mr. Hayes: For example, Mr. Goodman's point is that if a man gives his property, his summer camp, and the charity needs it and uses it for ten years but on the eleventh year the whole concept in our welfare society is changed and summer camps of this kind are no longer part of the mores of the community, it could be a terrible imposition on it then to have to pay the realizable value.

Mr. Goodman: That is right.

Senator Hays: On the other hand, I know of churches in expanding cities that have bought corner lots every four blocks and have not been taxed on them, knowing that they were not going to put churches on them.

Senator Connolly: But they are going to put churches on them.

Senator Hays: No, they do not. I happen to know that many of them have sold those lots and have taken the profit. They sell them as the cities expand. I think the tax people have a concern in matters of that kind where there should be a deemed realization of the sale.

The Chairman: I was simply pointing out that there are two routes open: one is to transfer; and the other is to defer. If you transfer the incidence of capital gains tax from the testator, then you are not inhibiting giving, because you are not putting any extra burden on his estate. If you impose the gain and defer the tax until the depreciable property has been realized on, at least you are not defeating the tax revenues completely. Whether this is a retrograde step in the business of charitable giving I do not know. All I was looking at was how you could make the incidence of tax the least onerous.

In the example of the camp property, what would the least onerous be? If it had no further use for such purposes but was in the centre of a large development for real estate and subdivision purposes, or parks, where it might produce a lot of money, then either the charity would enjoy all that fortuitous gain or the tax revenues would gain a bit. It would be one or the other. The question is which way would you go.

Mr. Poissant: Mr. Chairman, I think the roll-over free of tax is a good sign, but perhaps there should be some measure to control the avoidance of tax such as, for example, the institution having to keep the gift for a certain number of years after which it would be homefree and would not be penalized unduly. On the other hand, we should make sure that the charitable organization is not used as a conduit for avoiding tax. Perhaps there could be a certain provision that would help to overcome the possibility of such abuses at least for inter-vivos gifts.

Hon. Mr. Phillips: Mr. Chairman, I should like to take a hand in this. If I may respectfully say so, I think we are off on the wrong foot. It is not the duty of this committee to consider taxation of charitable institutions on certain conditions. That is a positive act of tax policy. What we are considering is whether there should be a tax on the donor in an *inter vivos* gift or the person who died on a testate succession. That is our problem. It is not the problem of going into the whole area of whether charitable organizations or museums or universities, et cetera, should be taxed.

In my humble view, the situation is simple by precedent. It has never been accepted as a tax avoidance or a tax minimization if on death money was given to a charitable foundation or to museums or hospitals. You could give away your entire estate to a hospital and you would not only minimize taxation but would eliminate it completely. That is an important social concept, and there is no reason why that concept should not apply simply because we eliminate succession duties and replace them by a capital gains tax. If we eliminate succession duties federally and introduce a capital gains tax, then we should give to the donor and to the testator the same privileges they had in respect to succession duties. In other words, no deemed realization of any nature whatsoever to a donor or a testator in respect of deemed to be capital gains. Period.

Whether you have the odd case of playing around with situations in which there are listed securities and all the rest of it, once you introduce qualifications into that rule you are striking at the very heart of the point that Mr. Hayes presented here, that we are dealing with a sector of the community that is not indulging in profit. We have already, since 1917, introduced the concept under succession duties that that sector is free of taxes. Why should we not adopt the same principle now that we are eliminating succession duties and introducing capital gains simply by saying that the exemption in toto which was given for succession duties be now given for capital gains—period.

You may get the odd case of the kind to which Mr. Goodman referred, where persons will in certain instances handle the securities by way of gift. So what? It goes to an institution that will be using the money for humanitarian and social purposes.

The Chairman: The principle is just the same.

Hon. Mr. Phillips: The principle is just the same, yes.

The Chairman: Whether I make a gift of securities which have a built-in capital gain or make a gift of a property which, by the time I die, has a large built-in capital gain feature, the principle is the same. What you are looking at is the same. Are you going to look at the end view, which is charity? And if you are going to look at it in that light, then it may well be that this is what we should say and that, therefore, capital gain should not be brought into that picture.

Hon. Mr. Phillips: Why should capital gains which now replace the succession duty receive worse treatment than succession duties received by way of total elimination of tax liability on disposition?

Senator Connolly: I should like to make one remark, Mr. Chairman, arising out of the point that Senator Hays made. If the charitable organization is engaged in the business of real estate, and if it is buying real estate and not using it for its own charitable purposes, that is a different kind of thing and it is covered by the present legislation.

Mr. Goodman: May I say that that would be illegal anyway, because the corporate powers of a particular charity would not allow it.

Mr. B. Clamen, C.A. Canadian Jewish Congress: Mr. Chairman, I think it is important to note that if there is no exemption from the capital gains tax, then charities are the ones who are going to suffer as a result of that. To go back to Mr. Poissant's example of the estate with $10,000 in cash and $10,000 in some asset which has appreciated and which might trigger a capital gains tax on death—if there was the exemption, I think the point that Mr. Poissant was making was, of course, that the testator would give the asset which had appreciated to the charitable organization in order to avoid the capital gains tax and give the $10,000 to his family. But I think the reverse situation would be that if there is no exemption, he would give the appreciating asset to his family, but he would not give the full $10,000 to the charity. He would have to hold back $2,000 or $3,000 in order to pay the tax which has accrued on that appreciating asset, and I think that is the important point.

The Chairman: The sum total of what you are saying is that if this proposal remains the way it is, you are inhibiting charitable giving.

Senator Molson: Mr. Chairman, I am somewhat puzzled at a good deal of this development, because I do not think it matters at all if somebody gives away a property worth $10,000 to a charity because it makes his estate look better, as long as he gives it to charity. I do not know why we are spending all this time questioning his motives. I do not think that aspect should come into the picture at all.

The Chairman: Well, Mr. Clamen and I have reached that conclusion now, that the end use is what we should look at. And that is precisely the point you are making.

Senator Molson: Well, I have been listening for some time to Mr. Poissant's example, and I am not in the least disturbed if the man should give $10,000 one way or another, as long as he gives it, unless we want to eliminate the whole principle of giving to charity, in which case let us tax it and tax the capital gain, and so on. Otherwise it seems to me that this is quite unreasonable.

The Chairman: But we moved along the line of the process of elimination and we tested all these things and have now eliminated them and you approve of the elimination.

Senator Molson: We have eliminated them in our ideas.

Mr. Clamen: In addition, Mr. Chairman, there would be sufficient anti-avoidance there provided the testator did not receive anything in return for divesting himself of an asset for charitable purposes. To my mind that is sufficient anti-avoidance.

The Chairman: It may well be too that the will speaks at death, so I suppose the latest point in time at which the man is making the gift and the value of it is at his death.

Hon. Mr. Phillips: And he does not enjoy the tax benefits; the poor devil is buried.

The Chairman: Maybe that is one way of avoiding it.

Mr. Hayes: That is called the final solution.

Senator Connolly: A consummation devoutly to be wished. That is what Hamlet says.

The Chairman: Is this the sum and substance of your presentation?

Mr. Goodman: Yes, sir. I should like to add just one comment. The concept of deemed realization at death has apparently been adopted in our legislation from the British legislation of 1965, and it is of some interest that in 1971 the United Kingdom Parliament abolished deemed realization at death. I suspect that one of the reasons for the abolition is the sort of problem that is before us today.

The Chairman: And a new government.

Mr. Hayes: Mr. Chairman, I thank you very much for listening to us and appreciating our point of view.

Mr. Poissant: Mr. Chairman, may I also record that the remarks I made here were just to bring up the arguments. Otherwise I entirely agree with your point of view.

The Chairman: That is quite all right.

Gentlemen, we resume our sitting at 2.15 when we will hear from Alcan Finances Limited. That will involve some variations as to form and fact of the principles that were dealt with by Massey-Ferguson this morning.

Then, tomorrow we have a busy day. We have The Canadian Bar Association at 9.30 in the morning and we have the Independent Petroleum Association of Canada, and Simpsons-Sears Limited. In the case of the last named, their presentation will be dealing with the question

of deferred profit-sharing plans. If you remember, last week we had Allstate Insurance here and their presentation involved profit-sharing plans. There are differences between the two categories of profit-sharing plans. This fits in very nicely, because it will enable you to take a broader look at the provisions in the bill dealing with trust, and where they exclude from the benefit of being a trust profit-sharing plans, deferred profit-sharing plans, registered retirement savings plans, pension plans, etcetera and the element of taxation involved in doing that.

So this will enlarge the area and we will have the problem in greater depth, to decide just how we are going to deal with it.

We will adjourn until 2.15 p.m.

The committee adjourned.

Upon resuming at 2.15 p.m.

The Chairman: Honourable senators, I call the meeting to order. This afternoon we have the submission by Alcan Aluminium Limited. Those appearing are: Mr. John G. Lees, Vice-President, Taxes, Alcan Finances Limited; and Mr. William J. Reid, Vice-President and Treasurer, Aluminum Company of Canada Limited.

I understand that Mr. Reid is going to make an opening statement. Then the questions can follow.

Mr. William J. Reid, Vice-President and Treasurer, Aluminum Company of Canada Limited: Thank you, Mr. Chairman. I would like to say in opening that I am pinch hitting for Mr. N. V. Davis, the President of Alcan, and for Mr. Paul Leman, President of Aluminum Company of Canada Limited. As some of you may know, Mr. Leman has been ill this past month, and Mr. Davis could not be with you today because of a board meeting, but he does send his apologies.

I would like to open my remarks, honourable senators, with a few words about the general state of our industry. The state is one, as you probably know, of over-capacity in the world, declining volume and prices, and inflationary pressure on our cost structure. I would draw to your attention that both Reynolds and Kaiser in the United States have recently declared losses for the third quarter of the year. Generally speaking, our industry is operating at between 80 and 85 per cent capacity. About one million tons of excess inventory is hanging over the world market.

We are entering a period of great uncertainty and economic difficulty and we feel, based on our present forecasts of demands supply, that this will continue for the next two or three years.

The President of Alcoa, Mr. Krome George, has recently expressed the public view that we are entering a critical period in the industry in which the survival of some of the runners may be at stake. Naturally, the management of Alcan is concerned that Alcan survives through this difficult period and that we will be in a position subsequently to grow and prosper. Thus, it seems to us that the foreign tax aspects of Bill C-259 presents us in Canada with another negative cost factor at a time when we do not need any more bad news.

I would like to refer to Bill C-259 in general. Our broad conclusions from a study of the bill are that we agree with many of the points raised by Massey-Ferguson Limited in their brief this morning. However, in our brief we have concentrated more on the passive income proposals of the bill which are naturally of vital interest to Alcan because of the increasing international and global character of our business. As Mr. Paul Leman has earlier pointed out to you, Alcan's effective income tax cost in consolidation is already higher than that of its major United States competitors. Moreover, these United States competitors and the United States itself appear to be moving in the direction of reducing the effective tax load on our competitors by such expansionary incentives as DISC and the investment tax credit which you are all aware of.

Alcan is looking for tax relief in Canada in order to maintain its competitive posture, and in this context, honourable senators, the foreign tax provisions of Bill C-259 threaten us with substantially increased direct tax expense. Moreover, the quantum of such increased expense is impossible to define precisely because of the uncertain definition of the terms. Exactly what is income from property under the terms of the act? Does it include profit from foreign exchange contracts? Does it include interest on receivables on short term investment proceeds? Does it include proceeds from the sale of technology locally developed, and so on and so forth? There is a great degree of uncertainty in the act.

In addition to the potential increase in the direct tax burden, there would be the administrative cost of compliance involving endless complexities, comparative national tax structures, and the necessary intrusion into the detailed affairs of our overseas affiliates. Such intrusion and the additional cost would be most unwelcome in such countries as Norway, Japan, India and Brazil. Alcan has major holdings in all of these countries and they value their national independence and local autonomy. Alcan does not willingly wish to incur the heavy compliance costs in Canada and abroad and the local suspicions which would be engendered by the intrusion of the Canadian head office and Canadian tax structure into local management, prerogatives and practice.

In this connection I would like to cite to you a practical case, that of the Nippon Light Metal Company in Japan. The Nippon Light Metal Company happens to be the largest aluminum producer in that country, much as Alcan is in Canada. Alcan owns 50 per cent of the shares and this is a company which lists in its statement approximately 125 investments in companies fully owned, partially owned, and minority investments. These, of course, are the investments where we feel the compliance cost would have to be borne in dealing with the provisions of this bill.

To think of the complexities of compliance in this one instance, to say nothing of our holdings in Norway, Brazil, India, and so on, involving a maze of subholdings which even we hardly know about in detail at this stage, the unusual tax structure of the country of Japan and, moreover, the necessity of working in the Japanese language—Japanese statements, and what-not—makes us literally recoil in shock at the prospect.

If the bill passes in its present form, Canada will be the only country in the world with such complex and intrusive rules governing the taxation of foreign affiliates.

Senator Connolly: Just on that point, sir, what you are suggesting is that under this bill, the head office of Alcan in Canada would be more and more involved in the day-to-day operations of the investment program, particularly as it relates to the Nippon Light Metal Company. Is that correct?

Mr. Reid: That is right.

The Chairman: Did I understand you to say, Mr. Reid, that they would or that they should? There is a big difference. Perhaps they should but by reason of the setups in those countries they cannot. In the interests of the requirement of compliance and the extent they may be able to protect themselves against some of these things, certainly they should interfere. Whether you can or not, I do not know.

Mr. John G. Lees, Vice-President, Taxation, Alcan Finances Limited: Is it timely to talk on this point?

The Chairman: Yes.

Mr. Lees: This is a classic example. We have 50 per cent of the shares. We do not have 51 per cent and we do not have the casting vote. Between the Government of Japan and the various establishments we know that we do not control that company. They will run it as they wish, consulting us when they wish to consult us.

Until we received this statement from Price, Waterhouse, prepared two years ago, we did not know that they had 125 subsidiaries. We were aware that they had a few, but not 125.

The Chairman: Do you not receive financial statements?

Mr. Lees: Yes, from the main company showing so much for investments, but it took Price, Waterhouse years of digging to get an analysis, and they produced a statement like this and one of the entries states "others, approximately 100 accounts less than 150 million yen each" and it tells us what the interest on the dividend income was. Even Price Waterhouse cannot find out what those hundred investments are. We have shown this to the department and have asked them what are we going to do.

Senator Desruisseaux: Not even a total?

Mr. Lees: We have total revenue, total investment, but no details.

Senator Connolly: No breakdown?

Mr. Lees: No breakdown.

Senator Connolly: And some are portfolio?

Mr. Reid: Yes, if we were to comply with the law it would force us to go back and investigate every one of those affiliates to find out if we had to pay tax on it or not.

Mr. Lees: We could go to the Japanese and say, "Sirs, do not invest in these companies unless you take at least 20 per cent so we will have at least 10 per cent." That is a rule regarding whether you have a so-called affiliate or not. We could ask them not to invest in companies less than 20 per cent owned, and right away the Japanese are going to say, "We will run this business." The next thing we could say to them is, "When you invest do invest by equity and not by debt, giving rise to interest." And they would say, "Everything is done on banking debt and over-priced interest in Japan and interest revenues"; and we will be in a conflicting position with the board of directors in Japan. Our president, Mr. Davis, has told us quite clearly that we should not discuss this with them. The Japanese affiliate will run this business; and if there is a tax problem we will absorb it in Canada because we have never asked them for this kind of information. They will question our motives. Price Waterhouse have told me that they will refuse to be put in a position of getting tax information because it would ruin their reputation as auditors because the Japanese would not believe that this was purely tax information they were seeking. They would be suspicious that we were trying to get something out of them.

Senator Desruisseaux: Are you the only Canadian company in this kind of situation with the Japanese?

Mr. Lees: The only one of which I know.

Mr. Reid: We are certainly the only Canadian company with a situation of this utter complexity. I am sure that other firms have Japanese subsidiaries, but not with such a large scope and not of this size.

Senator Connolly: But your comments are not restricted to Japan. You have chosen Japan as an illustration, but the same situation can apply—

Mr. Reid: Yes, we have chosen Japan because it seems the most outlandish in terms of language, custom, and general difficulty.

The Chairman: Let us analyse this a little bit. What you are saying is that in Japan, because you have only a 50 per cent interest, you do not control it; and, not being able to control it, there are certain accesses that you do not enjoy by way of getting information that would be pertinent to the compliance that ALCAN must make to this bill. So you are pointing out that that is a complexity. But Japan is just one instance. There are other countries where you have different problems I would imagine.

Mr. Reid: Yes.

The Chairman: Let us say that you are operating in a country where there are tax incentives; where you have a tax holiday. This is a more practical aspect of the matter, it strikes me, because you are going to pay tax on the incentive.

Mr. Lees: Let us stick with Japan for a moment. Their rate of tax, if you look at sheet 1 of Exhibit "B"—let us look at their rate of tax from the Price Waterhouse statement. This is the financial data and how we would comply with the law in respect to this company. This company had a rate of tax in 1970 which was 30 per cent of income, and in 1969 it was 41 per cent. This was because Japan enjoys incentives there. But the difference between that rate and the Canadian rate in that year would be a tax which Alcan Aluminium Limited would have to pay. So, even though this is a publicly registered company—in other words, you

can buy these shares on the Japanese stock market—they are registered in Japan, and taxes are being paid as on on-going business, it does not pay the same level of tax as you would in Canada. But this is a concern regarding every one of those examples you have touched on. These companies are paying taxes, but because of the difference in computing income tax, they would pay less than the Canadian rate and Alcan Aluminium Limited would have to pay the difference.

The Chairman: This is the point I am making. That is the effect in many countries, and the effect on you as a multinational company that if the provisions of Bill C-259 apply, Canada is going to tax away the incentives that you get in other countries.

Mr. Reid: Yes.

Senator Connolly: They are going to tax the incentives but would they be taxed away?

The Chairman: It depends on the rates. I mean, you will get an offset for the amount of the taxes that have been paid in the foreign country; but if that rate is lower than the Canadian rate, then you are going to be paying Canadian taxes on the rest of it.

Mr. Lees: At this point, we are only talking about passive income. And in our brief we are saying that every serious company worth its salt has some kind of passive income because it will have surplus cash. By definition, if it is successful it will have these problems. Most of the countries we deal with have rates of tax which are lower than the Canadian rates. So, by definition we will pay some tax, to the extent that they have these sundry incomes.

Hon. Mr. Phillips: Even though it is not related to the so-called diverted income?

Mr. Lees: Yes, sir, that is correct.

Senator Gélinas: How long have you had this investment with the Nippon Company?

Mr. Reid: Since 1952.

Senator Gélinas: And it is only recently that you found out what the investments were?

Mr. Reid: No, I think we have known that they had a large portfolio investment. We have known that there have been a large group of investments, but—

Senator Gélinas: But not 125?

Mr. Reid: Not to my knowledge. I worked on the Japanese situation a few years ago, but I did not realize that there were 125 of them. This is new information which defines the amounts and the scope and, of course, focuses it in the light of this new act. It is sharpening our vision a bit.

Mr. Lees: Sir, I suggest that the point here is that in looking at this kind of investment, Alcan's position has been to avoid asking for that kind of information.

Senator Isnor: Why would you not ask for that information?

Mr. Reid: They are operating quite well, and they are producing very good results, and as long as they are doing well, we tend to leave the subsidiaries alone.

Senator Isnor: That does not matter. You are still entitled to know what is going on, I would think.

Mr. Lees: You could say that, but if another person is extremely touchy and inclined to fly up at the least suggestion, it gives you cause for thought. You do not ask an idle question just to get information. You are very careful and you only ask what you need to ask. It is a prickly affair.

Mr. Reid: May I just speak to that for a moment? When we bought this interest in the company in Japan in 1952, we got it at a reasonable price. The Japanese have not forgotten that we bought in at a very propitious time. I feel it fair to say that we would never get that 50 per cent if we were trying now.

The Chairman: Mr. Reid, are we not runnning along a parallel line there? Let us get into what is the hard core of the problem. The hard core of the problem is the effect or the cost of compliance.

Mr. Reid: And the additional cost of taxation, or the additional taxation burden on us.

The Chairman: Yes, of course. When you used the expressed "compliance cost", did you mean the administrative cost of complying or the extra cost in the way of paying more taxes to Canada?

Mr. Reid: In my mind I separate the two into an additional effective tax cost to us as an industry, and compliance with the administrative information burdens both in Canada and with our subsidiaries to supply information.

The Chairman: But the major problem is the increased tax cost.

Mr. Reid: Yes, I would think that is the major problem.

The Chairman: Then the cost of compliance, administratively, develops this way: First, it involves substantially more work in documentation and information to be collected; second, in that connection having regard to the way in which operations are carried on and accounting is done in some countries, you may not be able to get all the information anyway.

Mr. Reid: We are not sure that we can get all the data. That is what we are saying, I think.

The Chairman: You might have to face an arbitrary assessment, if you did not produce all the information.

Mr. Reid: That is right, sir, and there would be a cost of compliance in terms of our relationships with these overseas affiliates, which jealously guard their national prerogatives.

Senator Connolly: Have you discussed this with the tax department?

Mr. Lees: Yes, sir.

Senator Connolly: Does the tax department see any way out of this for you?

Mr. Reid: Not yet.

Mr. Lees: They just buttoned their lips.

Senator Connolly: I guess they do not know.

Mr. Reid: I guess ours is a rather complex case in the general scheme of things.

Mr. Lees: They ended up by saying, "But you will comply, won't you?" They put the question mark there.

The Chairman: Well, gentlemen, you are here first of all because we invited you, but, in any event, it was even indicated in the Department of Finance that perhaps you should come before this committee. The way I interpret that is that perhaps they are looking for this committee to do some of the study in depth in order to see what the answers are rather than face the problem in the department itself at the stage at which they are now. If we accept that as being the job we should do, then let us get on with it, but you have to give us some of the answers.

We know what the problem is in Japan. While you can tell us a lot more about it, and we might want some more information about it at a very early stage, Japan does present a very complex problem in gathering the information and even in your giving them directions or ways in which they might go so that your increased burden of tax in Canada would not be as great. Is that right?

Mr. Reid: That is right, sir.

The Chairman: Let us take a few other countries and see how you get along. How about Norway?

Mr. Reid: Norway is a big investment. Fifty per cent is owned by the Norwegian government, with a number of subsidiaries as well. It is not nearly as complicated as the Japanese structure.

The Chairman: Would they be subsidiaries of the Norwegian company?

Mr. Reid: Of the Norwegian company, yes, sir.

The Chairman: Is that 50 per cent investment a statutory limitation in Norway? You cannot increase your 50 per cent?

Mr. Reid: Yes, by agreement we cannot increase our investment. The Norwegian government owns the balance of the shares.

The Chairman: Well, you cannot control the Norwegian government, so if you were desirous of acquiring any more they would have to be willing to sell.

Mr. Reid: That is right.

Mr. Lees: As this is the biggest smelter in Norway the chances are nil.

Mr. Poissant: You have referred to the Japanese companies and the Norwegian companies. Are those companies Japanese-based and Norwegian-based, or could they be deemed to be international companies? In other words, are they Japanese resident corporations or Norwegian resident corporations?

Mr. Lees: The Japanese have reached the growth point where they are ready to move out. For example, the Nippon Light Metal Company is now in the process of developing a mine in Fiji. It has a share interest with us in another mine in Malaya for raw materials—bauxite. It is not beyond the bounds to think that they will begin to move into the Philippines and other areas in the Far East.

The Chairman: By way of carrying their own Japanese company forward or by setting up a national company in the country where they are going to carry on operations?

Mr. Lees: One would imagine they would form their own subsidiary of which Nippon Light Metal would own 100 per cent of the shares, and it would evolve from there.

The Chairman: They would form it in the particular country.

Mr. Lees: In Thailand, for example, or wherever it was. It would be the normal type.

The Chairman: Is there a requirement in countries like Malaya, Thailand, and Fiji that there must be a percentage of domestic ownership?

Mr. Reid: Not in Malaya, to my knowledge. The company in Malaya is owned 75 per cent by Alcan and 25 per cent by Nippon Light Metal.

Senator Connolly: Generally, in the underdeveloped countries these rules are not as rigid as they are in the more developed countries like Japan and Norway.

Mr. Lees: That is right.

The Chairman: Are there incentives in these companies where it is proposed to carry on mining operations? Incentives like accelerated depreciation?

Mr. Lees: Yes. Malaya, for example, gives very generous investment allowances over and above bonus depreciation. All the countries have incentives of different kinds. Some are better; some worse.

The Chairman: Do they have in those countries periods of tax holidays, as I refer to them?

Mr. Lees: They have what is termed, in the British style, "pioneer legislation". Malaya has some of that, and Taiwan has a piece of it. Mind you, we are speculating. This Nippon Light Metal has been growing rapidly with the Japanese economy and has only gone abroad for raw materials.

Let us turn to Norway, which is in the position where the Aluminum Company was ten years ago. The Norwegian company is aggressively interested in seeking markets in Germany and in France and in Britain and would like to buy subsidiaries. We have been attempting to persuade them to stay with Alcan and not to buy their own subsidiaries. We have said that we would assure them a market for their aluminum through our subsidiaries. I do not think you can predict how that is going to come out five years from now. They may well invest and have their own foreign tributaries and subsidiaries.

The Chairman: I ask you stop right there. You can say without speculation, that the earnings generated in these

various parts, if this legislation should become effective, would come in to Alcan of Canada as earnings and the only deduction you would have would be whatever your tax cost was. If you are existing and progressing in those countries by reason of those tax benefits, then you are going to pay Canadian tax on those benefits.

Mr. Lees: To the extent that the participation in our hands was less than 10 per cent, this is correct. If we had more than 10 per cent, I would say that the only concern then is as to whether or not there is this so-called passive income. The legislation, as we know, is very complex and one has constantly to remember whether one has more than a 10 per cent interest in the underlying equity or less. Now where we have a 50 per cent interest in this Norwegian company, so long as it takes a 20 per cent or more interest in any other foreign venture, and they mind it simply as a branch plant with no sundry income, no interest income, we will get along. The tax bill would not be fair to say that it would penalize us on that.

The Chairman: All right; let us stop there and let us take a look at an example of that situation. Let us take Norway and let us say that you have a 50 per cent interest there. If this bill and its provisions on foreign income passes into law, will you be affected in relation to the earnings of that Norwegian company in any way in which you are not now affected so far as Canada is concerned?

Mr. Lees: Yes, sir.

The Chairman: Will you illustrate how?

Mr. Lees: This company is a specific example which is right in front of us today. Our engineers in Canada invented or devised a new scheme to control pollution in smelters. They devised it some years ago. What they needed was a big production-sized operation to test it out and to make sure it worked and was effective. The Norwegian Government was ahead of the rest of the world on pollution legislation. This Norwegian affiliate of ours said, "Please, come and try this new device in our operation; it is the best idea we have heard yet." With their help this device was perfected. Today the world is crying for this kind of technique and know-how. It is not a patentable idea, mind you, but it is one that people will pay you a royalty to get. The Norwegians say, "The deal is 50-50; it is half our idea too because we did the perfecting of it." Alcan agreed with them that it should be 50-50. We now have third parties, people in whom we have no interest in Germany and the States coming to us and saying, "Please sell us your know-how." So you are going to see profits in the books of this Norwegian company for their half of the income from royalty, and I say that is income from property.

The Chairman: But your half of what may be generated out of those royalties would be passive income.

Mr. Lees: There is one half that comes directly to the Aluminum Company and that is taxable income here, while half goes to Norway, and half of that half comes back here as passive income and is taxable, and this is the problem we are talking about.

The Chairman: Well, first of all, we eliminate the half that comes directly to Canada because even under the present law you are taxed on that. So then what we are dealing with and what we are concerned about is half of the half, and if that is passive income—

Mr. Lees: It is taxed.

The Chairman: Then you will be hurt in regard to taxes in a way that you are not presently being hurt.

Hon. Mr. Phillips: In addition you are taxed even though you do not receive it since it is permissive income.

Mr. Lees: That is correct. And the Norwegians are extremely tough with their dividends, and trying to get them to increase their normal dividend to give us something extra to pay the tax is another problem.

Hon. Mr. Phillips: Your only resource then would be to say that it is active business income rather than royalty income.

The Chairman: Either that or write something into the statute defining active business.

Senator Connolly: Mr. Chairman, could you direct me to where there is a definition of passive income?

The Chairman: It is in clause 95(1)(*a*).

Hon. Mr. Phillips: Did you intend to put a question, Senator Connolly, or may I continue?

Senator Connolly: I wondered whether the definition included tax incentives in the foreign country in question. I am looking at clause 95(1)(*a*), and at the subheadings (i) to (iv). I wonder whether the definitions there include things like tax incentives and tax holidays and things like that that the Chairman has been talking about.

The Chairman: The question of a tax holiday is that you are looking at offsets in the other country that you will get credit for on the Canadian tax rate. For instance in Thailand they give you a tax holiday, then you do not have a tax credit there and therefore you are paying tax on 100 per cent of the income that would come over. Something else I would draw your attention to is that they do not define "active business" so far as I can see. In 95(1)(*a*) they talk about "from businesses other than active businesses." Now what does that mean? It may well be that the income source in Norway originally may be from what you and I should understand to be an active business operation, but it can get converted en route to you, and may end up as passive income in your hands. It looks as though something needs to be rewritten there, but at the moment I cannot say what it is.

Hon. Mr. Phillips: Continuing along that line, Mr. Chairman, suppose we got away from this esoteric concept of an affiliate—which after all is a new concept and is not necessarily bad—and went back to a controlled corporation, and suppose that in that controlled corporation we could define "active business" as distinct from property or, broadly speaking, investment income then I think that substitution of investment income of some type for foreign accrual property income would improve the situation. "Property" can be derived from property used in active business activities, which is one of the confusions.

If we reverted to controlled company and investment income, could you live with that tax on permissive income?

Mr. Lees: If we took investment income, as I understand it.

Hon. Mr. Phillips: Royalty income in my opinion on that basis would be active business income.

Mr. Lees: I think it is money laid out to buy long-term bonds or shares in an amount of less than 10 per cent; just a few bonds.

Hon. Mr. Phillips: Surplus monies not needed for the active running of the business.

Mr. Lees: I would say it is probably zero. I gave some figures to Mr. Reid in Alcan's consolidation. There is a total of $30 million in the 70 accounts made up of inter-company dividends. Much of that is dividends from German subsidiaries to German parents. This with interest on bank accounts and so on, but almost all of it representing marketable securities, where we have bought and sold stocks and bonds, totals in the order of $300,000 or $400,000 in the whole group. We could live with a problem such as that.

The only area in which we have to be careful arises in our Indian subsidiary. It issues bonds, receives money a year in advance and puts it out at interest; I do not consider that to be investment.

Hon. Mr. Phillips: Let me put it this way: the Government is in love with FAPI and there is a romance with foreign accrual property income. We are faced with the situation in which we are asking, possibly, for a bill of divorcement, or we suggest to them that we wish to live in this romance under certain conditions.

Let us assume for the sake of argument that, even though some would go along with you, we ask for deferment of the section, or even complete elimination. Further, assume we must live with what I would call a romance, or let us call it FAPI or investment income. It would appear to me that, provided there was a control or, at least, proof of active participation in investment policy—one or the other—and provided the income was confined to investment income in the true sense of the word, that would be, at least, a common ground for compromise.

Mr. Lees: I agree. That is the sense of our brief. We have made specific textual language suggestions which we think accomplish precisely that purpose.

The Chairman: The word "dividends" somehow in the hands of those drafting this bill must have been equated with investment income. Apparently no thought was ever given to the fact the earnings from which those dividends were generated were the earnings on the active operating business. Why should they lose their character because the manner in which they are paid off is by declaration of a dividend? Why should they have another label because they are dividends? Should the basis not be to determine the origin or source and type of operation which produced this earning?

Mr. Lees: I would not condemn the bill on that basis. I think they endeavoured very hard to allow income to come from a factory in Germany. It goes from that subsidiary to a German parent, and from there to a holding company based in the Netherlands. Let us say we have a financial arrangement in this, and thence it goes to Canada. They have endeavoured very hard not to obstruct that flow of the earnings back to Canada.

A situation in which the money is taken in Germany and it is decided not to send it back to Canada, but to purchase bonds or shares in Bayer or Volkswagen in Germany, presents a problem.

I take it that Mr. Phillips is saying they do have a problem and if we are to have a marriage with FAPI, we must not quarrel if a German subsidiary buys shares in Volkswagen.

Hon. Mr. Phillips: It is merely postponement of a dividend out of surplus at that stage.

Mr. Lees: Yes, but the money might come back to Canada, where the shares would be bought.

Hon. Mr. Phillips: It is postponement of the increase of a dividend rate.

Mr. Lees: That is correct, but this is the purpose of our brief. We are not choosing to argue that issue.

Mr. Reid: Under your definition would a controlled company be one exceeding 50 per cent?

Hon. Mr. Phillips: That is my point. There should be no tax on permissive income unless it is diverted income; in other words, unless it is tainted. However, on the assumption that permissive income is taxed, surely it should only be taxed if the taxpayer had something to say about the policy of the investment. The control should be real control.

It would appear to me that the simplest alternative, as I said before, if the romance with FAPI is to continue, is to say, "For heaven's sake, if you are going to tax us, do not tax us on the value based on when we were in control and when, through control, were responsible for this permissive income".

Mr. Lees: That is correct. A Japanese example can be taken as a case in point.

Mr. Reid: That definition of control and a closer definition of the meaning of foreign accrual property income would narrow it down significantly.

Hon. Mr. Phillips: With that, plus the definition of an active business, you would be in the ballpark.

Mr. Lees: Broadly speaking I would say so. Let us take another example of a problem where that would not be perhaps an entirely adequate solution. We have a $10 million problem facing us in the next five years, $10 million of FAPI income in Britain. It is a holding company which issues convertible bonds in the British market. These bonds, if the company is successful, are ultimately converted into shares. This money is then left as an open account advance to a wholly-owned subsidiary to build a smelter permitted by British law due to the British need for smelters because of their balance of payment problem.

Under the British tax law, interest during construction cannot be capitalized. The advice was to keep the interest expense in the holding company and when the smelter goes into operation, instead of just charging that interest

at cost, add a point or two. For instance, if the interest rate had been 10 per cent, 12 per cent would be charged thereafter. Over a period of seven or eight years interest during construction will in effect be recouped against the smelter profits.

At this point I have to tell our management that the holding company will be generating a huge passive income which is now to the figure of $10 million, with $5 million Canadian tax to be paid.

They will recoup it in later years in Britain, but there will be no tax paid in Britain because of the large incentives. There will be no credit for British tax. It is a mess. Our answer to this is minimum exemption.

Hon. Mr. Phillips: Suppose we pushed this thing further and said that you were subjected to passive income provided you had control, and that it was passive income resulting from investment derived from retained earnings. That would cover the point.

The Chairman: It is not in any sense diverted.

Hon. Mr. Phillips: Of course, it does not answer all your problems.

Mr. Lees: Perhaps we could take a leaf from the American book. They refer to dealings between a subsidiary in the same country, all in Britain, Germany, or Japan, where you cannot have passive income. It is only when you deal with third parties, with independent people or foreigners from that country that you have passive income. Perhaps we could take a leaf from their book. It is one of our suggestions that where the transaction gives rise to this passive income all within one national boundary, it is then scratched out.

The Chairman: You say that there should be a common pocket.

Hon. Mr. Phillips: You say that it should apply when there is a bill of divorcement but not when there is a retained romance. But you will not get it, on the assumption that you will not be able to draw a distinction between territorial arm's length and non-arm's length. It appears to me that it would narrow it down very much. It would dilute it considerably by an extension of the meaning of actual business, plus passive income resulting from control, and from income resulting from retained earnings.

Senator Connolly: Senator Phillips, this might be the appropriate time for you to explain to us the meaning of diverted income.

Hon. Mr. Phillips: Diverted income is commonly expressed as being related to income subject to Canadian tax, and which because of its territorial use, is acquired in a foreign jurisdiction.

Senator Connolly: In that sense, would the term "diverted income" be used in connection with investment in a smelter in Britain, and invested in a new enterprise there? Would that be an example of it?

Hon. Mr. Phillips: I would say that is not diverted income at all. In my opinion it is strictly a bona fide extension of the company in the United Kingdom which has paid its business tax in the course of its business operations in the U.K. and then uses its surplus in the ordinary way of expansion. Surely that should not be regarded as passive income.

The Chairman: One of the difficulties here, Mr. Lees, is that if you are able to equate incentives and that sort of thing, which you enjoy in operations elsewhere in the world, to a tax credit that you would be entitled to apply against Canadian tax, it should be of considerable help, should it not?

Mr. Lees: I am not sure that I understand you.

The Chairman: I thought that one of your complaints was that in operating various offshore companies in different parts of the world you enjoy all the incentives, but that Canada taxes them because you have no offsetting tax credit. Is that not a problem for you?

Mr. Lees: In a way. We have many cases of perfectly fine companies where the statutory rate is only 40 per cent. I would not care to say that, even where they paid their full tax of 40 per cent, we should pay 10 per cent or 8 per cent in Canada on some transaction of the kind that we are talking about. I would use the analysis only for certain kinds of problems.

Mr. Reid: That is, of course, one of the worst examples of the tax differential.

The Chairman: If you have a tax incentive, the net result is that a corporate tax of 40 per cent in a foreign country might only be 20 per cent, which widens the gap and you would have to pay on that amount in Canada.

Mr. Lees: Another example where the bill reaches ridiculous heights is that where you have an American subsidiary which is trying to increase its business by acquisition, you buy 100 per cent shares and you do a merger. You merge that company into your base company so that it becomes a division, and the profits of the acquired company are available to use up your losses from investment credits.

The Chairman: If you use up your losses in a foreign jurisdiction you reduce the income.

Mr. Reid: You reduce the effective income tax.

The Chairman: Not only the income tax, but also the amount that would be attributable to you as earnings in Canada, in connection with FAPI.

Mr. Lees: You have to get the credits to offset FAPI.

The Chairman: You would have to equate the same amount of tax losses to the tax credit.

Mr. Reid: Or having used the losses from prior years, to offset them against the profits.

Mr. Lees: I would define the problem more carefully, rather than to compute what these credits would be, which in itself is very difficult.

Hon. Mr. Phillips: Would consolidation help you, in addition to the points that we have been discussing? Suppose the Government reversed its position generally on the whole question of consolidation, which was pressed by this

committee and supported in this instance by the committee in the other house—or alternatively we supported them. We have both pressed for it. If we succeeded in getting consolidation generally, not necessarily in any relationship to the subject matter that we are discussing, and if we confine passive income to the manner I have indicated—to wit, investment income, preceded by controls, and investment income resulting from surplus or retained earnings—would not the overall effect put you in a pretty fair position?

Mr. Lees: We opted very strongly for that. We still think it is a good idea.

Mr. Reid: It would help us in Canada. That would be another plus for us.

Hon. Mr. Phillips: I am taking the overall picture and pushing for the things that are arguable rather than dealing with some of the sophisticated and abstruse features like, for instance, your reference to the handling of the sitration in respect of particularly subsidiaries in one country as distinguished from other countries where there is a tendency to be bogged down when you begin to specialize in the repress for relief. We will shortly be asking your opinion on the question of deferment of the application of the section for a while in relation to tax freeze. Sticking to our knitting for the moment, suppose the suggestion were made along the lines that I am saying: back to consolidated tax returns, back to control instead of affiliate, back to business to be more specifically defined, and passive income to be the result of the use of retained earnings. It would appear to me that you would narrow down the area where you could be damaged.

Mr. Lees: That is correct.

Hon. Mr. Phillips: Very considerably.

Mr. Lees: Very considerably.

Hon Mr. Phillips: As a remedial measure, therapy rather than surgery at this stage.

The Chairman: It would be interesting to have your view on that point, Mr. Lees.

Mr. Lees: As a note of caution, I mention that Mr. Reid did not get a chance to finish his paper. In it he makes the point that our industry is reaching a crisis. Mr. Krome George, President of ALCOA (Aluminum Company of America), is suggesting somebody has to go out of this industry. When he met with Mr. Benson he said that somebody is going to be a gobblee and somebody is going to be a gobbler; what does he want Alcan to do? I would be worried that if we have to gobble up, or try to gobble up, our directors would have to be worried that they would be buying a horrible tax problem. That is what I have stressed, that one of the things we need is the American style 25 per cent of sales exemption. This is what worries me. I think that given the shape Alcan's business is in today your suggestion is adequate, we could live with it.

The Chairman: If you took 25 per cent of sales and put it in a pocket labelled, "untouchable profit", that is the profit of Alcan. Is that the way you want to do it?

Mr. Poissant: No. The 25 per cent is the passive income. If it is within 25 per cent there is no passive income. That would settle Alcan's problem. No doubt this is agreeable to you. How about the other companies? Would you have any ideas?

The Chairman: How can you jump to 25 per cent? How can you just say that if the amount of so-called passive income does not exceed 25 per cent of sales, then it is not to be treated as passive income? Is that what you are saying?

Mr. Poissant: That is what they say. That is what the Americans are using now. They say, "That would serve our purpose. Then we don't have to worry."

The Chairman: That is really very arbitrary.

Mr. Poissant: It is copied from the United States.

Mr. Lees: The American is 30 per cent. If you want to negotiate us down to 10 per cent, we could probably say we might live with 10 per cent, which is arbitrary.

Mr. Poissant: Which is not bad. It means to say that in any type of international co-operation there must be in some places a certain amount of passive income, or diverted income, but it could be for only a very short period, like your $10 million, which is not really your active business, but because of certain circumstances it must be, or as the chairman said before, perhaps it will lose its identity because income from one has become divided with the other one. If it was within a certain range—you say 25 per cent; the chairman may say we could use another percentage—that would solve a fair amount of problems, because then it would be treated as ordinary income, which because of the process is normal.

Mr. Lees: I think the American rationale is: "We don't mind if you have a little bit of passive income. We don't want you to be principally engaged in or primarily devoted to getting passive income". They use 30 per cent as an arbitrary mindless rule to say that if you get less than 30 per cent you do not even fill in the forms. This is all we are saying: give us that kind of a rule, plus these other two changes that Mr. Phillips mentioned, and we will live with it pretty well.

The Chairman: Mr. Lees, you started to analyze the so-called permissive or passive income. A great deal of it in a large multi-national operation is just the wise application of money that is available at the time and not needed in the active business operation to produce money.

Mr. Reid: Cash flow.

The Chairman: That is a sound economic pinciple, is it not?

Mr. Reid: Yes.

The Chairman: Therefore, maybe you should not correlate income produced in that fashion and call it diverted income, or passive income. In other words, you have to distinguish the character. If it is legitimate and makes economic sense and you are not doing it as a business, you are not doing it as a business, you are not in the business of doing it, then why should it come in that rule? It should

not come in the rule. Is that not right? Your idea of the American 25 per cent of sales as an arbitrary figure is perhaps a quick, short way of dealing with the problem and saving a lot of calculations, documentation, accounting and everything else. If you started with the kind of analysis I was talking about it might take a long time and cost a lot of money.

Mr. Lees: Oh yes.

The Chairman: I cannot understand why there should be penalty because a large multi-national company uses moneys not immediately required for the general purposes of the business. They use that to earn money which they will need in the future.

Senator Connolly: And the earnings from which they will ultimately take tax, and perhaps higher tax.

Mr. Reid: Let me give as an example the Indian operation, which is quite large. In the Indian Aluminum Company we have 65 per cent. They are allowed to pay their dividends once a year, with exchange control and whatnot. As they built up their cash flow to provide for dividends they would naturally invest it, presumably in securities and market instruments, and arrange some short term passive income, I suppose. This presumably would fall into the net of the present law, which seems undesirable.

The Chairman: You are referring to Bill C-259. Do not let us call it law before it is law.

Mr. Reid: I am sorry, the bill. You are quite right, senator.

Mr. Poissant: Mr. Lees, would you in those percentages exclude or include the know-how and royalties in your mind? You had in mind that one must be excluded before arriving at the calculation.

Mr. Lees: As I say, we made our own studies, which tell me that from what we have seen so far 10 per cent on a group basis, grouping all of them, is probably inadequate.

Mr. Poissant: Including or exluding royalties and know-how.

Mr. Lees: We would not mind. First of all, we say that any royalties coming to an affiliate of the company are out; you do not count it. Then we would not mind about the Norwegians. By definition, that is out, because it is not controlled. I think that kind of a problem gives one enough room, not to worry too much about defining too precisely what is income from property. Our sensitivity and worry on that level would go down, we would be less nervous.

Mr. Poissant: Say, 10 per cent in your case, based on your own experience, would do and you would be home free, there would be no problem? That means all we would have to do would be that "other than active business" would include less than 10 per cent, as it would be deemed to be passive income or other than active business. That would be included in the active business.

The Chairman: Not less than 10 per cent of what?

Mr. Poissant: Of sales.

Mr. Lees: Quite. I think we would be all right with that kind of rule. I am trying to think of the many situations we have. We constantly think of national groups, so that we have a holding company and a subsidiary and we have to add them together. Often our local managers want the holding company separate from the subsidiaries, for all manner of reasons. Sometimes this is royalty income, although attached to the holding company, which does not have much in the way of sales. It would be necessary to do some fine draftsmanship—which I think we have supplied.

Mr. Poissant: Is that 25 per cent included in your draft?

Mr. Lees: Yes, it is at 91.2. I have 10 per cent in there. There was a split conflict of interest. It is Exhibit C.

Mr. Poissant: You have 25 per cent. Shall we call it the Alcan amendment?

Mr. Lees: Right.

Mr. Poissant: Instead of the $500 suggested, which is too small.

The Chairman: It has been suggested that, due to the complications in this phase of the bill, international as well as income, where the provision is that it comes into force in 1973, that should be 1974; and where the provision is that it comes into force in 1976, that should be made 1977. In that way two things might be accomplished: there might be an opportunity to deal with treaties; and also a better understanding of the problems could be gathered in that further period of time. What would your view be on that?

Mr. Lees: Mr. Reid was quizzing me last night about administration. We could only applaud that step, because we are absolutely terrified as to whether we are going to have the staff to do the job. I think that is correct.

Mr. Reid: That is correct.

The Chairman: Remember that under our income tax law every taxpayer is his own assessor. You assess yourself, and if you go wrong you pay the penalty. All they do is tell you when you have not followed the right rules or got the right interpretation; but you have to be your own assessor in the first instance.

Mr. Lees: In our case, what it means is a lot of educating of people abroad, as to new forms to be designed and translations to be made. People in National Revenue who administer this tell me they are going to ask them to file a piece of paper for each subsidiary, with a copy of its tax return attached. In all innocence, what they do not realize is that in Brazil and in some of these places they do not prepare a tax return until two years later. And some of these tax returns are monumental in thickness. The tax return would become several bushel baskets of paper; this is what they literally ask for. I think we all need time to sort out that kind of thinking.

The Chairman: So you would approve such a recommendation?

Mr. Lees: Yes.

The Chairman: Failing that, you make some recommendations in your brief. They really involve modifications of sections in the bill, to lighten the impact on what you think the sections mean and the effect they will have on you. Would you feel that those recommendations, if they were

adopted, would meet your situation and perhaps make you a "globbler" instead of a "globblee"?

Mr. Lees: Yes, sir.

Hon. Mr. Phillips: May I put a further question, Mr. Chairman? A further approach by way of suggestion this morning was, that cumulatively, 1973 would read 1974 and 1976 would read 1977; and, in any event, that the sections themselves, with respect to passive income and dividends from affiliates, should not come into effect in respect of the passive income or the dividends of a particular country, until such time as it is established that the country from whence the passive income is deemed to come, or the dividend does come, is a treaty country, with a definitive treaty, or when it is established that there will be no treaty in respect to that country.

The background of that is that this committee—rightly, in my opinion—took the position in its report on the White Paper that we were putting the cart before the horse in dealing with this whole business of foreign income. There is acceptance of the principle, in the sense that we have a law which comes into force in 1972 and 1976, and so on, obviously for the purpose of getting the treaties put through. It has been suggested—and I personally like the suggestion—that we get back to logic and say, "Do not apply the new sections until such time as you have either worked out a treaty or have not worked out a treaty," because the method of treatment of the passive income and the dividend is related to the existence or non-existence of a treaty and, when there is a treaty, obviously to the terms of the treaty.

The Chairman: In doing that, you are not challenging any principle in the bill. All you do is defer its coming into effect for a further period of time.

Hon. Mr. Phillips: Frankly, the hope is, Mr. Chairman, that if that is done, the Government will have the opportunity to think it out a little more carefully . . .

The Chairman: That is right.

Hon. Mr. Phillips: . . . and will relate treaty negotiations to the problems that have been submitted to them for consideration.

The Chairman: If you interfere with something that is the pride and joy of the author, by direct attack, saying, "Suspend it," that is one thing. If you simply say, "We need more time to understand it," that is simply taken as meaning that you are not challenging the principle. Of course, time may challenge the principle.

Mr. Lees: Mr. Chairman, may I reply to Mr. Phillips? I would say sections 91 to 95 should not involve treaty negotiations in principle, because the whole sense of the sections, if they have any meaning, is to catch those Canadians who are avoiding Canadian tax.

The Chairman: Yes.

Mr. Lees: They should be looked at in that regard. I would not be prepared to negotiate that with a foreigner. That is a domestic problem; it has to be regarded as a domestic policy and it should be settled here. I do not think it is negotiable.

Hon. Mr. Phillips: But the question of tax relief on dividends, as distinguished from passive income in terms of credit, is closely connected with treaties. You have to have your treaties in order to know what you are paying. You are dealing with two factors. We have been concentrating on passive income, but the second one deals with the question of dividends.

Mr. Lees: If I were to approach it, I would get section 95 right. I believe they are gross now. Passive income should be aimed at diverted income. I believe we have suggestions for that.

The Chairman: When we put emphasis on the tax treaty side of it, that is not the important side which you feel the emphasis should be placed on.

Mr. Lees: Yes.

The Chairman: To the extent that these sections are intended to deal with tax avoidance, you are right. That is something that we can deal with in Canada and we now have enough law to deal with it.

Mr. Lees: I feel that government should retain somewhere, either by order in council or at the discretion of the minister, the right to permit a Canadian company to receive a tax-free dividend where the minister is satisfied that tax avoidance was not involved and the tax situation required the investment to be made in Uganda or in Mexico where the investor receives tax incentives. We will never negotiate treaties with some of these countries. I think the minister should have the authority to think it out and say, "Yes, we will give this one exemption; it deserves it".

The Chairman: If our reference to tax treaties bothers you a bit, we will forget that we said it. Let us take only the position that the chief design of section 95 is in connection with diverted income or tax avoidance. They are complicated and the taxpayer certainly is going to have to know his position. He could be inadvertently subjecting himself to penalties, so he should have the full time to study it and perhaps make full representations. Would you agree to that?

Mr. Lees: Yes, sir.

The Chairman: I have not mentioned tax treaties; I have not shocked you at all.

The Minister of Finance has stated on more than one occasion that the purpose of the provisions of the bill was to put a foreign affiliate in the same position as it would be if it were carrying on business in Canada. These provisions in the bill do not do that. They penalize the foreign affiliate as against a Canadian operation in Canada. Is that not correct?

Mr. Lees: That is correct.

The Chairman: So there is an over-exaggeration on this question of tax avoidance.

Senator Connolly: Mr. Chairman, could we have an example of just what you mean? I am not controverting it, but I think it would be helpful to have an example for the record.

The Chairman: What I am saying is that if your Japanese company was operating in Canada, I assume it would be part of the overall operation of the Aluminum Company of Canada Limited. Is that right?

Mr. Lees: Mr. Chairman, could I give three examples? This is a good question and it illustrates several points in our brief.

The Chairman: All right.

Mr. Lees: Many of our big Canadian companies are acquiring American subsidiaries, and if we take the example of an American subsidiary manager who wishes to acquire other companies, and the Canadian parent company gives him approval and agrees to raise money for him, he then buys up the shares and he makes a statutory amalgamation. However, he has been operating at a loss for the last two years; he has had losses, but he is seeing his way out. Now, if he makes an amalgamation, as I understand sections 86, 87 and 88 of the bill, he will be deemed to have realized a capital gain on anything he gets from that newly acquired subsidiary. The newly acquired subsidiary is an intangible asset—goodwill being a good example or some shares—anything which is in that subsidiary—he will have to deem an arbitrary capital gain. His American subsidiary is operating at a loss: it will not pay anything for the next two years, but the parent company in Canada will have to pay tax at the rate of 48 per cent on the deemed gain.

If a Canadian subsidiary purchased another Canadian company and made an amalgamation there are generous exceptions and reliefs and there would be no such tax. However, if your American manager said, "Look, I have this little division over in Chicago and I want to put it in a separate corporation—this guy is getting too big for his boots and I want to let him out"—he would transfer those assets to another company. This is covered under section 86 or section 87, I think. In Canada, if you took your Vancouver assets and put them in another subsidiary you pay no tax on the deemed gain on the transfer of those assets provided you retain 80 per cent of them, but if your American manager transfers assets you will have to pay tax on the deemed capital gain.

Senator Connolly: Simply because he is out of the country.

Mr. Lees: And there is no relief extended to the foreign corporation. I am sure it is an oversight, but it is in the bill.

Our English company is going to have losses for three more years because they are getting this smelter started. It is going to have sundry income. If our Canadian subsidiary had losses and at the same time had sundry income, obviously we would have some relief, but we will have to pay tax with respect to our English company because we have this FAPI. The company is operating at a loss and they do not allow us to take the loss on the ordinary basis to reduce the FAPI.

I would say those are the three most effective places where there is discrimination against our foreign affiliates.

The Chairman: Are there aspects here that we should discuss from your point of view? If there are, now is the acceptable time.

Mr. Lees: As Mr. Reid stated earlier, we did read the Massey-Ferguson brief with some appreciation because they did cover a great deal more ground than we did. We were rather single minded. We are terrified of this FAPI business. We would desire some of the points raised in the Massey-Ferguson brief to come to pass. I did notice that they neglected to talk about the instalment payment of income tax. I think it is depressing that Canada is the only country in the world which causes a corporation to pay income tax in January on its current year's liability.

The Chairman: Well, Mr. Lees, we have enough problems without attempting to rewrite accounting by corporations. It is really payment in advance; that is what it amounts to.

Mr. Lees: Yes.

The Chairman: I would think that FAPI could be made acceptable if you wrote a real definition of FAPI in terms of relating it to tax avoiding and diverted income. If you have any real FAPI income, you are prepared to pay tax on it, is that right—in the definition I have indicated?

Mr. Lees: That is correct. I would think that Alcan would not have very much of that sort of thing. It becomes so complex that as soon as you put down words to say these things, you have to be very cautious.

The Chairman: If you sit on money and you do not invest it in short-term investment while you are waiting to use it in your business operation, then, from a tax point of view, you are doing well and you are reducing the instance of tax. But the moment you apply it, you may fall into the category of passive income, depending on where you provided the money and where it is used. In any event, if you earn income on it, that income would be taxable. You would get caught in with FAPI, perhaps in a big way.

Senator Lang: The witness mentioned that he was terrified of the impact of these FAPI sections. If the bill went through in its present form and became law, could you re-organize the operations of Alcan to avoid this problem?

Mr. Lees: In my opinion, no.

Mr. Reid: You could take the ultimate step.

The Chairman: The ultimate step might be that what is left in Canada might be merged into a branch operation.

Senator Lang: That is what I am thinking of. You could convert your overall world operations so that the Canadian operation became a subsidiary rather than a parent.

Mr. Reid: Yes. It is a question of plus and minus. This is tipping head offices away from Canada and making them into branch companies.

Senator Hays: Would you consider a holding company in the United States controlling your Canadian operations?

Mr. Reid: We would have to think carefully about that.

The Chairman: Over the years much effort has been put into to ensuring that that situation did not exist.

Mr. Reid: But these things tilt towards those solutions.

The Chairman: They are tilted towards the United States or to the United Kingdom.

Mr. Lees: Or to Amsterdam.

The Chairman: It is a problem that should be avoided.

Mr. Lees: Alcan's Canadian shareholding has grown astronomically over the years. Canadian shareholders would have to be consulted. I do not think they would suffer economically if we were to go elsewhere.

Senator Isnor: Why do you paint such a dismal picture of the situation over the next two or three years?

Mr. Reid: The time factor arising out of aluminum investments is quite lengthy. For one reason or another excess capacity has been built into the world aluminum picture, largely through the coming into the industry of newcomers under incentives from government, which are attracting investment into the industry. The aluminum industry is over-built. For one reason or another the demand has not proceeded as anticipated. We anticipate there will be a period of over-capacity in the industry.

Senator Isnor: You mean in your own industry?

Mr. Reid: In the aluminum industry. Surplus inventory overhangs the market and we have to wait for growth to pick up the difference. We are suffering from competitive forces in the industry.

Senator Isnor: It appeared from the way you said it that it was a general statement.

Mr. Reid: It applies to the aluminum industry throughout the world.

Senator Lang: It applies also to the pulp and paper industry and to others.

The Chairman: No doubt we will hear the same story when representatives of the pulp and paper industry appear before us in a couple of weeks.

Hon. Mr. Phillips: They are hopeful that the new bill will get them into trouble with the amount of paper work required.

Mr. Reid: We have in our favour an average 8 per cent growth rate, which we hope will eventually eliminate this problem, provided that the production by newcomers into the industry does not proceed at a faster pace.

The Chairman: We shall have before us tomorrow morning representatives of the Canadian Bar Association, who have quite an extensive brief. We shall hear also from the Independent Petroleum Association of Canada and from Simpsons-Sears Limited. Simpsons-Sears will be dealing with the narrow point of the deferred profit-sharing plan and the treatment of trusts under the bill. The representatives from Simpsons-Sears will be appearing in the afternoon. The committee will adjourn until 9.30 tomorrow morning.

The committee adjourned.

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THIRD SESSION—TWENTY-EIGHTH PARLIAMENT

1970-71

THE SENATE OF CANADA

PROCEEDINGS

OF THE

STANDING SENATE COMMITTEE ON

BANKING, TRADE AND COMMERCE

The Honourable SALTER A. HAYDEN, *Chairman*

No. 43

THURSDAY, OCTOBER 21, 1971

Seventh Proceedings on:

"Summary of 1971 Tax Reform Legislation"

(Witnesses—See Minutes of Proceedings)

24287—1

THE STANDING SENATE COMMITTEE ON
BANKING, TRADE AND COMMERCE

The Honourable Salter A. Hayden, *Chairman*

The Honourable Senators,

Aird	Grosart
Beaubien	Haig
Benidickson	Hayden
Blois	Hays
Burchill	Isnor
Carter	Lang
Choquette	Macnaughton
Connolly (*Ottawa West*)	Molson
Cook	Smith
Croll	Sullivan
Desruisseaux	Walker
Everett	Welch
Gélinas	White
Giguère	Willis—(28)

Ex officio members: Flynn and Martin

(Quorum 7)

Order of Reference

Extract from the Minutes of the Proceedings of the Senate, September 14, 1971:

"With leave of the Senate,

The Honourable Senator Hayden moved, seconded by the Honourable Senator Denis, P.C.:

That the Standing Senate Committee on Banking, Trade and Commerce be authorized to examine and consider the Summary of 1971 Tax Reform Legislation, tabled this day, and any bills based on the Budget Resolutions in advance of the said bills coming before the Senate, and any other matters relating thereto; and

That the Committee have power to engage the services of such counsel, staff and technical advisers as many be necessary for the purpose of the said examination.

After debate, and—

The question being put on the motion, it was—

Resolved in the affirmative."

Robert Fortier,
Clerk of the Senate.

24287—1½

Minutes of Proceedings

Thursday, October 21, 1971.
(52)

Pursuant to adjournment and notice the Standing Senate Committee on Banking, Trade and Commerce met this day at 9:30 a.m. to further examine:

"Summary of 1971 Tax Reform Legislation"

Present: The Honourable Senators Hayden (*Chairman*), Beaubien, Benidickson, Carter, Connolly (*Ottawa West*), Everett, Gelinas, Haig, Hays, Isnor, Lang, Molson and Smith—(13).

Present, but not of the Committee: The Honourable Senator McDonald—(1).

In attendance: The Honourable Lazarus Phillips, Chief Counsel; Mr. C. Albert Poissant, C.A., Tax Consultant and Mr. Alan Irving, Legal Advisor.

WITNESSES:

Canadian Bar Association:

Mr. John L. Farris, Q.C., President (Vancouver);
Mr. H. Purdy, Crawford, Q.C., (Toronto); Chairman, Sub-Committee on Tax Legislation;
Mr. J. Albert Brulé, Q.C., (Toronto), Member, Sub-Committee on Tax Legislation;
Mr. Harold Buchwald, Q.C., (Winnipeg), Member, Sub-Committee on Tax Legislation;
Mr. Edwin C. Harris (Halifax), Member, Sub-Committee on Tax Legislation;
Mr. Ronald C. Merriam, Q.C., Executive Director, (Ottawa).

At 12:15 p.m. the Committee adjourned.

2:15 p.m.
(53)

At 2:15 p.m. the Committee resumed.

Present: The Honourable Senators Hayden (*Chairman*), Beaubien, Benidickson, Carter, Connolly (*Ottawa West*), Gelinas, Haig, Hays, Isnor, Molson and Smith—(11).

In attendance: The Honourable Lazarus Phillips, Chief Counsel, Mr. C. Albert Poissant, C.A., Tax Consultant and Mr. Alan Irving, Legal Advisor.

WITNESSES:

Simpson Sears Ltd. and Simpsons Limited:

Mr. E.A. Pickering, Vice-President, Simpson Sears Ltd.;
Mr. A. K. Hamilton, Corporate Comptroller, Simpson Sears Ltd.

Mr. D. A. McGregor, C. A., Clarkson, Gordon Company.

Independent Petroleum Association of Canada:

Mr. A. Ross, President (President, Western Decalta);
Mr. G. W. Cameron, General Manager.

At 3:30 p.m. the Chairman vacated the Chair and the Honourable Senator Connolly became *Acting Chairman.*

At 3:50 p.m. the Committee adjourned to the call of the Chairman.

ATTEST:

Frank A. Jackson,
Clerk of the Committee.

The Standing Senate Committee on Banking, Trade and Commerce

Evidence

Ottawa, Thursday, October 21, 1971

The Standing Senate Committee on Banking, Trade and Commerce met this day at 9.30 a.m. to give consideration to the Summary of 1971 Tax Reform Legislation, and any bills based on the Budget Resolutions in advance of the said bills coming before the Senate, and any other matters relating thereto.

Senator Salter A. Hayden (Chairman) in the Chair.

The Chairman: The first item that the committee has to consider this morning is the brief of the Canadian Bar Association. Those appearing are: Mr. John L. Farris, Q.C., President, Canadian Bar Association; Mr. H. Purdy Crawford, Q.C., Chairman, Sub-Committee on Tax Legislation, Canadian Bar Association—and honourable senators will recall that he was here before us on the Chamber of Commerce submission; Mr. J. Albert Brulé, Q.C., Member, Sub-Committee on Tax Legislation; Mr. Harold Buchwald, Q.C., Member, Sub-Committee on Tax Legislation; Mr. Edwin C. Harris, Member, Sub-Committee on Tax Legislation; and Mr. Ronald C. Merriam, Q.C., Executive Director, Canadian Bar Association.

Honourable senators all know Mr. Farris, whose name is well known in the Senate.

Mr. John L. Farris, Q.C., President, Canadian Bar Association: Thank you, Mr. Chairman.

Honourable senators, the Canadian Bar Association very much appreciates the opportunity of being heard by this committee. Our association has been very interested in tax laws and their administration, and our taxation section has been one of the most active in the Canadian Bar organization.

From the time of the Carter Commission we have had a special committee whose purpose has been to study tax reform in depth and to make recommendations. Briefs have been submitted on the Carter Report, on the White Paper, and on the legislation that is now before you.

While this committee has varied over the years, the nucleus has remained the same, and at all times it has included lawyers from coast to coast who are experts in the taxation field.

We continued this special committee in anticipation of this legislation, and it has continued its studies in depth.

With me to present the views of the association are the gentlemen whom the chairman has mentioned. Immediately on my right is Mr. Purdy Crawford of Toronto, Who is chairman of the special committee. Beside him is Mr. Buchwald, Q.C. of Winnipeg. Next to him is Mr. Brulé of Toronto, and on the far end is Mr. Harris of Halifax. Our executive director, Mr. Merriam, Q.C., is also present.

With your permission, Mr. Chairman, I will turn the matter over to Mr. Crawford.

Mr. H. Purdy Crawford, Q.C., Chairman, Sub-Committee on Tax Legislation, Canadian Bar Association: Thank you, Mr. Chairman. Last night, we gave some thought to how we would approach what we regard as some of the more significant issues facing your committee in connection with tax reform. We decided that we would raise those more significant issues by referring briefly to the introduction in our submission and by some of the other members of the delegation dealing with what we regard to be the most significant points. Following that, since our brief is long and technical, we would go back to the committee to deal with it further in whatever way they would like. That is our suggestion.

The Chairman: I indicated to you earlier that I have a question that I wish to ask you at some stage, and perhaps you had better be thinking about it now.

Would you give us your view of what the priorities should be in relation to the difficulties or objections to the bill?

Mr. Crawford: I think by the time we finish this opening part, on what we regard to be the most significant issues, we will have touched on most of the priority items. Then, if you would like to go back to them, Mr. Chairman, and have us write them and add any others you think are relevant, we will do that.

The Chairman: Fine.

Mr. Crawford: First of all, I want to refer to page 2 of the introduction. This introduction, although a bit hard-nosed, was worked out in late July here in Ottawa by fifteen lawyers from across Canada. These lawyers spent three days consulting with the Department of Finance officials and working on the approach of our submission. I am going to read a couple of sentences here:

> It is barely two short months since the budget speech and the publication of the first draft. The transitional provisions were not available until the beginning of July, the outline of the resource industry regulations and the international income regulations were even later. We have found it impossible in this short space of time to master the proposed legislation to the point where our criticisms can be in any

sense adequate. We do feel confident that for every problem or mistake, we have found in the statute, there are ten we have missed.

The Honourable Lazarus Phillips, Chief Counsel to the Committee: Mr. Crawford, just on that question of numerality and the missing ten, have you found 50 good sections in the statute which, on the basis of the Lord and Genesis, you could say "Sodom and Gomorrah" and save this bill.

Mr. Crawford: My colleague says we will leave the mathematics to the accountant.

I would just like to read on a little further, Mr. Chairman:

> In addition, we are sure that some of the possible problems or mistakes hereinafter referred to will, upon further study of the reform legislation, prove not to exist.

I want to emphasize that we think the group of people who did the work are of top-notch calibre. We are sure a good deal of it was done under tremendous pressure, and I do not care how bright and resourceful your people are, the problems we refer to are bound to come up. The second part in the introduction I wanted to touch on is at page 4. It is a general point and I would not put it forward as a priority item, Mr. Chairman, but it is an important item in terms of equity. It is at the top of page 4, where we state:

> We have indicated in this Submission, several places where reciprocity of treatment is not afforded to both sides of a transaction, as where a selling price is deemed to be some amount but the purchase price is not deemed so to be. We are sure we have overlooked many places where this will be a problem in the legislation and we suggest that a general section might be included to the effect that such reciprocity will always exist unless explicitly excluded in the statute.

That is the old problem that exists in Section 17 of the present act; and this comes up at least five or six times in our submission. This is a general point but we think it is important. There are two or three places where they have provided for reciprocity to both sides of a transaction. It is difficult to make an argument that the legislature intended reciprocity in the other places.

Finally, honourable senators, we state in the last paragraph:

> In view of the complexity of the draft legislation, we are certain that in the course of the next two or three years, many situations will come to light where the technical application of the legislation will be most unfair to taxpayers. We are equally certain that many "loopholes" will become obvious. We assume that it is for the latter reason that the tax collector has retained a broad discretion in cases where the equities clearly dictate a tax should be imposed, even if such a tax is inconsistent with the technical words of the Act. Surely, in fairness, this should be broadened so that the taxpayer has a similar right if he can convince the courts that to levy a tax would be a manifest inequity.

This is quite a novel suggestion. We put it forward seriously, however, in a day when all of the general provisions, the avoidance provisions—and they are becoming more—and the discretionary provisions are weighted in favour of the Revenue. It is time to start giving some serious thought to a provision that is also of general application weighted in favour of the taxpayer.

The Chairman: In ordinary language, you might say that equity is a two-way street.

Mr. Crawford: Yes.

Senator Connolly: Have you any specific suggestions you would like to point to in this connection, Mr. Crawford?

Mr. Crawford: At this point I would like Mr. Buchwald to speak on the administrative problems in this area.

Senator Connolly: I do not want to throw you off your general presentation.

Mr. Crawford: This is the way we planned on doing it.

Mr. Harold Buchwald, Q.C., Member, Sub-Committee On Tax Legislation, Canadian Bar Association: Senator, I believe that the answer to your question will become obvious as we get into the brief.

Senator Connolly: That is fine. Thank you.

Mr. Buchwald: Mr. Chairman, the comments on the administrative provisions of the statute appear at page 72 of the brief, the last section. The Canadian Bar Association feels a particular obligation to look very carefully at the administrative provisions because, after all, the enforcement and effective operation of the administrative provisions comprise our particular bailiwick.

We were pleased to note that the Minister of Finance remarked in his budget speech that when he got to the administration of the tax reform, many of the traditional civil rights and civil liberties of the taxpayers which had been agitated for over many years by the joint committee of the Canadian Bar Association and the Canadian Institute of Chartered Accountants had been incorporated in the tax reform measures. These, of course, are problems which have been brought to light from time to time by the joint committee of the two associations. Our concern is that while the minister and the Government have met some few of the civil liberty concerns that we have raised, there have only been a few of them. The thrust has not been adequate; it has been—and I am speaking personally and not on behalf of the association—not very much beyond tokenism. Throughout the drafting of the bill, the bill is an enforcement-oriented statute. It leans completely in favour of the revenue in almost all its approaches.

The key item that gives us the most cause for concern is the enshrinement in Bill C-259 of what the Minister of Finance of the day introduced in 1963 as a temporary expedient, the notion of ministerial discretion in the

assessment of two key areas of business activity; those being, surplus distributions and asset distributions, commonly called surplus stripping and dividend stripping.

The present odious section, to us anyway, Section 138A is now a permanent section of Bill C-259.

Hon. Mr. Phillips: What is the corresponding clause in the bill? Do you have that reference that handy?

Mr. Buchwald: Yes, I do. It is clause 247.

The Chairman: That corresponds to what?

Senator Connolly: Section 138A.

Mr. Buchwald: Section 138A(1).

The Chairman: I was wondering if you had gone back to look at the record of this committee and the Senate when that section was being considered. The then Minister of Finance was here, I think in December of that year. He was asked for an explanation, which he said he could not give. But they needed something because of a problem they were dealing with, and he said there would be another budget within four or five months and the matter could be picked up again, but it never was after that time. Even this bill does not propose to pick it up and deal with it.

Mr. Buchwald: That is correct. As a matter of fact, in the situation it was alleged to have been required for it appears not to have been legally necessary, because the decision of the Supreme Court of Canada in the *Smythe* case, which proceeded without the use of that section, indicated that the section was never required, that the Revenue, if it felt an improper surplus stripping scheme had been engaged in, already had within the present Income Tax Act sufficient ammunition and machinery to apprehend that kind of thing without having the ministerial discretion section. Now we find it, as we say, becoming part of the permanent law, for ever, in this temporary expedient in Bill C-259.

Senator Connolly: I just want to be clear on this one point in respect of the present bill. You say that under the old act section 138A would not have been required under the decisions.

Mr. Buchwald: That is right.

Senator Connolly: The equivalent of that, you say, is put in as clause 247 of this bill.

Mr. Buchwald: Yes.

Senator Connolly: Would you say that the scheme of the present bill is such that clause 247 is not required either in the light of these decisions?

Mr. Buchwald: Yes.

Mr. C. Albert Poissant, Tax Consultant to the Committee: There would certainly be less need with a capital gain, because certain of these transactions would become capital gains.

Mr. Buchwald: Precisely.

Senator Connolly: In ruling out clause 247, do you rule out only subsection 1, or the entire clause?

Mr. Buchwald: Just subsection 1. Subsection 2 deals with the exercise of ministerial discretion to associate corporations for the purpose of denying spin-off corporations the low base under the present act. It is comparable to section 138A(2).

Senator Connolly: The third part deals with appeals.

Mr. Buchwald: Yes.

Senator Connolly: That should remain.

Hon. Mr. Phillips: Are you satisfied with the rest of Part XVI, other than clause 247(1)?

Mr. Buchwald: Yes, I think so. We would concede that ministerial discretion is probably necessary if it is to be a business purpose test approach for associated companies. It was a problem, and it was met by section 138(2). Once you have subsection 2, with the minister exercising his discretion, I think you have to give the taxpayer a right of appeal so that he can challenge that discretion in the courts, and the courts can say whether it was exercised properly. As the chairman remarked earlier to Mr. Crawfold, the imposition must not be a one-way street. The associated companies provision has to prevail because the rest of the act is perpetuating the notion of a low rate in a small business incentive, and the Revenue has to be protected so that only one business can legitimately get the incentive and not a number of spin-off operations.

Hon. Mr. Phillips: But you are also satisfied with the retention of Treasury Board discretion of tax avoidance? Or to put it simply, as I said a moment ago, in Part XVI, which deals with tax evasion, there is nothing basically serious to which you object, other than clause 247(1)?

Mr. Buchwald: That is correct. I would hope there would be a scheme of legislation that would not require a broad sweeping artificial transaction section, as you find in sections 137 and 138, perpetuated in the counterpart clauses of the bill.

The Chairman: It indicates lack of faith in their drafting, does it not?

Mr. Buchwald: No, I do not think so. In fairness to the draftsmen, I do not think you can contemplate every business situation that will be promoted by tax planners and tax payers to avoid the intent of the legislation. I think the ground rules should always be clear on the business purpose or what it is that will attract tax, but until you have that there have to be artificial transaction provisions.

Hon. Mr. Phillips: Mr. Buchwald, may I put this question to you? Any suggestion from this committee that we eliminate clause 247(1) might be interpreted by the public at large as showing that we condone, directly or indirectly, minimization or avoidance of tax. Can you tell us, on behalf of the Canadian Bar Association officially, and more particularly through its tax committee, that you are satisfied the provisions of the proposed new bill simply

do not require the retention of this section, as a group of responsible lawyers across the country?

Mr. Buchwald: This is our unequivocal view, sir.

The Chairman: The plus that you add to it is the Supreme Court of Canada decision.

Senator Connolly: It is based on the decision in the *Smythe* case.

Mr. Buchwald: Yes.

Senator Connolly: I do not want to have a long discussion about this, but on the question of appeals from acts of ministerial discretion, one such appeal being given in clause 247(3) of the bill, the prospect of success in an appeal from ministerial discretion is fraught with considerable difficulty, is it not?

Mr. Buchwald: The minister's track record to date has been extremely successful, being 95 to 98 per cent.

Senator Connolly: In other words, for practical purposes there is no value in an appeal from a discretionary act, other than that it was palpably unreasonable, palpably inequitable. That kind of base perhaps might succeed, but it is a very difficult thing to achieve, is it not?

Mr. Buchwald: Yes, it is, but is there not this virtue, that the existence of the right of appeal perhaps acts as a restraining factor on an over-ambitious administration?

Senator Connolly: I am very glad you said that. I think that is very wise.

Mr. Buchwald: Knowing that their actions may be challenged, and perhaps they have to this point been quite circumspect in the exercise of that discretion.

Senator Connolly: Well, they are 95 per cent right.

Mr. Crawford: I should comment that the associated corporation provision appeals have not really worked too badly, because of the wording of the section. That is where they are 95 per cent right. Basically there have been no appeals on the dividend stripping discretion, because the minister has such a big stick when he comes to assess, and the risks of appealing are so great that he can force a reasonable settlement, or what he regards as a reasonable settlement.

Mr. Buchwald: It has been my experience, and the information I have from discussing this with other tax practitioners—and, if I may say so, Mr. Phillips, including an eminent partner of yours—is that businessmen are reluctant to engage in activities, to go into a venture, when their advisers indicate to them that they may be vulnerable to subsection 1 of section 138A. They will not know this, they will not have a tax ruling on it, until after the fact. So they have avoided that kind of transaction, rather than run the risk of having to face an assessment several years into the future, when they have re-arranged their affairs and have gone on to something else. But it might be interpreted in that way.

The Chairman: Mr. Buchwald, you must be familiar with something else that happened by reason of this section 138A. That is that purchasers on the other side of the transaction, if they are alert at all to this provision, and certainly their lawyers would do that, ask for an indemnification, to be indemnified against the possible exercise of this section.

Senator Connolly: May I make one further point about section 247(1)? Would you quarrel with the suggestion that was made by the departmental officials, that it is there for an over-abundance of caution? They may agree with you that the authority is in the act, based on the decisions that you have already cited, but the fact that it is there may not hurt. This follows what Mr. Phillips was discussing, but from another angle.

Mr. Buchwald: Yes, I agree they would say that. I would also agree with you that they would say—and we have heard them say—that its presence has apprehended, or brought to an end, a course of conduct they were trying to stop. Its very presence is acting like a big stick and has stopped dividend stripping. They would know this.

Senator Connolly: On balance, having said that, would you still adhere to the proposition that it should go?

Mr. Buchwald: If we are talking about tax reform, about trying to get for Canada a reformed, totally ideal tax system, then this ministerial discretion is not reform, it is "copping out," if I may say so, senator, on the notion of reform. They are admitting that they cannot clean up the statute in such a way that it will be clear and certainly that the administration will flow smoothly. So they have to go back to the big stick method.

I think that what Mr. Poissant said earlier is very appropriate—the introduction of a capital gains tax, and dividend stripping manoeuvres, were designed to create capital gains that would be tax free. A lot of the apprehension surely must go. Surely they are going to get at least 50 cents on the dollar—more than they did before.

Secondly, I think that any time there is ministerial discretion in a statute it ends up in trapping so many things that were never contemplated and it just leans on over-eager Revenue enforcement, not necessarily in the best interests of the taxpayer and thereby not necessarily in the best interests of the country.

Hon. Mr. Phillips: Mr. Buchwald, I would like to put a question to you now, but still sticking to section 247(1). Somewhere down the line we want to discuss with the association the desirability of eliminating designated surpluses under the new laws, which was closely connected with that section 138A setup. With the introduction of capital gains tax, I want to put a simple question to you. Would the elimination of designated surpluses, in addition to the introduction of the capital gains tax, further fortify your conclusions that section 247(1) would not be needed?

Mr. Buchwald: Yes, I would think so.

Hon. Mr. Phillips: Very well, that is all I want to know now. I do not wish to go into it.

Mr. Poissant: May I ask a question, Mr. Chairman?

The Chairman: Yes.

Mr. Poissant: Do you think that we would still need this in a transitional provision?

Mr. Buchwald: I would not think so. No, I would not think so.

Senator Connolly: I am sorry, I did not hear the question, Mr. Poissant.

Mr. Poissant: I am asking this. On January 1, 1972 when the new act comes into force, let us say, if there were still some stripping of surplus that had not been caught, I was wondering whether the department would still need to use section 138A of the old act to enforce its assessment policies. Do you think there would be a need to have it in the transitional provisions? It would be a kind of a phase out, in the transitional provisions, just like the others, but I am not too sure.

Mr. Buchwald: No, I would not think it would be required. However, let me put it this way, that we could achieve that compromise if we had to.

The Chairman: If you had to phase out.

Mr. Edwin C. Harris, member, Subcommittee on Tax Legislation, Canadian Bar Association: May I add one point here. This gets into the corporate tax area. The fact that there is the option now to pay a 15 per cent tax on existing corporate surplus makes the extraction of corporate surplus much simpler and much cheaper than it has been under the present act. Again, I think it makes dividend stripping much less attractive, relative to the alternatives.

Mr. Poissant: No doubt that is so. However, you realize, Mr. Harris that my question was not on this surplus income after January 1, 1972, but on this dividend stripping that could have taken effect before the tax reform.

Mr. Crawford: There is one point we should put on the record, particularly with reference to the question which Hon. Mr. Phillips asked. It is not just the *Smythe* case that leads us to say that section 247(1) should be taken out of the act and not even put in the transitional provisions either. It is the whole approach of the courts in interpreting the taxing statutes in the last five years. I have really no doubt, if there is a vigorous assessing policy followed by the Department of National Revenue, you would not need section 247(1). You might, through the court cases, throw up an area where there is a problem which can be changed by a specific piece of legislation rather than by a discretionary act.

Mr. Buchwald: Mr. Chairman, there are two or three other items which I would like to highlight and leave it at that, because there are so many other things in the bill. We mentioned in our brief, on page 72, that we are concerned with the perpetuation of the double jeopardy or double penalty method, that is perpetuated in the tax reform. The double penalty appears in section 163 and section 239. We feel that that is not consistent and we do not feel that that is tax reform, we feel that that is over-enforcement.

Talking on ministerial discretion in another area, there is a lot of discretion in a number of other places in the act, and it is perpetuated, we think to the detriment of the taxpayer, in Bill C-259. The minister has discretion as to whether he will register or not register pension plans, applications to be treated as charitable institutions, Canadian sports, authorized sports organizations, and so on.

There is a provision in the new bill, which is not in the present act, for appealing his refusal to register or his decision to deregister once he has granted registration. I do not intend to expand on this, but we do tell you on page 73 what we think the weaknesses are in the proposals outlined, and why we think that the procedure should allow the taxpayer to test the minister's discretion in a court dealing with facts rather than just dealing with law, because of the problems of trying to challenge a minister's exercise of discretion.

Then another thing that gives us a great deal of civil liberties concern is something that the Canadian Bar Association, I am proud to say, has agitated for many years—and on which we thought we had made some yards—and that has to do with investigations and inquiries conducted by the minister into the affairs of the taxpayer that may or may not lead to a prosecution or an assessment of his affairs, and so on. Courts have held that these inquiries are administrative procedures and, as a consequence, the taxpayer has no rights under these inquiries. He cannot refuse to attend. He is not entitled to be represented by counsel. He is not entitled to cross-examine anybody. He is not entitled to a transcript of the proceedings, and so on. To the credit of the minister and of the Government, and to the credit of the officials of the Department of National Revenue, the tax reform bill now tries to meet these requests. They have acknowledged that there is some merit in the requests the Canadian Bar Association has made and they have tried to meet them. We do not think they meet them adequately, and we say that with the utmost respect and appreciation for the gesture that the Government has made in this matter.

The legislation allows the witness to be represented by counsel, but then it goes on to say, however, that if the Department of Revenue feels that this would not be in the best interests of the administration, then the entitlement of counsel to be present and to cross-examine, or what have you, can be eliminated on the volition of the Department of Revenue because the department might feel it would impede the proceedings.

We think that it is fundamental that anybody whose rights are being looked into in this fashion should not be able to have those rights taken away on any pretext—a whim or otherwise, and we mention at page 75 of the brief the key things that bother us.

We note that under section 231 (15) the hearing officer may take away the fundamental right there set out of a

person to be present at any inquiry into his own affairs. We feel most strongly this denial of right under section 231 (15) should only be allowed on application by the minister to a Federal Court judge, where he justifies to the court why it should be necessary to deny this fundamental right to the taxpayer.

In this same area we also urge that consideration be given again to the right of the taxpayer or his counsel to cross-examine at such inquiries and to be entitled to a transcript of the evidence.

This has not been forthcoming, although we have recommended and requested it over the years.

The Chairman: Mr. Buchwald, on that point, we did put such provisions into the Estate Tax Act when it originally came in. These were amendments that the Senate added.

Senator Connolly: I am not familiar enough with the new bulk amendments we have had, but they do not cover these points, do they?

Mr. Buchwald: No.

The Chairman: The amendments I was referring to, Senator Connolly, were ones the Senate made to the Estate Tax Act some years ago.

Senator Connolly: I realize that, but I was wondering if the bulk amendments to this act covered the points at all, and I gather from Mr. Buchwald that they do not.

Mr. Buchwald: The point is that with respect to the taxpayer it ends up as a civil liberties tokenism if the rights that are conferred can be unilaterally withdrawn or denied or do not go far enough. That is the point.

Hon. Mr. Phillips: Do you think the repeal of section 231 (15) would do the trick, or are there any other danger points, danger sections or subsections, on this particular subject?

Mr. Buchwald: Yes, sir, there are some other danger points, and we have attempted to catalogue them on page 75 of our brief.

Senator Connolly: Mr. Buchwald, section 231 (15) provides that a person whose affairs are investigated is entitled to be present and to be represented by counsel throughout the inquiry unless the hearing officer appointed orders otherwise. What do you want to eliminate?

Mr. Buchwald: "...unless the hearing officer orders otherwise".

Senator Connolly: That is right, and you would also like to have inserted there, "the right to cross-examination and to transcript".

Mr. Buchwald: Yes.

Senator Connolly: Are there any other insertions you would like to see?

Mr. Buchwald: Those are the fundamental rights, I think.

Senator Connolly: These are the things which the Canadian Bar Association has made the subject matter of representations to the minister, and you say that he has met them up to a point but has not met them fully enough.

Mr. Buchwald: That is right.

Senator Connolly: What you propose now is that he go the full way.

Hon. Mr. Phillips: If I may make the suggestion through you, Mr. Chairman, I would suggest to the Canadian Bar Association that they let us have as quickly as possible the amendments dealing with this question of dividend stripping, secton 247 (1) and this whole question of the liberty of the subject and so on. I would ask them to stick to those two main points and give us their draft amendments as quickly as possible.

Mr. Buchwald: We would be happy to provide you with that.

Mr. Harris: Our position on section 247 (1) is simply that it should not be there.

Hon. Mr. Phillips: That is simple, yes, but I would like to see something in more compact form on the question of inquiries and the liberty of the taxpayer and so on in the form of a real amendment.

Senator Connolly: That would be a redrafting of section 231 (15).

Hon. Mr. Phillips: Yes, a real technical amendment.

Mr. Crawford: Mr. Chairman, we should be able to have that to you in a week or so.

Hon. Mr. Phillips: We want to have it before then.

Mr. Poissant: Mr. Buchwald, do you remember in the original bill that there was no provision for this section 245 (2), the old section 137 (2)? They had left out the deemed gift. Now it has been amended and that has been added. Considering the fact that there is no deemed gift under the new Bill C-259, would you feel satisfied as lawyers that the old section 113, which was part of Part IV which has now been completely deleted, should be repeated in the new bill or that the matters involved have been covered by other clauses in Bill C-259? It is now 245 (2) which they have added together with items (a) and (b) while (c) was left out. They have added item (c), by amendment last week, by saying that it is deemed to be disposition by way of a gift. But nowhere in Bill C-259 do we have what is deemed to be a gift as we had in the section in the previous statute. In view of the fact that they removed all the gift tax provisions in which was included section 113 dealing with deemed gifts and valuation thereof, do you think that the new Bill C-259 would have sufficient coverage to have here and there these deemed gifts?

Mr. Buchwald: The intention is to make sure that no income tax arises on a situation where there is a gift other than a deemed capital gain.

Mr. Poissant: I am sorry, I did not hear the answer.

Mr. Buchwald: I was just thinking out loud in reacting to your question. The scheme of the legislation is that there is to be no gift tax and no income tax arising under the new régime on the making of a gift other than a capital gain or recapture on the disposition of the property. The concern was that by having subsection 3 of former section 137 you are limiting it and you do not cover gift situations.

Mr. Poissant: It did not cover gift situations before, so I think that now we are pleased that this is being inserted.

Mr. Crawford: Perhaps it would help if you would remind us of these particular sections because we do not have the act with us.

Mr. Poissant: Well, it is section 113 of the present act whereby certain transactions were deemed to be gifts. Now we do not have it in the new one. We may say that something would be considered as being a gift, but they do not say what is deemed to be a gift.

Mr. Crawford: I see your point, but I cannot recall for sure what are deemed to be gifts. I would say that obviously it would help the scheme of the legislation if the concept of section 113 were carried forward to clarify that certain things would be treated as gifts with the results that follow and not treated as income.

Mr. Poissant: This is what my question is directed at. If there is no provision for deemed gifts, they may treat that as ordinary income for the recipient. But if it were a gift, the treatment would be altogether different.

Mr. Crawford: Bearing in mind that from the legal point of view a peppercorn takes you away from the gift, I think your point is well taken.

Senator Connolly: I take it the point of Mr. Poissant's question is that if a gift is taken as a deemed gift, then the substance of that gift should not be taken into income.

The Chairman: Well, the point he was really making was that in the present act you have a list of what are considered to be deemed gifts. Now they have not carried forward section 113 in that form to give you that list. So what happens if there are gifts now under the new bill that would fit into the old section 113 if section 113 is no longer there?

Mr. Crawford: They might be treated as income.

Senator Connolly: Where would the section be inserted if it were to be placed in the bill? You have not worked that out, Mr. Poissant?

Mr. Poissant: No.

The Chairman: Are there any suggestions?

Mr. Crawford: In clause 245, subclause 2, subclause 3 or subclause 4.

Senator Connolly: Or we could put it in the definition section.

The Chairman: As long as we put it somewhere.

Mr. Crawford: Well, we want to put it in so that it has the broad sweep, and that it is not limited just to one particular area.

The Chairman: You could put it anywhere in the gift area.

Hon. Mr. Phillips: I would think that this calls for study and supplementary submissions.

Mr. Harris: Just by way of example, Mr. Chairman, in section 69 (1)(b), which is a section dealing with inadequate consideration and is a modification of the present section, it specifically refers to a gift *inter vivos*. There are other places in the act too where this is dealt with.

Senator Connolly: It seems to me, Mr. Chairman, in view of the very rough taxing provisions in 245(2) it would highlight the matter if the deemed gift provision were included in 245(2) or somehwere close to it.

Mr. Harris: Of course, I do not like this sort of thing being put under the heading of tax evasion.

Senator Connolly: I am sorry, I did not look at the headings.

The Chairman: Well, I think we have taken this far enough. We understand that there is something that should be done there and we will find where. You referred to 69(1)(b).

Mr. Harris: Just as an illustration of the problem.

Mr. Crawford: One of the areas that has not been covered very much in terms of submissions, Mr. Chairman, has to do with some of the provisions in the reform legislation with respect to trusts, and Mr. Brulé, who is Chairman of the Wills and Trusts Subsection for Ontario in the Canadian Bar Association is here this morning and he is going to speak to this point.

Mr. J. Albert Brule, C.C., Member, Sub-Committee on Tax Legislation, Canadian Bar Association: Mr. Chairman, the section on trusts in the brief submitted to you is itself rather brief compared to the rest of the submissions. It commences at page 63. It has been given a great deal of concern to those particular lawyers dealing with this particular area more than others, generally because it is an area that comes into play quite actively in the practice of law.

I might say at the outset that we believe that a great number of the changes in the new bill are directed at the trust, which I suppose could be classified under the general heading of tax avoidance rather than the normal trust we find from day to day in existence and which has been employed over the years to help an individual provide assets for future generations—children and grandchildren—and also in the area of providing needed assistance for incompetents, invalids and so on.

Some of the provisions we set out here in our brief have been amended, I am happy to say, by the new changes introduced in the House last week.

The Chairman: Would you indicate what you mean?

Mr. Brulé: Yes, specifically on page 64 in the second paragraph on the definition of the word "income", this has now been corrected under section 108(3).

The Chairman: You are satisfied with the amendment?

Mr. Brule: Yes, we are. Then if you would turn over to page 65, the second paragraph concerning the definition of spouse trust—section 104(15)(a) has been amended. So that paragraph we feel has been corrected and we have no further complaint or suggestion to make. The third paragraph on that page which begins subsection (6) of section 104; this has also been corrected by making reference to section 105(2).

The Chairman: Mr. Brulé, I am going to ask you a question which you may not want to answer. With respect to these three places in your brief where you have referred to sections having been changed by the amendments which have come forward, what comment would you make as to the nature of those sections in the first place, which makes these amendments necessary? Is it an obvious error, or a lack of appreciation?

Mr. Brule: Perhaps I might deal with them individually. First of all, the word "income" as it has been known in the trust law is substantially different from that contemplated by Bill C-259. There are certain situations that exist from time to time where it may be classified as income for one purpose but it is not income for our purpose. We felt this was a rather obvious error, and that has been corrected. So deemed dividends as we have mentioned are obviously one example.

Let us move on to the second amendment which concerns us regarding what has been referred to as spouse trust. We would lose the context when the spouse died but the trust might not be distributed. So it was necessary to make an amendment referring to the rules which apply when the spouse is alive as to the attribution of income to the children where income was being accumulated, and they were not entitled to it at their early age.

Senator Connolly: I am sorry, I did not follow you. Perhaps you would give us an example. It is good for the record, in any event.

Mr. Brule: As an example, you have a trust which pays income to the widow while she is living, and after her death, the income accumulates until the children are a certain age. The act did omit the rules respecting attribution of that income to the infants during that particular period. This has now been corrected.

Senator Connolly: Now it will be attributed to the children?

Mr. Brule: Yes, there is provision for that. Then our third reference was to section 105(2) which deals with the necessary expenses for the upkeep of the trust and the allocation of that trust income to beneficiaries. I am sure this was an oversight and it has been readily changed to make it more equitable.

The Chairman: When you use the word "obvious" in connection with these sections, in your brief you indicate that there may be many more.

Mr. Brule: Mr. Chairman, I feel that we have found more perhaps because in the section dealing with wills and trusts at the time this brief was presented as Mr. Crawford has suggested at the outset, it was rather early in the game. Since then we have had several meetings of our group and we also have had meetings with the Department of Finance. They have been most co-operative and they have asked us to continue these meetings with them. There is a great deal more we have to say that is not in this brief which we are prepared to submit almost at any time.

Hon. Mr. Phillips: I hope you do not make it too simple and eliminate the practice.

Mr. Brule: No, sir. Now, I go back to my original point which was introduced in the first paragraph on page 63 where we indicate that it is rather complex. We have a concept introduced to us wheby a settlor of a trust could change if certain of the ground rules on contribution of capital to the trust changed by different parties. We have certain rules respecting preferred beneficiaries. We believe, as I have said earlier, that it is part of our later thinking that this could be simplified by classifying the trusts and by doing what is being done in certainly one other jurisdiction, that is submitting the trust at the end of the first year of taxation and allowing the minister to decide where this trust fits in, and tax it accordingly. The so-called legitimate trust for children and grandchildren would not be prejudiced. One of our biggest errors at the present time is that an existing trust may fall into a trap, as indeed many of them have, where they find it is subjected to the 50 per cent tax. We feel this is most unfair. A trust that is in existence on June 18, and to which money has been added since that time will find itself taxed at the 50 per cent rate. There has been necessity, in certain cases, to add money to the trust where it has been for the benefit of an incompetent.

Senator Connolly: On what basis would it attract a tax?

Mr. Brule: Under section 122 of the bill, because there is no specific exemption for particular trusts. Any trust that has been in existence as of June 18 and has had new assets added to it is now being taxed at the rate of 50 per cent. We thought that we would have had at least until the end of this year to look at this more closely. We still have gift tax provisions, and no one can indiscriminately add larger amounts to that trust during this period. Other trusts have now been tainted because we do have simple trusts for children and grandchildren, such things as baby bonuses which are simply added to the child's trust and the child can benefit from it in the future. But it then becomes subject to the 50 per cent rate of tax.

Senator Connolly: Under section 122 of the bill?

Mr. Brule: I am speaking without reference to the particular section. This is where we find our taxation rules.

Senator Connolly: Mr. Chairman, this would seem to be a point which we should go into.

The Chairman: This is exactly what we are doing, senator.

Senator Connolly: I do not mean to hold up the committee unnecessarily.

Mr. Poissant: In other words, Mr. Brulé, what you are asking is that in respect of a trust that was formed under a gift program of, let us say, $2,000 a year, which was a bona fide trust prior to June 18, 1971, they should have the right to continue on that program...

Mr. Brule: At least until the end of the year, if not indefinitely.

Mr. Poissant: I would go further than that. If they were originally formed for that purpose under the existing law at that time why would you not go so far as to say they should carry on the same, not adding more assets than their privilege in the prior period?

Mr. Brule: Mr. Poissant, we have suggested that a trust could be classified and if a trust fell into this category—I have referred to it as a so-called trust for a child, or a protective trust—it would only be taxed on the same basis on which it is now being taxed, at the present rate without exemptions.

Mr. Poissant: Would you have that apply for all trusts?

Mr. Brule: No, not for all trusts. We do believe that in a classification there are certain trusts, especially the so-called tax avoidance trusts, where they should, in fact, be taxed at the 50 per cent rate.

Mr. Poissant: What is the position of a trust that could borrow or had more capital than in previous years? Would that not be a type of tax avoidance?

Mr. Brule: That is correct; that is why we feel that it should not be given special treatment. Otherwise it could result in a form of income splitting by allowing the trust to borrow and make profits at a lower rate than an individual. However, that would manifest itself in two ways: First of all, if the trust itself had the right to borrow and the department saw the trust; secondly, if during the action of its yearly transactions, as evidenced by its income tax return, it did in fact borrow, the minister would have the right to move it from one to another classification.

The Chairman: It would appear that clause 122(2) aims at that.

Mr. Brule: That is correct; I would have no quarrel with that.

The Chairman: I can see uses for it.

Mr. Brule: We believe that at the outset the legislation was drafted, perhaps, solely thinking of tax avoidance and not return on tax planning.

The Chairman: That was admittedly the plan; the design of this bill is to close all gaps that existed. They did not say anything about opening others.

Mr. Brule: No, they closed some that we feel should be closed.

The Chairman: What would you suggest by way of amendment in order to cure this problem?

Mr. Brule: We feel that trusts should be classified and put into regulation. Then, depending on what category each trust found itself in, it would be taxed accordingly. That is spouses' trusts, children's trusts, certain protective trusts.

The Chairman: That may be a long range view.

Mr. Brule: It is not difficult; as a matter of fact, we feel this is simpler than the provision contained in the bill. We have already discussed it with the Department of Finance.

The Chairman: With that introduction by you and the simplicity of it being so apparent to you, we would say that you should draft it and send it to us.

Mr. Brule: As a matter of fact, senator, we have it almost done.

The Chairman: When will we receive it?

Mr. Brule: As soon as I can assemble my committee. We have already submitted this to the Department of Finance and discussed it with them.

The Chairman: But they have not dealt with it?

Mr. Brule: They have neither dealt with it nor returned it to us.

The Chairman: Perhaps we will.

Mr. Brule: Thank you.

Mr. Poissant: As an alternative in the event the definitions of the various trusts were not accepted, would it be acceptable that at least those bona fide trusts now in existence that have been receiving money over the past years be allowed to continue doing so, and be treated as previously?

Mr. Brule: Yes, and it should go one step further. There will certainly be occasions in the future to create trusts, again with respect to the incompetent or invalid who will need monies placed in trust for his care and well-being. It is certainly unfair to have that particular money taxed as income earned by the trust, at the rate of 50 per cent. He could be given the money personally today and personal rates would be paid The individual being an incompetent, that cannot be done; a trust must be created, which would be taxed at 50 per cent.

The Chairman: In your opinion the creation of classes of trust is in essence simple. However it may be a basis

for the department to say this is a new idea and they wish some time to consider it.

Against that possibility we should have an alternative amendment to deal with the problem you put forward.

Mr. Brule: We will put both forward.

Senator Carter: I am not sure whether this situation would be termed a trust. I am thinking of benevolent funds for the army and navy, which originally were made up of funds accumulated in canteens. Subsequently, veterans' organizations have added to them and I think occasionally there is a Government grant. I assume that these funds are an income. Would you put them into a separate category? Are they taxable under this law?

Hon. Mr. Phillips: It is a different clause.

Mr. Brule: They do not come under these provisions at all; they are charitable organizations, depending on their operation. I think the department adjudicates whether they are charitable; if they are, there is no income to them.

Senator Carter: What would be the position of a single veteran who is in a mental institution and entitled to free treatment and his pension builds up into a sort of trust? He is not in a position to administer his own funds.

Mr. Brule: That situation, I believe, is governed by a separate statute. However, the funds were deemed to be deposited in a trust to be used for his benefit, administered by an individual or corporate trustee, the income earned on it would be taxed at 50 per cent.

Senator Beaubien: 50 per cent is a new rate for this.

Mr. Brule: Correct; previously it was a personal rate for taxing a trust as an individual, with no exemptions.

Senator Connolly: Have you any comments to make with regard to the percentage of tax?

The Chairman: Senator Connolly, the whole design of this section was based on tax avoidance. The rate prescribed indicates that; it is a penalizing rate. Therefore everything not considered to be taxable income should be removed from this clause.

Senator Connolly: Yes, Mr. Chairman; the only specific example given by Mr. Brulé, is the case of an individual who sets up a trust, for instance, for a disabled child and pays the maximum annual amount of gift into it, of $2,000.

Mr. Brule: The maximum tax-exempt amount.

Senator Connolly: Precisely. Under the present act the income from that trust is taxable at the beneficiary's rate.

Mr. Brule: Yes, if there is a designated beneficiary and the money is paid to or on his behalf.

Senator Connolly: Or attributable to him.

Mr. Brule: Yes.

Senator Connolly: The new scheme proposes not to use the marginal rate of the beneficiary, but a flat 50 per cent rate.

Mr. Brule: That is correct.

Senator Connolly: And, as the Chairman says, for the purpose, perhaps, of curing a situation which might be tax avoidance.

Mr. Brule: It is the higher of the individual or corporate rate; 50 per cent would be the floor rate.

The Chairman: This clause does not apply, of course, to every type of trust. Perhaps I should put it this way: Senator Connolly's illustration depends on whether this contribution of $2,000 per year had started before June 18. If it had started and then was being continued by these $2,000 contributions, it would be caught under clause 122.

Mr. Brule: That is correct.

The Chairman: But if the trust were set up as a new item in January, 1972 the $2,000 contributions each year would not be affected by clause 122.

Mr. Brule: You would be caught at the outset, depending on what is happening with regard to the attribution of the income.

The Chairman: Supposing this trust that Senator Connolly was talking about was established on January 18, 1972?

Mr. Brule: Then we would follow the provisions of Bill 259 on attribution.

Mr. Buchwald: Let us take a long-established trust that has been set up to fund a child's education. The deposit of the July 1 asset under the Family Allowances Act would cause that trust to be taxed at the 50 per cent rate for this year.

The Chairman: A lot of parents would deposit in some kind of a trust fund even the $8 or $10 cheque per month that would come to the child.

Mr. Brule: Our major concern has been that there was no period in which you could alert the thousands of trusts that are in existence on what they could or could not do, and many of them are saying "What do we do?" We thought that these provisions could apply until the commencement of the new bill.

The Chairman: The amendments that we have talked about and which you are going to forward to us will deal completely with the situation, and we would not need to suspend the application of this section until January 1, 1972?

Mr. Brulé: That is correct.

The Chairman: In doing that suspension we would be permitting a continuance of tax avoidance.

Mr. Brule: I have a few other comments that I should like to make. Without elaborating on them, they are

covered in the brief, the first being on page 63. I do not intend to take you through the exercise. You will find that under a so-called legitimate situation where money is paid out to a beneficiary, we could have double taxation.

Nothing has been done to correct that. To put it simply, where an encroachment is made for a child who needs something, and to make the encroachment something has to be sold for a capital gain, the child in turn makes the asset, he himself makes a capital gain, and there could be double taxation.

The Chairman: Is that part of the submission that you made to the minister?

Mr. Brule: Yes.

The Chairman: And it has not been included in the amendments?

Mr. Brule: No, it has not. I wish to comment on that.

Senator Connolly: Are you going to submit an amendment to the section in question, to the effect that you think it might create double taxation?

Mr. Brule: Yes. In other words, that relief would be given in such a situation so that there would be no double taxation.

The Chairman: Do you have a draft of that?

Mr. Brule: Yes. I wished also to make reference to the bottom of page 64, subsection 75(1), concerning attribution of capital gains. If money is transferred to a minor and a capital gain results, there is no attribution tax to the donor of the gift. However, if the donor makes such a gift to a spouse or to a trust, there is attribution.

What we really wanted to find out is why in one case and why not in the other. Perhaps we are helping the department in this situation. There could have been an omission. That is what we say in our brief.

The Chairman: The principle might be to put the burden on the transferor, if the transferor is an adult and the transferee is a minor.

Mr. Brule: A minor can, however, assume a capital gain, perhaps at a better tax rate that the parent.

The Chairman: You say there should be an option.

Mr. Brule: We are saying in an indirect way that if it is available to a minor, then why not to a trust, especially if the trust is for the minor. In other words, if you give it to the minor, he could make a tax-free gain. If you give it to a trust for his benefit, there is an attribution tax to the donor.

The Chairman: Are you suggesting enlarging the tax provisions in the case of a minor?

Mr. Brule: Yes. I think I have spoken sufficiently about trusts and the classification regarding protected trusts and child trusts. We will bring something forward for the committee.

Mr. Poissant: Somewhere you have mentioned the minority age.

Mr. Brule: I am sorry. That has been changed. In other words, because most provinces are reducing the age of majority to 18 years, it was suggested that former reference to attribution for minors under 19 years should be changed to 18 years. That has been corrected.

Mr. Poissant: And you are satisfied with the amendment?

Mr. Brule: Yes; we suggested it.

Mr. Poissant: No. You suggested that the age should be according to the majority age legally by provinces.

Mr. Brule: I am sorry. We specifically said in our other brief that we had talked with the department, and we assumed that they followed that.

The Chairman: Have they followed the reduction to 18 years in the amendment?

Mr. Brule: Yes.

Mr. Harris: I propose to deal with business and property income. Mr. Chairman and honourable senators, I want to speak at length on this area. I may perhaps make the general comment that in this area, perhaps more so than in any other, the so-called tax reform is not reform at all. Our chief complaint concerns not so much the changes that have been made, but those that have not been made. In the business and property income area, apart from a few amendments, the provision have been carried forward essentially unchanged from the old act.

The proposal in the Carter Report for the streamlining and simplification of the provisions dealing with the measurement of business income has been completely ignored by Bill 259.

The Chairman: To what section does your comment apply, that there is no essential change in the provisions contained in the old act dealing with business and property income?

Mr. Harris: They are scattered.

The Chairman: Are they listed in your brief?

Mr. Harris: Not as such. I am referring in particular to section 12 of the bill regarding amounts to be included from income of business and property, and section 20, which is the deduction side.

There are a number of other sections, but it would take too long to list them all. There are sections concerned particularly with the measurement, the timing, and the recognition of income. There are other sections concerned with so-called reserves. The old section 85B has now been split up between sections 12 and 20. It seems to me that the Carter Report was very valid in its suggestion that this could be considerably simplified. Many of these provisions came in ad hoc by amendment over several years. The changes that have been made are particularly in the area of goodwill and other nothings.

Our objection to the treatment of these items is two-fold. First of all, we are concerned with the transitional provisions under which a gradually increasing proportion of the sale price of these rights and assets on hand at the commencement of the new system become taxable when they are sold afterwards. The argument we made at the time the proposal in the White Paper came out was that this represented an arbitrary and, to some extent, a retroactive taxation of goodwill and similar assets. Granted, the bill, with its transitional provision, will now tax only half rather than the entire asset, but the retroactive aspect remains.

Senator Connolly: Mr. Harris, before you go any further I want to make an admission and then ask you to clarify it. In the discussions on the White Paper, and now on the new bill, we have talked a great deal about "nothings", and I have yet to know what people mean by "nothings". They say, "goodwill and nothings". What are "nothings", or is it because they are nothings they cannot be defined?

Mr. Harris: That has been the difficulty. Many of these so-called nothings could have been recognized as proper business expenses if the courts had, in their interpretation of the act...

Senator Connolly: They are nothings in the sense of assets?

Mr. Harris: They are nothings in the sense of non-deductibles. In other words, these are business-related expenses which the courts have treated as being capital expenditures and therefore are not currently deductible as a business expense under the act. At the same time, they do not qualify for depreciation because they do not fit under one of the capital gains cost allowance classes.

Senator Connolly: Well, you are doing something for history, so could you give us some examples?

Mr. Harris: There is a long list of them, senator. An example might be the amount paid to acquire certain intangible rights of which goodwill is only an example. You might pay for a list of customers or you might pay to acquire a contract.

Mr. Buchwald: Is not the obvious one, senator, incorporation costs? When you incorporate a company it costs you $500 for legal fees and departmental fees and this expense is not deductible.

Senator Connolly: That is a nothing. Put it the other way, "that ain't hay."

The Chairman: To give it its right description, Senator Connolly, just call it a non-deductible expense!

Mr. Harris: Never deductible; neither currently nor in the future by depreciation.

The Chairman: Because they classify them, as the courts have, as capital items.

Mr. Harris: Yes, and they do not fit under the depreciation class.

There have been a great many complaints about this over the years and the new bill states in essence, "We are not going to give you full deductibility, but we will give you half deductibility". In other words, "if any of these so-called nothings turn into saleable assets, we will tax you on half of the proceeds".

If you accept the department's philosophy with respect to half taxation, we would suggest that the easiest thing to do would be to classify these nothings as another class of depreciable property, rather than giving them a separate status under the act. This would considerably simplify the treatment of goodwill and other nothings, and you could arrive at essentially the same results as the bill does without creating a separate category of property which is what has been done.

The Chairman: And without reducing tax revenue?

Mr. Harris: Yes, and without reducing the tax revenue.

Senator Connolly: When these nothings are sold, if you can say that, then there would be recapture.

Mr. Harris: There would be both recapture and, if the sale price were high enough, capital gains. This is the same as happens with respect to depreciable property under the act.

Senator Connolly: Are you suggesting that the rules respecting depreciable property be applied to them?

Mr. Harris: Yes.

The Chairman: And in that area, there should be an enlargement. Is this area specifically covered in your brief?

Mr. Harris: Yes, it is, Mr. Chairman.

The Chairman: At what page?

Mr. Harris: It is at page 34.

The Chairman: Have you a draft of the amendment?

Mr. Harris: No.

The Chairman: This item in your submission was discussed with the department, was it?

Mr. Harris: This is our brief that went in to the Minister of Finance.

The Chairman: In this form?

Mr. Harris: Yes.

The Chairman: And you did not present the department with any particular form of amendment?

Mr. Harris: No. We did not have time to draft amendments when we submitted this brief.

Senator Connolly: Would you have time to do it for us?

Mr. Buchwald: It is a big amendment. The concept of eligible capital property, which is your new goodwill concept, permeates the bill.

Mr. Harris: There may be 15 or 20 places where amendments may be required.

The Chairman: Can you do it in an omnibus way with one item?

Mr. Buchwald: You would have to delete provisions and make appropriate changes and cross references in other parts of the bill in order to do it.

Senator Connolly: Even if you did not get them all, would it not be helpful to have some, and then let the department worry about the rest?

The Chairman: If we feel strongly enough about it, the alternative would be to suggest that a study be carried out.

Mr. Harris: I rather suspect, Mr. Chairman—and this is just a guess on my part—that in the course of the testing and drafting of the legislation the department probably has some draft with respect to this approach to the tax reform in their file. I am not sure; that is just a guess.

The Chairman: The feeling, as stated in our original report on the White Paper, was that they had better do some studies.

Mr. Harris: The other recommendations we have in this area, Mr. Chairman, are rather technical and, unless the committee has specific questions, I do not think I should take the time of the committee on them.

Senator Connolly: Are they the subject matter of specific amendments which you are proposing?

Mr. Harris: There are some, yes. For example, a company-owned car might be taxed in the hands of several individuals at the same time so that there would be an overlapping of taxation. I do not think this is covered in the recent amendments. I have not had a chance to look at them.

The Chairman: What I am looking at, Mr. Harris, is at page 35 where you are talking about section 131(4) relating to the receipt by holders of mutual fund shares deemed dividends. After you explain the effect of this particular provision, you say:

> We assume this was not intended and could be corrected by adding a paragraph (*g*) to section 15(1) to exclude payments to which subsection 131(4) applies.

Mr. Harris: Yes. I have not had a chance to look through all of the amendments, Mr. Chairman, but this was not done in the amendments that were presented last week. I think it would be quite a simple amendment to add.

The Chairman: Are you able to assess the importance of the effect on the holder of mutual fund shares if this exception was not made?

Mr. Harris: It seems to us that this was a fairly unintended result in that the holder of mutual fund shares might be taxed on what is considered to be a benefit as a result of the redemption of mutual fund shares. We do not feel this was intended at all. It would be, in effect, double taxation.

The Chairman: If that is the concept, if we had a lead in with that concept, do you think the statement at page 35 of your brief is clear enough on the effect, and why we say it was not intended, or could not have been intended, as a basis for suggesting an amendment?

Mr. Crawford: If I might interrupt, I think this deficiency would be overcome by an amendment to clause 15(1)(*d*) in the amendments tabled.

Mr. Harris: Yes, I think it has been overcome now I look at it.

The Chairman: That is one less thing, then.

Senator Connolly: I was going to ask for an example of it, but if it is fixed up I do not want the example.

The Chairman: No, that is taken care of. By the way, in the area to which you are addressing yourself, have you analyzed what points you have developed have been taken care of by the amendments?

Mr. Harris: No. Unfortunately I did not see the amendments until late last night, but I do not believe most of the points we have made have been dealt with.

Mr. Crawford: When did you get the amendments?

Mr. Harris: Yesterday.

The Chairman: The minister undertook that we would get them the moment they were tabled, but it even took us a couple of days to get them. I think the breakdown was in the printing. I do not mean breakdown in the literal sense, but that is where the lag came.

Mr. Crawford: It is probably nobody's fault, but we have not had an opportunity to analyze our submission in the light of all the amendments.

The Chairman: I was wondering whether on this score Mr. Harris is satisfied that we accept the statement that the amendments that were tabled by the minister on Wednesday do not affect the points you have raised in the brief your under heading.

Mr. Harris: Not entirely, Mr. Chairman. For example, in clause 18, which is the thin capitalization provisions on interest paid to non-residents, there has been a helpful amendment that I see, where the only interest that would be disallowed is interest that is paid to non-residents, which is a point in our brief. That has been dealt with. We can submit a supplementary memorandum in the light of this.

The Chairman: We are not trying to pile ourselves up with paper.

Mr. Crawford: I suspect that you or your advisers have probably done that already.

The Chairman: I am trying to share the load, that is all. Asking you to do it means this is one area that you explore. Mr. Poissant has to cover all areas and at the same time work with us on the preparation of a report. In fact, I can tell you that we are working on an interim report right now. We are trying to keep up to date. At the end of the day we may very well be talking about what you have said this morning.

Mr. Crawford: I think we could undertake to give you an analysis of our submissions that have been accepted in whole or in part by the amendments tabled to date.

The Chairman: Mr. Harris, were there any other comments?

Mr. Harris: No, Mr. Chairman, there are no other points I wish to raise.

The Chairman: Mr. Crawford, as the master of ceremonies here, are there any other areas you want to take us into?

Mr. Crawford: Yes, I would like Mr. Buchwald to say something about capital gains, and Mr. Harris to say something about corporations.

Mr. Buchwald: The whole character of the tax reform bill, it seems, stems from the introduction of capital gains into the system, and that is why you end up, it seems to me, with this kind of a regime or scheme of taxation, a scheme that relies primarily on sources of income. The capital gains portion is the largest part of our brief, and appears at pages 5 to 20 inclusive. We list there a number of administrative matters that give us some cause for concern. Some of them are fairly technical. We have tried to point out, I hope as lucidly as we were able, our concensus conclusions as to the problems that could arise with the legislation as presently drafted. We have to say that we think the approach is an overly complex one. I am sure you have heard that before, Mr. Chairman.

The Chairman: Yes.

Mr. Buchwald: Turning to page 6, we have to say we are very concerned with the notion of deemed capital gains. People should know that it is one thing to pay tax on a profit made, or a disposition of an asset when you have a profit in hand, or you have moneys worth, or a receivable that is then negotiable or discountable at a bank, so that you have the funds with which to pay the tax. It is quite another thing to have a deemed disposition where you are notionally taken to have disposed of the assets, realized a gain and have tax to pay on that technical realization when you do not have the cash in hand. This occurs under the bill in two serious areas—death and leaving Canada. The deemed realization on death is the answer to elimination of estate taxes, although Senator Haig will be happy to hear that the premier of our province wants to bring back estate taxes, and is going to fill the gap. He announced that in Winnipeg on Monday, so Manitoba will have estate taxes and capital gains deemed realizations on death.

The other areas we have been hearing most about from our clients, almost universally across the country, from what we were told at our annual meeting in Banff and what we have been told since, concerns people who are planning to retire and leave Canada, to change their residence for a warmer climate or what have you, as well as itinerant executives who have come here from elsewhere and will be returning to their countries of origin. They are quite concerned about the deemed disposition or deemed capital gains situation when they change residence.

The Chairman: On the question of these itinerant executives, do you think there should be an exclusion of everything except gains that they may have made while they were here?

Mr. Buchwald: That is exactly what we say in this submission. We are concerned about a couple of inequities that will occur in this situation, with people who have come to this country to work in good faith and then get trapped by a system that is designed to do something else. In determining their rate, all of their income for the year of disposition will be taken into consideration. For purposes of apprehending a capital gain on departure, they will be deemed to be residents of Canada. So all income will be taxed and they run the risk of being double taxed in their country of relocation in the same year.

The Chairman: Is there not a real danger, in their being deemed to continue their residence here, that they might be caught up in all other legislation that deals with residents—that is, if the federal authority says they are residents?

Mr. Buchwald: Assessments for the purposes of this act, for the purposes of levying the tax.

The Chairman: But you do not know what a provincial statute might say.

Mr. Buchwald: That is correct. This is an area that is difficult, I believe. You could run into an additional situation, Mr. Chairman, that is, that the taxing of capital gains on departure, deemed taxing, is an accrual form of tax. If the country to which the person changing his residence is going, taxes him on a cash basis, is he going to be caught twice and at two different times—once on the actual disposition and once on the deemed disposition here in Canada? We highlight and pinpoint all of these things.

The Chairman: On the tax credit you would pay less.

Senator Connolly: If you have a treaty.

Mr. Buchwald: If you have the right treaties and if they are appropriate. What is the situation if the treaty with the United Kingdom is one way and the treaty with the United States is a different way? The other party to the treaty has different considerations. This is of some considerable concern to us.

Hon. Mr. Phillips: Mr. Buchwald, we have dealt with that subject in the committee here and, under the senators' direction, with staff. The exemptions that are being

considered by way of suggestion are these: itinerant executives, to which you referred, who leave legitimately because of employment in another country; those prompted by ill health or necessitated by ill health, who are obliged to leave; and thirdly, a sort of blanket provision, that in other cases there is a right of application to the minister, where it is felt that the minister would be justified in granting the exemption. Can you think of any other headings?

It is not likely that the exit tax on deemed-to-be capital gains will be eliminated completely, nor does this committee want to support tax avoidance by people, or even tax deferral in cases where there is no legitimacy for leaving the country, having made a living here or even having benefited by the use of natural resources and building up significant capital. The thinking of some of us is that instead of asking for complete elimination—and it is not likely to be obtained—we would be better off asking for exemptions. Can you think of any exemptions other than executive itinerants, sick people, and applications to the minister?

Mr. Buchwald: I think I can add one to the list, if I can be so presumptuous.

Hon. Mr. Phillips: I want you to be, not presumptuous—you are never that—but to tell us.

Mr. Buchwald: Let me say this, Mr. Phillips. The Bar would, I think, 110 per cent endorse everything you said. There is no suggesting in anything we put forward that a person leaving Canada should not pay their capital gains commitment, and this is the only way to do it.

There will be problems, and I am concerned that they should be equitably resolved. I would respectfully submit that you could add to that list, with some profit, the elimination of the...

Hon. Mr. Phillips: Deemed to be?

Mr. Buchwald: ...the accrual versus cash situation, and the elimination of the taxation of all of the non-resident income for the purpose of taxing the capital gain.

In other words, the scheme of the legislation says that for this purpose the departing resident will be deemed to be a Canadian resident, which then means that his income from all sources, including the capital gains, will be taxed in that year.

The Chairman: And including his income from abroad?

Mr. Buchwald: Yes. That might be fair. I do not believe it is. Perhaps someone can make a case to bring in all of his income for purposes of arriving at a rate of deemed capital gains tax without taxing that other income. After all, the objective is only to tax the capital gains, earned in Canada, on departure; and to tax them then because you may not be able to reach them many years later when he ultimately actually disposes of them in some far-off location.

The Chairman: Yes, Mr. Buchwald, but right there, if a man is going to depart from this country, say in September of a year, then he is faced with this situation, that he has to account for his capital gains and, secondly, he has to make an income tax return; so he is going to be taxed on anything that qualifies as income in the year of leaving.

Senator Lang: Are there any averaging provisions applicable?

Mr. Poissant: On "ceasing to be". I guess not. The forward averaging does not apply.

Hon. Mr. Phillips: That is what I was thinking about.

Mr. Crawford: Mr. Chairman, there is this provision where you elect to defer the tax. If you defer, when you do realize the capital gain, you are deemed to be a resident at that time for purposes of the act. It was an oversight, and they really meant that it was intended only for purposes of setting the rate for capital gains tax. We were surprised that this oversight was not cleared up in the amendment.

Hon. Mr. Phillips: How would you deal with that now? The man is leaving and he does not come under any of the three headings I have mentioned. How would you tax him on the deemed capital gains?

Mr. Poissant: This is in the case of an election, that is, in the case of a man who elects to be taxed afterwards.

The Chairman: In order to get that, he has to put up security.

Hon. Mr. Phillips: Leave out the election. Let us say he is to be taxed.

Mr. Crawford: I am not sure I would add anything to the list. Mr. Phillips. I suppose the third item in your list is really a discretionary matter, in the application to the minister, where the minister thinks it is equitable.

Hon. Mr. Phillips: Yes.

Senator Connolly: The discussion so far has dealt with "itinerant executives". There may be people who do not belong to the executive class, who come here, benefit the economy because we use their skills and knowhow, and then go back to their own country, whether it be Europe, the United States or somewhere else. I would hope that people like that, with special skills that are brought here, would be entitled to the same exemptions as we are thinking of in connection with executives.

Hon. Mr. Phillips: Senator Connolly, it is a misnomer. I apologize for the use of the phrase "itinerant executives". I think we mean persons who move their place of employment. It may be an ordinary unskilled labourer, that he should have the same privilege if he is leaving the country. I speak of persons who leave the country legitimately for the purpose of taking employment elsewhere.

Mr. Buchwald: I think Senator Connolly's point is the one we are trying to get at, that you should not suffer a penalty for coming to work in Canada by having been

fortuitous enough to have been deemed to have made a capital gain.

The Chairman: This might become a privilege tax.

Hon. Mr. Phillips: Just coming to the point, those are the only three that we can think of at this stage. Unless you give us any more, because you are the body that would be competent to give them to us, we just have not come up with any more.

The Chairman: Mr. Crawford thinks that we have a good recital. Is that right?

Mr. Crawford: Yes.

Mr. Poissant: Mr. Buchwald, to take care of the non-resident who has elected to be taxed on disposal or when he has a capital gain in future years, would you be agreeable that the section could be amended to read that the income for this non-resident would be only his capital gain? We would be satisfied with that. We would be satisfied with the normal exemption even, I would say.

Mr. Buchwald: Yes.

Mr. Poissant: The normal deductions would be allowed, if he wanted to be a resident, but his income for the purpose of this capital gain would be taxed as if it were his only source of income for that year.

Mr. Buchwald: Yes.

Mr. Harris: Is it only half of the capital gain or is it all of it?

Mr. Poissant: It is the same treatment as if he were a resident. He is deemed to be a resident anyway. The only thing is that we have to make sure that the income on which he is going to be taxed would be only the capital gain.

Mr. Harris: The department might feel that that is an inappropriately low marginal rate of tax. The person might otherwise be very wealthy.

Mr. Crawford: Well, the other income was not earned in Canada.

The Chairman: You cannot make him a resident for the purposes of income tax after he has left the country physically and is attracting income tax wherever he re-establishes himself.

Mr. Crawford: As an alternative, if you carried the $2,500 exemption through to the election of the taxpayer, you might come up with an arbitrary percentage rather than trying to calculate it.

Hon. Mr. Phillips: We try to be more scientific than that.

Mr. Poissant: You are saying that the $5,000 will be deducted in his gain in a year of realization. You are suggesting that, Mr. Crawford, am I right? By that you mean to say that if he has a gain of $10,000, the first $5,000, even after he has left the country, will still not be taxable in that year. Then the rest would be taxable at half of that rate, as in the existing formula.

Mr. Crawford: Yes.

Senator Hays: Mr. Chairman, what would the situation be in the case of a resident moving from the United States into Canada? What would the American situation on capital gains be?

Mr. Poissant: There is no tax. There is no deemed realization when you leave the United States.

Senator Hays: If he sells his home, there is no tax?

Mr. Poissant: If he were to realize the gain then, yes, but there is no accrual gain at the time of leaving the United States, except if he were to sell his house on that day, in which case he would be taxed on the capital gain, of course.

Senator Connolly: What we are talking about here is deemed gains, and that would not be a deemed gain.

The Chairman: Senator Hays was asking what would happen in the reverse situation when the U.S. person changed his residence and came to Canada.

Mr. Poissant: As a matter of fact, if he retained his American citizenship, Mr. Chairman, he would be taxed twice. He could be taxed again.

The Chairman: In a limited way, yes. If he were to retain his American citizenship and came here to live with the expectation of some day going back to the United States, then he should certainly keep in touch with the American Department of Internal Revenue and file annual returns. In any event, he would be taxed only on certain parts of his income.

Senator Lang: For purposes of rates, should that departing person not be able to average backwards? In other words, if he has realized a capital gain on departure, shouldn't the rate applied to his total income, that is capital and normal income, be on an average rate?

The Chairman: You mean at his option?

Senator Lang: Yes.

The Chairman: He might not want to be compelled to do that.

Mr. Poissant: He would automatically be under the blocking average, because this is done automatically for five years. He will get that.

Senator Beaubien: Mr. Chairman, suppose there is a valuation date some time before the end of the year and then a gentleman at the beginning of next year sells everything he has at prices that are about what they were on valuation day and he then leaves the country. He has no tax to pay at all, has he?

The Chairman: He would not have incurred any capital gain.

Senator Beaubien: Then there would be no tax. He could take his money out, in other words.

The Chairman: Assuming that the prices would not have changed between valuation day and the time he left.

Senator Beaubien: That is what I mean. Ordinarily speaking, if there is no change, anybody leaving the country next year would pay no tax.

Mr. Buchwald: Mr. Chairman, there are just a couple of points on capital gains and then I will come to roll-overs.

At the bottom of page 10 of our brief we make the point that as a basic concept we object to capital gains being taxable where capital losses with respect to the same property are not deductible, even from gains from other like property. Accordingly, it is our view that if the capital loss on the disposition of personal-use property—other than listed personal property—is to be non-deductible, then the capital gains on such property should also not be taxable. We think that point should be underscored.

Another important point we have heard raised has to do with valuations. If the system is going to oblige people to have authoritative valuations prepared, we believe they should get the cost of those valuations as part of the cost of the asset above which any gain would be taxed. That point is mentioned in our brief.

Let me simply draw your attention to page 14 of the brief, Mr. Chairman. That deals with the apparent confusion with reference to section 53 (1) of the bill. If I may, I should just like to leave with you the illustration that is in the brief. Then on page 16 we raise our concerns about the proposal in the transitional provisions that there could be two valuation days designated. We hope that will not be necessary, because, obviously, if you have two days, you could have one day for the value of shares of a company and a second day for the value of the assets of that company at different times.

Senator Isnor: What is wrong with that?

Mr. Buchwald: It gives you an untrue value, senator, on your shares, if your assets have one value for gain purposes and then the underlying shares have a different value.

The Chairman: In other words, if the marketplace gives an inflated value.

Mr. Buchwald: Yes.

Mr. Poissant: Is there a conflict there, though, Mr. Buchwald? The first valuation you are referring to, really, would be only to the listed shares, and would not the listed shares be the market value of all the underlying assets?

Mr. Buchwald: No. I think they would be what they are trading at, which is not necessarily a break-up value.

Mr. Poissant: But are there not provisions for special cases where with a block of shares a different value might be taken than the value listed on that day. I know you need to have the valuation for the capital gains for the company or its equivalent, but the value of the shares, in my mind, will be the value and the sole value for the purpose of the shareholders. That is the only value you need really, because you are talking of two different entities; you are talking of the capital gain incurred by the company in the first place, and secondly the capital gain incurred by the shareholders. They are two different persons. So if they have two different dates, it makes no difference to my mind.

Mr. Crawford: That may be right, but there is a problem, mowever, if the valuation date is too far away from the start of the new system.

Mr. Poissant: Well, we do not worry too much about that; it will probably be December 31. I see there is a need for the distinction, but the capital gain is realized by two different persons, and therefore I do not see why there should be two dates.

Mr. Buchwald: Well, as long as you do not have inconsistency, that is fine. If they are in fact two different persons and if they have in fact two different aspirations—one is a speculator on a piece of paper and the other is an entrepreneur who is realizing on the turnover of capital assets. That is on the one hand the investing shareholder and on the other hand the managing operator of the business. That is all right as long as the aspirations of the two remain separate, but it is when they are the same you may have your contradictions. That is why the Bar raised this point.

The Chairman: Well, we will have a look at it.

Mr. Buchwald: Then very briefly, Mr. Chairman, we come to the question of roll-overs which are dealt with on page 68 of the brief. What is a roll-over but a deferred taxing of a capital gain to a more propitious time to pay that tax because the asset is really being replaced with another like asset for the same purpose? So if you do not tax it at this time, tax it at the end of the line when the ultimate disposition takes place. That theoretically is the theory of the roll-over. One of our main criticisms in our initial reaction to the bill is that it does not provide enough statutory sanctioned rol-overs, and we propose at the end of the first paragraph on page 68 what we think should be done. We say:

> But some effort should be made to provide for roll-overs where the facts show that inequities would otherwise exist. It may be impossible to draft satisfactory rules before January 1972. As an interim solution, we would recommend that the Minister be given a discretion to approve non-recognition of gains where there is a continuity of economic interest or where the only change is a change in the form of property holding.

Then, Mr. Chairman, we go on to say quite sincerely and quite respectfully—because it may seem to be rather presumptuous on our part—that:

> Perhaps a joint committee, including members of the Department of Finance, the Canadian Bar Association and the Canadian Institute of Chartered Accounts, should be struck to develop acceptable

> statutory standards for other situations than those presenty covered.

These we could not begin to catalogue when we were preparing this brief. Now we think we can draw upon the wide experience of a variety of different business situations being brought to our attention and to the attention of accountants day by day to catalogue this matter and we most respectfully commend it to you.

The next couple of pages of the brief deal with specific areas of concern in the roll-over situation that we ask you and we ask the Minister of Finance to take a look at.

Mr. Crawford: I have just one additional point on the roll-overs. Some people have said that the point is not too serious early on because your values will not have built up. There is however the problem that the roll-overs with respect to capita cost recapture are being removed from the act. In fact for a corporation with a fiscal year ending after December 31, or early in the new system, they have already been removed provided that the tax law becomes effective on January 1. That does cause an immediate problem.

Hon. Mr. Phillips: Are you considering that that should also be covered on an interim basis with ministerial discretion?

Mr. Crawford: Yes. The roll-over provisions for the most part in the bill now that actually do exist provide for roll-overs with respect to capital cost recapture as well as with respect to capital gains.

Hon. Mr. Phillips: The way I see this, Mr. Chairman—because we are dealing with a very important item and time is pressing us—is that you are directing yourself to capital gains, and that you are reconciled to deemed capital gain on death, but we have covered the subject matter on leaving Canada. On roll-overs you have a specific example at the bottom of page 10 and at the top of page 11 which speaks for itself. And then you are more or less in despair for the present and Mr. Crawford says that we may not have an immediate problem other than in relation to recapture so let us give the Minister discretion for the present.

Mr. Buchwald: On an interim basis.

Hon. Mr. Phillips: Yes, on an interim basis. Those are the highlights of what you are saying on capital gains.

Mr. Crawford: Mr. Harris is going to speak about corporations.

Hon. Mr. Phillips: Mr. Chairman, may I, with your approval, ask Mr. Harris that when he deals with corporation shareholders he deal with two items as major priorities that we are considering in this committee? The first is the question of consolidations which are referred to at the bottom of page 22 and on page 23 of your brief. Now I do not want to take you away from anything else you want to say, but I want to get the high spots. Then, secondly, I should like you to deal with the item at the bottom of page 21 where you say:

> Basically, it is hoped to clear out the 1971 undistributed income on hand and the 1971 capital surplus . . .

etcetera.

Under the heading of surpluses, has your committee given any consideration to the desirability of eliminating designated surpluses from the new bill and assimilating them or causing them to form part of undistributed earned income? And if you have not done so, are either you or your colleagues ready to express an opinion thereon? Then on the question of consolidations, are you still of the same opinion as reflected in page 22 of your brief?

Mr. Harris: I shall deal with the second question first, if I may. It seems to me that again you cannot have a real tax reform unless you get by the artificial boundaries that separate one corporation from another, and that because you are starting a new business in particular, although not combining the situations, you are suffering losses and there should be some way in which other corporations associated with the corporations suffering the loss can absorb that loss currently. We realize that there are some technical problems which the department would face in trying to allow consolidation, and this is a matter on which we referred to the United Kingdom subvention proposal. This is not given in great detail, but there are some suggestions.

Hon. Mr. Phillips: All right. Now would you go back to deal with the question of surplus referred to on page 21?

Mr. Harris: Yes, surplus on page 21. Let me deal with the designated surplus issue. The designated surplus issue, with which you are familiar, arose as an early approach to blocking dividend distributing, the conversion of what would have been taxable income of the capital gain. In the department's view, that danger still exists. We commenced our discussion on this point when he were talking about section 138A. The department is still of the opinion that the opportunity of converting what would be full rate taxed income into half rate taxed income is still going to be attractive enough and people are going to sell shares of corporations rather than collect the dividends in order to reduce the burden of tax on what is really undistributed income.

Hon. Mr. Phillips: May I interrupt you, sir? If you believe that the department is wrong and you press for the elimination of section 247(1), as Mr. Buchwald has dealt with, tax evasion, do you not logically come to the conclusion that you should be in favour of the elimination of designated surplus?

Senator Benidickson: Mr. Phillips, you say the department is wrong. What do you mean by that?

Hon. Mr. Phillips: You were not here earlier, Senator Benidickson, but the recommendation of the Canadian Bar Association that section 138, one of the subsections, which is now in section 247(1) need not be in the new act because of the introduction of the capital gains tax.

Senator Benidickson: My point is, is the department wrong?

Hon. Mr. Phillips: This section is not needed—perhaps that is a better expression. I do apologize. The department is never wrong; the section is not needed.

Mr. Harris: Mr. Phillips, I do not think that it necessarily follows that because section 247(1) is not needed, therefore designated surplus is not needed. Indeed, without section 247(1), perhaps we desperately need the designated surplus provision to maintain the integrity of our tax system. I am not saying that all the designated surplus provisions that are in the act are ideal; but I feel that the concept is probably needed if we should eliminate section 247(1).

The Chairman: Mr. Harris, if you leave the designated surplus provisions in, the way in which the new act deals with the whole question of capital gains and income tax, would be burden of carrying this section in the act be great on the taxpayer in situations other than where there is tax avoidance?

Mr. Harris: I would hope not, senator. We have had the concept of designated surplus in the tax system and we have learned to live with it. We do not always like it. But it is not as pervasive and not nearly as distorting to what might otherwise be a normal business transaction as is section 138A.

Mr. Crawford: What will happen, however, Mr. Harris, is that we are now moving forward into a new system and as time goes on new surpluses will build up, as it would seem they have, along with the assistance of the courts which effectively block any possibility of giving the new system surplus out other than at the effective rates for public corporations. You are going to have surplus built up over many years; and again pressures will come and they will be seeking new ways to get that surplus out at 15 per cent.

Mr. Harris: I do not say that we are entirely happy with the concepts. We would like an opportunity to go into it more fully.

Hon. Mr. Phillips: Could I press you a bit further? Is there some support among members of the Canadian Bar Association that designated surplus be eliminated—let us say, individual support?

The Chairman: Mr. Harris has indicated they would like some time to think about it.

Mr. Harris: I think we would appreciate some time.

Mr. Crawford: I might add to that point, as you know the Bar and the Institute have a joint committee; and it is our intention that as soon as this reform legislation becomes enacted this committee will become active and at that point it will be able to look at some of the problems in the legislation in more depth with the Department of Finance and the Department of National Revenue officials.

Hon. Mr. Phillips: I apologize for having interrupted.

Mr. Harris: That is quite all right. It leads me to the third point which I feel is quite urgent, that is the question of paying 15 per cent tax on existing undistributed income, thereby freeing the remainder, plus any capital surplus, for tax-free distribution after the beginning of 1972. This is a current problem. The intent is most commendable. It would at least permit the clearing up of existing surplus except for the pitfall of Part III, the tax under section 184. If there is a miscalculation of the undistributed income on hand, there is a penalty tax of 100 per cent.

The Chairman: You do not need to worry very much about that because, to the extent that we are able to influence the course of events, we find it difficult to justify that kind of penalty. There are, or may be, difficulties in determining exactly the amount of undistributed income. But if you should miss out by one cent, you have a 100 per cent penalty.

Mr. Harris: On the whole distribution.

Mr. Crawford: It is hard to imagine corporations of any size that do not face potential reassessment problems.

Mr. Harris: Prior to 1972.

The Chairman: That is right.

Hon. Mr. Phillips: I was wondering whether the Bar would support me in this, that instead of putting the blame on the taxpayer we put the blame on the accountants who compute the surplus. Perhaps that would solve the problem.

Mr. Buchwald: It is already on the accountants.

The Chairman: It is already on them, I am sure.

Mr. Harris: This is a serious problem because the philosophy of the act, I feel, is to encourage corporations, and particularly private corporations, to clear up old surplus. But if they have this axe hanging over their head, it will defeat this purpose. I can see the difficulty in amending the section. What will happen is that these amounts will paid out to the shareholders, many of whom are totally innocent, and they are going to be told that they are dividends out of the tax-paid undistributed surplus for 1971 as capital surplus, and they will be told how to treat it for tax purposes—as capital distribution. Subsequently it is determined that they should not be treated as capital distribution at all. Where does the department get the money? Does it go after the shareholder or the corporation? We have a policy decision to go after the corporation, but the tax penalty to the corporation is intolerable.

The Chairman: What would you think of a tolerance level, if the particular error is in excess of 25 per cent?

Mr. Harris: No, I would not think that the percentage of error should be the criteria, Mr. Chairman. I would suggest that the rate of penalty should be reduced.

Mr. Poissant: Why should it be reduced when the problem is in assessing the amounts? I prefer the chair-

man's suggestion, and there is a principle like this in the Income Tax Act regarding instalments. If the percentage of your calculated income of the present year is within the percentage of what would be the final income at the end of the year, if you are within a certain percentage you would have felt that you made a good estimate of your income for that year. There is a precedent here. Why do we not accept this? If the calculation is within 20 per cent of the estimate it is all right; if it is in excess of that it is a gross error.

Mr. Harris: With respect, I do not think the principle applies. Consider the case of a corporation which has been in existence only two years and has made modest profits. It has only $10,000 of what all would agree is undistributed income on hand at the end of its 1971 year. During that period it sold a very substantial piece of real estate on which it made a gain, because of a windfall, of $200,000. It has taken the attitude that it is a capital gain and four years later the department decides that it is taxable income. This completely overwhelms the undistributed income on hand. As a result of your suggested percentage criterion, they are ruined.

Their position should not be any worse than that of a large corporation with $1 million of undistributed income on hand engaging in this questionable transaction. I do not know on what basis a small corporation should be penalized more severely than a large one.

The Chairman: I do not think reducing the penalty is the cure; the argument for a reduction of the penalty is the degree of error.

Mr. Crawford: The percentage may be helpful but it is not the only solution. The problem of the calculation of the 1971 income remains.

The Chairman: You are faced now with whether this remains in its present form in the bill. You do not have time to study and examine in depth all the methods by which the problem should be met. Certainly a tolerance method by which there would be no penalty if the limit were complied with would be an easier and quicker way of drafting. Let the future take care of all the niceties of methods that should be used.

Mr. Crawford: The difficulty is that the future takes care of niceties sometimes by never changing them.

The Chairman: That is a well-known characteristic of taxing legislation.

Mr. Harris: The ideal would be to force the department to make its assessment quickly as to the amount of the actual undistributed income on hand, so that all parties are agreed on undistributed surplus before the tax is paid.

The Chairman: That is wishful thinking with regard to the period of time we are discussing.

Mr. Harris: One other point might be worth specifically mentioning. We are, of course, again in a huge amount of technical detail as to the definition of the private corporation and its right to distribute one-half of its capital gains tax-free to its shareholders under clause 83. This is a right that only the private corporation has. Therefore it can be a very valuable right. The definition of "private corporation" causes us some concern.

The Chairman: Is it not broad enough?

Mr. Harris: It may be discriminatory. For example, at the top of page 25 of our brief, beginning at the second line, we state:

> It appears that a Canadian subsidiary of a foreign public corporation could take advantage of section 83(2) while the Canadian subsidiary of a Canadian public corporation could not. In addition, the option is not available to public corporations which means that if Ford allows the public of Canada to participate in its Canadian operations it is penalized in capital dividend treatment as compared to G.M. which has a wholly-owned Canadian subsidiary, which is accorded the status of a private corporation.

In our view, this seems to be discriminatory.

Senator Isnor: Are there any private organizations such as that?

Mr. Harris: General Motors of Canada does not, as I understand it, allow public investment in its corporation. Investment can only be made in the parent corporation; therefore General Motors of Canada would qualify as a private corporation under this definition and could distribute its capital gains.

Mr. Buchwald: And Eaton's.

Mr. Harris: Yes; although we are considering a foreign corporation and Ford of Canada, by virtue of bringing in foreign investors, cannot do that.

The Chairman: We have noted it. Is there anything else?

Mr. Poissant: May I ask Mr. Harris another question now that we are endeavouring to solve the problem of the under-elected amount? Let us say we elected to pay on $100,000, and finally it is determined that it should have been $150,000. Instead of having to pay 100 per cent on the $50,000, why do we not allow a rate of 15 per cent and perhaps a somewhat greater rate than normal of interest?

Mr. Harris: If the corporation in your example had elected properly, in other words computed the surplus properly, they would have paid tax on only $100,000 instead of $150,000. The distribution to a shareholder that is treated as a distribution of capital should have been treated as a taxable dividend in the hands of the shareholder: the shareholder is receiving a benefit on his tax. That is the concern. The real question probably should be: What additional tax would the shareholder have paid if this amount were distributed as a taxable dividend?

Mr. Poissant: No, it was to be considered as undistributed income on hand, which normally could come out at 15 per cent. Let us apply 15 per cent to it, plus a rate of interest because it should have been paid in year one

and it is only caught by the department in year five. In that case should not the actual tax on the difference, plus a rate of interest of perhaps 10 or 15 per cent on the 15 per cent, be paid?

Mr. Harris: I think that is well worth considering.

The Chairman: We have noted it and will give it careful consideration.

Mr. Crawford, have you exhausted the panel? We are still waiting, if you have anything more to add?

Mr. Crawford: Mr. Buchwald will speak to the small business.

Mr. Buchwald: Mr. Chairman, this point is spoken to at pages 31 to 33 of the submission. We feel that the observation must be reiterated that the percentage appears to us to have been very, very grudgingly given and very carefully curtailed. Our main objection is that it is very complex for the average small businessman; it would create far more serious accounting problems.

The Chairman: We have already had that comment, Mr. Buchwald, as to the complexity that seems to be necessary in order to grant a benefit. Certainly, it is complex, but I think you can find your way through it. Is there something there that should not be there?

Mr. Buchwald: The first thing that we observed is that the benefit is really available only to incorporated companies and not to other forms of small business activities, partnerships, proprietorships, and so on. We think that is unfortunate.

We also think there could have been more generosity in allowing things like capital losses on assets used in the operation of a business, from disposition of assets used in the operation of a business, as opposed to portfolio assets or investment assets, allowing capital losses to be deducted to perpetuate small business incentives.

The Chairman: Portfolio losses are not deductible.

Mr. Buchwald: No. Losses from capital assets used in the operation of a small business that suffers a capital loss or moves to other premises cannot be used to reduce this accumulative deduction account.

The Chairman: Would not that depend on the source of the capital originally? We have had the opposite picture presented to us by credit unions, et cetera. They feel that since they must transfer a percentage of their earnings to a reserve by provincial and federal statute, they want the position that when you come to calculate the $400,000, even though the source of this reserve stemmed originally from earnings, it should not be an item for the build-up of the $400,000.

Mr. Buchwald: But they have a special situation.

The Chairman: What you are presenting to us is something in reverse of that.

Mr. Buchwald: I am thinking of a small business that is having difficulties, and its banker or adviser suggests that the business should be transferred to rented premises and the plant moved. The company disposes of its plant and equipment and suffers a loss.

Mr. Poissant: But they would get a terminal loss there.

Mr. Buchwald: Not necessarily.

Mr. Poissant: Oh yes. That becomes a deductible item. The only item that they would not get is loss on the land, which is not a depreciable asset. There is no such thing as capital loss on depreciable property. It is a terminal loss which is deductible from your income.

Mr. Buchwald: Is your transfer loss deductible from your business income?

Mr. Poissant: Yes. That would be a terminal loss deductible, and it would create an operating loss, if any, for that year, which is carried forward by the regular route.

Mr. Buchwald: The final point that we are concerned about is the refundable tax on ineligible investments, which can present cash-flow problems.

The attitude is that if you make an ineligible investment you should pay this tax. If you convert that ineligible investment into an eligible investment or distribute it, it appears that you might have to wait up to four years or longer to get a refund. If that was not the intent of the legislation, it should be clarified or it will present some cash-flow problems. It is an unnecessary hardship connected with the operation of a small business.

Hon. Mr. Phillips: Did you express in your brief to the minister your concern about small business relief not being granted to individuals and partnerships?

Mr. Buchwald: Yes, on page 31, in the middle paragraph.

Hon. Mr. Phillips: That is all I wanted to know.

The Chairman: Are there any further questions?

Mr. Crawford: There are other things that I would like to mention, but this could go on endlessly. We have not touched on international income, primarily because our submission on the White Paper dealt with the substantive issues involved.

The Chairman: We have had two excellent submissions, one from Massey-Ferguson and one from Alcan, which in my estimation, appear to cover the entire subject, from people who have actual knowledge and experience. From hearing them speak so knowledgeably, we feel that we obtained complete understanding of the subject. At least, we think we have. We have already been talking about our approach to it. Therefore, if there is anything that you wish to submit on international income, we shall be glad to hear it.

Mr. Crawford: We have recommendations in our submission. They are technical, and we will write you about the points that have been picked up in our amendments. We feel rather pleased that the minister has indicated

that some reconsideration is taking place with respect to foreign-source income.

You ask for priorities. Everybody has his own list of priorities, and I will give you mine. If you did it properly, you would have to measure them in terms of their impact. I would start with roll-overs and corporate re-organizations. Secondly, we have the international.

The Chairman: The only difference so far between your list and mine is that I would have the international first.

Mr. Crawford: Thirdly, I have the existing surplus problem. It is easily cured, but it is a serious problem. Mr. Harris has spoken about the excessive election problem. Fourthly, I have the tax discretion, the evasion right. Fifthly, I think the eligible capital property should be moved back to a capital cost basis.

The Chairman: I would say, without admitting anything, that three out of the five are on our list.

Mr. Crawford: I would have put roll-over and corporate re-organizations in consolidations or subvention payments in with them.

Mr. Poissant: The rule will be fair market value for any transaction between companies. Is there anything in your brief where a company would sell to its parent or sister company and incur a loss? Have you anything to say in that regard?

Mr. Buchwald: I believe we deal with it in our brief. I recall reading it last night. I hope there is a suggestion there. I believe it is also covered in our general introduction on the reciprocity problem, but it is also dealt with specifically in the brief.

Mr. Poissant: Thank you.

Senator Gelinas: Mr. Chairman, may I ask a short question? The answer should be short.

The Chairman: Senator Gelinas has a short question which he says should merit a short answer.

Senator Gelinas: In view of the complexities of the proposed legislation, has the association given any thought to recommending the establishment of a temporary tax review board where the taxpayer could have recourse if he felt he was unfairly assessed?

The Chairman: Really, an advisory board as to how they should proceed; not a board to determine their liability?

Senator Gelinas: An advisory board or tax review board to which the taxpayer could have recourse.

Mr. Buchwald: In the terms that you put the question, senator, the answer is "no". If you are talking about a tax review board, the legislation does contemplate such a board.

Senator Gelinas: A temporary tax review board.

Mr. Buchwald: There is a tax review board in the appeal system now.

Senator Gelinas: Yes, but I am speaking of a temporary tax review board specifically to look after questions and problems that would arise with this complex legislation.

Mr. Buchwald: Until this legislation can be tried, amended and worked out it will result in manifest inequity situations where persons are taxed when they feel they should not be taxed, and that is covered in our submission. We do not suggest that it should be done by a tax review board; we suggest, in effect, that the court should have the right to do it. We really have not thought in terms of an ombudsman.

The Chairman: Are there any other questions?

Thank you for your assistance, gentlemen.

Mr. Farris: Thank you, Mr. Chairman.

The Chairman: Honourable senators, we have two other submissions on our list. The second delegation, the Independent Petroleum Association of Canada, has been delayed in landing at the airport, so it will not be available until 2.15 p.m.

The submission by Simpsons-Sears is quite a short one; it is a simple point. Mr. Pickering is appearing on behalf of Simpsons-Sears.

Mr. Pickering, how long do you think your presentation will take? The point, as I know it, is quite a simple one.

Mr. Pickering: I have a written statement, Mr. Chairman, which would perhaps take seven or eight minutes to review. As you say, it boils down to one question. It would probably take 20 or 25 minutes.

The Chairman: On that basis, Mr. Pickering, I think it should be left until this afternoon.

Is it agreed that we resume at 2 o'clock?

Senator Beaubien: Once we have our quorum, we can start.

The Chairman: Then we will adjourn until 2 p.m.

The committee adjourned.

Upon resuming at 2 p.m.

The Chairman: Honourable senators, the first submission we have this afternoon is from Simpsons-Sears Limited. We have here: Mr. E. A. Pickering, the Vice-President, Simpsons-Sears Limited; and Mr. A. K. Hamilton, the Corporate Comptroller.

This submission concerns a deferred profit sharing plan and the effect Bill C-259 has on it. The other day we had Allstate here, whose problem was a profit sharing plan, where various elements in the plan were being taxed currently in each year. This is a deferred profit sharing plan, which involves some element of deferred tax.

Mr. Pickering, would you briefly tell us your problem?

Mr. E. A. Pickering, Vice-President, Simpsons-Sears Limited: Thank you, Mr. Chairman. After this morning's

very learned presentation and examination, I should point out at the outset that I am neither a lawyer nor a tax expert nor an accountant. I am a plain, simple layman, whose only reason for being here is that, like Mr. Hamilton, I have been actively involved in profit sharing in our company and in association with profit sharing industries for some 33 years. I have seen a number of tax treatments of profit sharing come and go.

If it is agreeable to you, Mr. Chairman, I think the simplest way of putting the whole picture before you, and in the end perhaps the most helpful in terms of brevity, would be to review the first few pages of this memorandum.

Since 1961 deferred profit sharing has operated under section 79C. Tax on the company's contribution, earnings on investments and on the capital gains in a member's account is paid by him at the time of withdrawal, usually at the time he retires or leaves the employ of the company, under the averaging provisions of section 36. There thus has in effect been a kind of capital gains tax on deferred profit sharing for some years. The amount of tax paid by deferred profit sharing members in our plan withdrawing balances under section 36 has been substantial, as you will see in a moment when we look at column 1 of the exhibit. In our own plan alone we have since 1962 withheld and transmitted $1,180,000 to National Revenue. With the disappearance of section 36, the Tax Reform Bill proposes to tax deferred profit sharing in either of two ways.

If the employee elects to use the lump sum which he receives on retirement to purchase an annuity, he will pay on the annuity income spread over the years in which it is received. Because income is usually lower after an employee retires, the amount of tax paid on the annuity income purchased by the withdrawal would, in the great majority of cases in our plan, be nominal, and indeed in a substantial portion of them it would be nil. This is indicated in column 2, and perhaps we might now look at the exhibit, which is the third-last sheet in the papers in front of you.

This is a group of some 10 or 12 actual cases in the membership of our fund. Employee A has been a member of the fund for 24 years. Her earnings in the last year she was employed were $5,125, so you see this is a lower paid employee. The market value of the profit sharing she took out when she retired was $20,981, part of which was tax-free, the taxable portion being $14,841. Column 1 shows the tax that has been paid by each of these typical example cases, or would be paid under section 36 as it now stands.

The Chairman: Of the present act?

Mr. Pickering: Of the present act. In column 2 we show what the tax would be if under the proposed tax reform bill the employee elected the option of buying an annuity and took the benefit, not as a lump sum, but as an annuity over 10 years.

As you can see, in the first four cases, with people on earnings of $7,000 and under there would be no tax. This is an estimate, prepared by Mr. Hamilton and our tax people, and reviewed with those in the Department of Finance, of the amount of tax that will be payable by the employee over and above other income. In the first four cases there would be no tax if the employee bought the annuity. In the fifth there would be only $280, as against $2,800 under section 36. When you get up to about $10,000 the payment would be $2,000 as against $3,200.

Suppose the employee elects to take the benefit in the form of a lump sum. The lump sum is the historic pattern in deferred profit sharing. If the employee says "I don't want an annuity; I want a lump sum", the entire amount, except his own contribution on which he has already paid tax, is taxed as ordinary income subject to the general averaging provisions. The amount of that tax is shown in column 3, and I think you will agree there is an inordinate tax penalty here. Indeed, we are almost certain that in practice the benefit would be taken by our employees, in all but the rare exceptional case, in the form of an annuity.

Senator Isnor: You say he has already paid the tax on his own portion?

Mr. Pickering: Yes.

Senator Isnor: Does that apply to approved schemes?

Mr. Pickering: Yes.

Mr. A. K. Hamilton, Corporate Comptroller, Simpsons-Sears Limited: The employee's deposit is not deductible from income.

Mr. Pickering: Unlike a pension plan, where the employee puts money in and what he puts in he pays no tax on, it is deductible from income. In the case of a profit-sharing plan, that privilege does not exist; the employee has to pay the tax on it, and then he puts into the fund.

Senator Isnor: I just wanted to be clear on that point.

Mr. Pickering: We say here that the crux of the whole matter is that the availability of a lump sum on retirement is really the prime feature of deferred profit sharing. If you take that away by law or by effect, you destroy the fundamental dynamic motivating force of deferred profit sharing. In our case it has had a very long and honourable history. The taking of a lump sum on retirement has been the practice in the plans of Simpsons and Simpsons-Sears for over 50 years, and over 99 per cent of the employees who have retired in our two companies have elected to take a lump sum rather than an annuity.

Senator Beaubien: Do you say 99 per cent?

Mr. Hamilton: Yes.

Mr. Pickering: I make this next statement on my own responsibility as an officer of the company, and out of my own personal knowledge of what has happened in our company and in Simpsons. The lump sum has helped thousands of employees plan and finance their retirement. There is usually some annuity income, social

security, we have a supplementary pension plan. The lump sum is something that enables the employee to pay off the mortgage on the house, to set up a contingency reserve; some have bought a little business; most people want to have a farm or a cottage, and many people have acquired a summer cottage and winterized it so that they have a place to live in when they retire. In no case in our experience in the two companies has the lump sum ever been prodigally spent or the employee become needy. Now, if the tax law in effect makes it impossible for the employee to benefit from the lump sum provision, it removes the basic reason for having a deferred profit-sharing plan at all. If retirement security, because of the inordinate penalty on the lump sum, must take the form of an annuity, it will be simpler and more favourable to operate a pension plan, particularly since the payout under the pension format gives the employee the major advantage of deducting his own contribution from the taxable income during the years of his employment.

This next part is frightfully important to an appreciation of how deeply distressed and concerned we are, along with our employees, at the implications of the bill. In many deferred profit-sharing plans there is an additional feature. The trustees allocate to members of the fund shares of the company in accordance with their participation and in accordance with the growth of their accounts. This makes the employee a shareholder of the company; and more than that, it makes him a working partner in the enterprise in a way he has never been before. A little under one million shares of Simpsons-Sears stock is actually assigned and allocated to members of our profit-sharing fund.

The Chairman: To the employees?

Mr. Pickering: Yes, this is about 6 per cent of the outstanding shares, and 38 per cent of all the assets of our two funds are invested in the common stock of the parent company.

Senator Connolly: How long has this been going on, Mr. Pickering?

Mr. Pickering: The allocation of shares?

Senator Connolly: Yes.

Mr. Pickering: This started when we got deferment in 1962, for reasons which I could go into. It was impossible to do it before this because our people could not afford to pay the tax on the accumulation. In our plan, no one earning more than $10,000 can take out additional profit-sharing during their period of service. This same principle applies to people earning less than this amount. So someone on low income can get a very big accumulation under our fund. The largest withdrawal ever made was $55,000 by a girl who never earned more than $100 a week. We had to get out of this tax arrangement because these people could not find the money to pay the tax year by year; so we asked for a deferment and we got it under section 36.

Now when employees retire they can take the shares with them, and a great majority of them elect to do so. They do this, first of all, because they know the company, they have worked for it for years, and they have identified with it while they were working and want to remain identified with it. They want to share in what they think will be the continuing growth of the firm. Furthermore, the shares are a hedge against inflation, or at least we think so. And for these reasons they elect to take the lump sum in the form of shares. There is no point in going through the entire procedure of doing this. If the employee cannot in fact take possession of these shares, he must take the equivalent in cash in order to buy an annuity to get this favourable tax treatment. The thing we have been stressing, and which we stressed with the department, is that it would be a tragedy, and we feel an unnecessary tragedy, if the introduction of tax reform in Canada should have the unnecessary effect of destroying the deferred profit-sharing plan. We feel that our problem, and to some extent, the problem of other deferred plans, could be solved if the Government would apply to deferred profit sharing the basic principle of its own tax reform bill. We have proposed to the minister that the amount taken by the employee when he retires, which is represented by the company's contribution of the earnings in the fund, be treated as ordinary income added to other income in the year in which the employee retires and taxed as income subject to the general averaging provisions. We recommend that the realized capital gain from that withdrawal be included in income at 50 per cent rather than 100 per cent.

Hon. Mr. Phillips: Are you talking about realized capital gains in the accretion in value of shares or the dollar increase over and above the contributions that were made? I am not clear on what you mean by capital gains at the time of the deferred profit-sharing plan coming into effect.

Mr. Hamilton: The two sources of funds going into a deferred profit-sharing plan are the customers' contribution and the company's contribution. These funds are invested. As I have said earlier, in our case about 40 per cent is invested in the shares of the company and they are allocated and assigned to the members in accordance with their participation in the plan. Then there are earnings from the investment. What we are saying is that the company's contribution and the earnings on the investment should be taxed as income.

Hon. Mr. Phillips: When the person withdraws?

Mr. Hamilton: When the person withdraws.

Hon. Mr. Phillips: Are you suggesting a situation where you are dealing only with securities that have increased in value over and above their cost?

The Chairman: Not so far as he has gone.

Mr. Hamilton: Perhaps I could qualify this. The member's account is divided into two sections, in effect. One section is represented by cash and general investment in the fund, that is, investment other than company shares. Those investments are revalued each year from time to time; and a portion of the appreciation in the capital value of those investments is credited to the member's

account, and when he withdraws the shares of these general investments they are revalued at the time of his withdrawal. And he gets his share of the appreciation of capital gain on those investments in cash.

Hon. Mr. Phillips: In dollars.

Mr. Hamilton: So, in effect, that is realized gain to him.

The Chairman: It is realized gain at a time when there is no such thing as capital gains tax.

Mr. Hamilton: Yes, that is right. It has been taxed in the past, even though it was a capital gain.

The Chairman: That was part of your agreement when section 36 was brought in.

Mr. Hamilton: Yes, it was part of the price we paid for the deferment.

The Chairman: Yes, there will be tax at the marginal income rate on the company's contribution, and you get the benefit of the averaging under section 36. You would also include in income the realized gain that has accumulated in the trust fund.

Mr. Hamilton: They may not have been realized by the trust because the trust has not sold its securities. But they are actually realized in cash by the member when he withdraws because he is paid in cash for his share.

The Chairman: Each year some part of that would be allocated to each member and that portion would be subject to deferred tax payment, income tax payment.

Mr. Hamilton: Yes, that is correct. In addition to that, each year the fund purchases a certain number of company shares, most of which have been purchased from the treasury, at the market value at the time. Then at the end of each year, based on a formula, the shares acquired by the fund during the year are allocated to the members. These are the shares that the member can withdraw in kind rather than in cash.

Hon. Mr. Phillips: So you want a roll-over on these shares?

Mr. Pickering: That is it exactly.

Mr. Hamilton: We are asking for a roll-over on that part. Under the present law those shares are valued at market value when he withdraws. But he pays tax on the whole capital gain included in that, but under section 36.

The Chairman: And he pays it at the marginal rate governed by what the averaging process produces.

Mr. Hamilton: That is right. However, I think that now we have a whole new ball game; we have a capital gains tax which we never had before, so we do not really see any reason why this unrealized capital gain, which is in the value of the shares which he takes out or withdraws, cannot be treated as a capital gain and taxed when realized.

The Chairman: Well, let us take it by stages, Mr. Hamilton. We know now the various elements in the fund and Bill C-259 would start to operate on January 1, and you have different elements in there. There has been accumulated up to that time the company's contribution and tax has been deferred on that. Now you draw a line there. What are you suggesting with respect to the company contributions up to the beginning of the new law, and how are you suggesting that it should be treated?

Mr. Hamilton: Well, Bill C-259 provides that, at the election of the employee, amounts that he could have withdrawn which were cumulative as of January 1, 1972 can still be taxed, in effect, under section 36.

The Chairman: But my question was not concerned with what the bill does. The bill would preserve that deferred tax as being a liability of the employee. Is that not right?

Mr. Hamilton: Yes.

The Chairman: So what I am asking you is this: What do you propose in order to get away from that? The employer's contribution in the fund has gone in there over the years.

Mr. Hamilton: Well, with respect to the accumulation to December 31, 1971, I think the bill is satisfactory.

The Chairman: But then with the incidence of tax the amount may be very substantial. Are you going to assume that every employee withdraws from the plan?

Mr. Hamilton: That is the fact now under the present act.

Mr. Poissant: Yes, because of section 36. What you were saying was that you get the relieving provision here. But now you are saying that in the absence of an equivalent to section 36 your employee will be penalized, and you would like a formula which will in fact take into account what he would have been taxed previous to section 36.

Mr. Hamilton: We are talking about future accumulations after December 31.

The Chairman: Let us not jump ahead. I am still staying with the first law, and I want you to tell us about when you come to January 1, 1972. We know what the bill does in relation to the accumulation of employers' contributions it preserves the taxation of them.

Mr. Hamilton: Partially only.

The Chairman: Partially only, yes. But in relation to those you get the benefit of averaging under section 36.

Mr. Hamilton: No, the bill provides that an employee who withdraws from a deferred plan up to the end of 1973 can withdraw the full amount, in effect, under section 36 of the present act. If he withdraws subsequent to December 31, 1973—and this is section 40 of the transitional provisions—he can still make an election to be taxed, in effect, under section 36, but the amount on which he can elect is restricted to the amount that he could have withdrawn had he in effect withdrawn on January 1, 1972.

The Chairman: They are dividing the accumulation in two and they are saying that any part of that accumulation that he might have taken out if he had retired on December 31, 1971 is an amount that he can pay tax on and get the benefit of averaging under section 36.

Mr. Hamilton: In other words, they are not making the bill retroactive in that respect.

The Chairman: No. And you are prepared to accept that.

Mr. Hamilton: That is something we can accept. However, the bill goes further, and in section 88 of the transitional provisions it says that if the employee makes any election under section 40, then general averaging and forward income averaging does not apply to any other income of that year. So, in effect, if the employee does not withdraw until 1980, he can elect on his accumulations to December 31, 1971 to have section 36 apply. But then he is denied any averaging on his subsequent accumulations from January 1, 1972 until 1980, when in fact he withdraws, and he will be taxed on that portion as ordinary income when he withdraws.

The Chairman: That will not be annually; it will be when he withdraws?

Mr. Hamilton: Yes. So that this, in effect, could result in such substantial tax on subsequent accumulations under the new act as to make it impossible for him to elect under section 36. Section 38(2) denies general averaging and forward income averaging if any election is made under section 40. So what I am saying is that the denial of section 38(2) really denies to the employee who withdraws, say, in 1980 the application of section 36 to his accumulations prior to the introduction of the bill, and in that way it is retroactive.

Mr. Pickering: Mr. Chairman, could I suggest that, leaving aside the transitional provisions, what we are interested in as to the future treatment of withdrawals is that the company's contributions and the earnings of the fund would be treated as ordinary income? Any realized capital gains withdrawn would be included in income at 50 per cent rather than at 100 per cent, and that the unrealized capital gains on securities withdrawn or taken in kind would be rolled over and taxed as capital gains at the time the gains are realized. Along with this we would recommend that the option remain of taking out an annuity, so that the employee would have the choice of taking the benefit as a pension or as a lump sum. We believe that this proposal is generally consistent with the application of the capital gains tax in other situations. Capital gains of trusts in general are taxed in the hands of a beneficiary as capital gains when realized by the trust. Any gain on trust assets transferred in kind to the beneficiary of an ordinary trust is deferred until the beneficiary realizes that gain.

What we are asking is that the rules applicable to trusts in general be applied in the case of deferred profit-sharing plans.

The Chairman: Could you pause there for a moment, Mr. Pickering?

Mr. Pickering: Yes.

The Chairman: That is really the point of difference. You are ready to accept the treatment proposed in the bill in relation to the portion of the accumulated contributions by the employer as at December 31, 1971. You are prepared to accept that amount on the basis that the employee had withdrawn on that day, and you are prepared to accept what the bill says; that is, that you get the benefit of the averaging under section 36 and you pay income tax.

Mr. Pickering: I am glad that I said at the outset that I am not a tax lawyer, because I am not sure. We are certainly prepared to accept the future treatment.

Mr. Hamilton: I believe what the chairman says is correct. We would be prepared to accept it, with the qualification that the limitation in section 38(2) of the transitional rules is, we feel, unfair in that it denies section 36 retroactively, in effet, to an employee who withdraws at any time after December 31.

The Chairman: Let us put it this way: You have the accumulation of the employee's contributions and so you draw a line at December 31 , 1971, and that is one accumulation; you arrive at a total amount as though the employee had retired and withdrawn on that date. The bill deals with a way of taxing that and it does give you the benefit of section 36 and the averaging provisions.

Mr. Hamilton: Correct.

The Chairman: But the employee has not actually withdrawn and the employee's contributions continue to come in. There may be a balance left in the accumulation of the employee's contributions in the calculation that you make at that date, but he does not retire until 1980. Under the new bill that is an entirely new ball game, is it not? The whole accumulation is shared in that accumulation, and whatever balance, if any, that is left after you do your arithmetic for December 31, 1971, and for the accumulation right down to the date he actually withdraws, is subject to income tax at the marginal rate, and you do not get the benefit of section 36 of the present act. Is that right?

Mr. Hamilton: Yes, including capital gains at 100 per cent.

The Chairman: Yes.

Mr. Hamilton: Realized or unrealized.

The Chairman: Yes, and included in it would be capital gains that the fund may have made during that period, and it would be taxed at income rates.

Mr. Hamilton: Yes.

Senator Connolly: When does the tax on the first accumulation become exigible under the new bill? Does it become exigible on January 1, 1972?

The Chairman: That is right.

Mr. Hamilton: No, only when the employee withdraws.

The Chairman: I think your question has been misunderstood.

Mr. Hamilton: When is it payable?

The Chairman: Yes.

Mr. Hamilton: When the employee actually retires.

Senator Connolly: In other words, in the year of his retirement he is going to have a very complicated return. He is going to have to figure his taxable income from the fund to the January 1, 1972 with the provisions of the act as the act now exists. He is going to have to make a calculation of tax owing.

Mr. Hamilton: That is not quite correct. Section 36 disappears from the bill. The taxing section levies a tax in a similar way to section 36, but it is no longer section 36. For example, if he retired in 1980 the three years average would be the years 1977, 1978, and 1979.

Hon. Mr. Phillips: We are here to find out what relief you want, as opposed to an analysis of the new bill. What relief do you want? Do I understand that when an employee receives his share of the deferred profit-sharing plan, to the extent that the portion received consists of shares of the company that employed him, he would not be taxed but he gets the benefit of a roll-over until he sells the shares?

Mr. Pickering: Right.

Hon. Mr. Phillips: Is that not the basic point you are asking?

Mr. Pickering: Yes, and one other point.

Hon. Mr. Phillips: Suppose he were to receive shares in companies other than those of your company? Are you asking for the roll-over on those shares as well?

Mr. Pickering: Yes.

Hon. Mr. Phillips: So what you are saying is that to the extent that he receives securities of companies, the capital gains tax be deferred until he realizes on those shares. Is that it?

The Chairman: Yes, and it would follow the ordinary rules in relation to the assessment of capital gains.

Mr. Hamilton: And that they be taxed at the rate of 50 per cent.

The Chairman: That is the capital gains rate.

Hon. Mr. Phillips: That would follow.

Mr. Pickering: If the capital gain is realized, he will add that to his income.

Hon. Mr. Phillips: He will pay that at the time of realization.

Mr. Pickering: Yes, and if the capital gain is not realized then it will be rolled over.

Hon. Mr. Phillips: I know that. At what cost does he get those shares from the point of view of the roll-over?

Mr. Pickering: In our proposal to the department we proposed that it be at the cost at which it was acquired by the trust which, hopefully, will be lower than the cost on Vday and, therefore, that would create a larger capital gains eventually, but we felt this was the fair and proper way of putting this proposal forward.

The Chairman: That only leaves the other situation, and I am not sure that Mr. Hamilton has given us an assessment of it.

Mr. Poissant: Mr. Chairman, may I clarify something?

The Chairman: Yes.

Mr. Poissant: We should divide the problems into two areas. You are satisfied with the situation prior to 1971, are you?

Mr. Hamilton: Yes.

Mr. Poissant: Your problem is from 1972 on respecting the portion of capital gains that would be accredited to that separate pool you were telling us about?

Hon. Mr. Phillips: No. As I understand it, Mr. Chairman, as at the end of 1971, if it includes securities then those securities should be subject to roll-over.

Mr. Poissant: In 1971 they can elect on this so they are not too worried about it. The taxpayer has the right to deem that amount out of the fund.

Am I right?

Mr. Hamilton: Yes.

Mr. Poissant: And you are satisfied with that treatment?

Mr. Hamilton: Yes.

Mr. Poissant: What you are interested in is the accumulation after that period, and you say you do not have the equivalent to section 36, or the transitional provisions for that, and because of section 38(2) you would not be able to have the averaging provisions apply.

Let us say the roll-over has solved part of the problem and let us say there would not be a roll-over and there would be a capital gain in 1980 for that portion accrued from 1971 on. Are you telling us there will be no averaging provision available for that taxpayer for that period?

Mr. Hamilton: If the employee has elected in respect of the accumulation to December 31, 1971.

Mr. Poissant: He does not get a second averaging provision for the years 1972-80?

Mr. Hamilton: Right.

The Chairman: Which averaging are you talking about?

Mr. Poissant: The forward averaging.

Mr. Pickering: He certainly does not get that.

The Chairman: In other words, to identify it, he does not get the benefit of averaging under the bill.

Mr. Poissant: Once he gets it, when the system starts he no longer has the right. In other words, I am just suggesting at this time that perhaps he should be permitted to make an election again, figure out the tax and maybe deduct the previous accumulation as of December, 1971. Would that be agreeable? That is, if there is no roll-over again. The roll-over would reduce the impact of taxation drastically. Is that right on the roll-over?

Mr. Hamilton: Oh yes.

Mr. Poissant: It will reduce it drastically, so we do not have to worry so much about that, if there is a roll-over.

Mr. Hamilton: If there is a roll-over, we are not concerned.

Mr. Poissant: Assume he does not get a roll-over, and in 1980 he withdraws from the plan; he has made an election as of 1971, but then there were other accumulations for, let us say, 10 years. Because he has already made an election, he is forbidden to make another one at the end of 1980. Is that right?

Mr. Hamilton: He does not in fact make any election until 1980, when he withdraws.

Mr. Poissant: But he would not be able to make one, because the act says that if you have made one previously you cannot make one again. Is that what you say?

Mr. Pickering: It is the transitional features that make the problem complex. Perhaps we could go back to the table of comparisons.

Hon. Mr. Phillips: We have another applicant here, and time is getting to be of the essence. I really would like to crystallize it, or shall I say "coagulate" it, in some form, because we must give time to others and I am watching the clock.

The Chairman: Can you just tell us what it is you want?

Hon. Mr. Phillips: I understand the roll-over provision in respect of securities, and you have indicated at what price you want to cost it. You have stated that it is the only thing you wish. We have been told there is something more you want; you want some form of averaging provision as well.

Mr. Hamilton: No.

Hon. Mr. Phillips: You do not?

Mr. Hamilton: We do not.

Hon. Mr. Phillips: Do you want anything other than roll-over in respect of securities that the employee receives at the cost you have indicated? Is there anything more that you wish?

The Chairman: There must be.

Mr. Poissant: There is the reference to that 50 per cent.

Hon. Mr. Phillips: I would rather the witnesses answered.

Mr. Pickering: What we are asking for is that the realized capital gains in the amount withdrawn be taxed as a capital gain; that the unrealized capital gain in the amount withdrawn be rolled-over and taxed eventually as a capital gain; and that anything else be put into income at the time of withdrawal and taxed under the general averaging provisions.

Hon. Mr. Phillips: I do not seem to get beyond a request of the roll-over in respect of securities acquired by the employee at the time of withdrawal. Is there any other request?

Mr. Pickering: As the bill stands, the realized capital gain which would be transmitted to the employee at the time he withdraws would be put into income at 100 per cent. We are asking that it be treated as a capital gain and put into income at 50 per cent. There are the two major things.

Hon. Mr. Phillips: Then there is more than one.

Mr. Pickering: Yes, right.

Hon. Mr. Phillips: Where do we find that, on what page?

Mr. Pickering: Perhaps you would look at page 4, the first full paragraph:

> We have proposed that the part of the withdrawal represented by the company's contribution and earnings of the fund be treated as ordinary income and taxed subject to the general averaging provisions; that the realized capital gains be included in income at 50 per cent rather than 100 per cent; and that the unrealized capital gains on securities withdrawn and taken in kind be rolled-over and taxed as capital gains at the time the gains are realized.

Hon. Mr. Phillips: Would there ever be a question that the realized capital gains be included in income at more than 50 per cent?

Mr. Pickering: Yes, the present bill says 100 per cent.

The Chairman: The bill says 100 per cent.

Hon. Mr. Phillips: So that is the crucial point.

Mr. Pickering: It is making the tax under Bill C-259 prohibitive, as these tables show.

Hon. Mr. Phillips: So the two points you wish are found in that paragraph on page 4?

Mr. Pickering: Right.

Hon. Mr. Phillips: As far as I am concerned, that is it.

The Chairman: There is one additional point. They want to preserve the right to be able to take the annuity course if the employee wants it.

Hon. Mr. Phillips: That is assumed.

Mr. Pickering: I would add one other thing...

Hon. Mr. Phillips: May I, at the risk of being repetitious, say that the key to the point, that I certainly did not get, and which perhaps some honourable senators did not get, is that the realized capital gain at the time the employee gets it is now to be taxed at the full rate rather than at the capital gains rate.

Mr. Pickering: That is right.

Hon. Mr. Phillips: Now we have it.

Mr. Pickering: I think there is a subsidiary matter, in which Mr. Hamilton has been involved, and that is that the so-called transitional provisions do not solve the problem in its entirety. It is rather a technical matter and I personally do not want to get into that, but we have attached to these papers a statement of what the problem is. It is on the last page, which is not numbered.

The Chairman: Mr. Pickering, what I would like to know is this. When you talk about general averaging provisions on page 4, what general averaging provisions are you talking about? Are you talking about the ones dealt with in section 36?

Mr. Hamilton: No.

The Chairman: Or the ones that are available under this bill?

Mr. Pickering: Under this bill.

Mr. Hamilton: Under this bill yes. What in effect we are saying is that it does not seem fair that in order to maintain section 36 for accumulations prior to the introduction of this bill the employee has to give up his right to general averaging under the new bill for all future accumulations.

The Chairman: You mean he is being made a second-class citizen?

Mr. Hamilton: Yes.

Hon. Mr. Phillips: So we have three points now.

Mr. Hamilton: He gives it up not only in respect of future accumulations under profit sharing, but all other income that he may have on the early withdrawal.

The Chairman: I think we have an understanding of it now, and of what you want. We have the material here. I do not think we need any additional reasons in support of what you are asking. We understand the why and the wherefore.

Mr. Poissant: Mr. Chairman, would you permit me a question?

The Chairman: Go ahead.

Mr. Poissant: You said the roll-over should be transferred at the cost that it was transferred to the trust.

Mr. Pickering: Yes, that is right.

Mr. Poissant: What will happen? The share will be valued at V day. Should not they be transferred either at the cost to the trust or the fair market value on V day? You will take the benefit of the appreciation as of V day.

Mr. Pickering: If we had proposed that it be valued at market value on V day, presumably that would be higher than cost, and therefore eventually the capital gain would be less. We felt that valuing them at cost was a reasonable...

The Chairman: Do not be generous. This is a right which you have. Do not be generous and give away a right which you enjoy under the bill. That is the purpose of the valuation day, you can select either your cost or the value on that day.

Mr. Pickering: I think we would be very happy...

Hon. Mr. Phillips: Whichever is higher.

The Chairman: Do we have the point you are making?

Senator Isnor: I am not clear on that point, Mr. Chairman. Mr. Pickering, you pay by the week?

Mr. Hamilton: I am sorry, every two weeks.

Senator Isnor: Every two weeks. Was this pension plan approved by any particular body?

Mr. Hamilton: It is accepted, or rather, it is registered as a deferred plan.

Senator Isnor: As a deferred plan. Do you charge up your shares to the pension plan? Do you charge up in your salary total on each pay day the amount paid up?

Mr. Hamilton: We make a deduction each pay day from the employee.

Senator Isnor: I asked if you charged up the full amount each pay day.

Mr. Hamilton: To expenses do you mean?

Senator Isnor: To expenses.

Mr. Hamilton: Yes, we do.

Senator Isnor: Then you are getting credit from the Government on your income tax return for an amount larger than what you...

The Chairman: No.

Senator Isnor: Just a minute.

The Chairman: You can wrestle with the answer afterwards. I have a number of different answers.

Mr. Hamilton: I think what you are saying is that the company is getting a greater deduction than the amount of money the employee receives.

Senator Isnor: I just want to make sure.

Mr. Hamilton: The employee is not permitted to deduct this from his income. So while the company is claiming this as an expense, the employee is paying tax on it.

Mr. Poissant: So the average tax is not less.

The Chairman: No.

Senator Isnor: You do charge up the full amount of that man's salary?

Mr. Hamilton: Yes.

Senator Isnor: And notwithstanding that, you want a rebate at the end of the year for pension purposes?

The Chairman: No.

Senator Isnor: Who is saying no?

The Chairman: I said no. If this is a private conversation between the two of you across the table, Senator Isnor...

Senator Isnor: I want the witness to answer the question. He has an approved pension plan and charges up the full salary of the employee over the year.

Mr. Hamilton: It is not a pension plan.

Senator Isnor: It is not a pension plan?

Mr. Pickering: No, it is a deferred profit sharing plan.

Mr. Hamilton: I think that the distinction, senator, is in the registered pension plan where the employee gets a deduction from taxable income of his contribution to the plan as he comes into the plan. He does not pay tax on it. Under the profit-sharing plan he does not get the deduction. He pays tax each year as he goes along.

The Chairman: Under this deferred profit-sharing plan, the employee has to pay his own marginal rate of tax on what he contributes. That is the difference. With respect to contributions to a pension plan he gets a deduction up to a certain limit for the amount that he pays in each year. This is one of the restrictions on obtaining a qualification for this type of plan. They pay a tax on their own contribution.

Mr. Hamilton: I wonder if this would be helpful. While the company makes a deduction from the employee, nevertheless, it pays out the gross amount of the salary. It pays so much to the employee; and the amount which is deducted it pays to the credit of the employee in the plan.

Senator Connolly: That is vested in the trustee of the plan.

The Chairman: That is right.

Mr. Hamilton: So the company is paying out as an expense everything it is being allowed. And the employee is either receiving all of it in cash, or getting credit for the part which he does not receive.

The Chairman: Are there any other questions, Senator Isnor? As soon as you are through we want to hear the next group—but not until you are through.

Senator Isnor: Then you are seeking benefits two ways, are you; first, by charging up the full amount of the salary, and later on...

The Chairman: I do not know what you are talking about. What is this reference to charging up the full amount of the salary?

Mr. Hamilton: I do not know either. It is an expense to the company.

The Chairman: The company pays the salary of the workmen. The company makes a contribution to the plan. The employees in the plan pay at the ordinary income tax rate on the company's contribution.

Senator Hays: Which contribution they receive.

The Chairman: Yes, and because they receive it, they pay income tax on it like any other income they receive. Is there anything more, Senator Isnor?

Senator Isnor: No.

The Chairman: Thank you very much, sir.

The Chairman: We come now to our last hearing for today. These gentlemen were delayed in landing by the fog this morning. I can tell them that during the morning there was no fog here, but, we had a very good discussion. We have before us the Independent Petroleum Association of Canada, represented by Mr. A. Ross, President of Western Decalta, and Mr. G. W. Cameron, the General Manager of the Independent Petroleum Association of Canada.

I should tell you that when we conclude this hearing today we will adjourn until Wednesday, October 27, at 9.30 in the morning. At the present time we have four appointments on that day; and on Thursday, October 28, we have an additional four appointments. So we have a lot of work to do.

Who is going to make the opening statement?

Mr. A. Ross, President, Independent Petroleum Association of Canada: I will make the opening statement.

The Chairman: At some point a little later on the chairman has other obligations that he must deal with, and is going to vacate the Chair in favour of Senator Connolly, who has been kind enough to agree to take over. I hope the committee will accept that.

Hon. Senators: Agreed.

The Chairman: Go ahead, Mr. Ross.

Mr. Ross: Gentlemen, we wish to thank you very much for continuing this hearing this afternoon and for allowing us to appear before you. There may have been no fog on the ground, but I can assure you there was fog up in the air because we were up there for about two and a half hours waiting to land.

At this time I would like to introduce Mr. D. A. McGregor, a partner with Clarkson, Gordon & Company in Calgary.

In so far as our submission is concerned, the general remarks are pretty straightforward. We will deal at this point with probably the most important section regarding depletion. Our Association feels now, as it felt when we

appeared before the house committee on a prior date that goss depletion is much more acceptable to the industry and to the investing community. We recognize that neither your committee nor the house went along with our recommendation. However, we would like to suggest this to you. On the other hand, in the event that we are going to end up with earned depletion as proposed in the new bill we would like to see the base of the earned depletion broadened. We believe that all land cost should earn depletion.

The Chairman: On what page is that set out in your brief?

Mr. Ross: On page 2.

Hon. Mr. Phillips: It is in the third paragraph.

Mr. Ross: Failing the acceptance of the "gross depletion" concept, our association recommends that all "Canadian exploration and development expenses" as defined in section 66(15)(b) of Bill C-259 should be included in determining the earned depletion base. To avoid any abuse in the sale of properties between companies, it is suggested that the income from such sales by each taxpayer should be credited to "Canadian exploration and development expenses" and thus the total earned depletion base is unchanged. We also recommend that tangible equipment such as wellhead equipment and tubular goods for productive wells, battery equipment, processing plant costs and other equipment necessary to recover hydrocarbons be included in the earned depletion base. This is similar to what has been allowed to the mining industry.

The Chairman: Do you mean in the bill?

Mr. Ross: In the bill, yes. We also believe that it is inequitable that depletion on future production income from producing properties at January 1, 1972, should have to be earned without recognition of the expenditures made in the exploration for and development of such properties prior to November 7, 1969. We recommend that the effective date for eligible expenditures be retroactive to January 1, 1949, after reduction for the amount of any depletion allowed since that date.

Hon. Mr. Phillips: Why do you go back to 1949? Is that under the new act? Is there any significance to January 1st, 1949?

Mr. Ross: That was when there was change in the Income Tax Act and it is really a period which was picked as being easily distinguished.

The Chairman: That is the beginning date of the present act.

Senator Connolly: Would you say again, Mr. Ross, what it is you want in that respect. I have read this too, but I would like you to talk to it.

Mr. Ross: Do you want me to go back over the first part?

Senator Connolly: I think it is quite clear that you want additional property of various kinds included in the base for determining depletion.

Mr. Ross: Yes.

Senator Connolly: Now, what about the second point?

Mr. Ross: What we are saying in the second part is that expenditures which have been made in the past for exploration and development back to 1949 we believe should earn depletion as forwarded expenditures would earn depletion less the depletion that has been taken to date.

The Chairman: Well, Mr. Ross, what you are really saying is that you total up the total amount of money you spent on exploration and development since January 1, 1949, and on the other hand you total up the depletion allowances you have taken during that whole period, and if the difference is a plus—in other words, that you have spent more than you have written off—that you should be able to carry that forward.

Mr. Ross: That is it exactly. It is very similar to the recommendation by the House of Commons in this regard.

Senator Hays: How is it treated now?

Mr. Ross: At the moment we get what is called in the bill "automatic depletion" so consequently we do not have an earned depletion right now.

Senator Connolly: Well, in the unearned depletion which you are entitled to now and which is 33⅓ per cent...

Mr. Ross: Well, it is called automatic depletion.

Senator Connolly: Well, I call it unearned depletion as against the earned depletion concept of the White Paper and the bill. But are you entitled to go back to 1949?

Mr. Ross: Under the bill?

Senator Connolly: No, under the act, the existing law.

Mr. Ross: Well, under the present act your expenditures do not have any effect in calculating depletion. The depletion is 33⅓ per cent of the amount of production income left after you have deducted expenses. Very few companies are getting depletion right now.

Hon. Mr. Phillips: Because of the earned depletion concept?

Senator Connolly: It is the difference in the concept that makes this different.

Mr. Ross: It is an entirely different concept.

The Chairman: But there is a question as to why you should carry the difference in concept away back.

Mr. Ross: Well, I should think the reason for carrying the difference in concept away back is that on the converse side the expenditures were made on the basis of having an automatic depletion at 33⅓ per cent. and if

you are going to change the basis on which the expenditures were made, then we suggest that this is a reasonable way to do it.

The Chairman: You do have a run-in period under which you can operate under the present law?

Mr. Ross: Yes, until 1976. But that will only cover part of the production from the property, but at the time those expenditures were made we expected to have a 33⅓ per cent carry forward.

The Chairman: I assume that in that period somehow if you had any money to write off any expenses, you had earnings.

Mr. Ross: Well, you have earnings, but not according to the definition of earnings after eligible expenditures.

The Chairman: Did you enjoy a tax holiday? Was it profitable?

Mr. Ross: In most cases you would have to say in terms of profit that it was not profitable. Our company, for example, is spending more per year than we are earning. We have reserves somewhere down the line and we are going to end up making a profit, but at this point we are not in a profit position.

The Chairman: Your write-offs preserve your earnings and give you the cash flow but they are not called profits.

Mr. Ross: No, it is not called profit.

Hon. Mr. Phillips: Going back to page 2 where you speak about recommendations concerning tangible equipment such as wellhead equipment, et cetera, being included for your base, are you speaking of the extension of the category in respect of these types of items purchased after January 1st, 1972 or are you again going back to 1949?

Mr. Ross: Going back as well.

Hon. Mr. Phillips: So it is an extension of the base and retroactivity. Is that right?

The Chairman: But how can we do that? How can we enlarge the base?

Mr. Ross: Just the land acquisition costs, not the depreciables.

Hon. Mr. Phillips: Am I right in saying that you want the extension of the base back to 1949 only in respect of land acquisition costs?

Mr. Ross: And drilling and exploration costs.

Hon. Mr. Phillips: But with respect to section 72 onwards under the new bill you want the extension of the base, because of the earned depletion concept, to include the new items you referred to?

Mr. Ross: Yes.

Mr. Poissant: Referring to page 2, what is your interpretation of "gross depletion"?

Mr. Ross: Gross depletion is a fixed percentage of the gross revenue after royalties and before any other operating costs, as they have in the United States.

Mr. Poissant: This is something we do not have now.

Mr. Ross: No.

Mr. Poissant: And you are recommending something equivalent to that in the United States?

Mr. Ross: Yes. And the industry on balance has recommended this for 15 years.

Mr. Poissant: In the same paragraph you say again "To avoid any abuse in the sale of properties between companies it is suggested that the income from such sales ... should be credited to 'Canadian exploration and development expenses'." Do you mean to say that if there was a capital gain it should be all the gain?

Mr. D. A. McGregor, Independent Petroleum Association of Canada: In this respect we are talking about earned depletion and we are asking that land acquisition costs be included. Now if you did not include your sales as a credit against your pool of expenditures, abuses could arise by companies selling properties back and forth.

The Chairman: I think the White Paper mentioned that.

Is there any other point that you want to direct our attention to in particular, Mr. Ross?

Mr. Ross: Not in-so-far as depletion is concerned. I think we have covered that. Then going over to Canadian ownership, and this is called the principal business testing type of thing, what we would like to see is that all Canadians, individuals as well as corporations, should be allowed to deduct drilling and exploration costs against other income. We believe that this could have a material effect in increasing the amount of capital available in Canada by Canadians for expenditures in the oil and gas business. Your committee recommended that this be on the basis of 30 per cent on a declining balance. The House of Commons recommended it be on 20 per cent on a declining balance. We feel very strongly that we would like to see it at 100 per cent. We think that this is a very tangible way of increasing Canadian ownership.

Hon. Mr. Phillips: What does the act do?

Mr. Ross: The current act is strictly tied down to principal business companies, which are mining companies, drilling companies, exploration companies, and so on.

Mr. McGregor: Except to the extent that a non-qualifying corporation might have oil and gas.

The Chairman: They could write off expenses of the type you are talking about. Very well. What is the next point?

Mr. Ross: The next part is on foreign drilling expenses. The current bill has made provision for the ability to expense against the Canadian income 10 per cent on a

declining balance of expenditures made overseas. We feel that this should be broadened and should go to 100 per cent as well. We feel that if Canada wants to be a factor in world oil she has to recognize the facts of life. The facts of life are that the American companies can all do this, and as a result they have built multi-national corporations and now own most of the free world oil. We think this is extremely important and that Canada can end up with some sizeable companies as well. We recognize that on the one hand we are saying that we want to raise capital for the Canadian industry, while on the other hand we are saying that we want to spend some of the capital overseas. That is quite correct.

The Chairman: What is the advantage to Canada and to the tax revenues of Canada in your being permitted to spend some of your Canadian earnings on overseas development?

Mr. Ross: We think, in terms of the advantage to Canada overall, one is going overseas to look for smal oil fields. They are going over there to look for major oil fields. You have seen that many Canadian companies, even despite this lack of being able to do it, are over making applications in the North Sea, Norway, and so on. They are looking for major oil pools. We think that it is in our interest to get ourselves diversified around the world and to participate in some of the major oil pools in the world. This means that the Canadian company that is successful in finding a major amount of oil overseas has to reflect in the size of the company and the opportunities available to Canadians, and so on. So we think it is important that way.

The Chairman: It gives you a chance to battle your competitors abroad.

Mr. Ross: Exactly.

The Chairman: And it may be that you can keep more of the field here for yourself.

Mr. Ross: Well, it does other things, too. In this type of business you have to be worried about your shares price, because you have always got to be raising money. If you have interest in an attractive overseas area this will have an effect, because it will mean that you can raise more money either in this country or in the United States, and a lot of that money will be used in Canada. Certainly, that is one means of helping the Canadian companies materially.

Senator Connolly: I suppose too that overseas earnings ultimately, if they are high enough, all accrue to the benefit of the Canadian economy.

Mr. Ross: Right. We suggest here that overseas earnings be taxed as part of the Canadian income of the company.

Senator Connolly: You also suggest that the expenditures overseas be either a deduction from the profits, 100 per cent of the profits earned by the subsidiary, or, at the option of the company, be made available as a Canadian deduction.

Mr. Ross: Exactly. The American government did this quite some time ago, and as a result they ended up, as I said a moment ago, owning most of the oil of the free world. This has been extremely beneficial to the United States economy. There is no question about that. So far as we are concerned, the American government took a chance in allowing their companies to go over and in allowing them to have this deduction, but it has come back home very materially to them.

We think that exactly the same thing would happen in terms of Canadian companies. After all, there is no Canadian company that is going to go overseas to look for 25 barrels of oil a day, or that type of thing. They are going over there to look for major oil fields. We are satisfied that some of them will strike those oil fields. This is similar to the approach with regard to allowing Canadian individuals and companies to have drilling and exploration expenses in this country. We believe that if a company goes over there to look for oil it does not go there to lose money. Other people we have talked to down here have suggested, "Well, how much money is the Government going to lose?" I say nobody is going to go in there to lose money. They are going to go in there to make money, and we are satisfied that they are sensible people and that over a period of time they will be making an asset. Naturally you are gambling into the future, but that is what everybody does in the oil business.

Senator Hays: What other countries follow the same practice as the United States follows in this regard?

Mr. Ross: Senator Hays, I am really not too well aware of the taxation of other countries. The Americans are certainly the major example of it. I believe that the French have a certain amount of latitude in this direction.

Senator Connolly: What about the British?

Mr. Ross: No.

Senator Connolly: Through the years, when they had the Empire, did they not do it then?

Mr. Ross: The British have ended up fundamentally with one major oil company, which is BP, and a minority interest in Shell. The Americans have five major oil companies, plus a considerable number of other very sizeable companies. For example, a company such as Ashland is as big as Imperial Oil. They have many companies of that size. If you look at the world reserve of oil and gas you will see that the United States owns most of it. This results largely from the fact that they encouraged their nationals to go overseas. Admittedly, part of that encouragement, very frankly, was that the Americans became concerned in 1920, or so, that they were going to run out of oil. Therefore, they encouraged their people to go overseas.

The Chairman: Gentlemen, I am sorry, but I must excuse myself now. I will ask Senator Connolly to take the Chair while you deal with the subjects of stock options and tax-free re-organization. You may be sure that I have read your brief in its entirety.

Mr. Ross: Thank you very much, Mr. Chairman.

Senator John J. Connolly (*Acting Chairman*) in the Chair.

The Acting Chairman: Would you please continue, Mr. Ross?

Mr. Ross: Yes, senator. The next section of our brief deals with stock options. We anticipated earlier, before this bill came out, that stock options would be subject to capital gains tax. It would appear that stock options will be subject to the ordinary income rates after 1973, and we feel very strongly that stock options have been and are a very effective means of motivating technical people. Also in terms of an independent company, they are one of the few means by which you can attract extremely capable people to the company because an independent company, by the nature of its size, is much more risky than a larger company, and we have found this to be extremely effective in attracting people.

We recommend that stock options be subject to tax at capital gains rates at such time as the gain is realized. The reason for that is because there are many inter-listed stocks and you exercise a stock option which is considered to be a buying of stock in terms of the S.E.C., and you cannot trade in the stock for six months. As a result, we have had situations in the last few years where people have exercised stock options at one price and could not sell for six months...

The Acting Chairman: Because of the S.E.C. regulations?

Mr. Ross: Yes.

The Acting Chairman: Have we got a similar regulation in Canada?

Mr. Ross: No, we have not, but there are many inter-listed companies and, of course, with the amount of money we are talking about in this industry, unfortunately, you have to go to the American market quite often, so the only way you can sell securities there is through the S.E.C., and you are stuck with the regulation. As I say, there have been illustrations where people have exercised a stock option and they are taxable on it in Canada at that price, and six months later the price has dropped well below the option price, and so they end up owing the bank, owing the Canadian Government, and having securities which are less than the amount of the bank loan. We believe that can be cured by our suggestion here.

The Acting Chairman: Could you spell out your suggestion again, please?

Mr. Ross: Yes. Our suggestion is that the stock option—and we are only talking about proper ones that are 95 per cent of the market value of the shares on the date the option is granted—be subject to capital gains taxation at the time that the gain is actually realized. This means at the time the stock is sold and not at the time that the option is exercised, as currently is the case.

Mr. McGregor: This is really no different from what is happening now in a good many companies which are giving employees interest-free loans to purchase capital stock of a company, payable, perhaps, ten years down the road. Under the new bill, using that type of plan, that employee is only going to be subject to a capital gains tax on realization.

The Acting Chairman: In other words, the loan is used to buy stock today, and the loan is repaid, let us say, three years hence, and presumably the loan would be repaid out of whatever return the sale of the stock might produce.

Mr. McGregor: Most of them, senator, are going on ten years interest-free loans. That is really, in effect, the same as this proposal. I think you will see more of that.

Mr. Ross: If they do not change this I think you will see more of it.

The Acting Chairman: In other words, this is a loophole in the bill.

Mr. Alan Irving, Legal Adviser to the Committee: That has always existed. We have had stock options being taxed as income in the bill for some time.

Mr. Ross: Stock options as income?

Mr. Irving: When you exercise your option.

Mr. Ross: No.

Mr. Irving: Under section 85A.

Mr. McGregor: Yes, you are correct. The difference between the option price and the price that it was exercised at has been treated as income, and anything above that has been tax free.

Mr. Irving: Right.

Mr. Ross: But the way that is treated as income is very different than the way which is proposed under this bill. It is an averaged income over three years which is quite different.

Mr. Poissant: You do not have the averaging provisions under the new bill, but you will have forward averaging.

Mr. McGregor: We do not really consider that as a benefit.

Mr. Poissant: Going back to what we touched on before, it will continue to be treated as income.

Mr. Ross: Yes, but the difference is it was treated as income at the average income rate.

Mr. Poissant: Yes, you are right, and the only averaging provisions you are left with are the locking averaging or the forwarding averaging, and it is of no value to you.

Mr. Ross: The net effect really is that if the top part of your bracket is 50 per cent, under the current tax you are probably paying, let us say, 22 to 25 per cent or something in that order. Under this proposal you would be paying 50 per cent because it is the marginal end that

is going on. As Mr. McGregor suggested, there are loopholes like convertibles, debentures that you do not pay interest on, and so forth. Those things are all just getting around this and, of course, they mess up the capitalization of the company and they are difficult to do because the directors get themselves into a great sweat about paying out a few debentures here and there, or lending money to officers or individuals.

In our company, for example, we have stock options right from the chairman of the board right down to some of our third line accounting people, and there is just no question that we find they are extremely effective. It increases the amount of work these people do and their attitude is unbelievable. They used to go home at 4 o'clock and now they are there until 6 or 7 o'clock on weekends. Frankly, I do not believe Canada can take away this type of incentive.

Going to the next one, honourable senators, we have tax-free reorganizations; I would rather not deal with that at all, if you do not mind.

Mr. McGregor: Under section 17 of the current bill, it was possible to donate oil and gas properties to a wholly-owned subsidiary without tax incidents. This allowed companies which operated in different jurisdictions to bring their businesses together, and carry on in order to effect savings. The new bill takes that privilege of donation away from the companies and really sets up a barrier against any reorganization.

Mr. Ross: Has this been abused?

Mr. McGregor: No, not a bit. It has been used by American companies to form Canadian subsidiaries in order to get leases in the Northwest Territories and the Yukon. The only way they could obtain their properties there was to form a Canadian subsidiary and donate the property to it. It certainly has not been abused.

Senator Isnor: Are you making a brief on behalf of American companies or Canadian companies?

Mr. McGregor: I am simply saying it was used by American companies to become Canadianized. It has also been used by Canadian companies which might have half a dozen subsidiaries in order to get all of their properties into one operating company.

The Acting Chairman: This is a roll-over which could take place, as I understand it, between a Canadian parent company and a Canadian subsidiary or between an American parent company and a Canadian subsidiary, or vice versa.

Mr. McGregor: Yes, it is really a tax-free roll-over. It is the same principle as in the liquidation of a subsidiary.

The Acting Chairman: You used the words "tax-free reorganization"; the key to it is where there is a business reason.

Mr. Ross: It also states that you must get advance rulings which boils down to the fact that the tax department is going to look at it, and make sure it is a business reason.

The Acting Chairman: Will they give you a ruling on this in advance?

Mr. McGregor: They have been giving rulings on this very thing in advance, providing one did have a good business reason—and they are pretty tough about the business reasons, too.

The Acting Chairman: Advance rulings are not very easy to come by in other areas. In this area it has been satisfactory?

Mr. McGregor: Yes. The present bill will really stop any form of reorganization, because it taxes the roll-over.

The Acting Chairman: At what rate?

Mr. McGregor: As ordinary income.

Mr. Poissant: Mr. Ross, which subsection of section 17 were you referring to?

Mr. Ross: Section 17(7).

Mr. Poissant: That relates only to depreciable property, does it not?

Mr. McGregor: It may be subsection (5). I did not bring a copy.

Mr. Ross: Could we look it up for you and advise you of it?

Mr. Poissant: Yes.

Senator Benidickson: Mr. Chairman, for the record, may I admit that I have not been a constant participant at this committee, due to events that will culminate today.

This morning the chairman indicated that I had come late to this morning's meeting. I wish to indicate that I had been active on bilingualism by submitting myself from 8 o'clock on, before our meeting, to a little tutoring for two hours.

I am not acquainted with the gentleman who just spoke. Is he an adviser to this committee?

The Acting Chairman: Yes, he is a member of the staff.

Senator Benidickson: That is fine, and his bilingualism is of course perfect, but I did not understand.

The Acting Chairman: Mr. Mitchell is a member of Mr. Poissant's firm.

Mr. Poissant: Were you referring to me?

The Acting Chairman: Mr. Poissant is our chief adviser on the technical side.

Senator Benidickson: I explained why I was a little out of date and I recognized, perhaps, Mr. Poissant's skill, but I did want to point out that in *Hansard* we often raise a question, starting with "we".

Mr. Poissant: I apologize.

Senator Benidickson: I ask that in future in committee, the committee insist that only senators may use "we".

Mr. Poissant: It is well taken.

Senator Benidickson: I admire your bilingualism, Mr. Poissant, and regret mine, which I am trying to improve. That is why I was late this morning. But if you are our advocate, or our inquisitor...

The Acting Chairman: Our adviser.

Senator Benidickson: Oui. I want to make the suggestion that for the future you perhaps say: "The committee might want to know this."—not "we".

Mr. Poissant: Thank you very much, Senator.

Senator Benidickson: The committee could end up in a minority position, and you do not ask questions starting "we" or "nous".

Senator Smith: They might want to vote, at some future stage.

The Acting Chairman: We might need a vote right now. Mr. Ross, are there any other questions or is there anything else you want to deal with at this stage. With respect to this last point, you will write in about it. We thank you very much. You have been very helpful to us, and we appreciate your coming here.

The committee adjourned.

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THIRD SESSION—TWENTY-EIGHTH PARLIAMENT

1970-71

THE SENATE OF CANADA

PROCEEDINGS

OF THE

STANDING SENATE COMMITTEE ON

BANKING, TRADE AND COMMERCE

The Honourable SALTER A. HAYDEN, *Chairman*

No. 44

WEDNESDAY, OCTOBER 27, 1971

Eighth Proceedings on:

"Summary of 1971 Tax Reform Legislation"

(Witnesses—See Minutes of Proceedings)

24289—1

THE STANDING SENATE COMMITTEE ON
BANKING, TRADE AND COMMERCE

The Honourable Salter A. Hayden, *Chairman*

The Honourable Senators,

Aird	Grosart
Beaubien	Haig
Benidickson	Hayden
Blois	Hays
Burchill	Isnor
Carter	Lang
Choquette	Macnaughton
Connolly (*Ottawa West*)	Molson
Cook	Smith
Croll	Sullivan
Desruisseaux	Walker
Everett	Welch
Gélinas	White
Giguère	Willis–(28)

Ex officio members: Flynn and Martin

(Quorum 7)

Order of Reference

Extract from the Minutes of the Proceedings of the Senate, September 14, 1971:

"With leave of the Senate,

The Honourable Senator Hayden moved, seconded by the Honourable Senator Denis, P.C.:

That the Standing Senate Committee on Banking, Trade and Commerce be authorized to examine and consider the Summary of 1971 Tax Reform Legislation, tabled this day, and any bills based on the Budget Resolutions in advance of the said bills coming before the Senate, and any other matters relating thereto; and

That the Committee have power to engage the services of such counsel, staff and technical advisers as may be necessary for the purpose of the said examination.

After debate, and—

The question being put on the motion, it was—

Resolved in the affirmative."

Robert Fortier,
Clerk of the Senate.

Minutes of Proceedings

Wednesday, October 27, 1971.

(54)

Pursuant to adjournment and notice the Standing Senate Committee on Banking, Trade and Commerce met this day at 9:30 a.m. to further examine:

"Summary of 1971 Tax Reform Legislation".

Present: The Honourable Senators Hayden, (*Chairman*), Beaubien, Benidickson, Blois, Burchill, Carter, Connolly (*Ottawa West*), Desruisseaux, Flynn, Gélinas, Isnor, Macnaughton, Molson, Smith, Walker and Welch—(16).

Present, but not of the Committee: The Honourable Senator Laird—(1).

In attendance: The Honourable Lazarus Phillips, Chief Counsel.

WITNESSES:

Noranda Mines Limited:

Mr. Alfred Powis, President;

Mr. D. H. Ford, Director of Taxation.

Bethlehem Copper Corporation Ltd.:

Mr. B. J. Reynolds, Director and Legal Advisor;

Mr. K. E. Steeves, Vice-President, Finance and Treasury.

The Canadian Gas Association:

Mr. G. E. Miller, C.A., Comptroller and Assistant Treasurer, Union Gas Company of Canada Ltd.;

Mr. R. F. Sim, Assistant Secretary, TransCanada PipeLine Limited;

Mr. E.W.H. Tremaine, Treasurer and Assistant Secretary, The Consumers' Gas Company.

At 12:25 p.m. the Committee adjourned.

2:15 p.m.

(55)

At 2:15 p.m. the Committee resumed.

Present: The Honourable Senators Hayden (*Chairman*), Beaubien, Benidickson, Blois, Burchill, Carter, Connolly (*Ottawa West*), Desruisseaux, Gélinas, Isnor, Macnaughton, Molson, Smith, Sullivan, Walker and Willis—(16).

In attendance: The Honourable Lazarus Phillips, Chief Counsel.

WITNESSES:

ad hoc Committee of Voluntary Agencies:

Mr. Donald Pierce, McClintock, Devry and Pierce;

Mr. Menno Dirks, Canadian Bible College;

Mr. Ian J. Stanley, World Vision of Canada.

At 3:25 p.m. the Committee adjourned until Thursday, October 28, 1971 at 9:30 a.m.

ATTEST:

Frank A. Jackson,
Clerk of the Committee.

The Standing Senate Committee on Banking, Trade and Commerce

Evidence

Ottawa, Wednesday, October 27, 1971

The Standing Senate Committee on Banking, Trade and Commerce met this day at 9.30 a.m. to give consideration to the Summary of 1971 Tax Reform Legislation, and any bills based on the Budget Resolutions in advance of the said bills coming before the Senate, and any other matters relating thereto.

Senator Salter A. Hayden (*Chairman*) in the Chair.

The Chairman: Honourable senators, I call the meeting to order.

We have four appearances this morning: Noranda Mines Limited; Bethlehem Copper Corporation Ltd.; The Canadian Gas Association; and the ad hoc Committee of Supporting Voluntary Agencies. Noranda Mines Limited will be heard first, and the appearances on behalf of Noranda Mines Limited are: Mr. Alfred Powis, President; and Mr. D. H. Ford, Director of Taxation.

The usual practice, gentlemen, is that you make an opening statement, and then any questions honourable senators have will follow; after which you may develop any further matters you wish.

Mr. Alfred Powis, President, Noranda Mines Limited: Thank you, Mr. Chairman.

I might say at the outset, honourable senators, that we have submitted a brief which is really brief, which is unusual for us. I would like to apologize to honourable senators for a couple of spelling and typographical errors in the brief; which we prepared rather hurriedly with the thought that we would be appearing last week.

It was not our intention in this brief to revive the various arguments in favour of the existing incentives for the mining industry. The Government has apparently made a decision and, for the time being at least, it appears we will have to live with that decision.

Our submission focuses on two areas which are of particular concern to Noranda, where we believe that the intentions of the Government have been perverted by the proposed regulations in connection with Bill C-259.

In August, 1970, in response to many objections raised against the original proposals as they affected the mining industry, the Minister of Finance wrote to his provincial counterparts proposing, among other things, that the expenditures eligible to earn depletion would be expanded to include the cost of new facilities located in Canada to process mineral ores to the prime metal stage, and certain expenditures in connection with a major expansion of an existing Canadian mine.

Based on our understanding of this announcement, Noranda decided to proceed with a $120 million expansion of copper production in the Province of Quebec. Our problem with the proposed regulations really falls into two areas: the first is that we had understood that in connection with the announcement by the Minister of Finance in August, 1970, expenditures for new facilities to process ore to the prime metal stage in Canada would be eligible to earn depletion.

Senator Connolly: Would you just repeat that? You are going rather quickly.

Mr. Powis: I beg your pardon, sir. We had been led to believe by the letter from the Minister of Finance to his provincial counterparts, which he wrote in August, 1970, that expenditures for new facilities to process ore to the prime metal stage in Canada would be eligible to earn the depletion.

Senator Connolly: Facilities to process ore to the prime metal stage?

Mr. Powis: Yes; in other words, smelters and refineris. I might say that $30 million of this $120 million program involved expenditures of that nature. We now understand from officials of the Department of Finance that in order for such processing facilities to earn depletion, they must be new from the ground up and that facilities built to process ores on a custom basis—that is, for other mines—will not be eligible to earn depletion. In our case some $30 million of this $120 million program falls into that category.

The Chairman: Custom smelting?

Mr. Powis: Yes, custom smelting and refining, sir.

The second problem which we have is in connection with the establishment expenses which are an integral part of the expansion of our Gaspé mine.

Senator Connolly: Are you going to expand on the first point later?

Mr. Powis: I will if you wish, sir.

Senator Connolly: Shall we do it now, Mr. Chairman?

The Chairman: Is that convenient, Mr. Powis?

Mr. Powis: Yes.

Senator Walker: This letter left no question about it, did it? You felt you could rely on the letter you have referred to?

Mr. Powis: There was no question in our minds at all. As I say, we relied on this. As a matter of fact, shortly after these new regulations were put out we were contacted by Mr. Bourassa from Quebec who said, "Now we have the regulations which are specifically designed for cases of your type. This new proposal in terms of tax reform is

specifically designed for projects of your sort, and I hope you will now be able to get off the ground," which, of course, we did. We are completely committed to this project; it is well under way.

Senator Connolly: Is there a regulation in effect now, at least in draft form, which seems to be at variance with the terms of the letter of August, 1970?

Mr. Powis: No, sir, we have not seen a draft.

Senator Connolly: You have not seen one?

Mr. Powis: The regulations, as I understand it, do not form part of the bill at all. The regulations are something that will be promulgated by the minister following the enactment of the bill.

The Chairman: But the regulations must have their basis in the bill.

Mr. Powis: Yes.

Senator Connolly: Where did you get your information that the regulations are at variance with the letter and with the bill? Does the bill conform to the letter?

Mr. Powis: You have to take the bill plus the regulations in order for it to conform with the letter.

Senator Connolly: But you have not got the regulations. Is there anything in the bill that touches on the point that is made in the letter of August, 1970?

Mr. Powis: I would have to rely on Mr. Ford for this.

Mr. D. H. Ford, Director of Taxation, Noranda Mines Limited: The bill merely provides for deduction for depletion as allowed by regulation. That is the present situation. Then you must turn to the regulations for the determination of these allowances.

Senator Beaubien: But you have not got the regulations.

Mr. Ford: What we have is a news release of July 6.

Senator Connolly: This year?

Mr. Ford: Yes.

Senator Molson: By whom?

Mr. Ford: By the Department of Finance. It says in the first paragraph:

> Finance Minister E. J. Benson today released a paper outlining proposed regulations to apply to mining and petroleum.

This is all we have, and I understand this is all we are likely to have.

The Chairman: This was a press release?

Mr. Ford: A news release.

Senator Connolly: Would you read that again more slowly?

Mr. Ford: The first paragraph of the covering letter to the news release says:

> Finance Minister E. J. Benson today released a paper outlining proposed regulations to apply to mining and petroleum.

Senator Connolly: Have you those proposed regulations?

Mr. Ford: Yes, it is part of the news release.

Senator Connolly: What do they say?

Senator Walker: That is the part that is relevant.

Mr. Ford: It is what Mr. Powis has been saying. It is a four-page document.

Senator Connolly: Perhaps you would give us the salient points.

Senator Beaubien: That is what Mr. Powis has given.

Senator Connolly: But we did not realize they were tied in so closely, and I want to make sure we get the record straight.

Mr. Ford: With respect to earned depletion as it applies to the kind of expenditure Mr. Powis has referred to, it says:

> Eligible expenditures, include the following: . . .
>
> (c) Expenditures on new buildings and machinery, to the extent that they are to be used to process ore from Canadian mineral resources beyond the stage to which they were previously processed in Canada, up to but not beyond the prime metal stage or its equivalent.

On the face of it, that would cover a large part of Noranda's proposal, but we understand the interpretation given to that—

Senator Connolly: This is the point that is not in the regulations that you are now giving us?

Mr. Ford: Yes, sir.

Senator Connolly: You got this subsequent material from the Department of Finance?

Mr. Ford: Not material; this was an interpretation.

Senator Connolly: You got this interpretation from the Department of Finance?

Mr. Ford: Yes, sir.

Senator Connolly: Now would you tell us what it is? I just want to make the record crystal clear, if we can.

Mr. Ford: Expenditures on custom smelting refineries are entitled to earned depletion.

Senator Connolly: It seems to me Mr. Powis had another point as well. He covered custom refining, but he covered another point, did he not?

Senator Molson: Building.

Mr. Powis: The other point, the metal point, that I wanted to cover has to do with mining development.

Senator Connolly: But did you not also say that additions to existing facilities would not be included, that it had to be from the ground up?

Senator Walker: That would be new buildings.

Senator Connolly: Completely new.

Mr. Powis: Completely new from the ground up, that is correct. This again is an interpretation we were given by officials of the Department of Finance. I could argue, for example, our smelter expansion is in a sense new from the ground up, that it involves new building, new equipment and so on.

Senator Connolly: Certainly new expenditure.

Mr. Powis: Certainly new expenditure in any case, and a very substantial one.

Senator Connolly: And it is the kind of expenditure that seemed to be covered by the letter of August, 1970, upon which you relied.

Mr. Powis: Yes, sir.

Senator Connolly: That is the point.

Mr. Powis: That is correct.

Senator Connolly: I think that might be a little clearer to us, Mr. Chairman.

The Chairman: Except that there are a number of problems. First, you have regulations, and they have been read. Then on top of that you have at a later date interpretations. The interpretations are not in writing, and the interpretations have been made by somebody in the Department of Finance. Whether he knows much, a lot or a little about mining, I do not know. The question is: What is the position of those interpretations? I think you would have to force the issue in order to get some commitment. I think we have to look at it on the basis that administratively, on the basis of those interpretations, it is proposed to apply the regulations in that form, and yet when you analyze what is said, "expenditures on new buildings and machinery" is easily understandable.

> . . . to the extent they are to be used to process ore from Canadian mineral resources beyond the stage to which they were previously processed in Canada, up to but not beyond the prime metal stage or its equivalent.

What is the position with respect to the processing on which you have spent this amount of money, the processing facilities? They start with the raw ore?

Mr. Powis: Actually, they start normally with a concentrate, which is upgraded raw ore. They go then through a smelter, which produces metal that is roughly 99½ per cent pure. They then go through a refinery which purifies the smelted copper and extracts other valuable metals, such as silver and gold, from the smelted copper ore.

The Chairman: What was the stage of the processing of ore from Canadian mineral resources at the time they issued these regulations?

Mr. Powis: It varied. In the case of copper, a very high percentage of the copper produced in eastern Canada had been smelted and refined in Canada. In western Canada this is not so. Here again the difficulty is, taking the literal interpretation of that wording, if a new mine came into production and new production is created that had not previously been processed in Canada, you cannot process it beyond the stage to which it had been previously processed. The wording is somewhat confusing.

The Chairman: What was the stage in Canada in the processing of ore from Canadian mineral resources at the time they issued these regulations? Anywhere in Canada by anybody in Canada.

Mr. Powis: It is hard to generalize, but every important metal produced in Canada is now processed to the prime metal stage. However, the problem is that new mines are being developed. There has not been sufficient smelting refining capacity in Canada to handle the production of those new mines, and this is specifically what our expansion of Noranda Quebec and the expansion of Montreal East is designed to do; it is designed to treat the concentrate being produced by certain new mines in this country.

The Chairman: Let us pause for a moment to analyze that. In these allowances, they are going to authorize expenditures on new buildings and machinery. Surely we could eliminate right away that this means what it says; that is, it means expenditures in relation to the construction of new buildings and the installation of new machinery. If you have existing processing facilities, you might very well question whether you are going to replace them; but what you are contemplating in your development is new buildings, new machinery, in relation to new mineral production.

Mr. Powis: Yes, sir.

The Chairman: And if this wording does not cover it, someone is making an awful distortion, it appears to me.

Mr. Ford: The question is whether the expansion of an existing building is a new building.

Senator Connolly: This is a refinement, and a very important one.

Mr. Ford: It is one we are faced with.

Senator Connolly: That is the one you are faced with because you had an existing facility to which you are adding?

Mr. Powis: These are not regulations.

Senator Connolly: Would you answer that question? Did you have an existing facility to which you have added?

Mr. Ford: Yes.

Senator Connolly: You have expanded your facilities. It would seem, in the light of the letter of August, 1970, which you have given to us, that that addition, that expansion, should qualify as well.

Mr. Ford: According to our expectation, it would.

Senator Connolly: It was on that basis that you went ahead.

The Chairman: It is new building, new equipment.

Senator Connolly: Certainly.

The Chairman: I seem to recall that when this statement was originally made, in August, we wrote something in a prologue to deal with that announcement, because we thought these were the things that should happen. There was a press release at that time. Have you copies of it?

Senator Benidickson: A lot of people were refusing to go ahead with expansion in the mining industry, because of the uncertainty created by the White Paper.

The Chairman: It seems to me that what that release talked about was the expanding of the facilities that were in place. This was the whole burden of the release, and this was the signal for the industry to go ahead.

Senator Benidickson: Because they were mixed up. It seemed that they were just clouded in bewilderment about the White Paper.

The Chairman: Yes. Have you the press release?

Mr. Powis: No. It is a letter, actually.

Mr. Ford: It is the penultimate paragraph in the minister's brief.

The Chairman: Yes. Mr. Powis has handed me this. I have seen this before. It is a letter in the form of a news release from the Department of Finance, dated August 26, 1970. It says:

> Finance Minister E. J. Benson today sent provincial finance ministers and treasurers the attached letter which deals with taxation of the Canadian mining industry and proposed changes to the White Paper on tax reform.

After reciting the major proposals in the White Paper which would affect the incentives that were being granted to the mining industry, it goes on to say:

> We are now prepared to propose three further important changes affecting taxation of the mining industry.
>
> The first two changes would widen the definition of expenditures which would qualify for the "earned" depletion allowance. Several provincial governments have impressed us with their point that further incentives should be given to encourage the processing of Canadian ores in Canada. We would like to discuss with you a proposal to include in the base for earned depletion the costs of new facilities located in Canada to process mineral ores to the prime metal stage or its equivalent.

It does not say from what. It does say, "to the prime metal stage or its equivalent." Then it goes on to say:

> Secondly, we are also considering including in the expenditures that earn depletion those for mine buildings, and machinery and equipment acquired in connection with a major expansion of an existing Canadian mine. This extension would put the major expansion of an existing mine on a roughly comparable tax footing with the opening of a new mine. The more efficient alternative could be chosen on its own merits, not on its tax consequences.

The third change is not pertinent to this question. Those are two changes. That language does seem to be explicit and it does appear to deal with it in a similar fashion, whether it is an expansion, an extension of an existing mine or a new mine.

Senator Beaubien: Quite clearly.

The Chairman: Yes.

Senator Molson: Perhaps the only course open to us is to get someone from the department and ask them this question point blank.

The Chairman: That is right.

Senator Molson: The wording sounds explicit. The interpretation of that is not. It is contradictory.

The Chairman: I wonder who gave the interpretation, Mr. Powis.

Mr. Ford: It was in a meeting of the tax policy committee with the Department of Finance.

The Chairman: With whom?

Mr. Ford: It is the tax policy group.

The Chairman: A tax policy committee? I mean, did they all speak with one voice or was there a spokesman?

Senator Molson: They were speaking in different tongues!

Senator Walker: It was the voice of Esau but the hand of Jacob. Senator Phillips will appreciate that.

The Chairman: Yes.

Mr. Ford: It was a round-table discussion, and it seemed to me that it was a group.

The Chairman: Well, who addressed them?

Senator Benidickson: I think we could find that out, other than on the record.

The Chairman: We can find it out, but we would like to know whom to call before us.

The Honourable Lazarus Phillips, Chief Counsel to the Committee: Mr. Chairman there is a reference to this in the prologue, on pages 2 and 5.

The Chairman: Yes.

Senator Connolly: Before we continue, I should like to get one point clarified in my own mind. I take it that the letter of August, 1970, which the chairman has just read, covers not only the expansion of an existing mine but also facilities, either new or added to previously existing facilities to give new capacity. Is that right?

Mr. Powis: That was certainly our interpretation.

Senator Connolly: It seemed to me to be clear from the letter. The letter seemed to imply that.

The Chairman: Have we the letter?

Mr. Ford: Mr. Chairman, it seems to me that the intention of the Government clearly was to encourage the construction of additional processing facilities in Canada and to prevent the export of the raw concentrates.

Senator Connolly: That is it.

The Chairman: Honourable senators, may I recall to you what we said in our report? We had copies of the minister's release. You will find that we enumerate certain things that had occurred since the White Paper came forth. One of the items is given in the prologue on page 2 of our report of September, 1970:

> (4) The proposals made by the Minister of Finance on August 26, 1970, in a letter to the provincial Finance Ministers and Treasurers dealing with the taxation of the Canadian mining industry and the changes to the White Paper applicable to such industry.

In discussing it, we referred on page 5 to the paragraph which I have just read, and then we say, by way of continuing the discussion:

> The Minister proposes to widen the definition of eligible expenditures on which depletion may be earned, by including in eligible expenditures, expenditures made for replacement of mining machinery and mine buildings acquired in connection with expansion of an existing mine. This proposal, it is suggested, would put an *existing* mine on a comparable tax basis with the incentives available to a *new* mine in the White Paper. A further change is to lower the rate of federal tax on the industry from 40 per cent to 25 percent of taxable income. These changes proposed by the Minister represent a basic change in the incentives put forward in the White Paper. The industry in its submissions strenuously contended for such changes demonstrating that without them, existing mines would be subject to heavy additional tax with less retained earnings for development and with less opportunity to earn depletion by reason of the restrictive definition of eligible expenditures on which earned depletion was to be calculated.

Then we go on to say:

> A complete assessment of the extent and benefit of these changes cannot be made until the details of the new definition of eligible expenditures are settled and there is published the extent to which the incentives for new mines will be made fully available to existing mines. The changes proposed by the Minister represent a long step forward to meet the claims of the industry and to acknowledge the inadequacies of the White Paper proposals on these points. They also point up the less generous treatment inherent in the White Paper proposals which the White Paper originally stated was entirely sufficient and should make for a smooth transition for the industry from the old rules to the new rules. These changes are in line with recommendations of this Committee but the Committee wishes to stress that they do not deal fully with the needs of the industry in the way of special rules. Those mines that cannot earn depletion even with the enlarged definition of eligible expenditures are not helped.

That is a summary we made, proceeding on the basis of the minister's release, and it is a public document. It has been available for a long time. I should think the committee would be very much interested to know just how, in the light of that, the suggested interpretations could possibly be put forward. If the committee wishes, I will press the question I put to Mr. Ford as to who were the members; otherwise we will just ask somebody from the department to attend. We could have the deputy minister in the first instance, I would suggest, and if we do not get far enough with him, then I would suggest having the minister.

Hon. Senators: Agreed.

The Chairman: We do not need any further development on that point.

Mr. Powis: You have raised a second point of concern to us, sir. I refer to the letter of August, 1970, which purported to put the expansion of the existing mine on the same basis as the development of the new mine. As we understand these proposed regulations, this is not so. The proposal is that the expenditures eligible to earn depletion on the expansion of an existing mine will not allow development expenditures to be so included after a mine comes into production. Now, this is the expansion of an existing mine. In the case of our Gaspé mine, $10 million of total expenditure is involved in pre-production stripping.

The Chairman: You mean developing more ore?

Mr. Powis: Developing more ore body, yes, so that it can be mined at a higher rate.

The Chairman: Well, that is development, isn't it?

Mr. Powis: That is right.

The Chairman: And it is new development.

Mr. Powis: But it is not allowed as an expenditure eligible to earn depletion.

Senator Connolly: When you say it is not allowed, do you mean, rather, that the interpretation that you have been given by officials would appear to exclude it?

Mr. Powis: No, sir. This is in the press release explaining the proposed regulations. This is not an interpretation; it is the regulation.

Mr. Ford: May I read to you the words, sir?

Senator Connolly: Please, and would you identify the document.

Mr. Ford: Again it is the news release of July 6, 1971, containing the outline of the proposed regulations. In the section dealing with earned depletion, the press release reads:

> Eligible expenditures include the following:
>
> (a) Canadian exploration and development expenses in the mining and petroleum industries, except for:
>
> (iii) Canadian exploration and development expenses in the vicinity of a mine after it came into production

Senator Molson: What is the "vicinity"?

Mr. Ford: That is a very good question, sir. We have asked that question several times.

The Chairman: One reference to vicinity would be "in the neighbourhood."

Senator Beaubien: "Adjacent to."

Senator Flynn: Where does it stop, though?

Mr. Ford: We understand that they often have trouble putting distances in there, for example one mile, three miles or ten miles, because different mines have different areas.

Senator Benidickson: We had the same problem when we were considering the definition of a new mine.

Mr. Ford: Exactly.

Senator Connolly: Well, what character of expenditure did you incur which seems to be excluded by that section of the News Release?

Mr. Ford: $10 million of expenditures on developing the open pit of the Gaspé Copper Mine in order to increase the productive capacity upwards from about 6,000 tons a day.

Senator Connolly: What was the character of that work?

Mr. Ford: Stripping overburden.

Mr. Powis: Stripping overburden, waste rock, which is necessary to enlarge the pit so that we can get a higher grade of production from it.

This sort of expenditure in the case of a new mine is, of course, eligible to earn depletion. In the case of a mine expansion it is not, according to the proposed regulations.

Senator Beaubien: Mr. Powis, do you see any reason for that? Why would it be allowed in one case and not in the other?

Mr. Powis: The reason given, is that in the course of a normal mining operation you always have to do this stripping in any case. You have to strip away a certain amount of the waste rock in order to get at the ore as the pit expands. I understand the reason given for not including these pre-production expenses in connection with an enlarged pit is that it will be difficult for the department to establish what stripping is required in terms of the existing operation and what stripping you are doing in terms of enlarging the operation.

The Chairman: Well, does not any stripping you do enalrge the pit?

Mr. Powis: Yes, but we are talking here about the expansion of an existing operation. We are operating that pit now at the rate of 6,000 tons a day, say. In the course of that we are doing a certain amount of stripping just to keep ore developed ahead of the mining operation.

Senator Beaubien: Excuse me, Mr. Powis, but on this expansion that you have made, if it were not allowed for depletion, you would just charge it off to operating expenses.

Mr. Powis: Yes.

Senator Beaubien: I do not see, tax-wise, what the big difference is.

Mr. Powis: The big difference, tax-wise, is that, for example, if we expand an existing concentrator in connection with mining expansion we can write that off on a capital allowance basis against operations as well, but it also earns depletion. But just as important as the expansion of the concentrator is the great deal of additional stripping that is required in order to permit production on a vastly enlarged basis, and this is not allowed as an eligible expenditure to earn depletion. Therefore, it puts the expansion of the existing mine in a very much different position from the development of a new mine, contrary to what the minister said in his letter of August 26, 1970.

Senator Macnaughton: Mr. Powis, your case is summarized on page 4 of your brief.

Mr. Powis: That is right.

The Chairman: Honourable senators, for convenience in reading and for reference afterwards to this committee, I would suggest to the committee that the letter of August 26, 1970, together with the News Release of July 6, 1971, be incorporated in our proceedings today. Further, I would suggest that they be incorporated as part of the proceedings rather than as an appendix.

Hon. Senators: Agreed.

Texts of documents follow:

DEPARTMENT OF FINANCE

NEWS RELEASE

For release 7:00 p.m. EDT, August 26, 1970

Ottawa, August 26, 1970
70-104

Finance Minister E. J. Benson today sent provincial finance ministers and treasurers the attached letter which deals with taxation of the Canadian mining industry and proposed changes to the White Paper on tax reform.

As you know, the First Ministers intend to discuss tax reform at their meeting in Ottawa September 14-16. Provincial Ministers of Finance may also want to discuss the matter when we meet on September 17.

We have received the views of most provincial governments on the White Paper on tax reform and we will be prepared to discuss them. We will want to seek clarification of some of the provincial proposals that have been put forward.

You will appreciate that by mid-September the federal government will not have received the reports of the parliamentary committees on tax reform. Until we have received the reports and until we have an opportunity to hear any views provincial governments desire to express

on them, we will not be in a position to make final decisions on the legislative program.

The further steps required to implement reform suggest that we cannot now expect the new system to begin until January 1, 1972. As I told the House of Commons committee on August 5, it will take several months to draft amendments to the Income Tax Act, and after the bill is introduced next spring both the House of Commons and Senate will require time for a full debate. I also pointed out that provincial legislatures will need time to amend their tax legislation before 1972.

During our September meeting we would like to raise one particular matter which a number of provincial governments regard as urgent. This concerns the tax treatment of the mining industry. Uncertainty on this subject may be causing the postponement of important projects, particularly in some of the slow-growth regions where the federal and provincial governments are attempting to spur economic activity through other programs.

You will recall the major proposals in the White Paper that would affect the incentives granted to the mining industry:

The present three-year' tax exemption for new mines would be replaced by an entitlement to deduct certain costs from taxable income as quickly as profits from the new mine permit. These costs would include amounts for mine buildings, machinery and equipment acquired for the purpose of gaining or producing income from the new mine. (The existing system already permits a fast write-off for exploration and development expenditures.)

The percentage depletion allowance, which are at present automatically available to mining corporations, would after a transitional period be available only if sufficient amounts are spent for certain purposes. These purposes would include exploration in Canada, development of a new mine in Canada, and expenditures for those capital assets mentioned above as being eligible for accelerated write-off.

We are now prepared to propose three further important changes affecting taxation of the mining industry.

The first two changes would widen the definition of expenditures which would qualify for the "earned" depletion allowance. Several provincial governments have impressed us with their point that further incentives should be given to encourage the processing of Canadian ores in Canada. We would like to discuss with you a proposal to include in the base for earned depletion the costs of new facilities located in Canada to process mineral ores to the prime metal stage or its equivalent.

Secondly, we are also considering including in the expenditures that earn depletion those for mine buildings, and machinery and equipment acquired in connection with a major expansion of an existing Canadian mine. This extension would put the major expansion of an existing mine on a roughly comparable tax footing with the opening of a new mine. The more efficient alternative could be chosen on its own merits, not on its tax consequences.

The third change involves the maximum rates of tax on the industry. It has been argued that when the provincial mining taxes (up to 15 per cent in some provinces) are taken into account, the maximum tax rate on the taxable income from producing mines could under the system proposed in the White Paper be significantly higher than the rate on the taxable income of corporations in most other industries. It is contented that in some sectors of the industry—e.g., iron, potash, salt, and the tar sands—there would, under normal conditions, be insufficient earned depletion to bring the effective tax rate down to the rate that applied to other industries. The following simple example refers to the maximum taxes payable under the existing and White Paper systems by a mining company (in those provinces having a corporate income tax of 12 per cent) on $100 on taxable income from a producing mine. It illustrates a potential increase from a rate of 44.5 per cent (with the present automatic depletion allowance) to a rate of 59.2 per cent (assuming the corporation earns no depletion at all).

	Present System	White Paper Proposals
Taxable mining profits	$100	$100
Provincial mining taxes at 15%	$ 15	$ 15
Corporation income taxes:		
Federal, at 40% of ⅔ of $85	22.70	
at 40% of $85		34
Provincial, at 12% of ⅔ of $85	6.80	
at 12% of $85		10.20
	$ 44.50	$ 59.20

We are prepared to recommend to Parliament a change that would give provincial governments the opportunity to bring the taxation of mining profits into line with taxation of profits in other industries, and if the provinces wish, to exercise discretion in the application of their mining taxes. We would recommend that once the transitional period of automatic depletion ends, the federal abatement in respect of taxable production profits from a mine be increased to 25 percentage points from the present 10 percentage points and that the deduction for provincial mining taxes be ended. In other words, we would recommend that the effective rate of federal tax be reduced to 25 per cent from 40 per cent, but that this tax (and the corporate tax of those provinces that have entered into collection agreements with the federal government) be applied against the taxable mining profits of the company before deducting provincial mining taxes. This would mean an automatic increase in revenues for these provinces because the provincial corporate tax would then be applied against taxable income that had not been reduced by a deduction for provincial mining taxes.

The increased federal abatement would open up a number of alternatives to provincial governments.

They could increase their rates of corporation tax by the full amount of the federal reduction, and thereby increase provincial revenues.

They could leave their rates unchanged and permit the reduction to flow to the benefit of the industry if they consider this is necessary to encourage mineral development.

In that event, the potential maximum rate on the mining company that earns no depletion at all would be reduced to 52 per cent as follows:

	Revised System
Taxable mining profits	$100
Provincial mining taxes at 15%	15
Corporation income taxes:	
Federal, at 25% of $100	25
Provincial at 12% of $100	12
	$52

Finally, the provinces could combine these approaches by passing part or all of the benefit along to some sectors of the industry, while increasing their revenues to absorb the benefit with respect to those sectors which would or should earn significant amounts of depletion under the White Paper proposals.

The reduction in the federal rate would require an amendment to the integration proposals, because full integration could not be extended to closely-held mining corporations if the federal government retains only 25 points of tax. We believe that the most natural amendment would be to treat all Canadian mining corporations as widely-held corporations—that is, to give their Canadian shareholders credit for 25 percentage points of the corporation taxes paid by the corporation on the profits from which the dividends were paid. Many mining corporations would already receive this treatment under the White Paper proposals.

We believe that these proposals for broadening the base of the earned depletion allowance and increasing the federal abatement, taken together with the substantial incentives already proposed in the White Paper, will enable the federal and provincial governments to co-operate in maintaining an efficient stimulus to development of the Canadian mining industry in the future.

Because these are revisions to the White Paper proposals, I am making this letter public.

Yours sincerely,

E. J. Benson,
Minister of Finance.

DEPARTMENT OF FINANCE

NEWS RELEASE

For immediate release

Ottawa, July 6, 1971
71-80

Finance Minister E. J. Benson today released a paper outlining proposed regulations to apply to mining and petroleum.

The paper is released to permit taxpayers to plan their affairs during the period until the reform legislation is passed and the regulations are subsequently prescribed.

It deals with the classification of accelerated capital cost allowance, earned depletion, 15 percentage point abatement for provincial taxes, provincial mining taxes and shareholders' depletion.

MINING AND PETROLEUM REGULATIONS

The tax reform measures for the mining and petroleum industries include important changes which will be implemented by amendment of the Income Tax Regulations rather than by changes in the income tax itself. The main features of the proposed amendments to the regulations are set out below for the information of interested parties.

Accelerated Capital Cost Allowance

The accelerated capital cost allowance which takes the place of the three-year exemption of the income of new mines will be available in respect of specified depreciable assets related to a new mine or a major expansion of an existing mine.

For a new mine, the accelerated allowance will apply to the following types of new depreciable assets which were acquired before the mine came into production and for the purpose of gaining or producing income from the mine, including income from the processing of mineral ores up to the prime metal stage or its equivalent:

(1) a building (except an office building that is not situated on the mine property);

(2) mining machinery and equipment;

(3) electrical plant that would otherwise be included in class 10 of Schedule B by virtue of subsection 1102(9) of the Income Tax Regulations;

(4) houses, schools, hospitals, sidewalks, roads, sewers, sewage disposal plants, airports, docks and similar property (other than a railroad not situated on the mine property) acquired to establish community and transportation facilities necessary for the operation of the mine.

Depreciable property of the type listed above in (1), (2) and (3) will also qualify for the accelerated capital cost allowance where it is acquired in the course of the major expansion of an existing mine and before the commencement of production at the higher level of capacity. For this purpose a major expansion will be considered to have taken place if the productive capacity of the mine mill is increased by at least 25 per cent.

Expenditures incurred after November 7, 1969 on the above types of depreciable assets, and related to a new mine which came into production after that date or to a major expansion of an existing mine which took place after that date, will qualify for the accelerated allowance. The costs of the qualifying assets will be included in a special class for each mine, rather than in their usual classes. In respect of such a special class the taxpayer may claim the full amount of the undepreciated capital cost up to the amount of income from the mine, and in any event may claim at least 30 per cent of the undepreciated balance. Where the expenditures were incurred prior to the 1972 taxation year. If the taxpayer elects to claim exemption of the income of a new mine that is earned prior to 1974, he cannot also claim accelerated capital cost allowance on expenditures relating to that mine unless he reduces the depreciable cost by the amount of the exempt income.

Earned Depletion

As stated in the budget speech, eligible expenditures incurred after November 7, 1969 will earn depletion at the rate of $1 of depletion for every $3 of eligible expenditure. Eligible expenditures include the following:

(*a*) Canadian exploration and development expenses in the mining and petroleum industries, except for:

(i) the acquisition cost of Canadian resource properties,

(ii) such costs in respect of related community and transportation facilities of the type referred to in (4) above as may otherwise be included therein,

(iii) Canadian exploration and development expenses in the vicinity of a mine after it came into production, and

(iv) interest deemed to be included therein by virtue of paragraph 21(2)(*b*) of the amended Act.

(*b*) Depreciable mine assets listed under items (1), (2), and (3) above as being eligible for accelerated capital cost allowance in connection with a new mine or a major expansion of an existing mine.

(*c*) Expenditures on new buildings and machinery, to the extent they are to be used to process ore from Canadian mineral resources beyond the stage to which they were previously processed in Canada, up to but not beyond the prime metal stage or its equivalent.

Depletion earned in the above manner will become deductible in 1977 and subsequent taxation years at a maximum annual rate equal to 33-1/3 per cent of

(A) production profits for the taxation year as defined in paragraph 1201(2)(*a*) of the present Regulations, plus royalties from Canadian resources not operated by the taxpayer,

minus

(B) deductions as provided by subsections 1201(4) and 1201(4a) of the present regulations.

This general maximum rate of claiming earned depletion will also apply to Canadian coal and gold production, and to royalty income received from Canadian resources by non-operators.

Where there has been a statutory amalgamation of mining or petroleum corporations, or where one mining or petroleum corporation has taken over all or substantially all of the resource property of another such corporation, earned depletion of a predecessor corporation which has not been absorbed against its production income may be assumed by the continuing corporation to be claimed against production income from the properties which were taken over.

Abatement of 15 Percentage Points

Subsection 124(2) of the amended Act provides a 15 per cent point abatement from federal corporate tax in respect of "taxable production profits" from mineral resources (within the meaning assigned "mineral resources" by section 248 of the amended Act) in a province (including the Northwest Territories or the Yukon Territory), commencing in 1977. For purposes of this abatement, taxable production profits will be defined in the regulations to be the amount on which the present 33-1/3 per cent automatic depletion is claimed under subsection 1201(2) of the regulations, less the amount of any earned depletion allowance related to those profits.

Provincial Mining Taxes

Regulations 701 which at present prescribes the deduction for provincial mining taxes will be amended so that it no longer permits a deduction from income for provincial mining taxes which are based on or related to income from mineral resources eligible for the 15 per cent point abatement.

Shareholders' Depletion

Part XIII of the regulations, which at present permits a depletion allowance to shareholders in respect of dividends received from mining and petroleum corporations, will be repealed in respect of dividends received after 1971.

The Chairman: Is there anything more that you wish to stress on this point, Mr. Powis?

Mr. Powis: No, sir. Just to summarize: We embarked on this program involving the expenditure of $120 million with the understanding and expectation that all those expenditures would qualify to earn depletion. We are now in the position where it appears that one-third of those expenditures will not earn depletion.

The Chairman: Just on that point, you have given us the copy of the News Release by the Department of Finance at that time and I wondered if the parties who were going to be affected by that had made any public statement in connection with what was proposed in the News release.

Mr. Powis: Well, sir, I can refer to the press release that we issued when we announced the expansion of our operations.

The Chairman: When was that?

Mr. Powis: That was in February of this year, sir. What we said in the conclusion of that press release reads as follows:

> The full cooperation of the Governments of Quebec and Canada in making these projects possible is gratefully acknowledged. In particular, we could not have proceeded with our expansion programs in the absence of the changes made last August to the Proposals on Tax Reform.

The Chairman: Was that before or after you had appeared before this tax policy committee in the Department of Finance?

Mr. Powis: It was before, sir. It was only after the minister had presented his budget and Bill C-259 was presented, and after we had seen these various press releases that we became concerned. That was six or seven months later.

The Chairman: Is there any reason why we cannot have the statement that you made to the public?

Mr. Powis: It is in the brief, on page 2, sir.

Hon. Mr. Phillips: But we are not printing the brief.

Senator Connolly: Mr. Chairman, on that same point could I ask Mr. Powis this question: The letter of August, 1970 was addressed to the provincial authorities in all provinces. Has there been any discussion with them about the interpretation to which you refer? Have they made any statements about this interpretation, either publicly or privately?

Mr. Powis: No, sir. There have been discussions with Premier Bourassa of the Province of Quebec who, of course, was very interested in seeing this project, along with other projects, go forward. We have indicated to him that what we needed in order to get this project off the ground were exactly the changes that the minister announced in his letter of August, 1970. Of course, shortly thereafter we received a telephone call from the Premier saying, "Now that you have what you need, I hope you will go ahead with this project," which project we did proceed with. This, sir, is a copy.

The Chairman: Perhaps we should give some thought to inviting the Premier of the Province of Quebec to be with us.

Senator Molson: Do not tell me that he had anything to do with the tax reform!

The Chairman: I would not ask him about that.

Senator Connolly: Does Mr. Powis know the views of the Premier regarding the interpretation, or has he been informed of the interpretation?

Mr. Powis: Only in very general terms, sir. He has been informed that we are concerned about the potential interpretation. I should emphasize here that we are dealing in a fairly uncertain area, at least in so far as the metallurgical facilities are concerned, because this is what we believe and understand will be the interpretation of the regulation by the officials of the Department of Finance. To some extent, we are shooting at a moving target.

The Chairman: No, except that you want to establish this position.

Mr. Powis: We would like these regulations to spell out clearly the type of facilities.

Senator Connolly: I think you can go further than that. It seems to me that after talking with the officials in the department you have been led to believe that the interpretation is not going to be satisfactory.

Mr. Powis: That is correct, sir.

Hon. Mr. Phillips: Would you like to record your appreciation of the Bible which says: "Put not your trust in princes."?

Senator Walker: Our recent visitor, Mr. Kosygin, thinks that way also.

The Chairman: May I suggest that there be added to our printed record the press release by Noranda of March 5 this year?

Hon. Senators: Agreed.

(*Text of Press Release follows*):

NORANDA PRESS RELEASE

For release 3 p.m., March 5

TORONTO, March 5, 1971: The Noranda Group of Companies will undertake a $123 million program to expand its production of copper in the province of Quebec, Alfred Powis, President and Chief Executive Officer of Noranda Mines Limited announced today. Details of the mining, concentrating, smelting and refining projects were announced simultaneously by Premier Robert Bourassa in Quebec City.

Gaspe Copper Mines Limited, 99 per cent owned by Noranda Mines Limited, will triple its mining and concentrating capacity to 34,000 tons of sulphide ore per day and will install facilities for the leaching of low grade oxide ores at the rate of 5,000 tons per day. "Because lower grade material from the Copper Mountain mine will be treated," said Mr. Powis, "this expansion will more than double mine production of copper in concentrates from the present level of 36,000 tons per year. Total cost of the combined mining and concentrating project is estimated to be $85 million, including interest during construction and working capital."

Mr. Powis said that Gaspe Copper Mines will also increase smelting capacity by 27,000 tons of copper per year through construction of a roaster. In addition, a plant will be built to produce sulphuric acid from a portion of smelter gases. Capacity of the acid plant will be 132,000 tons per year, half of which will be consumed in the leaching operation and the remainder of which will be sold if markets can be found. Capital cost of this smelter expansion is estimated at $13 million.

Noranda Mines will expand capacity of its smelter in the Noranda area through construction of a commercial-sized prototype of the Noranda Continuous Smelting Process reactor. "This new process for the smelting of copper was

invented by the Noranda Research Centre in 1964 and," said Mr. Powis, "has been under test in a 100-ton per day pilot plant since 1968. A major feature of the new process is that all the sulphur in the concentrate can be recovered as sulphuric acid from the smelter gases. Construction of the reactor will demonstrate the commercial attractiveness of the new process and will add 55,000 tons of copper to capacity." The capital cost is estimated at $19 million.

At the two smelters, the programs include facilities to reduce substantially the emission of dust into the atmosphere. At each location the emission of sulphur dioxide will not be increased and will actually be reduced at Gaspe Copper Mines, provided that markets for sulphuric acid can be developed.

Canadian Copper Refiners, wholly owned by Noranda, will expand its plant at Montreal East by 58,000 tons of copper per year. Capital cost is estimated at $6 million. Current production capacity of CCR of 350,000 tons of refined copper per year make it one of the world's largest.

Taken together, these projects represent the largest single development program in the Company's history.

The Department of Regional Economic Expansion of the federal government has offered $4.7 million in grants against the $38 million cost of the smelting and refining projects.

"Construction at all three locations is expected to begin this spring, with completion during the second quarter of 1973," Mr. Powis stated. Peak employment during construction will be close to 2,000 people, with regular new employment following completion totalling nearly 600 people. Studies conducted by the mining industry indicate that normally six new jobs are indirectly related to each new job directly created by projects of this nature.

"The full cooperation of the Governments of Quebec and Canada in making these projects possible is gratefully acknowledged," said Mr. Powis. "In particular, we could not have proceeded with our expansion programs in the absence of the changes made last August to the Proposals on Tax Reform."

The Chairman: Is there anything else on this point, Mr. Powis?

Mr. Powis: No, sir. I believe there is a question regarding the amount of money involved in the expenditure in Montreal, which is in the order of $7 million. The major expenditure that we are concerned about is in Noranda, Quebec which is in the order of $23 million.

Senator Gélinas: If the regulations were not changed, is it too late for you to cut that expenditure?

Mr. Powis: We have spent a great amount of money already, sir. I think it is probably too late.

The Chairman: These moneys which you have spent you can charge to expense.

Mr. Powis: Yes, sir.

The Chairman: But you cannot earn depletion.

Mr. Powis: No, sir.

The Chairman: And this was the great benefit that the White Paper proposal was going to give in replacement for what you had enjoyed before, the tax holiday, and so on.

Mr. Powis: That is correct.

The Chairman: The automatic depletion.

Mr. Powis: Yes, sir.

Senator Gélinas: Mr. Powis, how much more employment would be created in the Gaspé copper development?

Mr. Powis: Perhaps I could refer to the press release, sir. The additional employment involved in the project as a whole was at the time for 600 people. It has been slightly expanded in scope since we made our announcement, and it is now in the order of 700 permanent employees. There are some 2,000 who are not permanent.

Senator Connolly: This is not employment during the construction and development stage; this is permanent employment?

Mr. Powis: Permanent, yes.

Senator Molson: Is this in Murdochville only?

Mr. Powis: No, this is everywhere. I think the figures for Murdochville are in the order of 400 people, and there are another 300 split between Noranda and Montreal.

The Chairman: As a result of your decision to go ahead on the basis of the original news release by the Department of Finance, up to this moment your total employment is how much?

Mr. Powis: At the moment i think we have probably around 1,500 people working on construction.

The Chairman: The plan which you embarked on regarding expansion, as a result of the encouragement from this press release, projects the employment of how many?

Mr. Powis: Seven hundred people.

The Chairman: Seven hundred more?

Mr. Powis: Yes, more than are presently employed.

The Chairman: More than the 1,500?

Mr. Powis: No, I am sorry, they are construction workers which do not involve permanent jobs. The 700 are permanent jobs.

The Chairman: How long will the construction workers be on the job?

Mr. Powis: Well, of course, it peaks. The construction period is for two years.

The Chairman: Then you have 700 permanent employees. Have you had to extend or create a townsite or any trackage, or anything of that kind?

Mr. Powis: The only infrastructure expenditure involved in this expansion program is the construction of some new houses at Murdochville, but this is not an overwhelming consideration in this connection.

The Chairman: I was wondering if, in this factor of increased employment, there is an increase in purchasing power in the area by reason of the development of these facilities?

Mr. Powis: It would be very considerable, yes.

The Chairman: When you say "very considerable," can you translate that into numbers or dollars?

Mr. Powis: Well, it is difficult to be precise, but our studies conducted by various people indicate that for every new job created in the mining industries there are six to seven jobs created indirectly. So I suppose you could say that the 700 we employ directly ought to have a rippling result, with a total of new employment of perhaps 4,200. It seems to work out that way.

The Chairman: Then there are also professional facilities for these people, which is an additional expenditure.

Mr. Powis: That is correct, sir. It involves a payroll between $5 million and $7 million a year.

The Chairman: That is direct?

Mr. Powis: Yes, direct.

The Chairman: And regarding all the people who come along to service these new jobs and the new people, there are payrolls involved there.

Mr. Powis: Yes, sir.

The Chairman: Is there anything else you want to add?

Mr. Powis: No, I do not think so.

The Chairman: Are there any further questions?

Senator Walker: To summarize, you would not have gone ahead with this if you had not expected that the minister's announcement would be as stated and that you would be allowed depletion on the whole operation?

Mr. Powis: That is right; at least, not on the scale we did. We might have gone ahead on a smaller program.

The Chairman: Honourable senators, the next group is the Bethlehem Copper Corporation Ltd., represented here by: Mr. B. J. Reynolds, Director and Legal Advisor; and Mr. K. E. Steeves, Vice-President, Finance and Treasury.

Mr. B. J. Reynolds, Director and Legal Advisor, Bethlehem Copper Corporation Ltd.: Mr. Chairman, the President of Bethlehem is attending a dinner tomorrow evening at Bethlehem's mine to honour the company's first 10-year employees and is therefore unable to be here. He has asked me to represent him.

Last year, at the invitation of the federal Government, Bethlehem submitted recommendations for improving the White Paper proposals relating to the taxation of the Canadian mining industry. Unfortunately, the federal Government has chosen to ignore our representations, those made by other representatives of the Canadian mining industry, and the recommendations of this committee.

At the time of our submissions with respect to the White Paper proposals, we stressed our concern that the proposals, if enacted, would lead to a substantial reduction in exploration and new mine development, particularly in the remote areas of Canada. Exhibits A, B and C to our written submission, now before you, which relate to the Yukon Territory, indicate that our concern was well founded.

The comments contained in our present submission are based on Bill C-259 and on the main features of the proposed regulations as outlined in Mr. Benson's news release of July 6, 1971, to which Mr. Powis has referred. We are particularly concerned with his latter document, as is Mr. Powis, not because of our specific problems, but because, although only an outline contained in a press release, it indicates that the regulations, when formulated after passage of the bill, will restrict what we consider are already inadequate replacements for reduced incentives contained in the bill. We feel this particularly because the press release to a large extent follows wording contained in that of August, 1970 and the letter to the provincial ministers which was issued at the same time.

Mr. Steeves will deal briefly with the specific points in the brief before you, starting with that of depletion, with which Mr. Powis has already dealt in a specific manner. We will then be pleased to answer questions in these areas.

The Chairman: Before Mr. Steeves proceeds, would you identify the information referred to in the last paragraph on page 1 of your brief, which reads as follows:

> It is already evident that the news release of July 6, 1971 differs substantially from the information released when the Tax Reform Legislation was introduced in the House on June 18, 1971.

Mr. Reynolds: The proposed regulations, as compared to this wine-coloured booklet.

The Chairman: You are referring to what I term the rasberry-coloured booklet.

Mr. K. E. Steeves, Vice-President, Finance and Treasury, Bethlehem Copper Corporation Ltd: Right.

The Chairman: Containing the features of the tax reform legislation.

Mr. Reynolds: With your permission, Mr. Chairman, Mr. Steeves will deal with depletion. Before he does so, perhaps I should say that Exhibits A, B and C to our submission are results which we feel bear out the concern we expressed at the time of our proposal last year. They relate to the Yukon Territory, which is used because, frankly, it is an extreme example. In 1969 the exploration and development expenditures in that territory amounted to approximately $17 million.

The Chairman: Where does that appear?

Mr. Reynolds: That is contained in Exhibit B. In this past year those expenditures amounted to approximately $9.5 million. This downtrend is evidenced to a greater extent in Exhibit A, which outlines the inflow of capital to the Yukon Territory. It is also contained in Exhibit C, which outlines capital expenditure within that territory.

We feel that to a large extent these reductions are a result of the tax changes proposed, which there appears to be no doubt will be adopted.

The Chairman: What is the percentage of reduction in the capital expenditures on exploration and development since the White Paper was issued?

Mr. Reynolds: I could not give you the figures from the specific date of November 7, 1969. However, in the year 1969 the exploration and development expenditures in the Yukon Territory were approximately $17 million and in the immediately following year $9.5 million.

The Chairman: Are you referring to Canadian expenditures in Canada?

Mr. Reynolds: I am referring to expenditures in the Yukon Territory, not necessarily only by Canadian companies.

The Chairman: It is in the Yukon Territory though?

Mr. Reynolds: That is right.

Mr. Steeves: The Mining Association of British Columbia has prepared economic studies of the Yukon Territory and of British Columbia, two separate studies.

The Chairman: The Mining Association will be appearing before us.

Mr. Steeves: I believe that is the Mining Association of Canada. If you wish I could send you copies of the reports made in the last two years by The Mining Association.

The Chairman: Yes; we would like to receive them as soon as possible, and we shall deal with them promptly.

Mr. Steeves: With respect to depletion, one of the major points of our submission is that referred to by Mr. Powis with respect to the severe restriction in the remaining so-called incentives, which is brought about by the proposed regulations released on July 6, 1971. Because this is such an important document to this discussion, I have included a photocopy of it as Exhibit D to the submission.

The Chairman: The committee will be pleased to note a comment in the third paragraph of the first page of this brief. It refers to conditions before and after the White Paper, and reads as follows:

> While the Senate report reduced the incentives to a greater extent than we recommended in our submission, it achieved a skillful compromise that would have resulted in the mining industry being able to continue its substantial contribution to the Canadian economy.

Senator Connolly: Bully for us!

Senator Macnaughton: You might read the following paragraph.

The Chairman:

> Unfortunately, the Federal Government has chosen to ignore our recommendations and those of your Committee. The Tax Reform Legislation will remove or so dilute the incentives that they will be completely inadequate to meet the essential needs of the mining industry.

I take it that it is this inadequacy that you are going to talk about, Mr. Steeves.

Mr. Steeves: I would like to start with the tax-exempt period and the fast write-off position. Our first statement is that we feel that the alteration of the tax-exempt period will have more serious consequences on the Canadian mining industry, particularly in western and northern Canada, than any other proposals in the act.

The Chairman: Why do you say, "particularly in western and northern Canada"?

Mr. Steeves: Because I think we are just getting started. We have not established the mining industry to the extent that it has been established elsewhere. Also, we face difficulties in the matter of population, transportation facilities, severe climatic conditions, and distances from markets. We do not have any processing facilities out there like the Cominco smelter, which is restricted to lead and zinc.

The Chairman: You can, of course, earn depletion, but earned depletion is not worth anything unless you have income.

Mr. Steeves: You have to get it off the ground first.

The Chairman: You have to get it off the ground first and earn income. The advantage of the system that we had concerning tax holiday was that you still had to get off the ground and earn income, but you could keep it all for a period.

Mr. Steeves: That is right.

The Chairman: You had automatic depletion, but you still had to earn the money in order to take advantage of it.

Mr. Steeves: You had to be successful in order to get any incentive.

The Chairman: Earned depletion is still on the basis that you have to earn money and be successful in order to gain any use from it. You say that what it offers you is not as broad in its sweep as what you did have.

Mr. Steeves: No. We think that the combination we had before was one best suited to the industry, for the types of mines that are now being developed in western and northern Canada, large low-grade mines that are generally in remote areas.

The July 6 press release, which severely restricts the write-off of assets, has been heralded as the replacement for the tax-free period. I make eight points where this is evident from the news release.

One serious mistake made is in the attempt to define the assets that are eligible rather than to exclude the assets that are not to be eligible.

Hon. Mr. Phillips: Are the eight points on the second page of your brief based upon your interpretation of the June 18, 1971 release, or do you have, by any chance, comple-

mentary or ancillary information based on contact with the Department of Finance?

Mr. Steeves: I received the same information that Mr. Ford received from discussions with the Department of Finance. The meeting was of The Mining Association of Canada Tax Committee with representatives of the Department of Finance.

Hon. Mr. Phillips: Was that at the same meeting attended by Mr. Ford?

Mr. Steeves: Yes. I personally was not in attendance, but I am a member of that committee and received a report of the meeting.

Hon. Mr. Phillips: And the report agrees with Mr. Fod's interpretation?

Mr. Steeves: Yes.

The Chairman: We will be hearing from he Mining Association of Canada. Proceed, Mr. Steeves.

Mr. Steeves: To summarize the assets that will not qualify, used assets is one, and we see no reason for eliminating them. If they are part of a new mine's assets, they will presumably be restricted to the recovery of depreciation, as any assets are when they are sold. There is no reason to exclude them.

Regarding minor points, the adjective "mining" is used when describing machinery and equipment. It would seem to imply that milling assets would not qualify. We cannot get a definite answer that this is not the intention. Social costs are grouped with transportation costs. Social costs will not qualify. Social costs are defined as housing, roads, schools, and that type of thing.

Senator Connolly: And hospitals that you might have to build.

Mr. Steeves: That is right. They are grouped with transportation costs and will not be eligible for a fast write-off if they are part of a major expansion; they will not earn depletion. This is in conflict with the June 18 announcement, where transportation assets were separate and only social assets were excluded.

Smelter and refining assets will qualify for the fast write-off only if they are part of a new mine, or if they can be considered an expansion of an existing mine. The addition of a smelter and refinery to an existing mine will not regarded as an expansion of that mine. The expansion is based on the expansion at the mill capacity only.

The Chairman: That is really only playing with words.

Mr. Steeves: Yes, it is. It is vital to us, because we do not have a proper smelter.

Senator Connolly: Can we document that for when we are discussing the problems with the officials?

Mr. Steeves: That is in paragraph "h", under tax exemption.

Senator Connolly: It is documented in your brief, but what is your authority for making the statement?

Mr. Reynolds: The news release. In the fourth line of paragraph "h", the quotation is directly from the recent news release outlining those regulations. It refers to an increase in "the productive capacity of the mine mill".

The Chairman: Let us assume that Bill C-259 exists in some form next year, and that you went out and developed a mining property and started milling and processing operations. To what extent would the regulations that are proposed help you?

Mr. Steeves: You would get a fast write-off on all new assets acquired before production commenced. If you had made a mistake anywhere along the line and had to add something afterwards, it would not qualify.

The Chairman: You mean the idea is to over-buy?

Mr. Steeves: Do not make a mistake, I guess. In the case of a new mine, the social costs would qualify. If you were able to add your processing facilities, your smelter and refinery before production commenced, it would qualify for the fast write-off; but if you had to earn a little money first, it would not.

The Chairman: In the area in which you operate, that is in the west and the north, what would be the period of time between commencing exploration and development and when you might expect to have some earning capacity?

Mr. Steeves: In the Bethlehem situation the property was acquired in 1953, and production commenced on December 1, 1962.

The Chairman: That is when you started to earn?

Mr. Steeves: Our first revenues were in December.

The Chairman: How fast would those revenues build up?

Mr. Steeves: We had a combination of an increase in the price of copper. Also it was quite a successful operation, and revenues built up so that we had recovered our investment of the tax-free period, and the under-depletion allowance, within three years.

The Chairman: Within three years.

Hon. Mr. Phillips: If I remember rightly, at the time of the White Paper hearings you were a rather unique case.

The Chairman: That is right.

Mr. Steeves: There are several things unique about Bethlehem Copper Corporation Ltd. I believe it was the first attempt at a low grade mine; I am not that conversant with the world-wide mining industry, but I believe it was unique in its grade. I think it was the first mine in Canada that introduced Japanese financing; this was done because it was impossible to get it anywhere else.

The Chairman: As I understand it, Mr. Steeves, the problem of financing is not an easy one. You do not simply go out and say, "We have very favourable regulations whereby you get your money back fast, and we need some millions of dollars, so please queue up and deliver it to us."

Mr. Steeves: I think it is even more difficult now, or as difficult now as it was then, because the markets are much tighter now.

The Chairman: The Assistant Deputy Minister of Energy, Mines and Resources, Mr. Austin, speaking in Vancouver the other day, talked about the expected considerable increase in Japanese equity and financing in the mining industry in Canada. Have you any comment on that?

Mr. Steeves: Not really. I am surprised at that statement, but I could not comment on it.

Hon. Mr. Phillips: That is a sufficient comment.

The Chairman: Yes.

Mr. Steeves: Just as an offset, I think a week ago Plaza Developments announced that the Japanese had demanded that they cut their production by 20 to 24 per cent on all of their world mines.

The Chairman: The reason being?

Mr. Steeves: They just do not need it.

The Chairman: Overproduction?

Mr. Steeves: That is right, and they are having smelter problems and pollution problems.

Senator Burchill: Is that with respect to world-wide ore production?

The Chairman: In some minerals.

Mr. Steeves: I think it is in some minerals. The pollution problem is world-wide. Smelters are being forced to cut back to get their emissions within acceptable limits, and one way of getting down to acceptable limits is to reduce production; this is universal, I think. It is particularly bad in the United States, and the Americans are now exporting concentrates where they never had before. They are having some difficulty with their markets.

The next point I would like to raise is with respect to the depletion provisions. The major point in that regard is that we feel the depletion allowance is inadequate; even the earned depletion is seriously restricted by the announcement of July 6, 1971.

The Chairman: Have you mentioned the custom milling and the attitudes?

Mr. Steeves: Yes.

The Chairman: I know it is in your brief, but have you mentioned it in the course of what you have had to say?

Mr. Steeves: I will mention it; it is point No. 7. The definition of the processing assets that would earn depletion is in quotation marks, but what it does not say, I think, is more important. That is in the next line, where we state:

> This will disallow all assets other than buildings and machinery, used assets, that portion of the assets used to custom process foreign ores and, most importantly, even new processing facilities unless they are part of the assets of a new mine or the expansion of an existing mine.

The Chairman: As I understand it, the great advantage of custom milling would be if you had a facility within an economic distance where the production of various new mines could be delivered resulting in a lower mining operation cost.

Mr. Steeves: Smelter studies are now going on in British Columbia; I think everyone is somehow involved in the smelter study. We do not have copper smelting in British Columbia at the present time.

Senator Connolly: You do not have what?

Mr. Steeves: A copper smelter in British Columbia. We are under some pressure from the provincial and federal governments to get one, and we are nationalistic enough that we want one there too. The main problem with the construction of a smelter is the pollution problem. The next smelter that is built has to be within acceptable limits as far as pollution is concerned, and this means it will have to be big enough so that money can be spent on it to control pollution.

Senator Connolly: Is there any possibility of an outfit establishing a new smelter getting any special help in connection with pollution control equipment?

Mr. Steeves: Pollution control equipment will be eligible, I believe, under Bill C-259 for write-off at the rate of 50 per cent.

Senator Connolly: But there is no such thing as direct assistance, either federal or provincial, in a case like the one you described?

Mr. Steeves: No, I do not think so.

Senator Connolly: There may be a tax incentive.

Mr. Steeves: There is a separate capital loss allowance class which allows a 50 per cent write-off on a straightline basis, so you would be able to write it off in two years.

The Chairman: But you do not earn depletion.

Mr. Steeves: No, not on that part of it that would be considered a custom smelter. What I am saying is one mine in British Columbia cannot support a smelter now because you cannot economically build a smelter that small. These feasability studies are not yet complete, so I cannot make that a positive statement.

The Chairman: If you had a smelter in British Columbia that was capable of taking the production from a number of mines, and the economy would justify the movement to the smelter of such production, to what extent would that add to employment and purchasing power?

Mr. Steeves: We are involved in a feasibility study right now; you are about six months too early. We hope to get our first report early in the spring.

The Chairman: Well, obviously, more hands would be required.

Mr. Steeves: I believe Mr. Powis stated that their expansion, which is related to the smelting and refining process, will involve 700 new jobs.

The Chairman: That will be direct employment. We can assume that if a smelter is involved, there will obviously be more hands required.

Mr. Steeves: Very definitely.

The Chairman: And to the extent of the numbers involved, there will be a substantial increase of all the ones who come in to service the people who are working, so it would be quite a contribution, would it not, to employment and to the development of certain areas?

Mr. Steeves: Very much so. I think the area where a smelter will be built will have to be one which is unpopulated. It is going to be a vital contribution wherever it is built and, hopefully, it will be built.

The Chairman: And you may have to develop a townsite?

Mr. Steeves: Yes, and railway lines.

The Chairman: If you were developing a townsite and railway lines in relation to the operation of a custom smelter, would those expenses qualify for earned depletion?

Mr. Steeves: Railway lines definitely would not; they are excluded altogether.

The Chairman: Yes.

Mr. Steeves: The townsite would also be excluded for depletion, unless it was connected with a new mine. The part connected with a new mine would be, but the part that was connected with the smelter would not.

The Chairman: So it looks as though there is an area where you have the provincial governments reaching in the direction of requiring further processing of Canadian mineral production in Canada. In British Columbia have they not introduced a provincial law?

Mr. Steeves: Yes.

The Chairman: The purpose of it, of course, is to have the production further processed in Canada so that Canada will get the benefit from employment and all the incidental expenses. Yet would you say that the thrust of Bill C-259 is such that it puts limits on being able to earn depletion, and therefore creates disadvantages as against encouragement?

Mr. Steeves: I think the limits give insufficient advantage to the importance that we place on the construction of new processing facilities.

Mr. Reynolds: Perhaps I could interject. A point that was made only very quickly, I think, was that if these smelting and refining facilities are not built in connection with a new mine or the expansion of an existing mine they do not qualify for the fast write-off.

The Chairman: That is right. This is the point I was making.

Mr. Reynolds: As well as the depletion.

The Chairman: They do not qualify for the fast write-off either.

Mr. Reynolds: If they are built by themselves.

The Chairman: So you have two handicaps in those circumstances. Firstly, if the smelter were built by itself in, say, British Columbia, you would not qualify for that fast write-off, which is 50 per cent a year.

Mr. Steeves: That is right.

The Chairman: Secondly, with those expenditures you could not earn depletion.

Mr. Steeves: That is right.

Senator Connolly: In other words, if you built a custom smelter without having a mine attached to it, if an independent operator established a smelter.

The Chairman: That may well be very uneconomic.

Senator Connolly: I think you are quite right, Mr. Chairman. I was going to ask the witnesses this. They seem to be talking about special conditions obtaining in northern British Columbia, the Yukon and the Northwest Territories, and to segregate those areas from the more populous areas of Canada. Would they think there should be some special arrangement made for tax inducements to spur development in the more remote areas? Can you envisage that as a possibility?

Mr. Steeves: I think it is important. It depends on how it is done. The first answer is to give sufficient incentives to keep mining in Canada, and then offer additional incentives for the remote areas. This has been recognized to some extent, because there was a bill before the House not long ago, Bill C-187, the Yukon Metals bill, which would have substantially increased the royalties payable in the Yukon. We were able to convince the Government at that time that this would not have left the Yukon even in a competitive position with British Columbia; that it would have been another factor that would reduce the activity up there, and it was withdrawn.

Hon. Mr. Phillips: I think, Senator Connolly, you raised that point last year as well, this whole question of special incentives for areas that are not populated, or are not even open yet.

Senator Connolly: I think it is the kind of thing you naturally think about when talking of mining development in Canada.

The Chairman: You did touch on it.

Senator Connolly: There is probably an inherent difficulty. If you go to certain parts of northern Ontario or northern Quebec, both of which are populous provinces, you may still be in territory that is just as virgin as some of the areas in northern British Columbia and the Yukon.

The Chairman: That is right.

Senator Connolly: If you have to open a townsite. Perhaps the best example is the iron ore development in Labrador and the north shore of the St. Lawrence 25 or 30 years ago, or perhaps a little longer than that. There was really nothing there, but now there are communities. I suppose there might have to be special legislation, such as that the

witness referred to, the Yukon metals bill, that kind of thing, over and above the provisions of the general Income Tax Act.

The Chairman: Of course, the earned depletion is spelled out, as to how you may earn it, and it is to be found in the brief in Exhibit D. If you are going into a new area such as you talk about it does cover a lot of things:

> houses, schools, hospitals, sidewalks, roads, sewers, sewage disposal plants, airports, docks and similar property (other than a railroad not situated on the mine property) acquired to establish community and transportation facilities necessary for the operation of the mine.

So the earned depletion does go some considerable . . .

Mr. Steeves: Excuse me, but that is the fast write-off.

The Chairman: Yes, that is the accelerated capital cost allowance.

Mr. Steeves: That is specifically excluded.

The Chairman: On the earned depletion you get your acquisition cost . . .

Mr. Steeves: No, that is an exclusion. Those are the exclusions there listed.

The Chairman: It says on page 3:

> Eligible expenditures include the following:
>
> (*a*) Canadian exploration and development expenses in the mining and petroleum industries, except for:

What would your view be in connection with "exploration and development expenses in the mining industry?"

Mr. Steeves: We believe this is a very serious limitation, that all exploration and development expenses should definitely earn depletion. We had understood they would, possibly because it is only equitable that they should. The acquisition costs of Canadian resource properties will be excluded, and we can see no reason why they should be excluded.

Senator Connolly: What do you think is the reason they do exclude them? What justification does the department give for excluding acquisition costs?

Mr. Steeves: I do not know. The proceeds of the sale of mineral properties will be taxed. For mining properties, under the tax reform legislation we will now be allowed to write them off, whereas before we were never allowed to write them off. They may feel that is encouragement enough.

The Chairman: On the point you were making a little while ago, while we did not attribute the statements to you, they may have been encouraged by what you said and what we said in our report at page 36, paragraph 3, talking about the representations made by the mining industry:

> All have pointed out that the extractive industries carry on operations on an internationally competitive basis and that any reduction in the incentives heretofore granted would seriously affect their future. They point out their importance in terms of Canada's balance of payments and they emphasize that the development of the Canadian hinterland, in some instances completely unoccupied and virgin territory, would not have taken place without these incentives and will not take place to the same degree in the future if these incentives are seriously reduced.

This is the point you were developing this morning.

Senator Connolly: I do not think it is personal to me. I think it was a general view of the committee.

The Chairman: That is the sum and substance of the submission. I am sorry I am cutting in, gentlemen, but this is the way we operate.

Mr. Steeves: I referred very briefly to paragraph (ii) on page 3 of Exhibit D, in my discussion on depletion. What this says is that any so-called social costs of exploration—remember, this is only exploration—such as housing, presumably camp costs, roads and exploration property, airports, docks, this type of thing, would not earn depletion, even as exploration costs. Paragraph (iii) refers to:

> Canadian exploration and development expenses in the vicinity of a mine.

When we asked what "in the vicinity of a mine" was, I think the answer they gave us was that the courts will decide.

The Chairman: That is interesting. You do not spend any money in the meantime.

Mr. Steeves: Bethlehem is a good example of a mining company that was unable, because of restricted finances, to complete its exploration on its present property, prior to going into production. We had to finance the rest of our exploration from production. In the last two years we financed two new ore bodies on our original properties. One was discovered eight years after we went into production and one was discovered nine years after we went into production. That is just this year.

The Chairman: They qualify as new mines, is that right?

Mr. Steeves: We hope they will, but there is no definition that they will. Neither one of them is in production, and this is just an extreme example. They would certainly be considered to be within the vicinity of the mine because neither of them is farther away than two and half miles from Bethlehem.

Senator Connolly: All the work was paid for out of earnings from the original discovery?

Mr. Steeves: That is right. The effect of this exclusion is that it rewards a company that has sufficient funds to do all of its exploration ahead of time and knows exactly what the ore body is, but a small company with limited finances cannot afford to do that.

The next point, the excluded interest on funded exploration projects, is not going to earn the depletion. That is just another penalty that the little fellow will have to pay.

The Chairman: You can have expenses.

Mr. Steeves: You can, but you cannot earn depletion.

The Chairman: The capitalization of interest provisions now in the Income Tax Act may mean that if you borrow money and before you apply it, to the extent that you do not apply it you can capitalize the interest cost on it.

Mr. Steeves: That is right.

The Chairman: And take the capital cost allowance on it.

Mr. Steeves: Yes. I think this is another argument on it. You can do this in writing up assets to earn the interest, but you cannot do it with exploration costs to earn depletion.

The Chairman: We have noted that. Have you something else?

Senator Connolly: There is one other observation I should like to make here. It applies not only to this set of witnesses but to many other witnesses we have had. There are a great many bits and pieces that we are picking up, on specific points in various submissions. Can we expect that the officials in the Department of Finance or in National Revenue will have their attention drawn to these points, before they come here, so that we can try to have them all dealt with?

The Chairman: Yes, we will draw their attention to these points.

Senator Connolly: It is hard on these witnesses to be put to the trouble and expense of coming here from so far away, without having their points ultimately decided, or at least ultimately discussed in this committee. We cannot do it here now when they are here, simply because the officials are not available to us.

The Chairman: Senator Connolly, ordinarily, when we invite departmental officers, we indicate the areas for discussion, for information and answers.

Senator Walker: Following questions, really, Mr. Chairman.

The Chairman: In substance, yes. That has been my practice as chairman, that they should come prepared.

Senator Walker: That is why they can say yes on the spot.

Senator Flynn: They receive transcripts of these proceedings.

Mr. Steeves: We send them copies of the submission.

The Chairman: And they will get copies of the transcript of our proceedings today and we will give them a summary of the points which we think should be discussed and where we want their answers. They can always say that it is a policy matter and that they cannot answer. However, that is some answer. It means we can go ahead on our own.

Senator Connolly: Yes. Then we can always get the minister, on a question of policy.

The Chairman: Yes, that is right. Is there anything else, Mr. Steeves?

Mr. Steeves: The next point is the abatement system. This first arose on August 26, 1970, in an announcement just prior to the meeting of the provincial ministers of finance. It is a method of attempting to ensure that the mining industry will not be taxed in excess of 50 per cent. In all the submissions that were presented on this point, it was obvious when the White Paper came down that the mining industry was facing a tax of 50 per cent, higher than in any other industry. Many representations were made, including our company, this committee and the Commons committee, on methods of ensuring that this did not happen. Basically they all followed two recommendations, which were included in our previous submission, and I have included them as Exhibit E on page 11. This is a simple method of avoiding something that would have been a very severe restriction on the mining industry and was creating an awful lot of uncertainty.

The abatement system that has been proposed has, we feel, increased the uncertainty rather than resolved it. It will extend it well beyond the date when the legislation will be adopted. The mining companies will be under threat, from the provincial governments, of the necessity of either increasing mining taxes or income taxes, both of which have been almost recommended in the news releases. That would put their tax rate here, as I have illustrated, up as high as 65 per cent. We think there is a much better solution to the problem in accepting any of the recommendations either of our company the other recommendations of this committee. This abatement system is difficult.

The Chairman: On the abatement situation, what would you ask for?

Mr. Steeves: We would prefer, rather than an increase in the abatement, an offset of mining taxes against income taxes, or some type of a floor depletion rate.

Senator Connolly: When you talk of mining taxes, you mean provincial taxes?

Mr. Steeves: Yes.

The Chairman: Expense, then?

Mr. Steeves: Yes.

The Chairman: And also floor depletion?

Mr. Steeves: Floor depletion.

The Chairman: A basic depletion, or what I call automatic depletion?

Mr. Steeves: Yes, a percentage depletion.

The Chairman: On a percentage basis. What percentage have you in mind?

Mr. Steeves: If you had an offset of mining taxes against income taxes, any percentage would reduce the tax rate below 50 per cent, so you could work at 16 per cent depletion allowance, which would give an effective tax rate of about 42 per cent, which we have now for producing mines.

The Chairman: And 42 per cent is a viable base?

Mr. Steeves: That is what we are operating on now.

The Chairman: Is there anything else?

Mr. Steeves: The second point on the abatement system is the illustration I gave here. I am not sure if it is true in all provinces, but I know it is in ours and in several others. Where the exploration is carried out in a province other than the province where you operate, you are still going to end up with a tax rate, as I illustrate here, of 64 per cent with full earned depletion; because the mining taxes are calculated on earnings in the province, excluding any exploration outside the province.

The Chairman: Earnings at the pithead, is it not?

Mr. Steeves: That is right. We have never received an answer on the solution to this.

Hon. Mr. Phillips: Would a simple deduction of mining taxes paid anywhere in Canada solve your problem?

Mr. Steeves: It would certainly relieve it to a great extent. That was one of the suggestions of this committee, a continued deduction of mining taxes, plus a small floor depletion.

Hon. Mr. Phillips: Do you need the floor part? It would be so much simpler if you could live with a straight deduction.

Mr. Steeves: We would prefer the floor, but we could live with the other—still at the same maximum of 33 1/3 per cent.

Senator Connolly: We discussed this at length when making our report on the White Paper. Did we have the minister here on this point?

The Chairman: No.

Senator Connolly: It is a matter of policy, I think, Mr. Chairman, as to whether the 15 per cent mixing tax in the province should be a deductible expense from the tax. It is an expense, as I understand it.

Mr. Steeves: It is going to be disallowed.

Senator Connolly: But at the present time it is an expense, is it not?

Mr. Steeves: Well, most of it is allowed under Regulation 701 as an expense.

Senator Connolly: But it is not a deduction from tax.

Mr. Steeves: That is right.

Senator Connolly: What you are looking for now is a deduction from tax after the tax has been computed.

Mr. Steeves: As Mr. Phillips has said, as an expense it would also probably the satisfactory if we had the depletion in addition.

The Chairman: Even without the basic depletion, deducting the tax as an expense, could you not just expense it? Would that not give you adequate relief?

Mr. Steeves: Plus earned depletion. That would probably be satisfactory.

The Chairman: Well, plus earned depletion; that is whatever you could earn under the rules.

Mr. Steeves: We would prefer to have a basic floor depreciation.

Senator Connolly: It is a matter of policy, I think.

The Chairman: Let us assume you cannot get the best of all these worlds.

Mr. Steeves: Well, I cannot speak for industry, but our company would be pleased to see mining taxes as a deduction plus earned depreciation.

The Chairman: Do you mean a deduction from earnings before?

Mr. Steeves: Either. Preferably from tax, but, if not, just as a straight expense.

The Chairman: A straight expense.

Mr. Steeves: Yes.

The Chairman: Is there anything else?

Mr. Steeves: Just as an example of the uncertainty of this, the original announcement was made on August 26, 1970, and to date only one provincial government has stated its position. Quebec has said that they would pass it on. There are thoughts that Ontario will do likewise, but I have not seen any public statement that that is the case. We have no idea what our provincial government is going to do as far as the abatement is concerned.

The Chairman: When you say, "pass it on," what are you referring to?

Mr. Steeves: This is the additional 15 percentage points that we are going to be allowed.

The Chairman: Yes.

Mr. Steeves: If it is taken up by the provincial government, and Mr. Benson has said they can do what they like with it, then we are facing a 65 per cent tax rate.

Briefly on prospectors, it was almost a unanimous recommendation that prospectors continue to be tax exempt on the proceeds from the sale of mineral properties. They will now be taxed on all of the proceeds. This is perhaps not generally known, but normally this is going to be ordinary income; it will be added right on to the ordinary income. There is one exception, where the prospector is able to sell his mineral properties to a company that will issue him shares. In that case when he sells the shares they are going to be taxed as a capital gain. That is the only exception.

Senator Flynn: On what basis? Will the shares be taxed on the value of the shares at the time of the sale?

Mr. Steeves: Yes, at the time of the sale.

Senator Flynn: By comparison with the selling price of shares later on?

Mr. Steeves: As he sells them, he will pay a capital gain on the proceeds from the disposal.

Senator Flynn: By comparison to the value placed on his shares when he disposes of the property?

Mr. Steeves: No, when he disposes of the shares.

Senator Flynn: Well, what will be the V day?

Mr. Reynolds: The value will be nothing; the full proceeds will be taxed.

Mr. Steeves: Mineral properties have no value on V day.

Senator Flynn: The whole price of the shares will be considered as capital gain?

The Chairman: Yes, and he will really be paying 50 per cent of the full value.

Senator Flynn: I know that, but at the time he disposes of his property to a company and receives shares, those shares could be valued at that time in order to determine the capital gain he will make later on when he disposes of the shares.

The Chairman: But the acquisition cost to him at that time will be pretty nominal.

Senator Flynn: It could vary from one case to the other.

The Chairman: Yes, but relatively the acquisition cost at that time will be pretty low.

Mr. Steeves: Generally his cost would be the cost to register.

The Chairman: And the money spent to develop the property.

Mr. Steeves: Yes, but generally his cost would be his cost to record.

Senator Flynn: Would it not be considered as the deemed realization at the time he disposes of the property?

The Chairman: No.

Mr. Steeves: It will, if he sells for anything other than shares. If he sells for anything other than shares, it will be deemed to be income and will be taxed as income.

Hon. Mr. Phillips: It is, in a sense, a roll-over awaiting the sale of shares.

The Chairman: That is right, if he does it that way.

Mr. Steeves: That is the only way he can claim it as a capital gain.

The Chairman: Is there anything else, Mr. Steeves?

Mr. Steeves: We have made a few points on mineral properties. As you know, mining properties will now be eligible for the write-off and the proceeds from sale will be taxed. There is a serious problem in that mineral properties will be given no value on V day.

Senator Beaubien: Why would that be? Why would mineral properties not have a value?

Mr. Steeves: Well, they are difficult to evaluate. What we have recommended in the brief is that the least that should be assigned to them is their cost, and, if they can be evaluated, that is the value that should be used. What really causes a problem is that surplus accounts are going to become very important. Surplus accounts of companies have extreme importance under the new system. This will influence surpluses and how they can be distributed. That is a very technical discussion and I would prefer that you discuss it with some tax technicians. But you can see some real problems there. Any asset not given a value on V day is going to cause problems.

The Chairman: Everything is going to be gain.

Senator Beaubien: That is nonsense.

Mr. Steeves: The proceeds are going to be taxed. Sixty per cent of the proceeds of mineral properties sold in the first year will be taxable, and then from then on it will increase by 5 per cent. I think it is in the thirteenth year that 100 per cent of the proceeds will be taxable. Costs are not going to be allowed as an expense, and what we are saying is that costs should be allowed as an expense, if you are going to tax the proceeds. It is only equitable. If you can establish the costs, you should be able to offset them against the proceeds.

The Chairman: Well, the only way in which you can resist that is to say that the proceeds of sale are income.

Mr. Steeves: They are classed as income now.

The Chairman: If they are income, there is no question of gain.

Mr. Steeves: That is our next point. We say that they are long-term assets and should be taxed as capital gains so that one-half of the gain would be taxed.

There are certain procedures in placing a mine into production. I think option agreements are unusual to mining companies. We described it in more detail in our original submission, but, generally, it would involve the transfer of properties into a new company at the time that you are ready to place them into production. This type of procedure will be frustrated by the provision that they will be taxable, and we think that there should be a provision for the tax-free roll-over of mineral properties, particularly in a related and non-arm's length transaction. We think there should be provision for roll-over in any case, but particularly if it is non-arm's length.

The Chairman: On the theory that really there is no change.

Mr. Steeves: That is right. It is only a corporate change.

The Chairman: The style is changing a bit.

Mr. Steeves: On the subject of capital gains, one point we have made here is that we feel capital losses should be deductible from other income of a corporation rather than from capital gains only, if not in whole then on some criminal rate as there is for individuals. We have suggested the 10 per cent reducing balance rate that they use for such items as intangible assets, goodwill, and this type of thing. One-half of all capital gains will be added to the income of individuals, and we feel that this could result in an increase in the marginal rate of individuals on total income. We think that the capital gains should be taxed separately.

The Chairman: Of course, Mr. Steeves, we went through that the first time around. We thought that the capital gains tax should be a separate tax, and this would have avoided that problem. But, having regard to the way it is written into this bill it may be too late on a substantial point such as this to make any change. You may just have to live with it.

Hon. Mr. Phillips: We had a major success on integration, and a major failure on that point.

Mr. Steeves: I hail your success on integration.

The Chairman: You cannot win all the time.

Mr. Steeves: No. The employees' share options—I think this is just a reiteration of the same point. This will add to the income of the employee and he could end up losing the whole advantage because his marginal rate would be such that he might lose the whole incentive. Our comments on the depletion allowance are the same.

The Chairman: The same as those of Mr. Powis?

Mr. Steeves: No, I am sorry, I am referring to the dividend tax credit. Since we were told that the integration was dropped, we think that the artificial gross-up of 33-1/3 per cent has no basis in equity or theory, or anything else any more, and it could result in an increase in the total marginal rate of the taxpayer.

The Chairman: As the document that has been produced says, it helps the people who have smaller dividend income and it may tax a little more heavily those who have a greater dividend income, which suggests that that is the way the tax burden is to be carried. Have you anything to say on that?

Mr. Steeves: Well, I would challenge the point that the gross-up itself helps anybody. I feel that the dividend tax credit is a good system, and this is something that this committee recommended.

The Chairman: Is not the gross-up part of the way in which, ultimately, when you are dealing with sufficient income of an individual, that you do tax him more?

Mr. Steeves: It could. I guess I would have to work out some examples.

The Chairman: They have some examples in the summary.

Senator Walker: What you are doing now is making a suggestion regarding the overall principle rather than confining it to your own mining operation?

Mr. Steeves: The specific example in our submission is the loss of the 20 per cent depletion allowance to individuals as well as the gross-up theory. They chose a tax increase of 39 per cent, but if the province does not pass along the dividend tax credit it could end up as a tax increase of 66 2/3 per cent.

Hon. Mr. Phillips: I think you will find, however, that isolated in the grossing-up item, the dividend tax credit now works in favour of those with lower incomes and adversely affects those with higher incomes.

The Chairman: I think the cut-off is supposed to be around 40 per cent.

Hon. Mr. Phillips: Forty per cent.

The Chairman: Below that cut-off there is some advantage. Above it there is none.

Senator Beaubien: Mr. Chairman, you need the co-operation of the province because the bill says that you take off four-fifths of the gross amounts, not 100 per cent. So the province has to give you the other one-fifth. And if you do not get it from the province the tax is tremendously increased.

The Chairman: It is bound to be. Is there anything else? These are your general observations. We have dealt with your special problems.

Mr. Steeves: In the area of property holdings—this is a point we made previously—the mining companies are required to provide housing in remote areas. We often operate them at a loss, and we hope that we will not be prevented from claiming the loss on the housing because it is cleared by depreciation. It is a very real loss.

In the section on non-residents I think the major point is what they call the thin capitalization theory. We try to restrict the amounts of equity that we give out when we arrange new financing on the property. This would seem to encourage financing to at least one-third of the equity in order to be able to claim interest as a deduction. It is an unusual provision in that it will penalize the Canadian company rather than the non-resident company at whom we feel it should be aimed. We have a section on partnerships—

The Chairman: We have had a pretty fair discussion on partnerships, Mr. Steeves, and our thinking has crystallized pretty much.

Mr. Steeves: Our only point there is that in order to spread the risk of increased costs in mining ventures we will often form syndicates.

The Chairman: Do you mean joint ventures?

Mr. Steeves: Yes.

The Chairman: Is there not an exclusion there?

Mr. Steeves: No, we have no exclusion.

The Chairman: Is not there an exclusion on partnerships in connection with explorations?

Hon. Mr. Phillips: I do not think so in the partnership document.

The Chairman: I thought there was. In any event we have had the problem presented to us regarding joint ventures in the development of mining properties, that very often they take the form of a joint venture agreement. The question we have to consider is whether the joint venture has the character of a partnership and, therefore, is subject to the partnership provisions.

Mr. Steeves: That is exactly my point.

The Chairman: We have had that point and we are looking at it. Is that all?

Mr. Steeves: That is all.

The Chairman: Thank you very much.

Senator Flynn: Mr. Chairman, may I say something? You will notice the arguments brought forward by our witnesses in quoting paragraphs 3 and 4. On page 1 the first sentence of paragraph 6 reads:

> We are puzzled that the Federal Government, now faced with rising unemployment, economic slowdowns and unsettled international conditions, is proceeding to implement legislation that would retard an industry that has displayed unprecedented growth and productivity.

Senator Burchill: Does your brief contain comparison with the regulations in the United States, particularly with respect to depletions and incentives to new mines?

Mr. Steeves: We made statements concerning that during our last appearance before this committee.

Senator Burchill: I know you did, but does the new legislation vary from the other in that respect?

Mr. Steeves: Not materially. After our last appearance I supplied some supplemental information with regard to Australia and the United States, in which the legislation was compared.

The Chairman: That is right.

Senator Burchill: I take it that the legislation in the United States is more favourable to the mining industry than this?

The Chairman: Mr. Steeves, clause 96(1)(*d*) will assist your consideration of the question of partnership and the exclusion to which I referred.

Mr. Steeves: Thank you very much, Mr. Chairman.

The Chairman: Thank you very much.

The Chairman: The next submission is by The Canadian Gas Association. Appearing are: Mr. G. E. Miller, C.A., Comptroller and Assistant Treasurer of Union Gas Company of Canada Ltd.; Mr. R. F. Sim, Assistant Secretary, TransCanada PipeLine Limited; and Mr. E. W. H. Tremaine, Treasurer and Assistant Secretary, The Consumers' Gas Company.

Do you intend to make an opening statement?

Mr. G. E. Miller, C.A., Comptroller and Assistant Treasurer, Union Gas Company of Canada Ltd.: Mr. Chairman and honourable senators, my name is Gerald E. Miller, Chairman of The Canadian Gas Association Taxation Committee, and Comptroller of Union Gas. On our panel we have Mr. Raymond Sim, sitting on my right, who is also a member of the Association's Taxation Committee. He is Assistant Secretary of TransCanada PipeLine. On my left is seated Mr. Edward Tremaine, Treasurer and Assistant Secretary of The Consumers' Gas Company.

Our brief deals with six points which we will discuss. I might also mention that it has been submitted to Mr. Benson in exactly the same form.

The Chairman: When was the submission made in relation to Bill C-259?

Mr. Miller: Before September 1.

Senator Walker: By "submitting", was it just handed to him, or did you appear before the minister?

Mr. Miller: We mailed it to him with a covering letter, to which we received a reply. We volunteered to meet the minister and he indicated that if he felt it was necessary to discuss the matters further with him he would invite us to appear before him.

The Chairman: And you had no subsequent invitation?

Mr. Miller: That is correct.

The Chairman: Well, here is your forum.

Mr. Miller: The attraction of adequate debt and equity capital at acceptable cost has always been a serious problem for the natural gas industry, which is very capital-intensive. This problem is becoming increasingly important as the industry is facing unprecedented demands for capital expansion to provide vital supplies of energy for the development of the Canadian economy.

As indicated by the Ontario Committee on Taxation in its 1967 report, Volume II, page 108, land, buildings and equipment represent for the transportation companies more than three times the proportion of total net assets and close to 10 times the proportion of total sales of all other Canadian companies. So we are in fact extremely capital-incentive.

Our first point is that we feel that Canadians should be encouraged to invest in equities of Canadian industry. We are concerned that the proposed dividend tax credit system and high rates of tax on capital gains substantially increase the tax burden on Canadian equity investments.

At page 8 of our brief we provide an example, headed "Schedule 1." The centre column takes us through the calculation of tax on the dividend tax credit system and capital gains tax system. At the foot of the page a tax increase of 97 per cent is indicated. So, for this particular example the result of the proposed bill C-259 would be to increase the tax burden by 97 per cent.

Hon. Mr. Phillips: That is, however, due basically to the capital gains tax, not to the treatment of the dividend tax credit.

Mr. Miller: Yes, that is true.

Senator Connolly: The capital gains tax shown on the table is $150.

Mr. Miller: No, it is $68; the $150 is the amount of the taxable capital gain.

Senator Connolly: The capital gains tax is $68 in each case?

Mr. Miller: That is right.

Senator Connolly: Mr. Chairman for the sake of the record perhaps we could have Schedule 1 reproduced at this point of the proceedings. It would not be possible to follow the proceedings without reference to this table.

Hon. Senators: Agreed.

The Chairman: Schedule 1 will be included in the record of the proceedings at this point.

Schedule 1 follows:

Schedule 1

COMBINED EFFECTS OF PROPOSED DIVIDEND TAX CREDIT AND CAPITAL GAINS TAX

A Canadian investor, with a marginal rate of tax of 45 per cent purchases shares in a Canadian corporation at a cost of $3,000. The shares are held for a two year period in which dividends at a rate of 5 per cent are received, and a capital gain of $300 is realized. His tax position under the present and proposed systems would be as follows:

Tax calculation	Proposed 4/5	Proposed using 5/5 credit	Present 20%
Dividends received	$300	$300	$300
Taxable credit	100	100	—
Taxable dividend	$400	$400	$300
Tax thereon	$180	$180	$135
Tax credits	80	100	60
Tax	$100	$ 80	$ 75
Taxable capital gain	$150	$150	
Tax	$ 68	$ 68	
Net cash income and tax increase			
Total cash received in excess of cost	$600	$600	$600
Taxes paid	168	148	75
Net cash income	$432	$452	$525
Tax increase	124%	97%	

Senator Connolly: It might be useful, Mr. Chairman, for the witness to take us through this table.

The Chairman: The witness should expand his points to whatever degree he feels necessary. If you wish, you may call on your colleagues on the panel for assistance.

Mr. Miller: Very well, I will call on Mr. Tremaine to explain Schedule 1, columns 2 and 3.

Mr. E. W. H. Tremaine, Treasurer and Assistant Secretary, the Consumers' Gas Company: A discussion of the schedule should ignore column 1, which indicates the effect of the provinces not adding the one-fifth. However, the indications are that they will do so.

The column to the right, the present 20 per cent tax credit, indicates the tax under the present tax act giving effect to the 20 per cent tax credit but ignoring capital gains, which does not exist today. The centre column, the 5/5 proposed, indicates a tax credit together with a capital gain. The total taxes payable under the proposals would amount to $148, as indicated at the foot of the table, compared to $75 in the past.

It was mentioned earlier that the principal amount of the increase is a result of capital gains. However, the tax on the dividend itself after deduction of the $68 tax on the capital gain would be $80, an increase of $5.

The Chairman: The figures in the schedule assume the taxable gain at $150.

Senator Beaubien: That is half the profit.

The Chairman: You have assumed that that would only occur with disposal of the shares.

Mr. Tremaine: That is correct.

The Chairman: So currently, from year to year there would just be tax at the marginal rate, and the dividend tax credit.

Mr. Miller: But assuming that stock market opportunities continue to rise over a period of years, and eventually, possibly many years later, you end up selling the stock, you are in fact accruing a tax cost.

The Chairman: Yes. But every year that you live, hopefully for a long period of time, you are accruing tax cost if you are earning more income.

Hon. Mr. Phillips: What you are saying is that because there is a capital gains tax, you simply get into a higher rate of taxation. Is that not elementary?

Mr. Miller: We are attempting to point out that with the change in the tax credit system, together with the capital gains tax, the attractiveness of the equity market for investment will be less than it was before.

We feel that the rates of capital gains tax are excessive. Possibly instead of one-half of the capital gains being taxed, in a developing country like Canada it would be more appropriately taxed at one-quarter.

Senator Connolly: This is a matter of policy. I do not say that you are precluded from discussing policy, because we are glad to hear your views on policy also. Firstly, it is policy, and secondly, it applies not only to the gas industry but to all of industry.

Mr. Miller: But the point of difference is that the natural gas industry is far more capital intensive and requires far more capital financing than Canadian business generally. It is far more critical to us.

The Chairman: You mean that the industry finances more by way of equity than by borrowing?

Mr. Miller: We are concerned about both equity and debt. We attract capital in balance of debt and equity. At the last meeting we attended, in our presentation we said that the industry's average is probably something like 60 per cent of debt and equity. We are concerned also about debt. That is our second point.

The Chairman: The situation you are developing is that it will affect your offering of shares. But it will affect any company that offers shares.

Mr. Miller: That is quite true.

The Chairman: The level of competition is not changed.

Mr. Miller: That is so. Our industry provides energy to the public generally. It is, if you like, a public service. Any increased capital cost has to be passed on to the customer. So it contributes towards inflation.

The Chairman: On the other hand, the Government has to finance its operations. There does not appear to be much of a limiting feature there up to the present time. They need it, so they tax.

Mr. Miller: That is true. Fortunately, if the yardstick is capital investment and we happen to be heavily capital-intensive, we get stuck with a higher portion of the burden.

The Chairman: What do you suggest should be done for your industry?

Mr. Miller: We have thought, in terms of the overall industry, of a lower capital gains tax rate. I think there is merit in considering a reduced capital gains rate for certain industries that are particularly capital-intensive.

Hon. Mr. Phillips: How would you determine that? What we are trying to do here is to suggest relief to cover specific economic segments of the community, having regard for their special problems. We are beyond the stage of considering whether a capital gains tax should be introduced, or whether it should be brought into income to the extent of 50 per cent thereof.

The Chairman: Or whether it should be selective.

Hon. Mr. Phillips: Yes. It would appear to us that to try to make it selective is a novel idea, but it would have to be specific in its application. We are looking to see whether you have special problems in your industry aside from the overall impact or thrust of the legislation.

Mr. Tremaine: One of the specific problems of our industry is that we have to raise a great deal of capital, both equity and debt. We feel that the equity capital should be raised in Canada if possible. We are afraid that some of the risk capital that is available today may be steered onto the debt side of the market rather than the equity side. If the general principle of capital gains has in effect been established, then we are suggesting that we revert back to the old dividend tax system and that possibly it be increased to 25 per cent.

Hon. Mr. Phillips: I think you make a point in an academic form, but I am not so sure that it can be of any value in terms of dealing with specific legislation.

Mr. Miller: We understand that. It is a matter of policy. It would be tough to change at this time. But we cannot get past the point that it will have an unfavourable and adverse effect on our particular industry, and we thought that we should point that out.

Senator Connolly: It is appropriate that you should point that out to us. An industry as important as this has an obligation to point it out so that we might have a better overall picture.

The Chairman: Attention will be focused on it at any time rates are increased. Some of the reasons given for a rate increase is the impact of the dividend grossing up and capital gains. The public generally may come to a realization then, more so than the investor.

Hon. Mr. Phillips: If you wanted to make something out of it, it would appear to me that you would have to suggest a ratio of funded debt to paid-in capital, so that if the paid-in capital was in excess of the funded debt, in such event the dividend tax credit should be handled in the following manner.

With the approval of the chairman, I would like you to consider that. If anything can be submitted to us under that heading, we would have something to work on. I can see your point about equity finances as against funded debt. If you said that equity paid in common stock was $2 for every $1 of funded debt, or $3 for every $1 of funded debt, and that in such event the dividend tax credit should be in the following manner, National Revenue could then look at the statement, and it would be simple for them to determine in which category the dividend tax credit should fall.

The Chairman: We know what the problem is. We are not making decisions right here and now. Have you something more to add?

Mr. Miller: Our second point is that Canadian industry must seek foreign capital in addition to Canadian funds, and we feel that foreign investors should be encouraged to invest in debt rather than equity capital of Canadian industry. We are particularly concerned about the proposal to increase the rate of withholding tax on interest paid to non-residents on debt capital.

Hon. Mr. Phillips: I believe somewhere down the line, Mr. Chairman, in our White Paper considerations, we suggested the elimination of withholding tax on foreign investment in order to encourage the inflow of foreign currencies provided it was invested in funded debt rather than in equity.

Mr. Miller: Mr. Chairman, we have found that section in your report; that is quite right.

Hon. Mr. Phillips: Are we not right on that?

The Chairman: Yes, but we were ignored.

Hon. Mr. Phillips: It is at page 77, paragraph 12; we are right on the point there.

Senator Connolly: Could we have it read?

The Chairman: At page 77, paragraph 12, we state:

> Your Committee strongly objects to the proposal of paragraph 6.36 of the White Paper to increase the Canadian withholding tax rate to 25 per cent except in the case of payments to countries with which Canada has a tax treaty. With particular reference to interest, the Committee feels it would be a grave mistake to inhibit the lending of money into Canada (in contradistinction to the acquisition by foreigners of equity share positions in Canadian corporations) and the Committee is convinced that a substantial portion of available funds from foreign jurisdictions will derive from countries with which Canada does not have a tax treaty, such as Switzerland. The Committee does suggest to government that it seriously consider the elimination of all withholding taxes on interest payments to arm's length foreign lenders.

Hon. Mr. Phillips: We took the position that we were saying to foreign investors, "Come into Canada as long as you do not take our patrimony—that belongs to us as much as we can retain it—and there will be no withholding tax on the interest paid to you." That is the recommendation we made, and we thought it made sense.

The Chairman: It was not accepted.

Senator Molson: It still makes sense, Mr. Chairman.

The Chairman: Is there anything else that you want to add?

Mr. Miller: Not really, except to say that in our presentation in June of 1970, we brought this point out and I believe another group brought out the same point at that time. We feel it is every bit as important now as it was then.

The Chairman: We are not receding from what we said. You just heard one of the senators make the comment that it still makes good sense, but what can you do about it at this stage?

Mr. Miller: Our third point, Mr. Chairman, is that the association feels that all expenditures laid out to earn income should be tax deductible.

The Chairman: That is supposed to be a generally accepted principle.

Mr. Miller: We find it not to be so. I believe Mr. Tremaine has something to say on this point.

Mr. Tremaine: I have just one specific item, and again it involves the raising of capital. The commissions payable to investment dealers on the issue of debt securities, both short term and long term, are not allowed under the proposed Tax Reform bill and they are not allowed under the present Tax Act. We feel quite strongly, because we represent a capital-intensive industry, that this would be an ordinary cost of carrying on our business.

The Chairman: On the other side of the coin, the recipient of the commissions pays income tax.

Mr. Tremaine: That is right.

Mr. Miller: I might add that the commissions on the issue of equity are similarly non-deductible, whereas other expenses involved in equity issue are deductible.

Senator Connolly: Such as?

Mr. Tremaine: Printing and legal costs, audit costs, and that type of thing.

The Chairman: What specific suggestion have you in relation to that? Have you thought of how it should be dealt with and where?

Mr. Miller: Yes, we have. Under the present Income Tax Act and the new bill expenses incurred to raise debt and equity capital, other than commissions, are currently deductible. We would simply change the wording of those sections to allow commissions as a current deduction as well.

The Chairman: In doing that the Government is getting its tax revenue on an acceptable basis; that is, anyone who receives income pays income tax on it, and then the theory is that if it is an expense item where you are putting out money to earn income, it should be deductible.

Mr. Miller: That is right.

Mr. Tremaine: There are specific recommendations at the bottom of page 10, where we suggest that section 20(1)(*e*)(iii) should be deleted.

Senator Connolly: Mr. Chairman, it seems to me that part of the rationale behind this section was to get at "expense account living" and perhaps other charges that we thought to be improper and, in any event, hard to police, but what the witnesses are talking about does not fall into that category at all. They are talking about legitimate expenses incurred in bond issues and stock issues, which is part of the normal business operation of firms in their industry.

The Chairman: Yes, I understand that.

Senator Connolly: I just want to make the point on the record that even though section 20(1)(*e*)(iii) does talk about the expense of issuing shares and of borrowing money, it is directed specifically to this.

Hon. Mr. Phillips: Except that in addition, Senator Connolly, on page 11 of the brief, the suggestion is made that in the overall conception of deductibility all expenses should be a charge against income, but to the extent that it is not presently a charge against income under the new bill, 10 per cent of the accumulated balance of that portion of the expense which is not presently allowed be allowed as a deduction. Let us assume you had $1 million worth of accumulated expenditures, which, under the bill, would not be allowed as an expense, the suggestion is that $200,000 of that be allowed as a deduction in a given year, so that ultimately it would all peter out and go into income.

That goes back to the old conception that all dollars that flow in are taxable income, and all dollars that flow out are an expense.

Senator Molson: This would be a deferred expense item.

Hon. Mr. Phillips: Yes. In other words, under the bill which we are considering, all non-deductible expenses

should be allowed to the extent of 10 per cent of the accumulated balance in a given year.

If we considered that, Mr. Chairman, then instead of dealing specifically with underwriting expenses and the like, we would, at least be dealing with a fundamental principle.

Mr. Miller: The point of difference might be, though, that we feel commissions should be currently deductible whereas other so-called "nothings" should be on a ten per cent basis.

Hon. Mr. Phillips: Amortized.

Mr. Miller: Yes.

Hon. Mr. Phillips: This is an interesting suggestion, Mr. Chairman, and worth considering.

Senator Molson: Are we not running into the question here of whether this expense is laid out in order to earn income?

Hon. Mr. Phillips: The answer is yes. We are back to a philosophic concept, that all moneys in are income; all expenditures are deductible.

Senator Molson: I think at times we have agreed with that principle.

The Chairman: There might be more justification for that now that we have broadened the tax base. it might be said under the present act that this was not laid out to earn income.

Senator Molson: No, now we have got capital gains that currently become income, and some other changes that you point out, Mr. Chairman, that perhaps does change this aspect a bit. It is possible.

Hon. Mr. Phillips: It is an interesting point.

The Chairman: It is an interesting thing, and we should have a good look at it.

Mr. R. F. Sim, Assistant Secretary, TransCanada Pipeline Limited: On page 11 of our brief we draw a differentiation between expenditures laid out to earn ordinary taxable income and expenditures laid out to earn taxable capital gains. I think under any income tax system you will still be faced with the present problem of determining what is allowed expenditure and what does not earn completely taxable income. We are suggesting here that clause 14(5)(*b*) of Bill C-259, as it is now written, will allow 50 per cent of this "tax nothing" category, and this is why we feel this if those expenditures are laid out to earn capital gains. An expenditure which earns a fully taxable income should be fully deductible, and we are suggesting the 10 per cent write-off.

The Chairman: If we are still talking about the financing of a company by means of debt, would you say that the cost of raising that money is laid out to earn a capital gain? Would you?

Mr. Sim: No.

The Chairman: I would not think so.

Mr. Sim: The debt would normally be used to supply working capital to the company, which goes again in turn for current expenditure to earn current income.

The Chairman: You look through the physical act of the getting of the money and you look at the purpose for which you got it. Maybe that is a sensible way of looking at it.

Senator Macnaughton: I think so.

The Chairman: If the purpose is to provide working capital as against providing capital assets in the form of buildings and such things, would you make that distinction?

Mr. Sim: No, I would include the acquisition of assets, because the assets are really part of the income earning process and they are depreciated under the act. They are as necessary to earn the income of business as working capital.

The Chairman: You say there is another link in the chain that should be forged there to get the use of the money, and if the use of the money is to earn money, whether it is by way of expenditure on capital assets or for working capital, the cost should be deductible.

Mr. Sim: Yes.

Mr. Tremaine: The cost of obtaining money is really no different from the cost of obtaining any other assets.

The Chairman: That is right. If you confine it to capital gains, maybe you are putting yourself in the position that you should only get the half rate.

Mr. Miller: We mentioned earlier that this was not really the sole item involved in the cost of raising money that was not 100 per cent deductible in a year. The cost of legal fees and suchlike involved in raising capital are in fact deductible; they meet the present test.

The Chairman: It is a very interesting point, and I think we should have a good look at it. Is there any other question anybody wants to ask?

Senator Burchill: How many companies does your association represent?

Mr. Miller: We represent production, transmission and distribution companies. We also represent manufacturers, but we are not speaking to their problems here; their associations speak for them.

Mr. Tremaine: There are 30 to 40; something in that area.

Senator Burchill: Where are they principally located?

Mr. Tremaine: Right across the country west of Quebec.

Senator Burchill: Nothing east?

Mr. Miller: Yes, we have Gaz Metropolitain, which is a distribution utility in Montreal, Quebec.

Mr. Tremaine: There are none east of Quebec.

Senator Flynn: Quebec City, do you mean?

Mr. Tremaine: I am not sure how far Gaz Metropolitain goes.

Mr. Miller: We do go across the country. We include Westcoast Transmission, TransCanada PipeLine Limited, the Alberta utilities, the Ontario utilities. Really the production, transmission and distribution facilities across Canada.

The Chairman: Are TransMountain included?

Mr. Tremaine: They are an oil pipeline.

Mr. Miller: I do not believe they are included.

The Chairman: Are there any other questions on this point? If not, we will move to your next point.

Mr. Miller: There were two other items that we might mention very briefly. We talked about them in our last brief. It is not at all clear that perpetual rights of way would qualify as eligible capital expenditures, subject to acquisition. We feel this should be clarified.

The Chairman: When you refer to perpetual rights of way, you mean for the laying of a pipeline?

Mr. Miller: Yes, sir.

The Chairman: What is the point on that?

Mr. Miller: A pipeline has a rather long life; how long a life is quite controversial. I would say it is as much as a hundred years, possibly. We cover ourselves by gaining a perpetual easement or right of way, so that we are covered on that line for its life. The right of way has a useful life similar to that of the pipeline itself, yet for business purposes we depreciate it in arriving at our income for shareholder reporting purposes, but for income tax purposes it is not tax deductible.

Senator Flynn: The right of way itself?

Mr. Miller: The cost of obtaining the right of way, the payment to the landowner. Under the present act such costs are not deductible in any way, shape or form.

Senator Flynn: Because they are capital assets?

Mr. Miller: That is right.

Senator Flynn: They are just like a piece of land.

Mr. Miller: Not really. A point of difference is that we acquire a right of way solely because we are putting a pipeline in. Once the pipeline has completed its useful life, that right of way has no further use either.

Senator Flynn: The pipeline has to be replaced.

Mr. Miller: It is most unusual to use the same right of way for a replacement line.

Senator Flynn: It seems to me this is the same problem as with water.

Senator Connolly: An aqueduct.

Senator Flynn: I know of some that have been in existence for 100 years, or perhaps 200 years.

Senator Connolly: Some of the Roman aqueducts are still used.

Senator Flynn: They are always in the same right of way, but are replaced. Do you figure that once the pipeline has served its time the right of way would not be used any more?

The Chairman: Do you depreciate the pipeline itself?

Mr. Miller: This might help explain the situation. For proper, generally accepted accounting shareholder purposes, it is typical to depreciate the pipeline, and also to amortize or depreciate the cost of the right of way.

The Chairman: Yes.

Mr. Miller: I cannot speak for the whole industry, but I would expect to see the same rate of depreciation generally for the right of way as for the pipeline.

The Chairman: You do presently depreciate the pipeline itself, as against the right of way or easement?

Mr. Miller: We depreciate both.

The Chairman: I am talking about for tax purposes.

Mr. Miller: For tax purposes we are denied it. We claimed it, but we were denied the deduction.

Hon. Mr. Phillips: The reaction is that if a person buys a piece of land and puts up an apartment on it, if he does not get an amortization on the capital cost allowance on the land, why should he get it on the right of way? Probably the answer is that this is probably a piece of land, in the ordinary sense, on which you can put up from time to time a different type of structure, to adjust itself to the economic needs or changing conditions or fashions of living or industrial development and the like. I suppose also that if you had absorption of the energy which you are pushing through that line, you may have a valueless right of way.

Mr. Miller: That is true. It is a specific matter.

Hon. Mr. Phillips: I am not quite trying to fathom Senator Flynn's mind, because I see the way it is working. There is a distinction. The question is whether it is sufficiently differentiated to warrant different treatment.

Senator Flynn: I doubt that very much. I cannot see it.

Senator Molson: There must be some precedent in the transmission lines for electric power, surely, that are fairly common. I wonder what has been the policy for the right of way for electrical transmission lines.

Hon. Mr. Phillips: Does anyone know?

Mr. Miller: To the extent that they are taxpaying investor-owned corporations, the same tax rules would have to apply.

Senator Molson: They have been in business a great deal longer than you have.

Mr. Miller: It is the same piece of land.

Senator Molson: The right of way is a piece of land, a strip of land, and it is the same general principle, surely, as the pipeline.

The Chairman: You can get an easement to walk over a strip of land or to drive over a strip of land.

Senator Flynn: If you buy a right of way, it is only because you do not need to buy the land itself. You save money by buying the right of way instead of the land.

The Chairman: That is right, except that if you put a pipeline on a piece of land it is pretty hard to use it for anything else.

Senator Flynn: You can use the surface for farming.

The Chairman: Yes.

Is there anything more on that?

Mr. Sim: Mr. Chairman, I think the distinction is between a lease and the land itself, a capital asset. Really a right of way is similar to a lease. In fact, it is a lease. You have the right to use someone else's property, but in this case for an indefinite period of time.

Hon. Mr. Phillips: I could argue it both ways, depending upon my retainer.

Senator Flynn: Which way would you win?

Senator Molson: Either way.

Senator Beaubien: When you have a right of way to place a pipeline, you cannot use it for something else.

The Chairman: If they buried the pipes there, the farmer could grow crops.

Senator Beaubien: I mean that whoever has the right of way can only use it for a pipeline.

The Chairman: Yes.

Senator Beaubien: And therefore if you have no more gas to put through the pipeline you lose the value of the right of way.

Senator Flynn: No, because you could sell it back or you could use it for something else.

Senator Beaubien: If people stopped using gas.

Senator Flynn: Then you asset becomes obsolete, like a railroad bed.

Senator Connolly: Perhaps I had better not summarize it. Perhaps I had better ask you to do so?

Mr. Sim: We feel there is an anomaly in the act, that leasehold cost or rentals, etcetera, if they are laid out to produce income are deductible, but in this case we have a perpetual lease and it is not deductible because there is no provision in the capital cost allowance regulations to cover perpetual leases.

Senator Connolly: If you are going to call an easement a perpetual lease, I suppose I can accept what you say. What you do is you prepay the rent, if you are going to call it a lease; but in fact you are buying an easement, and what you want here in both cases is a deduction as an expense incurred in earning income, just as much as an expense to buy and lay the pipeline is an expense. Is that so?

Senator Flynn: Or if you have to repair the pipeline?

Senator Beaubien: And if you sold it at a profit, you would have to pay a tax on the profit.

Mr. Miller: Mr. Chairman, our point here was that we were seeking clarification. There is a possibility that the section in the bill on eligible capital expenditures has been designed to allow or recognize these perpetual leases or rights of way. But it is not clear. It is section 14(5)(*b*), "eligible capital expenditure". Some people feel that it is covered and some feel that it is not. We feel that it should be clarified.

The Chairman: It says that "eligible capital expenditure" means:

> —the portion of any outlay or expense made or incurred by him, as a result of a transaction occurring after 1971, on account of capital for the purpose of gaining or producing income from the business, other than any such outlay or expense—

Then there are all the exclusions. It certainly takes some analysis to decide which way it goes.

Mr. Miller: We have had experts saying, "yes, it is included," and we have had experts saying' "No, it is not included."

The second point on it is that if there were an eligible capital expenditure it would be subject to tax deduction only to the extent of 50 per cent. What can be more a business expense, quite independent of capital gains, than a perpetual right of way? It should be allowed 100 per cent.

The Chairman: I suppose they provided the 50 per cent because they were thinking in terms of capital gains tax.

Mr. Miller: We think this is erroneous thinking.

The Chairman: I see. Is there anything else?

Mr. Miller: Our fifth point is this. We also feel that the base for earned depletion allowances should include all exploratory development expenditures as defined in the bill. Would you like to discuss that?

Mr. Sim: Again, this is a reference which was brought up in the two briefs prior to this and the Department of Finance news release which covers the proposed regulations on depletion allowance. The definition of eligible expenditures on exploration and development expenditures for purposes of computing depletion is different from that contained as deductible expenditures in the bill.

The Chairman: Have you suggested any language for meeting your point?

Mr. Sim: This would be in the regulation which would be forthcoming. We are suggesting that the definition in the regulation for this base of earned depletion be the same as the definition of exploration and development expenditures which are actually contained in Bill C-259, which includes the acquisition of oil and gas properties and like expenditures.

The other point was that the change in depletion from the old concept of 33 1/3 per cent of income to one-third of the eligible expenditures would greatly increase the tax burden.

The Chairman: Those regulations you are addressing yourself to came out in July, 1971. Do you think the exclusions in the earned depletion section should be changed?

Mr. Sim: Yes.

The Chairman: Well, that is in line with what the people we heard earlier had to say.

Mr. Miller: We are particularly concerned, for example, about the cost of the acquisition of Canadian reserves. We feel it should be a proper credit for expenditure in arriving at the earned depletion base.

The Chairman: You think the cost of the acquisition of reserves fits under the heading of exploration and development.

Mr. Miller: Yes, it does.

The Chairman: Are there any definitions anywhere that would include that?

Mr. Sim: Bill C-259 and the present Income Tax Act allow the cost of oil and gas properties in computing income. They are deductible from income in toto. Our suggestion is that the base for depletion or the definition of exploration and development expenditures under the regulations should coincide generally with the definition within the Income Tax Act itself.

Oil and gas properties are a major cost in exploring and developing gas reserves, and we feel that the depletion which is available, or would be available, to these companies under the regulations as they are proposed in the July news release would be greatly limited as compared to the present system.

The Chairman: Mr. Sim, what you want to say is that Canadian resource property includes the acquisition of oil reserves or gas reserves. Is that not correct?

Mr. Sim: The oil and gas exploration rights are now deductible under the present—

The Chairman: I know that. I heard you. But you want the oil and gas reserves to be defined to include the cost of the acquisition of the Canadian resource property.

Mr. Sim: Yes.

Senator Connolly: If your company explores and finds properties which have oil and gas reserves, is the cost of acquiring those properties deductible?

Mr. Sim: Yes.

Senator Connolly: On the other hand, if your company buys properties that have already been explored and where discoveries have already been made, are those costs deductible?

Mr. Sim: Yes. The cost of acquisition is deductible. At one stage or another the company will have to acquire property. It may acquire either unproven property or proven property. The cost of acquisition of both is deductible from the income which the company produces.

The Chairman: Mr. Sim, under the bill you get as a deduction under that heading of "Canadian resource property," the items you have been talking about. What you want now, in addition to that deduction, is to have that cost able to earn depletion.

Mr. Sim: Yes, that is quite right.

The Chairman: We heard that same point earlier. We could do that simply by enlarging slightly the regulations which were put out in July of this year. That is a simple point.

Mr. Sim: Yes, sir.

The Chairman: Is there anything else?

Mr. Miller: Mr. Chairman, the remaining point is quite important, particularly to the distribution utilities. It affects the tax rates on Class A utility income of electric, gas and steam investor-owned utilities.

Under section 85 of the present Income Tax Act, investor-owned electric, gas or steam corporations are granted a 2 per cent income tax rate reduction from the general corporate tax rate on Class A income from the sale for delivery in Canada of electrical energy, gas or steam. That is a 2 per cent lower tax rate.

The Chairman: Yes, that is a special rate.

Mr. Miller: Under section 143(3) of Bill C-259 the tax rate reduction would be phased out, and following the 1973 taxation year the general corporate tax rate provided under section 123 would apply equally to utility income of these utilities.

The Chairman: In other words, you would pay the full corporate rate.

Mr. Miller: That is correct. With regard to some background on the subject, in 1952 legislation was introduced to provide income tax rate relief for these public utility companies. Due to the nature of the business, these utilities are required to raise large amounts of capital for the expansion of public services within franchised areas served. Rates chargeable to the public for a service provided are subject to regulatory control and a limited rate of return is allowed on capital invested.

It was clearly a government intention that the tax rate relief granted should assist these companies in attracting the required capital.

The Chairman: And maintain lower rates.

Mr. Miller: This is true. There were all sorts of discussions on the subject in the 1951-52 budget speech, in the Commons debates and in the Senate debates. I believe you, Mr. Chairman, presented the bill in the Senate.

The Chairman: Yes.

Senator Connolly: Don't date him that way!

The Chairman: It is ancient history now, when you talk about 1951.

Senator Connolly: It was only nineteen years ago.

Mr. Miller: Our point now is that the conditions which originally prompted the allowance of this tax rate reduction exist even more so today than they did when the legislation was originally approved. These utilities must keep pace with rapidly-growing communities served, which necessitates increased capital financing needs.

There is another point as well, Mr. Chairman. Under section 123 of Bill C-259 the cumulative tax rate reductions of 4 per cent will be granted to all corporations on non-utility income by 1976. Everyone smiles to the extent of getting a 4 per cent tax reduction, and that is all very nice, except for the utilities, because, in contrast, the cumulative tax rate reduction on utility income will be limited to 2 per cent. So you can look at it the other way round as well. We will be required to take a greater share of the total tax burden.

Mr. Tremaine: Mr. Chairman, when we say "we", we mean the customer.

The Chairman: Oh, yes, the customer.

Mr. Miller: For every $100 of additional income tax burden it requires a gas sale increase of $200, so there is a compounding effect there as well.

The Chairman: What the bill is really doing is raising the taxes for your type of company and therefore, in effect, raising the rates.

Mr. Miller: That is quite true.

The Chairman: The rates that provide the only source of income, is that right?

Mr. Miller: Yes, sir.

The Chairman: And yet the general corporation provision provides for a scaling down of up to 4 per cent by 1976?

Mr. Miller: Yes, sir.

The Chairman: And you are only going to receive 2 per cent by that time. Is there any reason for that?

Mr. Miller: We have not found an explanation. It seems to have been an arbitrary decision, possibly a desire to put everybody on the same basis.

Mr. Tremaine: Or it is possible that they felt the job was done.

The Chairman: You are never through with rates, are you?

Mr. Tremaine: No, and we are never through laying new pipe either.

Senator Molson: Are the returns in this industry getting a little thin or marginal, or were they reasonably satisfied with the returns they were getting?

Mr. Miller: There was considerable discussion in 1951 and 1952; and the rates of return being allowed at that time, based on the cost of capital at that time, were not that much different from the rates allowed on the cost of capital now. Certainly the rates of return to the shareholders are higher; but the cost of capital is a lot higher in proportion. It is much the same.

The Chairman: In any event, there is a ceiling on the income they can make.

Senator Molson: Yes, I have looked at some of the statements, Mr. Chairman, and I think that by and large they seem to be holding their own. I am speaking in the context of the entire industry, that they seem to be more or less holding their own in the broad spectrum.

Mr. Miller: The energy boards or the regulatory boards have no desire to have unhealthy corporations, so they are prepared to allow a limited rate of return.

Senator Molson: Provided you can raise the capital which you need.

Mr. Tremaine: That is the important point. The interest coverage has to be there so that expansion can take place.

Senator Molson: Thank you, Mr. Chairman.

The Chairman: Is that all?

Mr. Miller: We have a recommendation on this point.

The Chairman: Is it in your brief?

Mr. Miller: Yes, it is in the brief. We recommend that clause 143(3) of Bill C-259 be amended to provide for corporate tax rate reductions on Class A utility income of one per cent annually, from 48 per cent in 1972 to 44 per cent for 1976 and subsequent years. This would maintain a 2 per cent differential.

The Chairman: What page are you reading from?

Mr. Miller: On page 1.

The Chairman: We have that now. Is that all?

Mr. Miller: That is all.

The Chairman: Thank you very much.

Honourable senators, we have one further brief to hear, and I notice it is 25 minutes after 12. If it meets with your wishes, perhaps we should deal with this at 2.15 p.m. I refer to the ad hoc Committee of Voluntary Agencies. I think that this is in line with some of the briefs we have had already in dealing with charities and matters of that kind. We would be rushing it if we tried to get it done this morning. I hope it does not inconvenience those who are appearing on this brief, but we will deal with it at 2.15 p.m. Is that agreed?

Some Hon. Senators: Agreed.

The committee adjourned.

Upon resuming at 2.15 p.m.

The Chairman: We have one submission this afternoon, that of the ad hoc Committee of Voluntary Agencies. Those appearing are: Mr. Donald Pierce, of McClintock, Devry and Pierce; Mr. Menno Dirks, of the Canadian Bible College; and Mr. Ian J. Stanley, of World Vision of Canada. Who will be speaking on behalf of the group?

Mr. Donald Pierce, secretary, ad hoc committee of supporting voluntary agencies: I shall, Mr. Chairman.

Honourable senators, I am the Secretary of the ad hoc committee representing supporting voluntary agencies. On my right is Mr. Ian Stanley, the Canadian Stewardship Consultant of World Vision International of Canada; and on my left is Mr. Menno Dirks, Director of Stewardship, Christian and Missionary Alliance Church in Canada.

We understand that the Canadian Jewish Congress made representations to this committee with respect to points that are included in part of the brief which we wish to present today. Because of that, I do not wish to make a lengthy opening statement or waste your time in going over the same ground.

Senator Walker: Do you adopt the Jewish presentation?

Mr. Pierce: Yes, in its entirety. If I might go over the points briefly, Bill C-259, in sections 69 and 70, provides for deemed realization of capital gains on gifts and bequests. There is no exception for such gifts or bequests of properties to registered Canadian charitable organizations.

In order to answer the question, which was also raised by the Canadian Jewish Congress, whether the Government should encourage charitable giving through tax incentives, we submit that it is a philosophical question, and I hope that we can at least persuade you . . .

Senator Connolly: The Government has made up its mind by doubling the allowable allowance.

Mr. Pierce: Yes, and that is a great encouragement to all registered charitable organizations.

Senator Connolly: So I think the philosophy is accepted.

The Chairman: It is a matter of quantum.

Mr. Pierce: That, as I understand it, is the brief that was submitted by the Canadian Jewish Congress. We have answered the question in the affirmative, and we trust that you will also answer the question in the affirmative.

Senator Walker: Have you any new points?

Mr. Pierce: Yes, we have. We have attempted to define various methods that would benefit donors and charitable organizations, and, in effect, encourage charitable giving. In particular I am referring to the points mentioned in my brief, namely, charitable remainder trusts, pooled income fund, short-term trusts, and extension of the one-year carry-over privilege. The gentlemen with me are stewards of registered Canadian charitable organizations. Other members of the committee have assisted us in determining the kinds of gifts that donors would like to make to registered charitable organizations. Mr. Chairman, should I go over the original point in any detail, which is deemed realization of capital?

The Chairman: Any point made by the Canadian Jewish Congress was clearly put. Since that time the staff, including the chairman, have made a complete analysis of their presentation and have reached the stage where they are ready to make a submission to the committee, seeking support for the recommendations we propose. Without indicating what those recommendations might be, I would say they are not unfavourable to the viewpoint presented by the Congress.

Mr. Pierce: I was not before you on that particular day.

The Chairman: It would be a repetition, and an unnecessary one, I would say, to go over the same ground.

Senator Walker: Unless you have new points to raise.

Mr. Pierce: The only point that I would raise is the question of the value at which the appreciated property should be transferred to the charitable organization. We take the view that the Government should encourage that giving, and that the value should be the fair market value.

Hon. Mr. Phillips: What is the significance of the value if, in respect of a bequest or a demise, the gift or bequest is not deemed to be realized capital gain?

Mr. Pierce: The significance is simply that the charitable annuity sections provide for a charity deduction for such gifts based upon the gift element of that gift. In other words, you expect to get an income of 8 per cent on a $100,000 gift of securities 70 years old.

Hon. Mr. Phillips: You are talking about a gift *inter vivos.*

Mr. Pierce: That is right. That is the only point I would raise with respect to that. Again, to support that, it requires a philosophical argument and not a dollar argument. We have attempted, in the last few pages of the brief, to come up with the concept of a detached revenue that might be expected to be lost if the Government eliminated the deemed realization gains.

Hon. Mr. Phillips: We now have under th enew act a 20 per cent deduction in respect of taxable income for charitable donations. We do not have to worry for the present in respect of deemed capital tax on demise. On the question of valuation on gifts *inter vivos*, is that not a question of fact at a particular time? Once it is not a deemed to be realization, how can you lay down any particular value in respect of that which is given? It is either money, securities, commodities, or real property.

Mr. Pierce: I do not understand the question.

Hon. Mr. Phillips: We do not have to deal with deemed realization in the event of death. We have restricted our observations to gifts *inter vivos.* We have 20 per cent deduction allowed under the proposed new bill. We have no problem, presumably, with respect to giving a gift *inter vivos* to charitable organizations. Therefore, we are back to the point of what is the credit to be given to the donor in respect of the value of that which he gives to the charitable organization. Do we have to concern ourselves with the donor? There are several types of donors. We are only interested in the position of the charitable organization. You are not concerning yourself about what valuation was placed upon the thing or the security given?

Mr. Pierce: Yes, we are, but only with respect to the amount of the charitable deduction that the donor may be entitled to.

Hon. Mr. Phillips: In respect of what type of asset?

Mr.Pierce: In respect of depreciated assets.

The Chairman: Other than dollars.

Mr. Pierce: Yes, other than dollars.

Hon. Mr. Phillips: Other than dollars and securities?

Mr. Pierce: Securities would be included with your real property and any other depreciable property.

Hon. Mr. Phillips: All right. We have narrowed it down.

Mr. Pierce: That is the only point that I have, as I understand it, in addition to the Canadian Jewish Congress issue.

I will now come to the description of the types of trust that we would like to see available to donors to charitable organizations. Quite frankly, a good many of these ideas may not be fashionable on this particular day, but the concepts we are talking about are taken primarily from the 1969 United States Tax Statute which, of course, is quite complicated in this area. We recognize the complexity and we certainly do not want to add to the complexity of the present Income Tax Act, but we feel these are the types of trust that donors would use and, in fact, would provide funds for charitable organizations to carry on the works which we feel are very useful.

The first one I would like to refer to is the Charitable Remainder Trusts. This, of course, deals with the question of depreciated properties, and under this type of trust the donor would grant some form of depreciated property. Let us say, for example, a donor had $100,000 worth of securities which he donated under that trust with instructions to pay him a fixed income, or possibly a flexible income, during his lifetime, and, possibly, upon his death that the same income, or some other income, be directed to his spouse or any other person, and then on the death of the person named as beneficiary of the trust, the remainder would go to the registered Canadian charitable organization.

The first of the benefits that we would like to see a donor have with respect to this type of trust is that the value at which it would be given to the trust would be the fair market value, and there would then be, for the donor, a charitable deduction based upon the gift element. That would be the amount of money left over after he gets his income from that gift, the value of which would be determined by life tables.

Senator Walker: And after his wife gets her income from it?

Mr. Pierce: Yes, exactly.

Senator Walker: And then you value it?

Mr. Pierce: Yes.

The Chairman: At what time would the calculations be made? Would they be made at the time the donor makes the gift to the trust?

Mr. Pierce: Yes.

The Chairman: And then you would attempt, on the basis of life tables, to calculate his life expectancy as well as the life expectancy of the spouse, and you would arrive at an amount which would be the gift element.

Mr. Pierce: The remainder would be the gift element.

The Chairman: Yes, the remainder would be the gift element. The remainder might have some capital element in it as well.

Mr. Pierce: Exactly, but, of course, the present bill, as does the Income Tax Act, provides for the capital element provisions. We are not concerned with that today.

The Chairman: The donor would have to be careful that he did not exceed the limit to which he could, without tax, make charitable contributions.

Mr. Pierce: That brings us to the next point.

The Chairman: The remainder would have to be within the limitations.

Mr. Pierce: What we are suggesting as well, Mr. Chairman, is an increase in the one-year carry-over privilege in order to permit donors to make better use of this type of trust.

At the present time the act permits a donor to claim his charitable deductions in excess of the existing 10 per cent deduction the year next following this particular taxation year.

Senator Gélinas: The excess over 10 per cent would carry over into the following year?

Mr. Pierce: Yes, and we are requesting an extension of that one-year carry-over privilege to make it a five-year carry-over privilege.

Senator Walker: Why?

Mr. Pierce: Because the size of the charitable deduction that would be involved here could possibly be substantial. For example, Mr. Dirks is from the west, and he has advised me that many farmers in the west, upon attaining a certain age, would like to donate their farms to a charitable organization, with the understanding that they can continue to live on the farm for the remainder of their lifetime and possibly gain some income from it as well. The value of that farm could be substantial, but the income from it could be quite low, and in order to permit them to take full advantage of the raised 20 per cent rate we want to give them a longer period of time over which they can apportion the once-in-a-lifetime gift. I should note at this point that for certain types of property in the United States the amount deductible actually goes as high as 50 per cent. I just mention that as a matter of interest.

At this point there are so few people who really take advantage of the existing 10 per cent rate that we feel an increase to 20 per cent no doubt will cover most instances that we are dealing with. Obviously, we will not turn down anything beyond that, but that is not a point which we are pressing strongly at this time.

The Chairman: You mentioned the once-in-a-lifetime gift. You are talking about the part of the gift that goes to the spouse, are you?

Senator Connolly: Surely, the concept of a once-in-a-lifetime gift does not enter into the discussion on the point you raised.

Mr. Pierce: No, it was a poor choice of words on my part.

Senator Connolly: A once-in-a-lifetime gift is something quite different. We are talking now about charitable donations which can be made by will or by deed *inter vivos* at any time and in any number.

Mr. Pierce: Exactly.

Senator Walker: Are you trying to bring in that once-in-a-lifetime gift provision?

Mr. Pierce: No.

The Chairman: That does not enter into the picture here at all.

Mr. Pierce: The next type of fund or trust that we would like to have encouraged is simply an extension of the remainder fund which is a pooled income fund. In this situation people have smaller amounts of money that they would like to invest and to give to charitable organizations and, or course, it is very difficult for an organization to invest $1,000 or $2,000 separately, so they would like to put it into a pooled fund and invest the entire fund. Each individual donor would be entitled, under the system we would like to see enforced, to a certain percentage of the income of the fund in proportion to the amount that he contributed to the fund. We would like to see the same type of benefit accrue to donors who make such gifts to pooled income funds.

Senator Connolly: Surely, that is possible under the scheme of the existing act and of the new act? Is it not purely a matter of segregating, say, the $2,000 gift, knowing what the income on that might be if it comes from pooled funds and is averaged? Then, under your first formula, if the income in one year was not sufficient to let them have the full value of the $2,000, let us say, they could spread it over a number of years. In this case one might be sufficient but it might not be, and perhaps you could have two or three.

Mr. Pierce: Certainly you can create these kinds of trusts under the existing act and under the proposed act. The problem is that there is no provision, that I can discover at least, for a charitable deduction to be granted to the donor at the time of the creation of the trust. This concept is recognized by the department, but only with respect to charitable annuities. All we are asking for is an expansion of that idea where a person need not transfer his cash to purchase an annuity. They should be permitted to transfer appreciated properties rather than purchasing an annuity which would permit the charitable organization more flexibility in its investments. That is very simply the difference. You are quite correct that it is possible to do this under the existing act. But as I understand it there are no charitable deductions permitted at the outset, and that is what we are directing our attention to at this time.

Senator Connolly: I would be surprised if you were correct.

Mr. Pierce: Well, I hope I am wrong. But this is my understanding of the situation at the present.

Senator Connolly: If a gift is made surely a claim for a deduction is available, and if it is hedged around with a return of income on the gift for a given number of years. I think this has always been possible under the existing act and will be under the proposed act.

The Chairman: One determination you would have to make is this: Is the pooled income fund a registered charity?

Senator Connolly: I was assuming that.

Mr. Pierce: Actually, under this system it need not be a registered charity. The ultimate beneficiary would be a registered Canadian charitable organization, but whether it would have the facilities to do the investing or not—

Senator Connolly: I am assuming that a gift is made to the organization and it becomes this organization's capital fund and it is invested. That is the assumption I have been working on. And in that case, I do not think you have any problem.

Mr. Pierce: That is very good to hear.

Senator Connolly: I may be wrong. I just put it to you that perhaps you have no worries.

Mr. Menno Dirks, Member ad hoc Committee of Supporting Voluntary Agencies: Mr. Chairman, where the problem might exist under this concept is that income that would be paid out would vary according to the experience of the organization; that is, income from the fund has to be paid out and this could vary from year to year.

Senator Connolly: That would not matter because that income is going to be taxable in the hands of the recipient.

Mr. Pierce: Senator Connolly, I do not wish to go into that point.

Senator Connolly: I do not say that you are wrong.

Mr. Pierce: I certainly cannot provide you with any statutory language which would permit that. The only language which I have found is in an interpretation in June of this year dealing with charitable annuities. This is why I made the statement. I have dealt with the department on this, and no one from the department has suggested this possibility under the existing act.

Senator Connolly: Do you mean they have told you this?

Mr. Pierce: They have not told me that; but they have not made the statement which you have just made, that it is possible under the existing statute.

Senator Connolly: Their authority has much more punch than mine.

The Chairman: You mean your punch is a delayed reaction.

Senator Walker: It depends on whose punch.

Mr. Pierce: They have not directed themselves to that particular point. They have not made the point you have just made.

The Chairman: Mr. Pierce, if you analyse this, you would have a group of people who would have contributed to a pooled income fund. Stopping there, in making contributions to the pooled income fund, that income fund had to pay out a certain amount of income each year to each participant who had contributed. At that stage, where does the charity come into it?

Mr. Pierce: The only stage the charity comes into it is that it would be an irrevocable gift which you would make to that trust, with the ultimate beneficiary being the registered Canadian charitable organization, and on his death to his spouse if he so directs the income to go there.

The Chairman: So the pooled fund would be administered by the trustee?

Mr. Pierce: Yes.

The Chairman: And the trustee would receive these contributions on certain terms?

Mr. Pierce: That is correct.

The Chairman: One term would be, as and when a particular donor and his spouse had passed on, whatever was left was to go to the registered charity.

Mr. Pierce: Yes.

Senator Connolly: Perhaps the registered charity might be paying out income under the terms of the trust and still administer the fund?

Mr. Pierce: Yes.

Senator Connolly: So the gift might be given in the first instance.

Mr. Pierce: Yes.

The Chairman: That is why I thought they might shortcut this situation, the pooled income fund being a registered charity.

Mr. Pierce: That is a possibility.

Hon. Mr. Phillips: I think we need a new law, honourable senators. Mr. Chairman, you are dealing with a crucial point on this pooled income fund that, in a sense the title of the asset given remains with the donor because the donor is getting the yield and, therefore, there is no gift tax. Despite of that, there is no gift tax being deposited. That is, in my opinion, the novel concept here, because in the case of a straight gift to a charitable organization, in the event of demise, there is a divorcement of ownership to the gift by survivors on death. Here you are introducing the concept of the yield remaining with the donor, and the capital must, by its legal nature, remain with the donor. Otherwise he is not entitled to the yield, other than the fact that you could say at a given moment of time the title passes to the charitable organization.

Senator Connolly: Does the trustee's title not intervene here?

Hon. Mr. Phillips: Yes, if the trustee's title intervened then there would be a gift; and if there is a gift we are back to the point where you would have to register a fund as a charitable organization in order to get the exemption from the gift tax.

Senator Connolly: Let us say, for the sake of argument, and we will use the University of Toronto as an illustration, ten other people and myself give $2,000 to the University of Toronto. We have given this money and they are going to hold it in trust. The trust is to pay the income to me during my lifetime and, following my death, to my wife during her lifetime. At the end of that time the remaining estate, for what it might be worth, belongs to the University of Toronto, and the trustee pays it to the university. But the trustee is also the university, so it is transfered from one book to another book.

Hon. Mr. Phillips: That is not what they are asking for. They are asking for a fund to be administered by a trustee, the income to go to the donor and the capital, at a given moment, to go to the charitable organization. If the capital were given outright to the charitable organization, then you value that which is given to the charitable organization as being exempt in relationship to the age of the donor or life expectancy—all that sort of thing, as Senator Hayden has suggested.

Here we are talking about an intervening trustee, and if the intervening trustee is not the owner of the assets given, then obviously ownership must remain with the donor. In order to prevent ownership remaining with the donor, you would have to get the trust so created to become a charitable organization.

The Chairman: Using the word "donor" is a little confusing. Mr. "A" might say, "I have $50,000 either in cash or securities, and I am going to set that up in a trust fund. The terms of the trust fund are that as long as I live the income from it must be paid to me; that when I die the income must be paid to my spouse; and that when she dies whatever remains is to go to a registered charity." At the first stage, the person puts the $50,000 in the trust fund, it produces some income, and is subject to income tax. I would think that he would also be subject to capital gains on gains that would be made in the fund. Is that not right?

Mr. Dirks: No.

The Chairman: So the donor is really the donor with respect to the remainder that is left at the end of the road. What happens if the amount of the remainder is greater than 20 per cent?

Mr. Pierce: Are you referring to at his death?

The Chairman: Yes. It is a point raised by the Congress.

Mr. Pierce: It refers to the carry-back provisions.

The Chairman: It is not up to us to lay out a plan on which you might operate. That is up to you. We do not want to be taking business away from your lawyers. Therefore we have to know your concept of a pooled income fund to see if it makes sufficient sense for us to deal with it.

Mr. Pierce: Your discription was the one that we intended. As to the question whether or not the trustee should be the same as a registered Canadian organization, there is

no reason why he could not be, although at this particular time some do not have the expertise and they would have to retain someone, such as a trust company, to do it.

Senator Connolly: The trust is just an agent in such cases. If you have an independent trustee, that trustee must be a recognized charitable organization, or you would not get the benefit of the gift.

Hon. Mr. Phillips: What these gentlemen want is very nice humanitarianwise, but it is technically difficult under charitable remainder trust.

Going back to page 3 of the brief, the key to what is suggested is in subparagraphs (*a*) and (*b*):

(*a*) that any capital gain on such disposition to the trust should not be deemed as taxable to either the donor or to the trust.

(*b*) that the gift value be based upon the fair market value of the assets on the date of transfer.

The Government would say to such representation, "You have killed the whole concept of a capital gains tax."

Mr. Pierce: There is no doubt that I could argue on the other side of this issue. It all depends upon the philosophical question that I put originally.

Hon. Mr. Phillips: You have discussed charitable remainder trusts, the difference between the value of the thing given and the income that is going to the annuitant or donor. You are either within the 20 per cent or you are not, and you pay your tax accordingly. The rest is this whole business of increase in value.

The Chairman: If there is to be a run-over of five years, you are then enlarging the amount that might not be subject to capital gains tax. You could make a lot of capital gain in those five years, and over the whole period the sum total might be only 20 per cent. Do you think that is the intention, or is this an extension, whether warranted or not, of the use of charitable gifts and avoiding capital gains tax?

After 20 per cent in a year that you are allowed for donations, if you give securities instead of cash, should you be permitted to avoid the capital gains tax?

Mr. Pierce: We take the view that the Government should encourage private individual donors to give money or securities, or whatever, to charitable organizations to facilitate those organizations in carrying out the very good works they are doing at this particular point in time. The way the population is growing, they will be required to do even more.

The Chairman: Supposing that we agree with that, let us then get down to the hard core.

Mr. Pierce: Clearly what we are doing here is encouraging to the fullest possible extent the view that any capital gains that might accrue, even during the lifetime of the individual or his spouse, should not be taxed, but should ultimately go to the Canadian registered charitable organization who would benefit by that much. We feel that it is a good thing.

The Chairman: Why do you not say that any gift to any registered charity, whatever the amount, should not be subject to any tax?

Mr. Pierce: You are referring now to the effect of the carry-over privilege. In order to encourage people to give gifts of this particular nature and size, we should permit them a charitable deduction, or as much as possible of the value of the gift. We are hoping that we will get these kinds of gifts, and we want the donors to take full advantage of them. That is why a period of time is necessary, because their income is probably quite low.

The Chairman: What do you propose in respect of losses?

Mr. Pierce: Capital losses?

The Chairman: Yes.

Mr. Pierce: We have made no proposals with respect to them, but there is no income tax with respect to charitable organizations.

The Chairman: No, but I am talking about the situation where you have a trust fund and you have various elements in the trust fund. You have the element in the fund that produces the income which goes to the donor, and you have the element that produces the income which, at some time in the lifetime of the fund, will go to the spouse and then there is the remainder.

Mr. Pierce: Yes.

The Chairman: In the period of the operation of that fund gains may accumulate, and gains may also accumulate in the period when the donor is the one who is drawing the income.

Mr. Pierce: Yes.

The Chairman: How do you propose to treat the gain at that stage?

Mr. Pierce: It would not be taxable under our proposal. There would be no tax, in fact, to the particular trust which in this case would be the registered Canadian charity organizations.

The Chairman: So at the end of the road the remainder of the gift from the donor to the charitable organization might be getting pretty close to zero.

Mr. Pierce: That is right. The value of it would be the value of the gift element plus the gains minus the losses.

The Chairman: And he would not have paid any capital gains tax in the meantime.

Mr. Pierce: Exactly.

The Chairman: Are there any other questions on that, or shall we move on to the next item?

Senator Walker: Let us deal with the next item.

Mr. Pierce: The last type of trust that we are proposing is the concept of a short-term trust. By this method, if a donor determined that his income in any particular year might be excessive, he could donate securities, or some form of property, to a charitable organization and thereby

reduce his income for that particular year, or for a five-year period, or whatever the term might be.

Senator Beaubien: Only for that period of time?

Mr. Pierce: Yes, just for that period of time.

Senator Walker: Just for the year?

Mr. Pierce: For whatever period of time it might be; it could be one year or five years, or whatever. The charitable organization would have the income from the fund during that period of time. At the end of that period of time, the donor could draw back the asset at the original cost base that he put it in at, so there would be no question of capital gains or losses. This is simply a method whereby the income from a particular property would go to the charitable organization. It is an artificial method whereby an individual can reduce his tax; there is no question about that.

Senator Molson: He can give that same sum of money in another way. You are just trying to provide a method whereby he can reduce his tax if he chooses to do it in that way.

Mr. Pierce: Yes.

Senator Walker: For the year.

Mr. Pierce: For whatever period of time is specified.

Senator Beaubien: Why does he not simply give the income from the security?

Hon. Mr. Phillips: He would be putting himself in a higher tax bracket, senator. For example, if he has $10,000 and he has a yield of, say, 6 per cent, and if he adds that to his income, it would put him in a higher bracket, so to avoid that he hands over the $10,000 to the charitable organization and the 6 per cent yield on that, or $600, goes to the foundation and it does not go into his income; and he is still protecting his capital as it reverts to him.

Mr. Pierce: But in the meantime the charitable organization has the income from that particular fund.

The Chairman: It is a conditional gift.

Mr. Pierce: I do not believe it is a conditional gift; it is an absolute gift for the period during which it is made.

The Chairman: Is there a limitation or a restriction?

Mr. Pierce: The only restriction is that it will revert to the donor after a specified period of time.

Senator Connolly: You could almost call it an "Indian gift".

The Chairman: It has a limitation in time; it is only good for a year.

Mr. Pierce: The time limitation is for whatever period is specified.

Senator Molson: It is not a gift, Mr. Chairman.

The Chairman: That is why I was querying it.

Mr. Pierce: It is a gift of the income; that is all it is.

Senator Molson: I do not think it is a gift because it has a time limitation, and to me that does not constitute a gift.

Senator Walker: A gift has to be outright.

The Chairman: Senator Molson, I suppose you might make a gift of securities or cash to a trustee to hold for a period of five years with instructions to pay the income annually during that time to a registered charity trust fund, and then at the end of that period of time to have the remainder of the principal revert to you. In that instance, all the donor has done, if you want to call him that, is avoid income tax on the income.

Senator Molson: Exactly.

Mr. Pierce: That is not quite all; he has also provided an income to the charitable organization.

Senator Molson: But he could have provided the income to the charitable organization in another way; that is not the only option available to him. In the situation we are discussing he is providing the income and taking care of his own tax position.

The Chairman: You will find quite often that a testator, under his will, leaves securities and directs that the securities are to go to a son or daughter, and also provides that there is a life interest in the income to another son or daughter. This may be a variation of this, except, of course, as far as the testator is concerned it does not come back to him.

Senator Connolly: He cannot take it with him and he cannot send for it.

Senator Beaubien: Mr. Chairman, in the case of this gift, does it have to be less than 20 per cent of his income?

Mr. Pierce: That is right.

The Chairman: Yes, but you can enlarge on the 20 per cent exemption in any year, and the statute will be amended to permit you to do that. They are asking here for a five-year carry-over provision which would mean that if there was more than the 20 per cent in the first year, you could carry the excess over into the next year and the next year, and this would continue for five years.

Senator Beaubien: Provided the five-year average is no more than 20 per cent?

The Chairman: Yes.

Mr. Pierce: That would not apply in this particular situation.

Hon. Mr. Phillips: Did you say the American revenue statute provides for this type of thing?

Mr. Pierce: Yes, it does.

Hon. Mr. Phillips: Under all headings?

Mr. Pierce: Yes, and many more, but I have not gone into the more intricate ones.

Senator Burchill: Is the 20 per cent subject to capital gains? At page 3 you state:

we would respectfully submit that gifts or bequests made by any person to registered Canadian charitable organizations should not be subjected to a capital gains tax—

Hon. Mr. Phillips: The answer, senator, is that under the proposed law there is a capital gains tax.

Senator Burchill: On gifts to charitable organizations?

Hon. Mr. Phillips: To the extent that your gift of capital property would now be subject to a capital gains tax if you gave it, unless the law was amended. That is, it would be taxable income of the testator on death.

Senator Connolly: Would you give Senator Burchill a concrete example of what you are referring to? I think it would be helpful to have it on the record.

Hon. Mr. Phillips: If a person has a revenue-bearing building for which he paid $100,000,—and we will forget recapture provisions and all that type of thing—and it is worth $300,000. If he makes a gift to a charitable organization he, of course, gets his 20 per cent exemption in respect to his taxable income for the year under the proposed act. But the $200,000 is deemed to be capital gain, and to the extent that 50 per cent would be part of his income in the year in which he makes the gift, you would have $100,000 added on to his other taxable income. He could give 20 per cent of his taxable income to charities at large. The same principle applies on death. He has paid $100,000 for the building. It is worth $300,000 on death. The $200,000 forms part of the taxable income in the year of death because it is deemed to be a capital gain. We are going back to the basic point.

Senator Burchill: How is the value ascertained?

The Chairman: At fair market value.

Hon. Mr. Phillips: That is the problem which always arises in handling estates. Sometimes it is based upon real estate valuation for tax purposes; sometimes it is based upon a valuation of contiguous properties; sometimes it is based upon an appraisal; sometimes it is based on offers that may have been made within a reasonable period prior to death. You could have ten, twelve, fifteen or twenty variations in determinig the value.

The Chairman: I should call your attention to section 56(2) of Bill C-259 which is headed "Indirect Payments". It says:

A payment or transfer of property made pursuant to the direction of, or with the concurrence of, a taxpayer to some other person for the benefit of the taxpayer or as a benefit that the taxpayer desired to have conferred on the other person shall be included in computing the taxpayer's income to the extent that it would be if the payment or transfer had been made to him. So you have quite a number of amendments.

Mr. Pierce: That is true.

The Chairman: Are there any other points?

Mr. Pierce: No, I think we have covered all our points.

The Chairman: Thank you very much. That concludes our business for today.

Senator Molson: Mr. Chairman, before the committee adjourns, I have one point I would like to raise in connection with this proposed bill which I spoke to our counsel about at lunchtime. Would I be in order in asking a question at random on this subject?

The Chairman: The only point I could quarrel with is that I could never conceive of you asking a question "at random."

Senator Molson: That is very gracious of you, Mr. Chairman, but I do not think that I can accept that compliment.

The Chairman: Whatever the question is, please go ahead and ask it. Then, if we should answer it *in camera,* I will say so.

Senator Molson: No, I think it is probably completely out of place, but I feel it is something which I would like to see appear in our record. If a person should die and leave his or her estate in trust for the benefit of the spouse; if there is a capital appreciation at the time of death; then, at a later date, if some of the assets are sold at a gain, where is the impact of the tax in this particular case? I assume that on death there is a deemed realization, so the capital gains on the estate would be taxed and would form part of the deceased's income for that year and would attract a 50 per cent tax added on to his income for the year.

The Chairman: Yes.

Senator Molson: The estate is held in trust for the benefit of the spouse of the deceased. Once the securities or properties are sold at a further gain or at an increased price—

The Chairman: By the spouse?

Senator Molson: Well, that is my question: Are they sold by the spouse or by the trust? Who is paying the tax, and when?

The Chairman: Well, if the husband makes a gift to the spouse—

Senator Molson: He may make a gift, but he has not. The husband has died, but he has not made a gift.

The Chairman: Either the assets that he dies with remain in his estate or they are disposed of in accordance with the terms of his will.

Senator Molson: And that sets up a trust for his spouse?

The Chairman: That sets up a trust for his spouse.

Senator Molson: And the income will go to the spouse, and the remainder will go—

Senator Walker: To the life interests and residue.

The Chairman: No, if you take the first instance where he gives certain assets to his spouse, which she enjoys during her lifetime, she is subject to a tax on it when she dies. If she is smart and there is not too much involved, she is only taxed on what she has left.

Senator Molson: If she realizes during that period and pays a capital gain on her income or on the trust income?

The Chairman: You are talking about two different things.

Senator Molson: No, sir, this is the reason I am asking this question, Mr. Chairman. I am seeking light and wisdom.

The Chairman: We will straighten this out. She would either receive it by way of life income or she would get it absolutely. Now, if she gets it absolutely it is hers, she makes a gain on it and she is subject to a capital gains tax.

Senator Molson: You mean if she gets it absolutely? Regardless of the value on the date of death, if she gets it absolutely there is no capital gains tax?

The Chairman: Yes.

Senator Molson: And the securities and properties pass from the deceased to his wife absolutely without any tax?

The Chairman: Yes.

Senator Beaubien: At his cost.

Senator Molson: Yes, at his cost or his valuation.

The Chairman: That is right.

Senator Molson: If he sets up a life interest trust for his wife, first of all, there is deemed realization on his death, is there not?

The Chairman: Yes.

Senator Molson: So there is a capital gain against—

The Chairman: No, there is a roll-over.

Senator Molson: If it is a trust and not absolute?

Hon. Mr. Phillips: If the income goes to the wife.

The Chairman: Yes, where the income goes to the wife only.

Senator Walker: The roll-over is postponed.

Senator Molson: I know if it goes directly to his wife there is no tax between the spouses. But I thought that possibly they could set it up as a trust in which the capital went to someone else and only the life interest went to the wife, and that possibly there was a deemed realization at that point.

The Chairman: When you refer to capital going to somebody else, it could only go after her death; it is a life interest.

Senator Molson: Yes. There is no capital gains tax at that point. If an asset is sold after the death of the testator, and there is a substantial sum realized on the capital gain and the wife is receiving all the income from the trust, who pays the tax and when? Is it a charge on the estate? Is it a charge on the wife's income? What happens if the wife's income is insufficient?

The Chairman: It cannot be a charge on the wife's income. She gets a life interest. So we eliminate that.

Senator Molson: For the sake of argument, the residue could go to either the grandchildren or the children. The wife has a life interest, and there is a substantial capital gain realized while she is enjoying the income. Who pays that?

The Chairman: The trust pays it.

Mr. Douglas Ewens, Assistant to the Chairman: The trust is subject to a rate which would apply if you assumed the trust to be an individual.

Senator Molson: If the total income of the trust were $10,000, and then there is a capital gain, 50 per cent of which is $10,000, does the trust pay tax on the two sums together, or $20,000?

Mr. Ewens: Including only one-half of the capital gain—

Senator Molson: Yes. It then pays income tax on the total income, plus half the total gain, and the rate applies to that dimension of sum.

Mr. Ewens: Not exactly. It gets a deduction if it is paying income out to the wife. It is only taxed on accumulating income. Your assumption was that the wife did not get the capital.

Senator Connolly: In that case the wife does not get the capital gain. That capital gain is an appreciation of capital. Does it not remain in the trust until the death of the life tenant, and then the capital gains tax applies and—

The Chairman: It is a roll-over; it goes back to the estate.

Senator Connolly: It would have to be paid by the trustee on behalf of the residual legatee.

Mr. Ewens: The tax is paid at the time the trust realizes the capital gain at the trust's "personal" rate. The trust may then re-invest those proceeds.

Senator Connolly: Senator Molson's example is that one of the capital assets is a security which, between the death of the husband and before the death of the wife, appreciates considerably in value. It is sold by the trust and presumably continues to be held as part of the capital of the trust, in cash or other securities. It may be re-invested. At the time that the grain is realized, it is still held by the trustee. Under the bill, is the capital gains tax assessed in the hands of the trustee at that time?

Mr. Ewens: I believe it is.

Senator Connolly: Under what section?

Mr. Ewens: Under section 104(2), which provides that the trust is taxed as an individual, and if that capital gain were realized by the individual it would be taxed in the year of such realization.

Senator Connolly: It would be a taxable capital gain that would affect the income received by the widow.

Mr. Evens: She would still be getting income from the realized capital gain, assuming it was earning income and not just held as cash. It would be put in a bank or would be re-invested in some way.

Senator Connolly: But the capital gain tax would be paid by the trustee.

Hon. Mr. Phillips: The capital gain would be taxed, and what would then remain to continue earning income would be the gross capital gain less the tax paid on it.

Senator Connolly: Is the capital gains tax paid at the time it is realized, when the wife was getting life income from this fund, or is it postponed until her death, in which event it would be payable presumably by the trustee on behalf of the residual beneficiaries?

The Chairman: If the trust has the capital, and the trust makes a gain, it is then a gain to the trust, and it will be subject to capital gains tax.

Mr. Ewens: The roll-over applies on the husband's death. If it is a qualifying trust, whereby the spouse is the sole beneficiary of the income and no other person is a capital beneficiary until after the wife's death, it qualifies for a roll-over and no capital gains tax is paid upon the husband's death. The capital is then considered to be the capital of the trust, the trust is deemed to be an individual, and it is subject to the rules and rates applying to ordinary individuals.

Senator Connolly: The whole estate is then looked at at the time of the wife's death, because presumably it is then going to the children, and capital gains which may be payable then fall in.

The Chairman: There would be a further appreciation.

Hon. Mr. Phillips: You may have two capital gains. You may have the roll-over capital gain going back to the time of the death of the testator, and the residual capital gain after taxes.

Senator Walker: Supposing the capital gain happens 10 years after the wife has been the recipient of a life income, and she dies 10 years later. Is that the time that the residual legatee or the trustee of the residue of the estate pays the capital gains tax?

Senator Molson: That was my original point. But they said that the capital gains of the assets disposed of are payable in the year when disposition occurs, and are paid by the estate.

Mr. Ewens: A further appreciation after that capital gain was realized by the trust and later was re-invested would certainly attract a tax on the death of the widow. There will also be a deemed realization every 21 years. You cannot go along indefinitely without incurring some tax.

Senator Molson: That is something that nobody had mentioned previously. This does not depend on that estate being a whole estate; it is whatever may be the life interest. It does not mean that the individual has to have his pictures, carpets, and everything he owns in that trust; it is whatever he sets up as a trust for his spouse.

Hon. Mr. Phillips: That is right; except that the remainder that he does not set up for his spouse is deemed to be realized.

Senator Molson: That is dealt with separately.

The Chairman: That is dealt with directly in his own estate.

Hon. Mr. Phillips: It is taxable income in the year of his demise.

Senator Connolly: If it goes to his wife, it is not taxable.

Mr. Ewens: There is always the 21-year limitation.

The Chairman: Tomorrow the following will be appearing before us: The Canadian Petroleum Association; The Mining Association of Canada; The Canadian Mutual Funds Association; and The Canadian Pulp and Paper Association. I suspect that The Canadian Pulp and Paper Association will be dealing with international source income, and I expect Mr. Fowler will be present he is always clear and concise, so it is a pleasure to listen to him.

I obtained some information which is highly speculative, and that is that Bill C-259 may be sent over to us on or before December 1. If that is the case, it would seem that we will be able to meet our dealine with respect to providing an interim report next Wednesday morning, and, if it is approved, tabling it in the Senate in the afternoon. That will deal with a substantial number of the problems that have been presented to us so far, and, of course, that will go to the other place right away, while they are still in Committee of the Whole.

Senator Walker: They are waiting for it, are they not?

The Chairman: I believe they are. The House of Commons members have had access to the briefs which have been filed here, and I expect they are making use of them. Perhaps they have also read some of our proceedings which are available.

Robert Thompson made a speech the other day and, with respect to parts of it, one would think be was reading the Canadian Jewish Congress brief on charitable gifts. That is a good thing; it was a sensible speech.

Senator Molson: It was a good speech.

Senator Walker: You will find most of the Tories will do that, but they are not gallant.

Senator Connolly: You mean just now, Senator Walker?

Senator Walker: Just give them a chance.

The Chairman: There is one other thing.

Mr. Ewens: Senator Molson, further to the discussion you commenced, at the time of the death of the widow who had obtained the benefit of a roll-over on her husband's death, her estate is deemed to realize the capital gain and no further roll-over is provided for her beneficiaries.

Hon. Mr. Phillips: You said there would be no further roll-over to the extent of the capital gain made by the trust.

Mr. Ewens: At any rate, on the spouse's death—that is, the wife's death—there is a deemed realization provided by section 104(4).

Senator Molson: Even if the capital is still designated as passing, on her death, to the children?

Mr. Ewens: Yes.

Senator Molson: There is no roll-over to the second generation then?

Mr. Ewens: That is right.

The Chairman: If she obtains capital, then there is a deemed realization.

Mr. Ewens: Only if she dies and the capital is to pass on to her children. You cannot defer it any longer than that.

Senator Beaubien: It cannot go to the grandchildren?

Mr. Ewens: It can go to them, but not tax-free.

Senator Molson: Why is there realization when it goes from the husband to the spouse?

The Chairman: That is just what it says.

Senator Walker: There is a roll-over to the wife when the husband dies. If there is a realized capital gain of $100,000 in the meantime, is there still a roll-over?

Senator Beaubien: No, the tax is paid.

Senator Walker: By her?

Senator Molson: By his estate.

Senator Walker: Once the estate has been settled, there is a roll-over. Five years later there is a capital gain in the amount of $100,000. Would that result in a roll-over on the wife's death?

Mr. Ewens: No. Her trustee pays the capital gains tax at the date that the trust realizes the gain.

Senator Walker: Out of the residual savings?

The Chairman: Yes.

Hon. Mr. Phillips: As an individual.

The Chairman: Yes.

Senator Molson: Why is there realization on her death if she was never been designated as the beneficiary of the capital? The capital is designated, by the poor chap who died, to go to the children, and his wife has a life interest and it is held in trust for this purpose. Why is there a roll-over on her death?

Mr. Ewens: An indirect answer, Senator Molson, would be that if the husband had bequeathed the property directly to the children, on his death there would be a deemed realization. The bill, however, creates relief if he leaves his estate to his widow or to a qualifying trust for her.

The Chairman: Honourable senators, we will adjourn until 9.30 tomorrow morning.

The committee adjourned.

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THIRD SESSION—TWENTY-EIGHTH PARLIAMENT

1970-71

THE SENATE OF CANADA

STANDING SENATE COMMITTEE ON

Banking, Trade and Commerce

The Honourable SALTER A. HAYDEN, *Chairman*

No. 45

THURSDAY, OCTOBER 28, 1971

Ninth Proceedings on:

"Summary of 1971 Tax Reform Legislation"

(Witnesses—See Minutes of Proceedings)

24291—1

THE STANDING SENATE COMMITTEE ON BANKING, TRADE AND COMMERCE

The Honourable Salter A. Hayden, *Chairman*

The Honourable Senators,

Aird	Grosart
Beaubien	Haig
Benidickson	Hayden
Blois	Hays
Burchill	Isnor
Carter	Lang
Choquette	Macnaughton
Connolly (*Ottawa West*)	Molson
Cook	Smith
Croll	Sullivan
Desruisseaux	Walker
Everett	Welch
Gélinas	White
Giguère	Willis—(28)

Ex officio members: Flynn and Martin

(Quorum 7)

Order of Reference

Extract from the Minutes of the Proceedings of the Senate, September 14, 1971:

"With leave of the Senate,

The Honourable Senator Hayden moved, seconded by the Honourable Senator Denis, P.C.:

That the Standing Senate Committee on Banking, Trade and Commerce be authorized to examine and consider the Summary of 1971 Tax Reform Legislation, tabled this day, and any bills based on the Budget Resolutions in advance of the said bills coming before the Senate, and any other matters relating thereto; and

That the Committee have power to engage the services of such counsel, staff and technical advisers as may be necessary for the purpose of the said examination.

After debate, and—

The question being put on the motion, it was—

Resolved in the affirmative."

Robert Fortier,
Clerk of the Senate.

24291—1½

Minutes of Proceedings

Thursday, October 28, 1971.
(56)

Pursuant to adjournment and notice the Standing Senate Committee on Banking, Trade and Commerce met this day at 9:30 a.m. to further examine:

"Summary of 1971 Tax Reform Legislation"

Present: The Honourable Senators Hayden (*Chairman*), Beaubien, Benidickson, Blois, Burchill, Connolly (*Ottawa West*), Desruisseaux, Gélinas, Macnaughton, Molson, Sullivan, Walker, Welch and Willis—(14).

Present, but not of the Committee: The Honourable Senator Laird—(1).

In attendance: The Honourable Lazarus Phillips, Chief Counsel.

WITNESSES:

Canadian Petroleum Association:

Mr. D.B. Furlong, Managing Director;

Mr. F.J. Mair, Manager, Administrative Services, Hudson's Bay Oil and Gas Company Limited;

Mr. R.C. McCallum, Treasurer, Canadian Fina Oil Limited.

The Mining Association of Canada:

Mr. C.R. Elliott, First Vice-President and Chairman, Tax Policy Group. (President, Conwest Exploration Limited);

Mr. J.L. Bonus, Managing Director and Chief Executive Officer;

Mr. D.H. Ford, Chairman, Tax Committee, (Director of Taxation, Noranda Mines Limited);

Mr. D.B. Craig, Member, Tax Committee, (Taxation Manager, International Nickel Company of Canada Limited);

Mr. K.E. Steeves, Member, Tax Committee, (Vice-President—Finance, Bethlehem Copper Corporation, Limited);

Mr. V. St. Onge, Member, Tax Committee, (Taxation Manager, Quebec Cartier Mining Company).

The Canadian Mutual Funds Association:

Mr. A.D. Johnstone, President, President, Mutual Funds Management Corporation Limited);

Mr. J.D. McAlduff, C.A., Chairman, Taxation Committee, Vice President and General Manager, Investors Group Trust Co. Limited);

Mr. W.R. Miller, Chairman, Administrative Committee, (Vice-President, United Funds Management Ltd.);

Mr. C.T. Grant, Vice Chairman, Taxation Committee, (Counsel, Commonwealth International Corporation Limited).

At 12:35 p.m. the Committee adjourned.

2:15 p.m.
(57)

At 2:15 p.m. the Committee resumed.

Present: The Honourable Senators Hayden (*Chairman*), Benidickson, Blois, Burchill, Connolly (*Ottawa West*), Desruisseaux, Gelinas, Macnaughton, Molson, Smith and Willis—(11).

Present, but not of the Committee: The Honourable Senator Thompson—(1).

In attendance: The Honourable Lazarus Phillips, Chief Counsel.

WITNESSES:

Canadian Pulp and Paper Association:

Mr. Howard Hart, Executive Vice President;

Mr. A. Hamilton, President, Domtar Limited;

Mr. T. Bell, President, Abitibi Paper Company;

Mr. Colin Brooke, Manager, Tax Division, Domtar Limited;

Mr. R.W. Wilson, Tax Specialist, Consolidated Bathurst Limited;

Mr. D. Ford, Northwood Pulp;

Mr. D.A. Wilson, Director, CPPA.

At 3:30 p.m. the Committee adjourned to the call of the Chairman.

ATTEST:

Frank A. Jackson,
Clerk of the Committee.

The Standing Senate Committee on Banking, Trade and Commerce

Evidence

Ottawa, Thursday, October 28, 1971

The Standing Senate Committee on Banking, Trade and Commerce met this day at 9.30 a.m. to give consideration to the Summary of 1971 Tax Reform Legislation, and any bills based on the Budget Resolutions in advance of the said bills coming before the Senate, and any other matters relating thereto.

Senator Salter A. Hayden (*Chairman*) in the Chair.

The Chairman: Honourable senators, as I told you yesterday, today we have a number of submissions. This morning we will hear from: the Canadian Petroleum Association; The Mining Association of Canada; and The Canadian Mutual Funds Association. We have fixed a hearing for the Canadian Pulp and Paper Association for 2.15 this afternoon.

We have here this morning representing the Canadian Petroleum Association: Mr. D. B. Furlong, who is the Chief Executive; Mr. F. J. Mair, Manager, Administrative Services, Hudson's Bay Oil and Gas Company Limited; and Mr. R. C. McCallum, Treasurer, Canadian Fina Oil Limited.

Mr. Furlong will make an opening statement, and then he will operate with his panel.

Mr. D. B. Furlong, Managing Director, Canadian Petroleum Association: Thank you, Mr. Chairman.

Honourable senators, we do appreciate this opportunity to meet with you today. Mr. Frank Mair is on my immediate right, and Mr. Ron McCallum is sitting next to him. We in the Canadian Petroleum Association represent over 200 companies engaged in exploration, development and transportation of oil and gas and their allied functions. These two gentlemen who are with me are part of a committee of income tax experts who have been concerned most of their professional lives with the tax problems of the oil and gas industry. In particular, this committee has actively participated in the last few years in reviewing the Government's tax proposals and the preparation of our communications to you and to others on this subject.

We recognize that we are speaking on behalf of a sectional group, the oil and gas group, and we also recognize that you gentlemen are looking to the interests of Canada as a whole. But we believe that our proposals are directed to the same broad interests as those you are concentrating upon, and that the comments we make, although they refer only to the oil and gas industry, are designed to be, and are, in the general interest of Canada.

We would like to say politely but forcibly that we believe many of the provisions of Bill C-259 will damage and not assist Canada's progress.

I would now like to call on Mr. Mair to specify the areas that we would like to highlight for your approval or discussion today.

Mr. F. J. Mair Manager, Administrative Services, Hudson's Bay Oil and Gas Company Limited: Honourable senators will recall that the Canadian Petroleum Association made a submission to this committee in May, 1970, and we still feel that the recommendations we made in that submission are applicable and should be considered. As the result of the various submissions, your committee recommended, for example, that the depletion base be broadened for earned depletion. That has not been done, and this is one of our main points.

I will summarize the comments we make in this submission. Firstly, we recommend that the earned depletion requirements be made consistent by providing a bank of earned depletion based on expenditures made since 1947, and also with respect to costs subsequent to that date such as the costs of resource properties, interest and of depreciable properties. Secondly, we recommend that where the act as it presently exists requires that a grouping of depletion be made, the earned depletion should follow the same pattern.

Thirdly, we recommend that proceeds from the sale of resource property should be treated in a manner that is consistent with the treatment of acquisition costs of those properties.

Fourthly, we recommend that mergers or amalgamations or the transfer of assets between companies, wholly-owned subsidiaries, should not be subjected to tax, as is proposed in this bill.

Fifthly, we recommend that the new act should not have a retroactive effect, as it does in some cases.

Finally, we would ask that much of this act be clarified, so that we can understand what it does say.

We are very concerned in many cases, particularly with respect to partnerships. We do not know whether we are a partnership when we go into a joint venture or not. We feel that if we are, this will cause a great deal of difficulty in the oil industry because, as you know, we do have many joint ventures.

We do have some specific recommendations as to what parts of this bill should be changed or amended. We can go into those later, but as of now we would be happy to answer any questions you may have with respect to our submission.

The Chairman: Mr. Mair, you were talking about the retroactive effect of this bill in relation to your industry. Would you illustrate that?

Mr. Mair: Yes. This is not specifically related to our industry. Section 80 of the proposed bill would tax gains

on the redemption of bonds and a gain on redemption of bonds is related to the issue price. To use Hudson's Bay Oil and Gas as an example, we issued bonds in 1955 and as of now they are at a substantial discount. The bill would tax any gains that we made on the redemption of those bonds.

I recognize too that those amendments which have recently been published change that. They did not amend section 80 but provided a new section, 39(3) in which they are still taxed, but they are taxed as a capital gain rather than as ordinary income. So it has changed to some extent, but it is retroactive legislation to the extent that these bonds are now at a discount.

Senator Connolly: If capital gains are to be taxed for everyone else and if you make a capital gain on redemption of one of your bonds, is it not equitable and reasonable to assume that you should have to pay the tax?

Mr. Mair: I would have no objection to paying a capital gains tax on any gain we made, if it were done consistently with other gains, which presumably are to be taxed on any gain after valuation day. But there is no provision to tax these on valuation day value: it takes them on the gain that has been made prior to that time.

Senator Beaubien: What would you have paid for the bonds?

Mr. Mair: As an example, those bonds were issued at 100. Recently, as you know, the price of the bonds has increased, but they were trading around 80 to 85.

Senator Beaubien: If you paid 100 for them, you would not be taxed?

Mr. Mair: No, we would not. My point is that if we bought the bonds today, we would not be taxed, but if we buy them next January we would be taxed on the 15 points difference.

The Honourable Lazarus Phillips, Chief Counsel to the Committee: Mr. Mair, if the chair approves, I think it would be more helpful to this committee if, instead of dealing with general roll-over and merger provisions, partnerships, retroactive features—some of which we have already studied and which are worthy of further study, if we have time—you concentrated on the earlier items that you mentioned, because they are specifically related to your industry, such as the extension of the base for earned depletion and this sort of thing. My feeling is that we should get through with the particular items that affect you most, and then let us see how much time the chair will give on the other items. Otherwise, I think we will have a tendency to roam all over the act.

The Chairman: I provoked this discussion, I asked the question. Mr. Mair, we have had some presentations here on the matter of earned depletion and the broadening of the qualification; and also on other works of the proposed regulations. I assume that both of these items are pertinent to your industry.

Mr. Mair: This is the most important item we have.

The Chairman: Would you develop this and tell us what your position is?

Mr. Mair: As we set out in our previous submission, we have properties now which have resulted from tremendous expenditures made over the past 20 years. Our feeling is that no recognition is being given to that. Production from these properties will require us to earn depletion so that, although we may have spent a lot of money in the past, we now will have to spend more moneys in order to get depletion on all those properties.

These investments were made with the carrot held in front of us that we were going to get depletion some day. As you people well know, the oil industry has gone for many years—which I think is reasonable—without being taxed, because of these tremendous expenditures, but always with the idea that when we get in to produce the properties we would get depletion. Now the new act proposes to restrict that depletion and you will not get it unless you continue to explore and develop.

The Chairman: In your operations to date, did you say you went without income or without profit?

Mr. Mair: Without taxable income. It is because of the provisions of the existing act, which recognizes the long pay-out period of the oil industry. That is, a company may have to spend 15 to 20 years before it finally reaches a position of getting a pay-out. Because of the provisions of the existing act, the company does not pay tax, but it does come to the point now where most companies are approaching the taxable position, and many of them are taxable now.

The Chairman: Let me analyze that for a minute. Going back to 1947, you spent a lot of money on development?

Mr. Mair: A tremendous amount.

The Chairman: And you have taken care of that through your earnings. So, you have increased your cash flow in that fashion, and in that way you have money available to pay dividends and thus keep the public interested in your shares.

Mr. Mair: That is what we are hoping to do. Of course, there is one other side of that picture. Most investors in the oil industry went into it with the idea of a capital gain too.

The Chairman: Whatever the ideals they went into it with, of course, the act down to this date has at least seen to it that if they earned money and spent money they did not pay any tax on what they earned, to the extent that they have expended moneys. So, only the net that they might have would have been taxable in that period.

Mr. Mair: That is true.

The Chairman: I am trying to figure out why you want to go back to 1947 now and want to include all those expenditures that you made as part of earned depletion. I can understand from here in, because you have two categories. You have your write-offs, that is, your capital cost allowances; and then you can earn depletion by defined expenditures. Why would you go back to 1947 and pick that up? I would like to know what your thinking is on that?

Mr. Mair: Perhaps I may illustrate that by an example. If we make an investment, say, in gas processing plant, we

use a discounted cash flow method of evaluating that gas plant. Up to this point we have said we will be able to get depletion on the sale of natural gas, liquids sulphur, and so on. So our evaluation of this project was based on the fact that we would get depletion. Now we have come to the point where we will not get that unless we go and spend money on exploration and drillings. Therefore, many of the evaluations of producing wells, gas plants and this sort of thing have been based on the fact that we expected to get depletion. Now the act is changed so that we will not get it unless we expend further amounts of money.

The Chairman: Except that, in the period down to this date, and before the new act comes into force, in relation to those expenditures you were reimbursed out of your earnings for the expenditures you made. What further did you get in that period? You got depletion?

Mr. Mair: No, you did not get depletion. Because of the way in which depletion is calculated, you do not get depletion until you are in a taxable position.

The Chairman: All these things do not matter unless you have earnings.

Mr. Mair: That is true. The point I am making is that the shareholders invested risk money, risk capital, and were encouraged to do so with the idea that, over a long period of time, say ten years or more, this capital would be spent and would develop properties which would produce income for them. We have now reached that point in the industry. We are reaching that sort of maturity where we would expect to get a return on our investments. But now the ball game has changed.

The Chairman: Well, just trying to relate the two, starting with the new act you know where you are at. You will get write-offs.

Mr. Mair: Yes.

The Chairman: And you will get what is called earned depletion within the conditions laid down for that. So two questions arise. I asked you only one. I asked you why you thought you should be able to bring what you have spent and deducted from income in the past into the new rules provided in the new act. The second question is: What is wrong with the conditions for qualifying for earned depletion? If they do not go far enough to suit your industry or meet the requirements of your industry, then what additional things are needed?

Mr. Mair: We feel that they are too restrictive and that any item which must be deducted in calculating the depletion should also qualify to earn depletion. For example, the acquisition cost of petroleum and natural gas rights must be deducted before you calculate depletion. We feel, therefore, that it should earn depletion. The same is true of interest expense which must be allocated and deducted before we calculate depletable profit. We feel it should also earn to the extent that you have it deducted.

In addition to that, the depreciable cost of assets—for instance, well heads, gas plants and that sort of thing—must be deducted. We feel again, therefore, that they should earn depletion.

The Chairman: You say that anything affecting your industry that is entitled to capital cost allowance should also qualify for earned depletion as well—that is, the particular thing should qualify?

Mr. Mair: I feel that is true, yes.

The Chairman: As a general principle.

Mr. Mair: As a general principle, yes. I think you will recall, Mr. Chairman, that your committee did recommend the broadening of this depletion base, and we are in complete agreement with what you suggested.

Senator Connolly: In effect, what you are saying is that the expenditures that you incur, whether they are to purchase properties or to erect plants or processing facilities, are first of all deductible from any income that you have.

Mr. Mair: Yes.

Senator Connolly: As such, those expenditures you get out of your revenues without paying tax on them. In addition to that, what you are claiming is a depletion allowance on those same expenditures, a return of capital. Will you tell us neatly what the justification is for the additional tax concession? I am not questioning it or quarrelling with it. I am simply asking you to state why it is required.

The Chairman: May I add, Senator Connolly, that that has been the "plus" in dealing with this industry as far back as you want to go. They did have write-offs and the sweetener was depletion.

Senator Beaubien: What is done in the United States? What is the law there?

Mr. Mair: Depletion is calculated on a completely different base in the United States. It is calculated on what we call gross depletion. That is, they have an alternative and they must use the better of the two methods of doing it. They calculate depreciation allowance based on the gross income from those properties, but it is limited to a percentage of the net profit; that is, 50 per cent of the net profit on a property-by-property basis. In Canada, on the other hand, we calculate depletion on a net basis—that is, the net profit—and we do it on an overall basis. All properties are thrown in together.

Senator Connolly: Would you care to answer my question?

Mr. Mair: I am not sure I can recall the exact question, Senator Connolly.

Senator Connolly: Well, I say that in the first instance, for all the expenditures that you make in establishing and operating a gas or oil field, you are allowed deductions from taxable income. In addition to that, you say the industry should have a further tax incentive, namely that all those items should qualify for depletion. This is a double incentive, is it not? I ask you why you should have it.

Mr. Mair: I think the simple answer might be that the rate of return in the oil industry, contrary to what most persons outside the industry might believe, is relatively low. It is in the range of 7 to 8 per cent; that is, with the existing

depletion law the rate of return is in the range of 7 to 8 per cent for the whole industry.

Senator Molson: Seven or 8 per cent of what?

Mr. Mair: Of capital invested. This is with the existing law. The proposed bill would restrict the amount of depletion we are allowed. We are saying that this restriction should not be as severe as proposed, and when we make expenditures to acquire acreage or equip wells, and so on, that should help us earn this depletion. That is, if we are to accept the concept of earned depletion, we propose that it should be broadened.

Senator Walker: You want to be paid twice, in other words. You are already being allowed all your expenses. Those expenses having been allowed, you now want depletion on what the expenditures have originally been. Is that correct?

Mr. Mair: We want depletion on the profit, after having deducted those expenses. The proposed bill would restrict that depletion by saying that you must spend money in order to earn that depletion. We are saying that if we spend money on developing these projects, that money should then earn the depletion.

Senator Connolly: Are you telling us that because this is a wasting asset it will finally be completely exhausted in time, and that, therefore, the capital that is required to develop it should be returned through the tax act?

Mr. Mair: That is the original basis on which depletion was set up, that it is a wasting asset and that the capital should be returned to the shareholders without tax. If you analyse it carefully, essentially the depletion is an incentive; that is, it is a reduction in the tax rate in order to encourage people to invest in that industry.

Senator Connolly: You are coming to the same point. Because it is a wasting asset, you are making the argument that you should have depletion as well as the write-off.

Mr. Mair: All industries have the write-off. They have the write-off of their expenditures. We do have that perhaps at an accelerated rate, but in addition to that it is normal in resource industries to provide this incentive of depletion, which, essentially, is just a lower tax rate in order to encourage development of those industries.

Senator Connolly: All right. That is the argument. I am glad to have that on record.

The Chairman: Senator Connolly, not only is that what the witness says, but that is what the summary of the tax reform legislation says.

Senator Connolly: Of course. I know.

The Chairman: It says that substantial tax incentives are maintained in the new bill. In other words, they existed prior to the new bill and they are maintained in the new bill to recognize the risks involved in exploration and development, the international competition for capital and the levels of incentives available in other countries. That is the reason why they continued the depletion in the form of earned depletion; they felt that it should not be automatic.

Senator Connolly: That not only applies to this industry; it applies to any resource industry. I think it is appropriate for us, when we have witnesses from a given industry, to determine if there should be two tax incentives, why the second incentive would be justified. I think you have given the reasons and the chairman has read from the summary which says that the principle is recognized in the law.

Senator Walker: Just the amount?

Mr. Mair: We are concerned with just the amount.

The Chairman: The attack here is that the definition of earned depletion is not broad enough.

Senator Molson: Mr. Chairman, surely we have dealt with this at great length on the White Paper and our recommendation at that time was that the base might be broadened.

The Chairman: We have not changed our ideas on that.

Senator Molson: The only question to be determined is whether there is a way in which we can help these people.

Senator Connolly: What we need are details as to the items that should be added to the definition of "earned depletion."

Senator Burchill: Is that what the term "broadened" means?

The Chairman: Yes, it means increasing the items.

Senator Burchill: You say you recommend that the grounds for depletion be broadened? You are recommending what this gentleman is asking?

The Chairman: In principle, yes.

Senator Walker: Only he feels, and probably quite properly, that the base should be broadened even more.

Senator Beaubien: Mr. Mair, if Bill C-259 had been the law 15 years ago would the different companies that make up the Canadian Petroleum Association have paid more taxes than they have over the last 15 years?

Mr. Mair: Many of the companies would have paid more taxes because they would not have earned sufficient depletion to claim a depletion allowance. I might go one step further. Many of the projects might not have been started at all if this earned depletion concept were as narrow as it is, because we would have had to take into account the fact that you might not get depletion. This is particularly important to our industry at this time. As you know, we are expanding into the northern parts of Canada, the Arctic islands, offshore; and the huge amounts of capital that are required for that exploration and development program would not be attractive if we are too restricted in our allowance for depletion.

Senator Connolly: Is the one-for-three formula too restrictive?

Mr. Mair: We argued in our previous submission that it should be no more than one-for-two and that it should be broadened. Now, they have not changed either of these items for the oil industry. In fact, they have made no changes at all except in the proposed regulations which

state that interest expense will not be an item which will earn depletion either.

Hon. Mr. Phillips: Mr. Chairman, may I draw your attention to the following item, and perhaps we can get back to the specific point. We are all in agreement, as quoted on page 4 of the brief, that both the Senate committee and the House of Commons committee recommended that the base for earned depletion should be broadened to include depreciable assets and the costs of resource properties. So both the Senate and the House of Commons committees were convinced on that point. Therefore there is no sense in carrying further coals to Newcastle on that. They were not reflected in the bill, however. That was the recommendation of these two committees. Then we go back to the earlier part of your present brief and on page 1, in the second paragraph, towards the end, you are saying:

> —therefore all "Canadian exploration and development expenses" as defined in the proposed legislation should earn depletion in addition to other costs such as interest and depreciables.

Mr. Mair: That is right.

Hon. Mr. Phillips: In effect, are you asking therefore that the earned depletion base include not only depreciable assets and the cost of resource properties, but also all Canadian exploration and development expenses, as defined in the proposed legislation? Broadly speaking, would that cover what you are asking?

Mr. Mair: Yes.

Hon. Mr. Phillips: So, in effect, you are asking for a recommendation that the base in respect to earned depletion be extended not only to cover depreciable assets and the cost of resource properties, which has already been recommended by this committee, but also in relationship to the wording of the new act to include all Canadian exploration and development expenses as defined in Bill C-259?

Mr. Mair: Yes, sir, that is right.

The Chairman: The committee might be interested in knowing the exact language of our prior recommendation. May I just refer you to page 41 of our Report on The White Paper, paragraphs 26 and 27:

> 26. Eligible expenditures for purposes of earning depletion under the White Paper proposals are section 83A expenditures excluding the cost of acquiring mineral rights. There expenditures are in respect of exploration and development. Many expenditures not included in these 83A costs so as to be entitled to 100 per cent write off are equally exploration and development expenses. Thus replacement of capital assets in expansion of refinery facilities and well and associated equipment are necessary costs in developing oil and gas reserves. Likewise expansion of refining facilities and replacement of equipment and buildings are necessary if continued operation is to be maintained. Gas plant facilities should be considered an integral part of any development program. Gas at the wellhead usually is not a saleable product and must be separated from certain components to bring the gas up to the standard set by the Gas Conservation Board. In addition government orders (provincial) require the conservation of gas that is produced with oil.
>
> 27. While the treatment of these facilities as depreciable assets subject to capital cost allowance may be justified rather than broadening the scope of exploration and development expenses under Section 83A of the Income Tax Act, your Committee is of the opinion that the basic character of these expenditures is part of any development program intended to lead to production in commercial form of oil and gas. Accordingly, your Committee is of the view that eligible expenditures to earn depletion should include all such expenditures for purposes of the determination of earned depletion.

This is exactly what you are asking for today and we have tried that once before, in our recommendation; and neither your recommendation nor ours was heeded.

Senator Connolly: And the House of Commons committee pretty well went along with this recommendation.

Hon. Mr. Phillips: The House of Commons committee went along to the extent that depreciable assets and costs of resource properties be included. I do not think they went quite as far as we did in respect to exploration and development expenses.

Mr. Mair: Mr. Chairman, the Commons committee recommended that we go back to the inception for past expenditures.

Hon. Mr. Phillips: That is a different point.

Mr. Mair: That is true.

The Chairman: Do you have any other questions on this point? It does not seem that much needs to be said to ascertain what our view is. It is already in writing.

Senator Connolly: We have said it, the Commons have said it, and the industry has said it. Has the witness any idea why the bill does not say it?

Mr. Mair: No, I do not. I thought that this was a fiarly logical and reasonable request, and I have no idea why there was no attention paid to the representations either of the Commons committee or of this committee.

Senator Connolly: Would it be that the tax savings represent money that the Treasury needs? Is that the only conslusion you can come to?

Mr. Mair: I think it might be. It may have some bearing, but this is some time down the road, and I really do not think that the immediate effect on tax revenue is being considered.

Hon. Mr. Phillips: Senator Connolly, you will see at least one of the reasons why the Minister of Finance has possibly excluded acquisition costs at the foot of page 2 of the brief.

Mr. Mair: I might say, Mr. Chairman, this is one of the answers we were given at one point. However, as we pointed out, this can easily be restricted and should not be a valid reason for rejecting this wholly.

The Chairman: Oh, no; there could be an exclusion for transactions of that type.

Mr. Mair: Quite.

Hon. Mr. Phillips: It is not for us as a Senate committee to play off one sector of the economy against another, but one question was not raised by the witness. At the foot of page 3 of the brief, where reference is made to eligible expenditures in relation to the broadening of the earning base, the comment is made that the mining industry has done very well but that it has been neglected. Representatives of the mining industry appeared here yesterday and they were very unhappy.

Mr. Mair: If they were very unhappy, then we are just slightly more than "very unhappy".

Hon. Mr. Phillips: They are unhappy, but you say they are well treated.

Mr. Mair: Particularly with the deputation we have here today, I would not like to make the point that they are well treated. I think they have received some concessions in this area of earned depletion which we were not given.

Hon. Mr. Phillips: The gravamen of their case is that they are not so sure they have it.

Mr. R. C. McCallum, Treasurer, Canadian Fina Oil Limited: If I may draw your attention to the chart appended to our brief, it depicts the difference in the treatment of certain items which we have been discussing today. You will see the relative treatment of the items which are eligible, presumed at least, between the two industries.

The Chairman: I do not understand. Please tell me if I am wrong in thinking you are putting your case forward on the basis that your neighbours, the mining industry, are better treated than you. You are putting forward the merits of your case.

Mr. McCallum: We are merely suggesting—and this is just one of the points raised in our brief—that we are in many instances treated comparably with the mining industry but in these specific cases, so far as earned depletion is concerned, we are not.

Mr. Furlong: We are in many ways similar industries, and it is only logical and proper to treat us in a similar manner.

Mr. Mair: That is not to say that the mining industry is getting too much, but that we are getting only one item under the category of earned depletion.

Mr. McCallum: Mr. Chairman, before we leave this matter of earned depletion, we should refer to one other aspect which is now of importance to the industry. As you well know, the industry is on the threshold of a new era as far as development is concerned. It is now expanding into the frontier areas, such as the Arctic islands and the offshore areas of Canada, on the east coast, the west coast and Hudson Bay.

The bill as presently drafted will reduce the expenditures which will fall under earned depletion proportionately to the total cost of finding reserves in the future. This is to say the exploration portion of our total cost of finding and development of oil will not in the future form the same proportion of our total costs as it has in the past.

Historically, these costs have amounted to approximately 60 per cent of the total, whereas in the future, while we do not have statistics available, we anticipate a substantial decrease.

The Chairman: Do you mean by that that once you find and prove a well which can be operated commercially you just go ahead and operate it?

Mr. McCallum: Our problem is that when we find oil in the Arctic islands, or offshore, there are tremendous additional costs involved in providing the equipment necessary to move the oil to market. As the legislation is presently constituted, all these costs will not earn depletion.

The Chairman: They will be entitled to capital write-off.

Mr. McCallum: They will be entitled to capital write-off, but they will not earn depletion.

Senator Connolly: When oil or gas is discovered in remote areas such as offshore or in the Arctic islands, does not the real responsibility of the producing companies cease? The matter of moving those products to the market is a problem for another industry, namely, the pipeline industry, although you may have interests in pipelines.

Mr. McCallum: Yes.

Senator Connolly: Are we referring to your industry or the transportation industry when we discuss the question of moving these remotely produced products to the market?

Mr. McCallum: I may have misled you when I referred to the cost of moving the products to the market. I am not referring to the pipeline or the transportation portion of the costs, but to the hardware and machinery necessary for production.

For example, operating offshore involves the construction of tremendously expensive production platforms which I understand can cost in the range of $20 million to $30 million depending on the size of the field. This type of operation has never before been encountered and, as we interpret the bill, will not qualify for earned depletion.

Senator Connolly: There has been considerable experience in offshore production in the Middle East, the North Sea and the Gulf of Mexico. What is the status of depletion for the structures in those areas?

Mr. McCallum: For example, under the United States law the costs do not particularly apply as far as the depletion calculation is concerned. As Mr. Mair indicated previously, it is calculated as a percentage of the gross income. There is not necessarily a relationship between the costs incurred and the depletion allowance.

Senator Beaubien: It does not have to be earned, but is received automatically.

The Chairman: Yes, that has also been the case here. It would be interesting if we could have an enumeration. The effect of these provisions on the offshore search for oil and the calculation of the costs for earned depletion is a

new consideration. It does qualify for capital cost allowance.

I have seen photographs of platforms and rigs, and everything else, but I am not an oil man and not many, if any, of the committee would qualify as experts. Therefore, if we are going to talk intelligently or deal intelligently with that subject, which may be a special feature now—

Senator Connolly: Especially with the present development in Nova Scotia.

The Chairman: —we should now have some help from you as to the set-up required and the cost of making such a step-up for those developments. The only value they have to us is that they may assist us in our consideration. But we should have them quickly, because these committee hearings will not go on very much longer and decisions will have to be made soon.

Mr. McCallum: I am not qualified to discuss the technical aspects.

The Chairman: I am not thinking of technical aspects, but of items.

Senator Connolly: Mr. Chairman, you are not thinking of getting it today. You are thinking of getting some material supplied to us reasonably quickly.

The Chairman: I would say within not more than a week.

Senator Connolly: Can you do it?

Mr. McCallum: I believe we can.

The Chairman: If you are talking about technical aspects, that is fine, if you wish to write a paragraph on that. But I am thinking about all the elements that go into this set-up that gives you the facility for making your search beneath the floor of the ocean, and even to penetrate that, in order to locate oil. What are the things that go into that? You will have a list, because you are writing them off for capital cost allowance.

Mr. McCallum: I attempted to get some statistical information before I came here. Unfortunately, we are at the stage where we are just getting involved in this type of operation in Canada. We do not have any statistics available. I attempted to obtain some from the United States, but was unable to do so.

The Chairman: Something is being built here now and is working. Therefore, the information must be available. This is an important development to the region where this is going on. I am thinking in terms of Nova Scotia, the Maritime Provinces, and out on the west coast. It is very important. It can improve the economy of those areas very substantially, and it can also improve the employment situation.

Senator Connolly: Mr. Chairman, I wish to make a correction in the record. I am urged to do this by our colleague, Senator Molson. He said that to be perfectly impartial, from the point of view of this committee, we should not talk about Nova Scotia, but about Sable Island.

The Chairman: The designation "Nova Scotia" was intended as a general location of an area. Certainly, Sable Island is closer to Nova Scotia than it is to Ottawa. Are there any other points that you wish to raise, Mr. McCallum?

Mr. McCallum: The only thing that I wish to add is that we will certainly attempt to have something in your hands within a week.

Senator Connolly: Do not fail to say what would be the impact on development offshore of the absence of depletion allowance under the proposed bill.

Hon. Mr. Phillips: The committee has been concerned with the distinction between partnerships and joint venture operations. Obviously, joint venture operations are closely connected with your segment of the economy. Can you help out a group of confused senators, including counsel, as to the basic distinction between a joint venture operation and a partnership, as defined under the new bill? We are trying to get a definition of a joint venture operation with a view to indicating where it differs from a partnership as covered by the statute. It is one of the problems that concerns us.

Mr. Mair: Under the terms of the new bill I could almost join you, because I am also confused. A description of a joint venture, which might help to distinguish it from a partnership, is that if two or more companies join together in what we call a joint venture, each has the right to take its product in kind. We have contacted the Department of Finance officials on this point, and they have told us that it is just a question of law. In other words, if you find an oil well, each can take his share of the production, and each can determine at which rate he wants to write off his capital cost allowance, and all that sort of thing, under the existing act.

We are not certain—and this is one of the points we have made in our submission—that we will not be classed as a partnership, despite the fact that we think we are different from a partnership.

Hon. Mr. Phillips: Do you merge ownership with fixed assets in a joint venture, or do you retain your own ownership?

Mr. Mair: It is owned jointly. All of the equipment is owned jointly. Another difference in a partnership is that each partnership can commit the partnership to whatever actions he may take. In a joint venture operation one partner is designated as the operator and is the person who has the authority to do all the various things necessary to develop and equip the property and to produce it.

The Chairman: That would not be an essential difference. The basics of a partnership would be the sharing of costs and profits.

Mr. Mair: We share the costs, but we hope that the distinction of being able to take the product in kind is something different from a normal partnership. We are not certain of this, and that is the reason why we have made the comment.

The Chairman: Is there not an exclusion in the bill—I do not pretend to know the whole thing—on the application of partnerships to exploration and development? Would that be a method of providing an exclusion?

Mr. Mair: There are some true partnerships, of course. They refer to partnerships in section 66 of the bill.

The Chairman: If, in attempting to deal with those various classes, you used the exclusion method and made it available at the option of the joint venturers as to whether they would go the partnership way or the other way—

Mr. Mair: That is what we recommend.

Senator Connolly: Do I understand that in your industry you have partnerships operating in certain instances and joint ventures in others?

Mr. Mair: That is true.

Senator Connolly: What is the difference between the two, in your industry?

Mr. Mair: In partnerships, individuals—it is because of the way the Income Tax Act is written that it has been done this way—join in a true partnership or a partnership agreement in which each is committed and is liable for any of the actions of the others; whereas, in a joint venture, it is an agreement drawn between two or more companies, generally speaking, in which they appoint one as operator. But he is operating merely to cut down expenses, so that you will not have two or three people operating in the same field.

We go further than that, of course. We then have what we call a unitization, in which all owners put their acreage or their rights into this agreement and one operator produces it. Each owner of rights in that unitization will receive a net amount, even though there may not be a well drilled on his property. A calculation is made of what reserves he has, or the company has, in the whole pool, and he receives his pro rata share of that.

Senator Connolly: This is still a joint venture?

Mr. Mair: It is one step further than a joint venture.

Senator Connolly: But it is still arising out of a joint venture.

Mr. Mair: that is true.

Senator Connolly: So the only distinction as between a joint venture and a partnership would be the arrangements as to the operation.

The Chairman: I do not think that is sufficent to make a real distinction.

Senator Connolly: I do not think it is a legal distinction.

The Chairman: As you know, senator, you can have a limited partnership. In other words, a partner can specify the limit of his liability in the partnership.

It seems to me that the only way to deal with this would be by the exclusion of certain types of operations—not an absolute exclusion, but just the exclusion at the option of the parties. There could conceivably be situations where you might want to espouse what is in the act.

Mr. Mair: That is true, Mr. Chairman, and that is why I agreed with you earlier when you mentioned we should be able to make an election as to whether we wish to be treated as a partnership or not. I might add further that in the tax statutes of the United States there is a provision whereby they can elect not to be treated as a partnership, and, for that reason, many of our agreements state that this is not a partnership.

Senator Molson: Mr. Chairman, is there an element of an agency in a joint verture? In other words, if one company is acting on behalf of the others, is that company not then an agent for these other participating companies?

The Chairman: I am not sure that is what they have described. There would be a boss man.

Senator Molson: Yes, but he is given powers by the other participating companies.

Senator Connolly: I would be inclined to feel that there would be an element of agency, Mr. Chairman.

Mr. Mair: Yes.

Senator Connolly: We are comparing oranges and apples, perhaps, because the legal definition of a partnership is one thing, and the practical operation of a partnership in the oil industry in Canada, as against the operation of a joint venture in the oil industry in Canada, is another thing. The witness is describing what the practical application is. I do not feel we should ask him to define a partnership because we cannot do it ourselves, and some of us are lawyers.

The Chairman: I was ready to concede. I was not ready to abandon the search for an alternative route. I feel the exclusion route is the way. If we attempt to define a partnership we would only create more litigation, but if we provide the exclusion route we would lessen the possibility of litigation.

Are there any other points you wish to develop?

Mr. Mair: There is one other point, and it is in regard to an anomaly under the present act which is carried forward into the new bill. Perhaps I can best illustrate it by using figures: If you were to purchase some petroleum and natural gas rights for, say, $900,000, and then you turned around and sold them to someone else for $900,000, you would be liable to pay $150,000 in income tax.

The Chairman: Where you have no income arising out of the deal?

Mr. Mair: That is right.

The Chairman: That is interesting.

Senator Molson: I wonder if we could learn how to do that, Mr. Chairman.

The Chairman: I was just wondering that myself. I know in the practice of law we have not found any way to do it.

Where is that dealt with in your brief?

Mr. McCallum: It is at page 5 of our brief.

The Chairman: At page 5, half way through the second paragraph, you state: "We know of no other case where a tax is levied without there being a profit".

Senator Connolly: What clause of the bill would this be under?

Mr. Mair: This arises out of a combination of sections 59 and 66.

Senator Connolly: What is your position with your company?

Mr. Mair: At the present time I am the General Manager, Administrative Services. Previously I was the Treasurer of Hudson's Bay Oil and Gas Company Limited.

Senator Connolly: You have not used a note since you started and now you are quoting us sections of the bill.

Senator Molson: Do not get worried, Senator Connolly.

Mr. Mair: A situation could arise where this might have an application. For example, two companies who are participating jointly in one area may have a clause or an agreement under which if one company purchases at a Crown sale, a certain acreage for the purchase price of, say, $900,000, the other company might have 24 hours or one week or one month in which to say it will purchase half of it at a purchase price of $450,000. In that instance you would be deemed to have bought that half at $450,000 and sold it for $450,000 and the tax on that would be $75,000.

Senator Beaubien: How can there be tax if there has been no profit? Is it deemed to be income?

Mr. Mair: It arises because when you acquire a ease you must write it off against depletable income, but when you sell it, it is considered to be non-depletable income, so when you buy it, it reduces the amount of depreciation you are able to claim, and when you sell it you do not get that back.

Senator Connolly: Mr. Chairman, perhaps this requires some explanation.

The Chairman: Yes, we will have a look at it and see what the basic explanation is.

Mr. Mair: I might add, Mr. Chairman, that the house committee did recommend that where there was no gain there should be no tax.

The Chairman: That is a logical principle; it is basic business.

Mr. Mair: Yes, but it is not necessarily logical.

The Chairman: I am not suggesting that they both go together. Is there anything else you wish to add?

Mr. Mair: Mr. Chairman, I have nothing further to bring forward, except that I do have a list of proposed amendments which we would recommend be made to the act.

The Chairman: Do you wish to file them?

Mr. Mair: Yes, I will file them, if I may.

The Chairman: We will have a look at them.

I would suggest, honourable senators, that these proposed amendments submitted by the Canadian Petroleum Assocation be printed in our record at this point.

Hon. Senators: Agreed.

Text of proposed amendment follows:

PROPOSED AMENDMENTS

The Canadian Petroleum Association recommends that the following amendments be made to Bill C-259 or the Regulations proposed as a part thereof:

1. that the Regulations proposed by Finance Minister Benson on July 6, 1971 be amended to cover expenditures from January 1, 1948 to November 7, 1969 in addition to the proposed provisions;

2. that Subsections (i) and (iv) of Section (*a*) of the proposed earned depletion regulations be deleted;

3. that the costs of depreciable assets which must be deducted in calculating depletion should also be eligible expenditures to earn depletion;

4. that Section 69 should be amended to allow the transfer of depreciable assets between taxpayers who are dealing at non-arms-length without attracting income tax;

5. that Section 59 or Section 66 be amended so that the purchase and sale of resource properties be treated in a consistent manner;

6. that the numerous provisions related to partnerships in Subdivision J of Division B of the proposed bill together with 66 (15) (*b*) (iv) and other parts of Bill C-259 be clarified so that our industry does not suffer adverse tax effects from normal joint venture operations.

We note that there are many amendments to the proposed bill, which our Association has not yet been able to completely evaluate but which do not solve all of our problems; for example, the proposed Section 39 (3) changes the impact of Section 80 of Bill C-259 but still remains retroactive taxation.

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The Chairman: We will discuss them later.

Does that close your submission?

Mr. Mair: Yes, Mr. Chairman.

The Chairman: We now have the representatives of the Mining Association of Canada. Mr. C. R. Elliott, First Vice-President and Chairman, Tax Policy Group will make an opening statement and introduce the panel.

Mr. C. R. Elliott, First Vice-President, and Chairman of Tax Policy Group, The Mining Association of Canada: Mr. Chairman, may I begin my introductory remarks by expressing my appreciation and that of my associates and the association, of having the opportunity to appear before you in respect of our views on Bill C-259.

I believe that the Senate's report on the White Paper would have eliminated most of the features of the bill that we now object to. Our association last appeared on June

18, 1970, at which time we discussed the White Paper on Tax Reform. We now have the actual bill before us, and this makes it somewhat easier to be specific. I hope that since we now have the bill you and your colleagues will find our remarks to be of a more particular nature.

We have endeavoured to express views objectively and to make constructive recommendations. You will note that our submission enters into some considerable comment on specific clauses and proposals contained in Bill C-259, and therefore our remarks made today will be concerned more with technical details of the bill than with its philosophical content. However, I should not like to leave you and your colleagues with the impression that there are not still certain philosophical considerations in the bill that remain of very great concern to our industry. The first section of our submission deals with broad non-technical considerations of concern to the Mining Industry.

With me today are the members of the taxation committee of the association. Your Chairman has already identified me. On my immediate right is Mr. John Bonus, the Managing Director and Chief Executive Officer of our association, who recently moved from Toronto to Ottawa, where he now carries out his functions in the executive offices in this city. We have Mr. Donald H. Ford, who is Chairman of the association's tax committee.

The Chairman: We had Mr. Ford here yesterday so we know him.

Mr. Elliott: Mr. David Craig I think you probably also know; he is at the far end of the line. We have Mr. Keith Steeves of Bethlehem Copper Corporation, who I think was here yesterday.

The Chairman: Yes, we know Mr. Steeves.

Mr. Elliott: He is also Chairman of the B.C. Mining Association's Tax Committee, and very familiar with the problems. We also have Mr. Keer Gibson of Clarkson, Gordon & Company, who acts as tax consultant to the Mining Association.

I would like Mr. Ford to comment briefly on two or three matters in the report which we regard as of most concern to us at present, and thereafter we are at your disposal.

The Chairman: I understand that this comment will be addressed to items that materially affect mining companies.

Mr. Elliott: That is correct.

The Chairman: Not general items in the bill.

Mr. Elliott: No.

Mr. D. H. Ford, Chairman, Tax Committee, The Mining Association of Canada: Mr. Chairman, honourable senators, I realize that some of what I propose to say has been said to you at least once before and I will try not to be any more repetitious than I have to be. However, some of these points are so important to us that I think they need emphasizing.

Our brief deals with problems we see in the bill itself and problems in the proposed regulations. As you know, the regulations governing the mining industry are not yet available. What we have is a news release issued by the Department of Finance in July of this year outlining the proposed regulations.

Senator Walker: This is what you were speaking about yesterday, is it not?

Mr. Ford: Yes, sir. There are two important points about this news release, although there are lots of others which we can discuss if there is time or interest. First I would like to discuss the exclusion of expenditures on Canadian exploration and development expenses in the vicinity of a mine after it comes into production. Both exploration and development expenditures in the vicinity of a mine should, we believe, earn depletion. First of all, the word "vicinity" has us puzzled. It is difficult to define. Somebody said that it means "in the neighbourhood of", but that is a fairly vague term. The exclusion of underground exploration is one which puzzles us. We believe that the reason for the exclusion is that the Department of Finance sees great difficulty in differentiating between underground exploration and on-going mining. I think they believe also that little incentive is required to encourage mining companies to undertake exploration underground.

The Chairman: You know, Mr. Ford, you say by way of explanation that the department is having difficulty in distinguishing between underground development and the development that flows along in the operation of the mine.

Mr. Ford: That is my inference, sir.

Mr. D. B. Craig, Member, Tax Committee, The Mining Association of Canada: We are specifically speaking at the moment of underground exploration.

The Chairman: I was going to comment that there are in litigation at this time issues which involve this very question, and these distinguish between the two bases. The Department of National Revenue has been able to make the distinction for purposes of making an assessment, and they have submitted their evidence in court. Therefore I am not sure it is a very good explanation as to why the difference cannot be recognized.

Mr. Ford: I think that is true. Essentially the words in the act governing exploration are "searching for minerals in Canada" as opposed to delimiting a known orebody, determining the extent of a known orebody. The element of search is not present in that situation, whereas in true exploration you are searching for minerals. These are the words of the present act.

The Chairman: Underground exploration would be the search and exploration for minerals.

Mr. Ford: Yes, sir. I do not think that many companies lightly undertake underground exploration in preference to surface exploration. It is an extremely expensive operation. The cost of driving a drift underground in order to explore is in the order of $100 a foot. A 2,000 foot drift is in the order of $200,000. It just is not possible to drill accurately at any depth from the surface. The point of a drill, as I understand it, tends to wander as you go deeper, so if you are looking at a 3,000 or 4,000-foot depth under the ground in the vicinity of an existing mine you must make your exploration expenditures from underground; this is a

high cost operation and is being excluded from the earning of depletion, which we think is unfair.

Senator Beaubien: What would be the reason for excluding it? Is there any reason, or is it an oversight, do you think?

Mr. Ford: I believe—and this is a personal opinion—that the exclusion arises out of the difficulty the Department of Finance sees in separating true underground exploration from ongoing exploration of a main orebody, which the chairman commented on.

The Chairman: If you are taking a mineral out of a certain level below ground, that is a well recognized type of operation. If you have drills working underground to go to much lower areas to see whether there is a continuity of ore and continuity in grade of what you have, these would appear to be assessments more closely related to exploration than to looking ahead to provide feed for your mill.

Mr. Ford: Yes, sir. Consider two situations. If you have the alternative of moving one hundred miles down the road and doing exploration from the surface you are assured that will earn depletion. If you have a good a prospect in an existing mine and you explore it from under the ground, you are assured that that will not earn depletion. What choice are you going to make? What implications are there here for an established mining community, perhaps, where additional ore would prolong its life?

The Chairman: Have you any suggestions on what language might be used to expand this item?

Mr. Ford: I think the exception needs to be removed. The exclusion from the element of expenditures to earned depletion, which is in the outline of the news release of July, 1967, should be removed.

The Chairman: What is the language of the exclusion?

Mr. Ford: Eligible expenditures include the following: Canadian exploration and development expenses in the mining and petroleum industry, except for Canadian exploration and development expenses in the vicinity of a mine, and after it came into production. There is a list of four exclusions there.

The Chairman: Yes.

Mr. Kerr Gibson, Tax Consultant to the Mining Association of Canada: It is probably contemplated that the regulations would use the expression "exploration and development" in searching for minerals. I think the industry's submission is that that would make a satisfactory distinction between exploration and ongoing development of the mine, so that no exclusion for exploration in searching for minerals in the vicinity of a mine would be dealt with.

Mr. Ford: Mr. Gibson is saying the key is the searching for minerals, which is the wording of the present act.

Mr. Gibson: If the company is merely doing development work in the extraction of known ore, it is not qualified as searching for minerals and the distinction will be made.

The Chairman: What you are saying is that once you open up a mine you cannot have exploration and development expenses thereafter.

Mr. Elliott: Mr. Chairman, I think what he is saying is that there is a distinction between underground exploration and the development of an already discovered ore body. They are two different things, and work carried on within the area of a known ore body would be mining operations, whereas exploration is work which is carried on, either from the surface or from underground, that is not within the area known to contain mineral of ore grade. I think that is pretty well what he was saying.

The Chairman: Anyway, I think you have told us enough to understand what the problem is, and whether you should and, if you should, how you would correlate underground work to exploration and development in an existing mine.

Senator Connolly: In a given situation I suppose that you could conceive of a possibility of confusion, as to whether you were working the existing ore body or in fact looking for a new body, exploring for new ore. I suppose there are particular problems in this area.

Mr. Ford: I believe, as the chairman said, that there have been some problems and they have been settled and the courts have decided.

The Chairman: Some of them are in litigation. The department has settled them by making assessments or re-assessments and they are in litigation.

Mr. K. E. Steeves, Member, Tax Committee, The Mining Association of Canada: Our recommendation would leave it so that the taxpayer would have the onus to prove that the expenditures were exploration rather than on normal development.

Senator Benidickson: May I point out that we had the problem of determining what was a new mine and thereby entitled to a three-year tax exempt period. The government had set up, for that determination, a committee. They did not leave it entirely to the Department of National Revenue. They had a committee representing certainly the mining department, the National Revenue Department, and probably the Department of Finance. It was not left entirely to the tax collector and the National Revenue people to determine whether it is a new mine. They did have a long-term practice of getting the technical assistance, for determination, of the mining experts in the Department of Mines. Problems of this kind may have to be worked out by the tax department, with some assistance from the other departments.

The Chairman: Except that they do not give themselves any leeway in the bill.

Senator Benidickson: In the statute.

The Chairman: There should be leeway in the bill for the determination.

Senator Benidickson: It may be a recommendation from this committee. We may see the necessity of recommending that something of this kind be continued, as was the

practice to determine what was in fact a new mine under the old principles.

Mr. Ford: If I may say so, the Department of National Revenue in fact does this in a determination of what is underground exploration now. I know the situation whereby the Department of Mines and National Resources was asked by the Department of National Revenue to advise whether expenses claimed by the taxpayer as underground explorations were in fact underground explorations.

The Chairman: But if you have an exclusion, the door is shut on that.

Mr. Ford: It is not quite shut, sir. It is the end of the matter, but then there are still the courts and they are called on to decide the matter in this instance.

Mr. Elliott: I suppose the regulations would shut the door.

The Chairman: Yes.

Mr. Gibson: It is noteworthy that while these distinctions can cause problems, they do not in fact decide many problems. There have been very few cases which have been brought to the attention of the courts to be resolved in the past.

The Chairman: I think we both know about one, anyway.

Mr. Gibson: Yes, but there have not been many and I think the main problem would be resolved.

Mr. Steeves: On the honourable senator's suggestion about this committee under the new act, the definition of a new mine is going to be every bit as important as it was before. In the past, there were the write-off provisions. So I think the continuation of this committee is assured, and this may probably be another factor that might be considered.

The Chairman: I think we have got a grasp of what the problem is and where there may be some remedy.

Mr. Craig: It is an important point, in the sense that, to the extent that it does not apply to underground exploration, because of the expenses, the companies perhaps will not do as much underground exploration. They will not find those ore bodies that might be near an existing mine—which may support the existing communities. To the extent that you do not continue to explore an existing mine or ore body area, the life of the community is shortened.

I think part of the history of the mining business has been that they do not like to leave communities in the lurch after the ore body is exhausted. What we are saying is that this kind of exploration should be encouraged, for that reason alone, not only because the other way produces inefficiencies as well. We think that the proposal is not efficient and also that it creates certain social upsets in those communities.

The Chairman: It is not unreasonable. As a matter of fact. I can recall a number of mines that carried on and, as they started to exhaust more and more of their known supply, it was only at that stage, by going underground and doing underground exploration and development, that they were able to enlarge and expand the life of the mine.

Senator Benidickson: That has happened in many cases.

The Chairman: Yes.

Mr. Craig: We have the history in our company, of the Creighton Mine, which is now down to its ninth shaft. Creighton has been dead, and advertised as dead I do not know how many times in its history, but it again continued underground exploration and has found ore bodies quite a way from the existing level. As a result, the mine continues and it is now down 7,000 feet and the community still exists.

Senator Connolly: Where is that?

Mr. Craig: It is the Creighton Mine, in the Sudbury area.

The Chairman: There is another one that you must recall, Preston East Dome. I think it is finally doomed now, but it lasted for many years longer than the available ores or reserves as they then knew them, over what would keep them going. But they kept poking out and down and up and drilling, and that would certainly be underground development.

Mr. Craig: Underground exploration is not difficult to define, because it is done by a quite different people in the mining field, the exploration people. They are usually away from the existing ore body rather than in the existing ore body, so we do not see a technical difficulty really in assessing that, as far as the department might be concerned.

The Chairman: Thank you very much. What is the next point?

Mr. Ford: The second half of this exclusion, sir, is the exclusion of development expenses in the vicinity of the mine after it came into production.

The Chairman: We talked about that yesterday.

Mr. Ford: That was in respect of an open pit mine. This relates to the underground mining operation. If you have two identical ore bodies and the owners of one are a wealthy mining company with access to capital while the owners of the second are a small company with less access to capital, an unfair situation can develop. Presumably, the first mine can be predeveloped to sink the shaft to the depth it needs to go eventually to drive the drifts and make all the workings for the extraction of the ore from the mine, because the first company has the capital to do so, and in that case every nickel it earns will earn depletion. The second mine, perhaps with no financing at all, will only sink its shaft part way. it will only spend as much on development as it needs to in order to generate a cash flow. The second mine, which will continue the development after it attains the cash flow, will finish up with a mine developed in the identical fashion as the first one except that the earned depletion of the first mine will be substantially greater than that of the second. This to us does not seem to make any sense.

The Chairman: I remember that yesterday we had this point developed by Bethlehem Copper.

Mr. Ford: Yes. We believe that the cost of permanent underground workings, the present class 12 in Schedule B

of the Income Tax Act, those expenditures should qualify to earn depletion regardless of the moment in time at which the money was spent—whether it was spent before or after the mine came into production.

The Chairman: Have you got language?

Mr. Craig: All exploration and permanent underground development should qualify to earn depletion. That is the way we would put it.

The Chairman: What is your next point?

Mr. Ford: The third point in this group, sir, is on the development costs of a major expansion of an open pit. I don't know whether you want me to spend any time on this.

The Chairman: We had something on that yesterday. Is there anything you wish to add?

Mr. Ford: I don't think so, sir.

The Chairman: It is all addressed to these proposed regulations and their provisions.

Mr. Ford: Yes.

The Chairman: I am not hurrying you but we did have it yesterday. We understand the point and, as a matter of fact, even now we are working on it.

Mr. Ford: Yes, sir. The second exclusion from earned depletion that I should like to mention is the exclusion of so-called social and industrial infrastructure expenditures from those which will earn depletion. To us it makes no sense that these expenditures should be excluded from earning depletion. I refer to expenditures such as railroads, off-property roads, docks that are distant from a mine, houses for the employees, recreational centres, hospitals, schools and the kinds of things that you can think of. We do not really see that the dollar you spend on a dock, which may be 30 miles from a mine but is necessary in order to move the product of the mine, is any different from the dollar that you spend on the concentrator, which produces the product you are going to ship to the dock. We don't see any difference in the dollar you spend on the employees either, because without houses you don't have employees.

Senator Benidickson: And without the ore the houses would be abandoned.

The Chairman: Without the ore they would not be built.

Senator Benidickson: Or they might have a shorter life than any other community.

The Chairman: We have had instances of that very recently in certain areas not too far from where you make your home base, senator.

Mr. Ford: Our industry is frequently required to make these expenditures in remote areas, you know, and I hope it is for the good of the country. But it is really a distinction which seems to us to be quite unnecessary, in saying that this dollar will earn depletion but that dollar will not. The thing is really a package and should not be separated.

I might mention in what you refer to as the "raspberry book", that the initial proposal was that the industrial infrastructure—that is, airports, docks and off-property roads—would earn depletion but the social capital, that is, the townsite and employee welfare expenditures, and so on, would not. That is part way to what we want, but in the outline of the proposed regulations those two have been put together and both are disallowed from earning depletion.

The Chairman: Social capital under the proposed regulations will qualify for a fast write-off.

Mr. Ford: Yes, they would, sir, but not on a major expansion of an existing mine, which seems to me to be a bit anomalous.

Mr. Craig: This particular proposal was almost universally recommended by your committee, by the Commons committee and by the province of Ontario and the province of Quebec. For some reason, however, it has been dropped. It is difficult to understand why they are not going to permit this to earn depletion. Perhaps the only answer we can get at the moment is that they suggest that the degree of risk involved in these kinds of expenditures is not as great as the degree of risk involved in the mining complex *per se*. But we would suggest that the degrees of risk involved are identical to the extent that you have ore. To that extent everything is involved in exactly the same risk. I am at a bit of a loss to understand why this was dropped.

The Chairman: If I understand the difference, it is that in relation to the expansion of an existing mine that is one category where you do not get entitlement.

Mr. Craig: The accelerated fast write-off?

The Chairman: Yes. If it is a new mine you would get the accelerated write-off.

Mr. Craig: So long as those expenditures were made before the mine came into production.

Mr. Gibson: In neither case would they qualify for the earned depletion allowance.

The Chairman: So the question we have to look at is why should there be a difference in treatment of identical expenditures between the category of a new mine and the category of an expansion of an existing mine. Is that right?

Mr. Ford: Yes, that is correct.

Mr. Steeves: There is the difference also that the one that earns depletion is the one that has the fast write-off. The problem that we have is that they are recognizing the fast write-off. The townsite expenditures are allowed to have the fast write-off for a new mine, but they are not allowed to earn depletion.

The Chairman: I understand that this is the difference. In the expansion of an existing mine, for those expenditures you can get your capital cost allowance, but you cannot earn depletion. Is that right?

Mr. Ford: That is with a new mine. With the expansion of an existing mine the infrastructure is not eligible for the fast write-off.

The Chairman: We are talking about two different things. There is a fast write-off and there is also a capital cost allowance which may be at whatever the regular rates are. In the expansion of an existing mine, certainly you would be entitled to the capital cost allowance, but you would not be entitled to the accelerated, which is 50 per cent a year.

Mr. Ford: No, it is up to the income from the expanded mine. That is, you can write off as fast as you have income from the expanded mine, which could be 100 per cent in one year and 10 per cent in another year.

Mr. Gibson: To the industry, much the more important point is the qualification for earned depletion.

The Chairman: Yes. The question there is why there should be a difference. Why on identical expenditures should you be able to earn depletion on a new mine but not be able to earn depletion on the expansion of an existing mine?

Mr. Gibson: Perhaps I should amplify the point a little. In the case of earned depletion, social and infrastructure expenditures would not qualify in the case of a new mine or an expanded mine. What the industry is saying is that this expenditure involves the same risk as the mine expenditure which qualifies.

Mr. Craig: Earned depletions simply do not qualify, period. None of these costs would give you $1 for every $3.

The Chairman: Then I guess you would subscribe to a statement made earlier in this committee that anything that is entitled to be written off in the course of the development of a mine should also qualify for earned depletion. Would you support that?

Mr. Gibson: Yes, that is right, that is anything related to bringing a new mine to production or an expanded mine, yes.

The Chairman: In relation to mining generally, whether it is in relation to the expansion of an existing mine or the development of a new mine, anything that is entitled to be written off by way of capital cost allowance, those write-off should also qualify for earned depletion.

Mr. Elliott: Those expenditures that are entitled to a capital cost allowance should qualify for earned depletion.

Mr. Ford: Including also development expense.

The Chairman: Everything that is done in the development of a mine to bring it to production, or everything that is done to expand an existing mine for the purpose of bringing it into production surely should qualify.

Hon. Mr. Phillips: That would eliminate the cost of roads and rights-of-ways. They are not subject to capital cost allowance, or should not be included.

Mr. Ford: Most of them are included because we have special categories.

Hon. Mr. Phillips: You are all right then in relating it to capital cost allowance?

Mr. Ford: What we are saying is that we have come a long way since the Carter Report, and we have come a long way, perhaps, since the White Paper. But we are unhappy with this concept of earned depletion on a too narrow base. If we could see some line of logic there—

Hon. Mr. Phillips: I was concerned for a moment that on expanding your depletion base to include expenditures involving capital cost allowances that you do not eliminate other expenditures that should be included in the base.

Mr. Steeves: Expansion and development expenses should also be included.

Hon. Mr. Phillips: But we have already covered that point.

The Chairman: Mr. Gibson, anything that would qualify for earned depletion qualifies for capital cost allowance.

Mr. Gibson: I do not think that is true in relation to exploration and development expenses. But apart from that I think basically that would be the case.

Hon. Mr. Phillips: Could you not get costs on acquisitions that might not qualify for capital cost allowance? Do you not need capital cost allowance on the costs of acquisitions and exploration and development expenses?

Mr. Gibson: That is right, we do. I thought the chairman's question was that at the present time as the rules are written I think anything apart from exploration and development expenses would qualify for earned depletion.

Hon. Mr. Phillips: Yes, but if we were looking for an expanded base for depletion purposes would we not have to say quite broadly—

Mr. Gibson: Yes, that would be very helpful.

Hon. Mr. Phillips: We were thinking of the earned depletion base being related to the cost of exploration and development expenses and all expenditures in respect of which capital cost allowances are allowed, whether they are accelerated or otherwise.

Mr. Ford: All costs which bring a mine to production or expanding an existing mine, the total input into the mine should be allowed.

Mr. Elliott: I think that for the record there may have been some confusion in the use of the technical term capital costs. All of these things are subject either to capital cost allowance as defined in the act or to an expense *per se* as in the case of acquisition of properties as it is under the bill we are considering. I feel that the chairman's point is well taken. There might be some of these which on the technical interpretation of the words "capital cost" we do not mean capital cost. However, all capital expenditures which are entitled to be claimed as a capital cost or write-off should qualify for earned depletion.

The Chairman: Yes.

Mr. Ford: We have not mentioned the 3-year tax exemption. But, of course, the accelerated write-off is designed to replace that.

The Chairman: I feel that at this stage we have tried to deal with the tax holiday situation and we did not succeed.

Mr. Ford: The only comment I would like to make in that respect is that, I believe in the August 1970 News letter, the letter to the provincial ministers of finance and treasurers, Mr. Benson made a statement to the effect that major expansion would be put on much the same basis as new mines by excluding the write-offs for infrastructure expenditures and by not putting them on the same basis.

The Chairman: What is the next point?

Mr. Ford: The next point is the expenditure of processing assets in Canada, to process Canadian ore, only to the stage it was previously processed in Canada. This apparently will not apply across the board although as we understand it the intention of the Government is to induce additional smeltering and refining facilities in Canada. Our understanding is that the earned depletion will not apply to expansions of existing smelters and refineries which, it appears to us, expresses two different wishes of the Government.

The Chairman: There are two different areas it will not cover. It will not cover the expansion of facilities of existing smelters, nor will it cover the situation where you are doing custom smeltering.

Mr. Ford: That is right. If it were associated with a major expansion of a mine, the expansion of the processing facilities would qualify; but on a custom operation it would not and this makes no sense to us at all. There is no spare smeltering or refining being done in Canada.

The Chairman: I think a simple comment would be that if you do not permit these write-offs on custom smeltering jobs, you are penalizing the industry by increasing the cost, or you are preventing the smaller mines from being developed and therefore you are lessening the provision for jobs . . .

Senator Connolly: Or you are exporting processing and employment

Mr. Ford: And you are running counter to the policy of the major provinces where mining is an important industry where they have certain penalties in the matter of royalties, leases and so on. They have imposed penalties where certain refinements and extra processing is done elsewhere outside the province or outside of the country.

The Chairman: That is right.

Mr. Ford: At least one province has encouraged processing in Canada by providing for additional write-offs.

Senator Benidickson: That is what I meant by running counter to provincial policies, which either provide incentives for further processing within the province or the country,—

The Chairman: Or penalties for not doing so.

Senator Benidickson: They either provide incentives or penalties for the purpose of encouraging further processing within this country. This seems to run counter to that.

Mr. Craig: In the situation of an existing mine and mill, the development of another mine and expansion of the existing mine will obviously necessitate the expansion of the existing milling operation. At that time it may be decided to smelt the ore on site. The expanded mill probably would not qualify because it is not new from the ground up. The smelter and part of the new mine would qualify but unless the expanded mine is 20 per cent of the existing milling capacity it does not. Therefore, it is really not known whether the smelter would qualify in full. Our suggestion is to erase that, because the name of the game is to generate more processing in Canada.

The Chairman: What would the language be?

Mr. Craig: Just that.

The Chairman: Maybe you have to use that many words in order that we understand. What would be the language for such a provision? The place, I take it, would be in the proposed or similar regulations.

Mr. Craig: Our point is that the cost of increasing Canadian processing should qualify for depletion.

The Chairman: We know the rationale and we will now go to the next point.

Mr. Ford: The next point arises from the statements of the previous witnesses. We are concerned with one or two sections of the industry which appear to be having hard times, particularly the potash group of mines, which generally came on stream in 1968 and 1969, before the publication of the White Paper. The expenditures made on their plants, which are very sizable, particularly in Saskatchewan where the shaft-sinking cost is enormous because of the underground zone which tends to let water in very readily, had no depletion.

The potash market itself has been in a depressed condition; there has been a provincial limitation upon production. Therefore the three-year tax holiday, or that part of it up to December 31, 1973, which they received and the present system of earned depletion, which continues to 1976, is really of very little value to those operators.

When the White Paper was under discussion there were suggestions that some relieving provision should be introduced. This follows the statements of the representatives of the oil industry this morning. The depletion that would have been earned from those expenditures to bring the mines into production should be calculated and the depletion actually claimed up to the introduction of the new system deducted. We have recommended before that it should be allowed to carry into the new system any balance of such depletion.

It seems to me that there is a hardship involved here through no fault of the operators of the mines.

The Chairman: Do you mean to the extent that they have not recovered their total outlay they should be able to carry it forward?

Mr. Ford: Yes, because their investment was made on the basis of the system as they knew it. They had every reason to believe that the depletion would continue and the three-year exemption would be of value. Because of the interference of one level of government, perhaps for its own reasons, in the production of those mines, they are unable to earn a reasonable rate of return on their investment.

Senator Benidickson: You are speaking of prorating, such as in potash because of poor markets.

Mr. Ford: That is right.

Senator Molson: In fairness, the price is also a factor.

The Chairman: Yes, but you have to live with the price.

Mr. Ford: It is a factor, but I believe some of those mines had already forecast the potash market and had made certain arrangements to sell their production. However, they were not allowed to produce all they could perhaps have sold.

Also in the field of earned depletion, we do not understand why although the purchase and sale of mineral properties will be taxable under the new system, the cost of the mineral property required to develop a mine should not qualify for depletion.

The Chairman: We have heard that before, that the cost is a deductible item and the sale price generates income.

Mr. Ford: Yes, fully taxed.

The Chairman: Would the pollution cost be a general expense, or is that considered to be a capital item?

Mr. Elliott: Under the new bill, as I understand it, the cost of acquisition qualifies as expense, whereas the sale will be taxable after the transition on the full amount realized without relation to any depletion allowance. The deduction of the original cost would have reduced the amount of depletion.

The Chairman: Maybe the answer is that the capital gain should apply, because the cost has been allowed as an expense, then the income, which should be the gain, would be received. Certainly it would be better to pay 50 per cent than 100 per cent.

Mr. Ford: There are transitional provisions to recognize that these properties have a cost, in that in the first year of the system only 60 per cent of the proceeds will be taxable and so on up to 1980, when the whole property will be taxable.

Our point is that the expenditure should earn depletion.

Mr. Elliott: that would be in accordance with the Chairman's suggestion or, alternatively, it should be determined as mining rather than general income.

The Chairman: As I understand you, Mr. Ford, you wish the cost of acquisition of properties to qualify for earned depletion.

Mr. Ford: Yes; it is presently excluded.

The Chairman: It seems sensible; all mining operations start from the acquisition of the property.

Mr. Ford: It is now a deductible expenditure similar to any other exploration expense.

Mr. Steeves: That points up the problem of the loss of depletion experienced by the previous witnesses.

Mr. Elliott: That would automatically be included in items necessary to earn depletion.

The Chairman: Certainly the acquisition of property would qualify.

Mr. Ford: The last point on the use of earned depletion is that there is an anomaly in the Income Tax Act which requires the deduction of exploration and development expenditures before arriving at the base upon which the present percentage of depletion is calculated. This is continued in the new act in that you will have to deduct exploration and development expenditures before arriving at the base, which tells you how much of your earnings have been used. The more you spend on exploration and development, the greater your earned depletion bank becomes, but the slower you can use it. You have to do your exploration in alternate years.

The Chairman: You would prefer to be able to earn depletion before you reduce your income or earnings by the deduction of all these expenses?

Mr. Ford: Yes, sir. The Department of Finance pointed out this anomaly in its White Paper, and it does not make sense to us to continue this.

The Chairman: There are quite a lot of ramifications in that.

Mr. Gibson: It is not such a major change. It really only affects the rate at which the depletion earned can be obtained by the company.

The Chairman: If you reduced your earnings by all these expense items, there is less against which you can charge your earned depletion, and, therefore, it is spread out over a longer period of time. But on your capital cost allowance you do not have to take them. You can take them whenever you have money.

Mr. Gibson: The industry's proposal, that this restriction be withdrawn, is not an enormously expensive proposal for the Government to consider. Mr. Ford's point could be demonstrated by the simple statement that when the system matures, a company that is spending more than half of its income on exploration would have earned depletion which it would not be able to claim.

The Chairman: If you charge off against your earnings all the items that you expend, and which will earn depletion for you, the base which you have to charge off those earned depletion allowances will be less.

Mr. Craig: The more you spend on exploration, the less you actually get in that year.

The Chairman: That is right, unless you increase your earnings by the expenditures.

Mr. Steeves: You have to recognize that exploration and development is something apart from your operations, and

you are allowed depletion against the operations. Perhaps you should lump the two together, but your limits would be the same.

The Chairman: We had this put forward at the time we were studying the White Paper.

Mr. Steeves: There is a paragraph about that in the White Paper.

Mr. Ford: As you know, the approach of the news release was to outline the new regulations and to describe the kinds of assets which would qualify for accelerated depreciation in the four categories. It then went on to earned depletion, and in that discussion it referred back to the categories of assets that would earn accelerated write-offs. There are a lot of small points in there.

The Chairman: Is it dealt with in your brief?

Mr. Ford: Yes, on page 16. In order for an asset to qualify for fast write-off, and therefore qualify for earned depletion, it must be new. This seems to be unreasonable, because it interferes with an economic decision of management. If a motor is available for $2,000 new and you can buy a good used one for $1,500, why should you be penalized and not earn depletion? There is a substantial market for used equipment. I could show you half a dozen catalogues listing various used mining equipment for sale. The important point is that it should be new to the taxpayer rather than brand new. It seems to be a distinction that serves no useful purpose.

Senator Connolly: In your example you talk about a motor that would cost $2,000 new and $1,500 used—

Mr. Ford: If you buy a used one you do not get an accelerated write-off and you do not earn depletion on the $1.500.

Senator Connolly: The person who originally bought it got the accelerated write-off.

Mr. Ford: The Government was trying to give him an incentive to develop a new mine.

Senator Connolly: And you want the same incentive for the second user.

Mr. Steeves: If you make the assets subject to recapture on sale, I do not think there is any loss to revenue.

Senator Connolly: That is right. There would be a recapture.

Mr. Ford: The second point in the same group of words is the requirement that the assets be acquired before the mine came into production. I believe you heard Mr. Steeves speak to this point yesterday. It seems to be an unreasonable requirement in that a decision to further develop the ore in an integrated mining operation may not be made immediately, or perhaps cash is not available to continue that further development.

Providing that the complex that is being constructed is attributable to the new mine, it seems that all those expenses should qualify. It may be a large mine and a decision is made to build a smelter. Perhaps the size of the mill has to be increased, and you would need some funds generated to do it.

It might arise that in your design of the mill you buy one kind of mining equipment, but it is not satisfactory and you decide to replace it with a more expensive kind. It seems to me that that is part of the real cost of mining production, and any increased costs should earn depletion. It sounds like a small point, but we can see difficulties arising from it.

Senator Connolly: Under the proposed regulations increased costs would not qualify?

Mr. Ford: No sir. The assets must be acquired "before the mine came into production".

Mr. Craig: Perhaps I can give you an example from the Thompson Mine. In the process of developing our mine, the decision was made that they were going to mill and smelt the ore only. Halfway through the development stage they decided to refine the material at Thompson. The mine came into commercial production before the refinery was completely built. Any additions to that refinery after the mine came into production would not qualify. We had certain infrastructure costs. The refinery was not quite completed before the mine came into production. Those infrastructure costs would not qualify after the mine came into production.

The Chairman: You could not earn depletion on it.

Mr. Craig: No. Not everything works as well as you would like it to work. You have equipment changes and de-bugging operations. These all relate to a new mining operation. We say that within a reasonable period of time, say two years after the mine comes into production, those costs should qualify for the fast write-off and consequently earn depletion.

Senator Connolly: Can you find any reason why the department drew the line that way?

Mr. Steeves: It is easy to administer. You had to set a date. Everything that is turning up on that day qualifies, and everything that is not, does not.

Another example would be mill deliveries from new mines. The number we have had in the last few years is quite small, and you will often get a mine starting at a slower rate, but it will end up in quite a reasonable time because the mills will be phased in as they are delivered. it is unreasonable that the second and third mill should not qualify.

The Chairman: I suppose it raises a question of replacement as against the completion of the mill or the project?

Mr. Craig: We are suggesting a two year period for the mine to come into production. I do not think that is unreasonable.

The Chairman: And whatever you have to do during those two years would be treated as part of the original development.

Mr. Craig: That is right. It would allow the replacement of an asset for two years . . .

Senator Benidickson: If there were bugs in it or because of late delivery.

Senator Beaubien: If it was defective you would have to replace it.

Senator Connolly: I am just wondering whether you are going far enough. I suppose there must be situations where you order some new, sophisticated type of equipment which, perhaps, you are going to try out and after it has been in for a couple of years you find it to be impractical and so you decide to remove it and put something in which has been tried and proven. In those circumstances, surely you are entitled to get depletion on that.

The Chairman: It is a question of whether they get earned depletion on it. They would certainly get write-off.

Senator Connolly: Yes, but earned depletion.

Mr. Craig: We would not get the benefit of a fast write-off.

The Chairman: When I say you would get the benefit of a write-off, I am referring to the regular—

Mr. Craig: It is rather confusing because some of the things in fast write-offs also apply to earned depletion.

Mr. Steeves: Another example similar to what you describe, and this happens quite frequently, is as much as you attempt to test the metallurgy in a new mine, you are doing it in a laboratory and quite often it works out differently when you get the machinery installed; when you first turn it over you are liable to find your recovery is not what it should be and you end up rushing in some grinding capacity or some crushing capacity, or some flotation equipment. You would probably have had it installed for six months and, therefore, it would not qualify, and you have enough problems as it is with the necessary changes which you did not contemplate, so, surely, you should get some depletion.

Senator Molson: Who decides when the mine comes into production?

Mr. Ford: The Department of Revenue.

Mr. Craig: There is a rule of thumb, senator, which says that it is into production when you are at 60 per cent capacity. This is a rule of thumb. I do not think this has been changed.

Mr. Elliott: I believe they would have to continue in the present committee system with regard to qualifying new mines for the tax holiday.

The Chairman: Yes, the same method.

Mr. Ford: This is an interesting question. This is not the law; it is a matter of interpretation, and as Mr. Craig said, it is when you are at 60 per cent of the capacity. In other areas, unrelated to mining, the rule of thumb is 25 per cent of production.

The Chairman: They have a purpose in reducing that and it is to give them the help of the money faster.

Are there any other points on this?

Mr. Ford: Not really. There are several small points where we see difficulty with the wording of the regulations in dealing with the Department of Revenue. These are covered quite adequately in the brief, so I will not take up your time with them.

In terms of the proposed act we have made some comments on several significant sections.

The Chairman: Where do these appear in your brief?

Mr. Ford: At pages 10 to 15. I do not think I need take your time unless you would like me to discuss the comments on foreign exploration and transfers of mineral property?

The Chairman: Have you drafted something in that regard?

Mr. Ford: We make comment on it in the brief.

The Chairman: That will be fine.

Mr. Ford: Mr. Steeves has a point he would like to make.

Mr. Steeves: In our discussions this morning we talked about earned depletion on further processing assets. One of the major points in that regard is that smelters and refineries will only be eligible for the fast write-off provision if they are part of a new mine or a major expansion; they themselves will not be considered a major expansion. I feel this is insufficient if we want to encourage further processing in Canada; we should allow the fast write-off.

Mr. Elliott: Mr. Chairman, we have probably covered the main points in our brief. There is just one suggestion which I would like to throw out to the committee, and that is this: There has been a suggestion from members of our association that they would be pleased to have officials of the Department of Finance who are struggling with these regulations to visit some mines. Many of them have indicated in private conversation that this is something they have never done and they would appreciate the opportunity to do so.

The Chairman: Have you made a written offer?

Mr. Elliott: This is now in Mr. Bonus' hands; he will proceed with that.

Senator Burchill: Have any officials visited the mines at all? This is a worthy suggestion.

Mr. Elliott: If your committee, sir, would add the weight of your approval to our invitation, it could smooth the way for those officials to accept our invitation.

The Chairman: We could note in our report that it might be advisable and educational.

Senator Benidickson: Mr. Chairman, going back to our many months of study with respect to the White Paper, my recollection is that the industry, when the White Paper was published, became alarmed to the extent that expenditures stopped; that, of course, had a significant effect on the designers of the White Paper and the Minister of Finance. At the time we were discussing the White Paper the industry got some support from the provincial governments, and it was quite obvious in midstream that the Minister of

Finance felt obliged to announce the cancellation of certain proposals in the White Paper.

He addressed his proposed changes not only to your association, to give you some encouragement in order to get going again, but he acknowledged that he had received protests from a number of provincial treasurers.

With respect to this new proposed act, which is another kettle of fish altogether, has your association made representations, as you did at the time of the White Paper study, to the provincial treasurers as regards the effects on your industry, and, if so, have you had any indication that they support you in any of the propositions that have been put forward in your presentation?

Mr. J. L. Bonus, Managing Director and Chief Executive Officer, the Mining Association of Canada: Perhaps I could answer that, Mr. Chairman. The point is covered in our brief to the extent that we do explain that if the tax abatement percentage points are now being made available to the provinces were to be taken up by the provinces the industry would be worse off than it was in the first place. Conceivably the industry could actually pay at that stage a tax level which would be higher than most of the other industries in Canada, let alone the other mining industries in the world. I believe that this point has been made by some of our provincial mining associations to the provincial authorities, and I believe that there are some assurances from some provinces to the effect that they do not intend to increase their mining taxes, but, of course, we do not know what the future may hold.

Senator Connolly: That is only as good as the undertaking of the government that gives it, I suppose, because another government would not necessarily feel bound by it.

Mr. Ford: If I may add this, the provincial mining associations' tax committees have made representations to the provincial mining ministers with respect to the very problems we have discussed here this morning. I know that on an individual company basis, discussions have been held in at least Ontario and Quebec with the revenue officials of those provinces, pointing out the problems we see.

Mr. Craig: We have been requested to clarify some aspects of the regulations, so we have done this, at least in our case with the Province of Ontario which did not understand the regulations in depth and asked for our clarification. This we have given.

Senator Benidickson: They have not indicated to you whether or not they will officially endorse any of your propositions, now that they have looked at the regulations, by communicating with the federal officials?

Mr. Craig: They need this data for the federal provincial conferences. Our part was really to try to be informative. What they take from that is entirely up to the provinces.

Mr. Ford: The problem is that we are not dealing with regulations but with an outline of proposed regulations. If we knew what the rules were, we would know better what to say about them.

Senator Molson: That is a good point.

The Chairman: Gentlemen, have we exhausted the subject?

Mr. Elliott: I think we have, Mr. Chairman. Thank you very much, Mr. Chairman for your time.

The Chairman: Thank you.

The Chairman: Honourable senators, the third brief this morning is from The Canadian Mutual Funds Association. I have on my immediate right Mr. A. D. Johnstone, who is President of the Mutual Funds Management Corporation Limited, and President of this association. He will introduce his panel.

Mr. A. D. Johnstone, President, The Canadian Mutual Funds Association: Mr. Chairman, honorable senators, as President of The Canadian Mutual Funds Association may I express our gratitude for the opportunity presented to us today to further our discussions with respect to several matters which we view with grave and serious concern.

With me today I have on my immediate right Mr. John McAlduff from Winnipeg, the Executive Vice-President of Investors Group Trust Co. Ltd., who is chairman of the association's taxation committee. Next to Mr. McAlduff is Mr. Carl T. Grant, of Toronto, of the prominent Toronto legal firm of Zimmerman and Winters. On the farm right is Mr. William r. Miller of Toronto, who is Treasurer of the United Investment Services Ltd.

As you have noted from the preamble to our brief, The Mutual Funds Association comprises approximately 90 per cent of the assets of the total mutal fund industry in Canada; but more importantly, it represents 90 per cent of the residents of Canada who employ mutual funds as their savings vehicle, and it is these roughly three-quarters of a million shareholders that essentially we represent today.

At its previous appearance before this committee in April, 1970, Mr. Godfrey, the then president, presented a verbal summation of a 50-page brief relating to the White Paper proposals. Our brief today is of an entirely different nature and does not lend itself to such summation.

The brief in your hands deals with six very specific problems, which have an important bearing on the financial wellbeing of these three-quarters of a million shareholders of mutual funds in Canada, and potentially of many, many hundreds of thousands more. The first four items we view as being of genuine and serious concern to our industry, and the last two items seem to be of lesser importance. The taxation committee has been hard at work for many months, and has sought answers to many of these questions in continuing dialogue with representatives of the department and spokesmen thereof whenever circumstances permitted it, but resolution of primarily these four specific problems has not been forthcoming.

Hon. Mr. Phillips: Does that mean with the Department of National Revenue or the Department of Finance, or both?

Mr. J. D. McAlduff, Chairman, Taxation Committee, The Canadian Mutual Funds Association: We have had meetings mainly with the Department of Finance. We have had some unofficial dialogue with officials of the Department of National Revenue.

Mr. Johnstone: Mr. Chairman, perhaps I might ask for some direction regarding your assessment of the best

means of furthering this discussion. Would it be in order for Mr. McAlduff to enunciate each specific problem and then turn to discussion following each separate section?

The Chairman: Yes.

Mr. McAlduff: With your permission, Mr. Chairman, I will do this. The first item, and probably the most important from the point of view of our member companies and their shareholders, concerns the retroactive effect of this tax reform bill on already existing registered retirement saving plans invested in mutual funds. This is a retroactive effect because of the new investment restrictions in the tax reform bill. Under the old Income Tax Act the only investment restriction for registered retirement savings plans was that 90 per cent of the income had to be from Canadian sources. This presented no problem to our member companies, because as Canadian corporations the dividends they paid to the registered retirement savings plans trusts that invested in them were 100 per cent Canadian. However, under the new bill, Bill C-259, a mutual fund trust or mutual fund corporation is now considered to be in its entirety "foreign property."

Senator Connolly: They are now considered to be what?

Mr. McAlduff: Foreign property, unless it is exempted by regulation. The new rules are that a registered retirement savings plan must have at least 90 per cent of its assets invested in Canadian property in order to avoid some very heavy penalty. It is unthinkable really to have more than 10 per cent of the assets of a registered retirement savings plan invested in foreign property. However, the new rules say that a mutual fund corporation will be deemed to be foreign property unless it complies with certain regulations yet to be issued. It is our understanding that these regulations will say that if at any time during a year the foreign property content of a mutual fund exceeds 10 per cent, then it will be foreign property.

Hon. Mr. Phillips: If you will pause for the benefit of honourable senators, your point is that that relates to the whole question of permissive income by being so described as being foreign property, under the international section of the act. What do you mean by the concept of foreign property? Within the meaning of Bill C-259?

Mr. McAlduff: That is right. The problem is that here is a tax penalty essentially. If a registered retirement savings plan has more than 10 per cent of its assets invested in foreign property it will be required to pay a tax of one per cent per month, which is 12 per cent per annum, off this excess. This penalty is so severe that certainly no registered retirement savings plan can be invested more than 10 per cent in securities which are considered to be foreign property.

Canadian mutual funds have been used by 75,000 registered retirement savings plans over the past 13 years. They have been a very popular form of investment media. There is approximately $200 million invested by registered retirement savings plans in Canadian Mutual Funds. I would estimate that at least 80 per cent of our present Canadian mutual funds will fail to qualify under this new legislation.

Here is what this means. It means that we will have to set up special mutual funds specifically for an investment by registered retirement savings plans, mutual funds that will at all times keep their foreign asset content down below the 10 per cent maximum. We are not quarrelling with this. We have accepted it and we are going to do it, and most of our member companies are embarked on this right now.

What we have objected to is the forced transfer of moneys already invested by 70,000 registered retirement savings plans in mutual funds, into these new vehicles. For one thing, we think it is unreasonable to try to force this transfer. For another thing, we think it is virtually impossible to effect it, to get 70,000 people to make that transfer before the end of 1973.

Senator Beaubien: Mr. McAlduff, are you not given any time to conform to this?

Mr. McAlduff: Yes, we have been given until the end of 1973.

Senator Walker: Are you suggesting then that it is not merely a question of time, but that this whole thing would be interfered with?

Mr. McAlduff: The ones that are presently investing. Indeed, the Minister of Finance, in tabling this legislation, indicated that moneys already invested in foreign property could remain invested. But it so happens, because of a peculiarity of our industry, this will not be the case under the legislation as written. Here is the reason why. We set up a separate registered retirement savings plan for every type of mutual fund investment. In other words, if a person invests in Investors Growth Fund and wants it registered, then we set up a registered retirement savings plan trust for him, for his Investors Growth Fund shares. If he wants to invest in shares of Investors Mutual, we have to set up a separate registered retirement savings trust. This is an administrative necessity.

Senator Connolly: You are going very quickly on this. I am sure it is clear, but I have lost you, or you have lost me, if I may put it that way. Will you start again?

Senator Beaubien: Mr. McAlduff, are you doing that now, before this, or because of Bill C-259?

Mr. McAlduff: No, we have always done that.

Senator Connolly: This is very easy for Senator Beaubien to understand because he is an expert, but we are just "ordinary Joes" here, so perhaps you had better tell us again.

The Chairman: Let us take an example and follow it through.

Mr. McAlduff: An example would be a person who would like to set up a registered retirement savings plan. Say he would like this money to be invested in shares of one of our mutual funds. We will use as an example Investors Growth Fund in Canada. A special registered retirement savings plan trust will be instituted or will be set up, and all the moneys paid into that trust will be invested in shares of Investors Growth Fund. The point here is that, as part of this arrangement, all dividends that will be paid in future on those Investors Growth Fund shares must be re-invested automatically in additional shares. This is the

base problem that we have here. According to the legislation, the money that is already invested by that registered retirement savings plan in those growth fund shares is all right, but any re-invested dividends will be subject to the tax penalty.

There is no way administratively whereby these dividends that will be paid next year or the year after, and every year until this person retires, can be invested elsewhere; they must be re-invested in shares of Investors Growth Fund.

Senator Connolly: Because that was the original stipulation.

Mr. McAlduff: Yes, that was the original stipulation.

Senator Molson: It is in the contract.

Mr. McAlduff: It is the only way. Therefore, in order to avoid this tax penalty, all of the moneys in this registered retirement savings plan that are currently invested in shares of Investors Growth Fund must be transferred to some other investment vehicle.

Senator Connolly: Under the new bill.

Mr. McAlduff: Under the new bill.

Senator Connolly: What you want is the right to continue the investment for that portfolio as it was originally contracted.

Mr. McAlduff: That is right.

The Chairman: To continue in respect of the production or earnings in the fund.

Senator Connolly: Yes.

The Chairman: From what they have when this act becomes operative.

Mr. McAlduff: That is right. We have asked for a grandfather clause to provide that where moneys on June 18 were invested in shares of this mutual fund that any dividends which must be reinvested automatically in additional shares of that mutual fund will be deemed to be foreign property acquired before June 18, 1971. That was the first grandfather clause we asked for. We asked for one other grandfather clause, and that dealt with contractual share purchase plans. These are plans whereby a person agrees to invest anywhere from $15 a month up to $200 a month in shares of a mutual fund. They can register that. In other words, this can be shares owned by their registered retirement savings plan trust. The acquisition fee in the first year in these plans is high. It is 30 to 50 per cent of the amount invested. In subsequent years it is much lower. It is somewhere in the neighbourhood of 5 per cent to 7 per cent.

Senator Connolly: Would you explain that term, the acquisition fee?

Mr. McAlduff: That is the sales charge.

Senator Benidickson: It is like the commission a salesman receives for selling an insurance policy.

Mr. McAlduff: That is right. The great bulk of it is paid by the investor in the first year. We estimate that there are somewhere in the neighbourhood of 15,000 to 20,000 of these contractual share purchase plans right at the present time. These people have paid the heavy sales charge at the front end and they would like to recoup or get the benefit of this by carrying the contract through to completion, which will usually be a 10- or 15-year period. Most of these contractual plans, or the great majority of them, are using funds which will be classified as foreign property under Bill C-259. What we have asked is for a grandfather clause that will again say that any future contributions to these contractual share purchase plans entered into before June 18, 1971—any future contributions that we must accept according to the terms of these plans—will be considered to be foreign property acquired before June 18, 1971. In other words, if people had entered into contracts before this new law was announced, they will be able to complete their contracts.

Senator Connolly: You have counsel with you. Is there a form of words that you are going to suggest to us by way of an amendment to this section?

Senator Beaubien: Or if not, could you send such a form of words to us?

The Chairman: Do you have a draft?

Mr. C. T. Grant, Vice-Chairman, Taxation Committee, The Canadian Mutual Funds Association: The minister announced on October 13 that the Government was going to propose certain changes to deal on a temporary basis with the contractual plan problem which Mr. McAlduff has outlined. I think it would be premature for us to suggest any change in wording until we hear those proposals.

Senator Connolly: On the contrary. It would be helpful if you could get those changes to us as quickly as possible.

Mr. McAlduff: I believe we could do this, Senator Connolly.

The Chairman: Senator Connolly, I think you are right in saying that, because if this is a duplication between what the minister proposes and what we may propose as a result of information we obtain, then no harm has been done. If there are differences we will see which way they go on the matter.

Mr. McAlduff: We have had dialogue with the Department of Finance on this matter and they were sympathetic to our problem. However, instead of giving us these two grandfather clauses which we were asking for, they gave us until the end of 1973 in order to regularize the situation.

Senator Connolly: That will not solve the problem.

Mr. McAlduff: No, that will not solve the problem. Our feeling is that even having this extra two years it will be an enormous problem transferring 70,000 existing plan holders out of the investments they are presently in and into a new investment. And we think it is unreasonable to ask them to do this because the amounts involved are not that significant in relation to the problem the Government is trying to solve.

Senator Macnaughton: May I ask a question, Mr. Chairman? What is your average industry charge on the purchase of these plans?

Mr. Johnstone: The industry average would be approximately somewhere between 8-1/2 per cent and 9 per cent, let us say, for example, 8-3/4 per cent.

Senator Connolly: Has that varied?

Mr. Johnstone: Yes, in its history it has, but the increase has been slight. In 1950 the average would have been 7 to 7-1/2 per cent.

Senator Gélinas: Mr. McAlduff, what would be the penalty if 20,000 of the 70,000 people in the plan did not change?

Mr. McAlduff: There would be two penalties. The new moneys invested in these plans would be subject to this tax of one per cent per month. Also, if they invest in a mutual fund which is not an investment corporation mutual fund there is an additional penalty in that these amounts invested would be added to the plan-holders' income and his contribution would be disallowed.

The Chairman: He could avoid the second one, could he not? He would have a right of election which would not expose him to the second penalty.

Mr. W. R. Miller, Chairman, Administrative Committee, The Canadian Mutual Funds Association: If he did not invest he would not expose himself, and he would merely lose some of the sales charges which may have been paid in advance. But in respect to dividends paid into the fund . . .

The Chairman: Is there any investment he could make at that stage that would not subject him to this second penalty?

Mr. McAlduff: Yes, he could transfer all of the moneys presently existing in that registered retirement savings plan into another fund, in which event additions can be made to the new fund. But in order to avoid these taxes he has two choices: either he has to stop making additional contributions to the plan; or, alternatively, he can transfer his existing money into another mutual fund. All our companies will have mutual funds by the end of this year which will comply with this new regulation.

Senator Gélinas: Then he will have another commission to pay?

Mr. McAlduff: No, we would allow them a roll-over. But the problem is we cannot force him to do this unilaterally. And to approach 70,000 people, many of whom are not sophisticated . . .

Senator Connolly: And many of them are in the low-income bracket.

Mr. McAlduff: Yes, very much so, because the people who invest in mutual funds are not, by and large, wealthy. This is an investment medium for the average person. It is extremely difficult to explain to them why they must cash in their investment and transfer it to another mutual fund. After all, some years back they were encouraged to select this particular fund. We will have enough trouble persuading them to direct their future moneys to the other fund. However, to tell them that they must cash in their existing investment and transfer it will be difficult, if not impossible.

Senator Burchill: Would "cashing in" mean the disposal of foreign securities?

Mr. McAlduff: Yes; in most instances the underlying securities owned by these mutual funds, which are not really foreign securities, but just deemed to be so under this bill, are 75 per cent Canadian.

Senator Desruisseaux: What would be the situation if some refused to change?

Mr. McAlduff: This will definitely happen. In respect of every one of those we will have to file an income tax return each year for each registered retirement savings plan trust and calculate the tax for each month of each year on the excess holdings in foreign securities at each month end, which would be the investments made after this act comes into force.

Senator Burchill: That is in excess of 10 per cent.

Mr. McAlduff: They would all be in excess of 10 per cent because all the funds presently existing would be deemed to be foreign securities. Therefore, any addition will be in excess of 10 per cent.

We will have to calculate tax at 1 per cent per month, file the return and pay the tax. We made a calculation for the Department of Finance and determined that at the outset the only tax payable would be about $5 per return. It would not pay the Department of National Revenue to process it and it would be very, very expensive for us to handle. The tax is negligible and we hoped, for these reasons, that we would obtain the grandfather clauses we requested. However, instead of that we were given until 1974 which, in our considered opinion, is not sufficient.

Senator Connolly: Has the amendment to extend the period to 1974 been introduced?

Mr. McAlduff: No, it was announced by the Minister of Finance when he tabled the 96 amendments, but none of these amendments covered the transitional provisions.

Senator Connolly: Will you suggest a draft amendment?

Mr. McAlduff: Yes.

Senator Connolly: Will the increase in the amount that can be contributed to a retirement savings plan make an appreciable difference?

Mr. McAlduff: Yes, we believe it will make quite a big difference.

Senator Connolly: Therefore, the industry in respect of retirement savings plans is bound to become bigger and more important to many more people. Does that not accentuate your problem?

Mr. McAlduff: No, not this particular problem; this is concerned only with existing plans. Additions in the future are not involved here. I believe that all our member companies by the end of this year will have set up special

mutual funds which conform and are specifically for registered retirement savings plans.

Senator Benidickson: You said that supposing somebody prior to June 18 had a retirement savings plan. You would like that undisturbed. But for the future, because of this new law, you would have a fund other than investor's growth that would comply with the law and make it attractive.

Mr. McAlduff: That is correct. I should make one other point. Someone might question it and say, "Why don't you adjust the investment portfolio of investor's growth so it complies with this?"

Senator Benidickson: It might be the wrong time to divest yourself of some foreign securities.

Mr. McAlduff: Yes. The main reason why we feel that we cannot do so is that some 92 per cent of the assets of Investors Growth Fund are earned not by registered retirement savings plans but by ordinary investors. We have to operate that fund in the best interests of all the people in it. For a small minority, we cannot work in a structuring-off of the investment portfolio which would, in our estimation, be detrimental to the majority.

The Chairman: You would have to divorce this element from the general operations of your business.

Mr. McAlduff: That is right. We would set up special funds for registered clients. We have no quarrel with that. All we are asking is that this be done with the least possible disruption to these who have invested their money with us in the past.

Senator Benidickson: You would have to consider the many who are not in a fund, like investor's growth, for retirement plan purposes.

Mr. McAlduff: That is correct.

Hon. Mr. Phillips: Would you not be subject to breach of contract if the dissident shareholder refused to consent, as Senator Desruisseaux mentioned? You would still have the problem that under the existing contract you agreed to proceed along certain lines. Is there not a breach of civil rights involved?

The Chairman: They do not guarantee them against taxes and increases.

Hon. Mr. Phillips: I am not saying that they are guaranteeing them against taxes or increases. Clearly, the consequent penalties are related to the individual dissident, but nevertheless you have breached the contract and you affect the investors at large.

Mr. McAlduff: That is right. We cannot change these contracts unilaterally. In other words, we cannot go to the 70,000 investors, even if we wanted to, and say "You have to switch from Investors Growth Fund into our new investor's registered mutual fund."

The Chairman: That is the real point. You are stuck with a contract. If there is not a switch, or something done, the holder of that contract suffers a severe penalty.

Mr. McAlduff: That is correct.

Senator Benidickson: Retroactive.

The Chairman: Yes. What is your next point?

Mr. McAlduff: The next point deals with the taxation of death benefits from registered retirement savings plans. Under the present legislation a refund or payment to a person's estate upon the death of a registered retirement savings plan holder is subject to a flat 15 per cent tax. It is a very generous provision, and it is one that is now being changed. That 15 per cent tax is now being removed. In future, where the proceeds of a registered retirement savings plan are paid to an estate, it is subject to tax at ordinary rates.

There was one saving provision proposed in the Tax Reform Bill, namely, that where the widow of a deceased plan holder receives such a refund she could roll this money into another registered retirement savings plan tax-free, or into a forward averaging annuity.

However, because of the fact that registered retirement savings plans invested in mutual funds cannot designate a beneficiary, the proceeds must be paid to the estate, and because of the way in which the proposed act is worded this benefit would be lost to the widow.

The Chairman: Would it be? If the beneficiary is the estate and the testator, before he dies, designates the disposition of this in his will—

Mr. McAlduff: He could do that, but, nonetheless, the payment will still be made to his estate. It will be included in the income of the estate under section 146(8). The estate, if it pays this money to the beneficiary, can deduct it, and it would then be taxable to the beneficiary, but not under section 146(8); it would be taxable under section 104, and the way in which the proposed Income Tax Act is worded, it is only amounts included in the recipient's income pursuant to section 146(8) of the tax reform bill that are eligible for this roll-over.

The Chairman: Perhaps that is where we should attack the question. Is that what you are suggesting?

Mr. McAlduff: Yes. We have a suggestion which we could put into writing, Mr. Chairman.

The Chairman: How quickly could it be done?

Mr. McAlduff: I would say within one week.

Senator Beaubien: It would have to be; we could not wait any longer than one week.

The Chairman: Yes, we cannot afford any longer than a week because we are going to stop hearings on November 10. We have already commenced writing our report, and we hope to be through with all this by the end of November.

Mr. McAlduff: Just to give you some idea of the seriousness of this, I worked out an illustration, and it is this: If a plan holder who dies has $90,000 invested in his registered retirement savings plan there would be a tax of 15 per cent, which is $13,500 under the present law, and the

proceeds to the widow would be $76,500; if the widow is 60 years of age she could probably buy an annuity for life of approximately $500 a month. Under the revised bill this $90,000 would be taxable in her income or in the income of the estate at the normal rate. For example, the tax on that $90,000 in the Province of Manitoba would be $51,795, and the net proceeds available to the widow would be only $38,205, and with this she could purchase an annuity for life which would give her approximately $250 a month. This illustration gives you some idea of the severity of the proposed law. This would be the immediate effect. It would not only affect people who die after January 1, but it could well affect people who die before January 1 but in respect of whom payments could not be made until after December 31, 1971, which is often the case because we cannot make a payment out until we get estate tax and succession duty releases.

Hon. Mr. Phillips: You are worried about the beneficiary.

Mr. McAlduff: Yes.

Senator Molson: The rate of tax you just quoted is higher than is contemplated under the proposed act, is it not?

Mr. McAlduff: No, senator, that is exactly what is contemplated.

Mr. Molson: It seems extraordinarily high; what was the figure again?

Mr. McAlduff: On $90,000 of taxable income the amount of tax, without provincial taxes added on, would be $46,663. The example I gave was a Manitoba example where the tax is 11 per cent greater than that thereby bringing the total tax up to $51,795.

Senator Molson: It is a very impressive figure.

Senator Benidickson: We have been talking about the death of a spouse, Mr. Chairman, and I thought that was exempt from estate tax. I can imagine that if the beneficiary of the retirement plan was someone other than a spouse there would be a tax, but I thought we had eliminated the tax if the beneficiary was the spouse.

The Chairman: The problem might occur, Senator Benidickson, if the money goes from the plan to the estate, but if the testator makes a will and makes a grant or confers a benefit on his spouse, on the movement of that the wife would take that without tax.

Mr. Grant: It loses its character.

The Chairman: This is the problem, whether there is a change in character between the time the money leaves the fund and gets to the spouse, and whether the fact that it has to go to the estate first takes away that benefit.

Hon. Mr. Phillips: I am puzzled in the same way Senator Benidickson is. If on January 1, 1972 we have no federal estate taxes, and if there is no deemed to be capital gain realization on the death of the investor, where does the element of tax liability come for the widow?

Senator Burchill: That is it.

Senator Molson: The suggestion was that it was treated as income. That was your suggestion.

Hon. Mr. Phillips: Generally speaking we have the roll-over provision on the death of the testator.

The Chairman: The point is that the money on the death of the investor goes to his estate, whether it is estate tax, succession duties or anything else.

Senator Molson: It is not income, surely.

The Chairman: No.

Senator Molson: The rate he gave us was the income tax rate.

The Chairman: It becomes income when the estate pays it to the widow, for instance. This, I understand Mr. Grant to say, is the effect of these sections in the bill.

Hon. Mr. Phillips: But we have no federal estate taxes on January 1, 1972.

The Chairman: It is not an estate tax.

Mr. McAlduff: This is income tax really; it is not an estate tax.

Senator Molson: But surely it is not income.

Mr. McAlduff: It is deemed to be income under the Income Tax Act.

Mr. Grant: We have something similar at the moment. If an individual dies with a retirement savings plan, by taking out all the money in that plan and passing it to the widow there is a 15 per cent income tax imposed on the withdrawal of those moneys. That concept has been abandoned under the new system. Under the new system either his estate will end up with the liability for income tax, or the person who actually receives, in Mr. McAlduff's example, $90,000 will end up with a liability for income tax. There is an exception made when those moneys are passed directly from the retirement savings plan to the spouse.

Senator Benidickson: That is the point I wanted to clear up.

Mr. Grant: In those circumstances the spouse is not required to include that $90,000 in her income. The point we are endeavouring to make, which I think is the weakness in the act, about which we have had some discussions with the department, is that it is impossible legally for a person to designate a beneficiary of retirement savings plan money as he can in insurance, because the civil laws of the provinces do not permit that. Therefore, what happens when an individual dies is that the money of his R.S.P. goes technically through his executors, and even though he may have designated in his will that it should go to his wife, it loses its character within the meaning of the bill as money coming from an R.S.P. The technical point we would like to have clarified by the Government is that it should not do that; that even if it goes through the will and ends up in the hands of the widow it should be still possible for her to benefit from the roll-over. I think it is an oversight.

The Chairman: Oversight or not, it looks as though something should be corrected. Your job is to give us the language. If we like it we may act.

Senator Desruisseaux: The Canadian investors in a mutual fund have a position. A Canadian investor in a mutual fund can also buy an offshore mutual fund. What is the position with this new taxation system? They can buy into, let us say, an American or an English fund, and they can, if they wish, invest their money fully there. Is that correct?

Mr. McAlduff: Yes. If we are talking about registered retirement savings plans, in future a registered retirement savings plan would be precluded from investing more than 10 per cent of its assets in such a form of offshore mutual fund. Offshore mutual funds, to the best of my knowledge, have never been an important media of investment for Canadian registered retirement savings plans. Certainly they will be even less so in the future.

The Chairman: Can we move along, because our time is moving along.

Mr. McAlduff: The next point is conduit treatment for mutual funds. I should probably start by defining what we mean by "conduit treatment". "Conduit treatment" simply means that a person who invests in the media of a mutual fund would pay no more and no less tax than they would pay if they had owned the underlying securities directly.

The principle of conduit treatment seems to be accepted by everyone. In the summary of the tax reform legislation it is stated that the main objective of the new legislation is to treat mutual funds and investment corporations essentially as conduits between the shareholders or investors and the sources from which their income is derived.

The Senate committee concluded, on the subject of mutual funds, that the present conduit treatment of mutual funds should be continued by one method or another.

The Commons committee said something essentially the same when they were studying the White Paper. They said:

> The committee therefore states only that it supports the common views of the Government and the funds that the tax results should be as close as possible to being identical with the results it would obtain if members had held the assets of the funds directly.

So the principle seems to be well established. Unfortunately, it did not work out in practice, in the case of mutual fund corporations that do not qualify as investment fund corporations.

In the case of those companies, there is a very substantial tax penalty to the shareholder who invests through the media of such a mutual fund. One way of illustrating it is in the Institute of Chartered Accountants' book called "Tomorrow's Taxes" in which they show, on page 138, an illustration of the conduit principle for an open end mutual fund corporation not qualifying as an investment corporation. They use as an example a shareholder in a 40 per cent tax bracket, and they show that in respect of the income from inverest, rents or foreign dividends that he receives through the medium of such a mutual fund, he pays not a 40 per cent tax but rather a 60 per cent tax. That is quite a tax penalty.

Senator Benidickson: Would you give me the title of the publication again?

Mr. McAlduff: It is called "Tomorrow's Taxes" a book put out by the Canadian Institute of Chartered Accountants. It is a very good one.

Senator Molson: Would you give the page or section?

Mr. McAlduff: It is page 138, and it is part of section G-20, an illustration of the conduit principle.

We also put an illustration in the brief that we sent to you, which shows that one-third of such income is taken away through this tax penalty; that if a person who received $300 interest or foreign dividends, as a direct investor, invested in that same security through the media of a mutual fund that is not an investment corporation he would have that income scaled down to $200 through this additional tax.

Senator Molson: That is at the bottom of page 4 of your brief?

Mr. McAlduff: That is correct, sir.

The Chairman: Are you going to give us some language on that?

Mr. McAlduff: Yes, we can. We have had a dialogue with the Department of Finance on this and we have made suggestions to them, but we have been told that there are, as they called it, "systems problems". We do not agree. If there are systems problems, we have not been able to see them. We believe that we could suggest language which is workable and which would result in equitable conduit treatment.

The Chairman: If you give it to us, we will assess it.

Mr. Grant: One of the simple things we suggested is to allow mutual fund corporations to elect to be taxed in the same manner as mutual funds trusts, which the Government does recognize. This would, in fact, work.

The Chairman: What else?

Mr. McAlduff: The next item has to do with income averaging annuities. These are the new forward averaging annuities. This is a new concept, a very novel one, under the Income Tax Act, one that we think will be valuable and very popular with the taxpayers of this country. It is a means whereby certain types of income—such as capital gains and lump sum payments out of pension plans or retirement plans, or incomes of athletes or performers—can be deferred to future years by purchasing one of these forward-averaging annuity contracts. Our complaint here is that under the legislation as it is presently written the issuance of these forward averaging annuity contracts is limited to all intents and purposes to life insurance companies, the people with whom we compete very vigorously for this particular type of savings dollar. We believe that the act should be broadened to permit a similar type of vehicle to be issued by mutual fund corporations.

The Chairman: All right. We have that.

Senator Benidickson: Notwithstanding that, many mutual funds have close relationships in their sales forces with insurance companies?

Mr. McAlduff: That is correct. We are appearing here not just on behalf of our corporations but, we believe, also on behalf of the shareholders. We know for a fact that a great many of the people who are presently clients with us would much rather enter into a forward averaging annuity contract invested in a mutual fund, that one invested in an insurance company contract.

The Chairman: You suggest that an amendment is needed to section 61(4)(*b*).

Mr. McAlduff: That is correct.

Mr. Grant: It is my responsibility to deal with the next two points which are really fairly short and of rather a technical nature. The first point relates to the capital gains credited to non-residents by a mutual fund trust. It appears to us in our examination of the bill that section 212(1)(*c*) could have an unintentional effect, because although that section deals with the imposition of withholding tax on payment to non-residents, since the section exempts from the application of withholding tax taxable capital gains paid to non-residents, and since taxable capital gains by definition are equal to one-half of capital gains, we are concerned that the other half might be subject to withholding tax, and we do not think that that was the intention. We raise this as a technical matter.

The Chairman: You think the part exempt from tax should have a free ride.

Mr. Grant: Yes. The last point is that in the case of mutual funds the use of loss carry-back in the case of capital losses is not particularly suitable since mutual funds traditionally, and certainly in these circumstances, contribute their capital gains annually. You could have the anomalous situation arise where, for exemple, in 1972 a mutual fund corporation has made substantial capital gains, all of which it has distributed to its shareholders. In 1973 it suffers a capital loss. The present provisions of the bill provide that the mutual fund corporation in 1973 should carry back its loss to 1972. Well, the fact is that in 1972 the mutual fund corporation would not have paid any capital gains tax, effectively, since it would have distributed those gains to its shareholders.

Here we again point out the anomaly and suggest that the requirement to carry back the loss first before you carry it forward, should be limited to the amount of the capital gains reported by the mutual fund corporation in the previous year. So that if, in my example, the mutual fund corporation had no net capital gains in 1972 because it distributed them to its shareholders, then it would not carry back at all but would carry the loss forward from that time on. If it had $100,000 which it had retained undistributed to its shareholders, then in those circumstances it would be required to carry back $100,000. We think it is a technical problem and we think the Department of Finance is sympathetic. But we also think we should record it here since we have already made submissions on it.

The Chairman: What section do you think should be amended?

Mr. Grant: It is really section 111(1)(*b*) which deals with the loss carry-back. Once again, sir, we would be quite pleased to submit language.

The Chairman: There is one limitation on that; we must get it very promptly.

That would appear to conclude your presentation this morning.

Mr. Grant: I think so, sir.

The Chairman: Thank you. We have another hearing at 2.15 p.m.

The Committee adjourned until 2.15 p.m.

Upon resuming at 2.15 p.m.

The Chairman: Honourable senators, I call the meeting to order.

We have the submission of the Canadian Pulp and Paper Association this afternoon, and their presentation will be introduced by Mr. Hamilton who is President of Domtar Limited.

Mr. A. Hamilton, President, Domtar Limited: Mr. Chairman, it is a pleasure for us to appear before you again this afternoon. Before continuing, I would like to introduce the members of the Canadian Pulp and Paper Association who are participating in today's presentation. On my right is Mr. Howard Hart, Executive Vice-President. Next to him is Mr. Tom bell, President of Abitibi Paper Company. Behind him is Mr. Colin Brooke of Domtar Limited; Mr. D. A. Wilson, Director of Canadian Pulp and Paper Association; and in front of Mr. Wilson, another Mr. Wilson, Mr. R. W. Wilson of Consolidated Bathurst Limited. Next is Mr. D. Ford of Northwood Pulp.

Before we get down to the nitty-gritty of our presentation, I would like to say a few words about the Canadian pulp and paper industry. I think that everyone in this room is very much aware that we are having our problems; and we consider that some of these problems are of a severity which the industry has not had to face in the last four or five decades. To keep the problem in perspective we should not that the pulp and paper industry throughout the world is in a rather poor state. When I say this, I am referring to the industry in Japan, the United States, Italy, France, Germany, the United Kingdom, and Scandinavia. We are all facing the kind of problem, that of over-capacity for what has been, in the short run, a slump demand, and the problem of rapidly rising costs. It is only natural that we have to address ourselves to these problems if we are to establish a profitable industry which in the long run is good for the country or countries concerned.

Senator Connolly: Has the demand or the drop in demand a direct bearing on costs?

Mr. Hamilton: No, we consider a drop in demand is more a result of the general slowdown that has occurred in the economic activity. All of our statistics indicate that the demand for pulp and paper products in general follows population growth and economic growth. There are other shortterm conditions as well; but if these two major fac-

tors occur there is a fall-off in the demand for the industry. We would be the first to admit that some of the reductions in demand, particularly in the United States market and some parts of Europe, is of a nature which would indicate that it is more than proportional to the drop-off in economic activity. The analysis is apparently under way, but we have not an answer to the problem.

Senator Connolly: Might it be costs?

Mr. Hamilton: It certainly could be costs.

Senator Connolly: Costs could a factor?

Mr. Hamilton: Costs do cause an increase in price, and an increase in price makes paper less competitive with other competing materials. So this chain of events can happen. There have been some people in Canada who have publicly questioned whether or not there is a long-run future for the Canadian pulp and paper industry. We would greatly like to debate this point, because those of us in the industry are completely convinced that the long-run balance will tip in our favour.

We have disadvantages and we also have advantages. Some of the advantages we enjoyed in the past have been eroded away or have become less of an advantage through technological changes and advances in other parts of the world. We do have a strong position in world markets. We do have a wide range of manufacturing know-how for a wide range of products. We also have a highly skilled working force. We think we have a reasonably skilled management, but we are not going to talk very much about that.

We think there are disadvantages in particular in the transportation line. Transportation is one of our major disadvantages that is inherent in the Canadian picture. Fifty or sixty years ago the trees were much closer to the mills than they are today. Now we are cutting farther away and the costs rise. Then a well-known fact is that transportation costs of all finished products, whether by rail or by ship, have increased at an alarming rate; and this is one of the disadvantages inherent in our geographic location.

We come to the particular reason for being before you today, and that is to talk about another disadvantage we have, that is basically associated with the tax structure that this industry faces, compared to the tax structures faced by our major competitors in the world market, the United States and Scandinavia. We are producing in a Canadian environment but we are selling in a world environment. And this is a fact we have to keep in front of us at all times.

To repeat what I have said earlier, we welcome this opportunity to come before you and talk with you in some detail, or at your wish, Mr. Chairman, about this tax reform bill. I would like at this point to ask Mr. Howard Hart to take over the presentation of our position.

The Chairman: Mr. Hart, I notice that some of the comments in your brief deal with general tax provisions in Bill C-259, such as corporate tax instalments and things of that kind. If it does not disrupt your presentation, what are your basic concerns that arise out of the provisions of Bill C-259 that bear on the operations of your industry? We would like to get at them first.

Mr. Howard Hart, Executive Vice-President, Canadian Pulp and Paper Association: Mr. Chairman and honorable senators, as Mr. Hamilton has said, we are addressing ourselves to one of the major disadvantages that we see facing the Canadian pulp and paper industry, and indeed, that forest product industries of Canada are facing. Certainly tax reform bears directly on this, either by omission or commission. We have listed in our presentation to the Government—copies of which are before each of you—13 or 14 very specific items which we feel would be detrimental to this industry, but possibly also to other industries. But in the overall context of tax reform, which has been going on longer than any of us would care to think about, we feel our basic disadvantage flows from the tax burden that falls on Canadian forest products as compared with the major bulk producing forest product companies that operate in the United States and Scandinavia. There are some basic principles that we feel are very important, and we have proposed to the Government that they be encompassed in the tax reform. I would like if I may, Mr. Chairman, to touch on one or two of these areas.

The Chairman: Very well.

Mr. Hart: First and foremost, Mr. Chairman, we believe that the tax burden that any particular Canadian company has to face must be in reasonable proportion to the tax burden that its major competitors face if it is selling in the world markets. We think this is absolutely critical. The forest products industry in Canada has for many years borne a substantially higher corporate tax burden than its competitors in the United States and Scandinavia. We have set out in our submissions to the Government,—which were also reviewed with this committee about a year ago—some figures relative to the tax burdens on forest products here as compared to the United States. At that time we pointed out that, on the average, forest products in Canada had a corporate tax burden of about 49 per cent. On the other hand, our competitors in the United States—the big bulk producers—will have, on the average, a corporate tax burden of about 34 per cent.

We have had some difficulty, quite frankly, convincing people that this difference does, in fact, exist, and only yesterday we spent some time with Department of Finance officials trying to demonstrate, by extracting material from the financial statements of major companies, that this difference in corporate tax burden does, in fact, exist.

Hon. Mr. Phillips: Mr. Chairman, may I put a question to the witness?

The Chairman: Yes.

Hon. Mr. Phillips: This is a point which I was going to put to you in due course.

You make a case against the United States and Sweden in relationship to your tax burdens. Do you not think it would be helpful if you were to give us *ad hoc*, in addition to this, proof of this by way of a schedule in relationship to the actual taxable income? Are you ready to give us that as quickly as possible, instead of dealing with generalities?

Mr. Hart: We would be quite anxious and willing to provide you with that material if you would like to have it. It was provided in considerable detail to Department of

Finance officials. It is a complicated schedule, but we would be delighted to provide you with it.

Hon. Mr. Phillips: The second part of my question is this: When you say "submission to", is this submission similar to the one presently before the Department of Finance?

Mr. Hart: You asked for schedules, I take it, sir.

Hon. Mr. Phillips: I am speaking of the document now before us. You say you have submitted material to the Department of Finance. We are dealing now with the document that is presently before the Department of Finance, are we?

Mr. Hart: Yes, sir.

Hon. Mr. Phillips: So we need not specifically draw it to their attention?

Mr. Hart: That is correct, sir.

Hon. Mr. Phillips: I would like to suggest, sir, that you provide us with a sample of an average American company, an average Canadian company and an average Swedish company for the same fiscal year, say, 1970—and if you cannot get 1970, then, 1969—and let us see, chapter and verse, what the results are.

Senator Benidickson: I was about to make a similar suggestion, Mr. Chairman, and I feel it is all the more desirable that we get examples of particular comparable cases. Unlike our proceedings on the White Paper, we are not appending to the proceedings of these hearings the briefs submitted, but I feel in a matter of this type that a motion probably could be made that the particular papers filed, giving specific examples of comparable tax rates, should be made an exception to our policy and be made an appendix to the record. If this was done, the readers of our proceedings would get the benefit of seeing what the witnesses are talking about.

The Chairman: There is no question about that. The only question is: How soon can we get these examples?

Mr. Hart: Within one or two days.

The Chairman: That is fine. We will close our hearings on November 10, and we hope to have our report submitted by the end of November.

Mr. Hart: We will have specific examples in your hands by Monday or Tuesday next.

The Chairman: That is fine.

Mr. Hart: Mr. Chairman, if I may continue in that same context, it may interest you that in the paper you have before you—that is, the one printed on its side—we have endeavoured to make a similar calculation for the year 1972. When I mentioned to you earlier the differential we were talking, more or less, historically, 49 per cent in Canada and 34 per cent in the United States. If you will look at this example which takes into account the tax changes that have been announced in Canada and in the United States—and I should mention this is a hypothetical case—you will see the average tax rate in Ontario, Quebec, and British Columbia might be about 48 per cent and in the United States it might be about 37 per cent. The purpose of the example is merely to indicate that, despite the announcements that have been made about reductions in corporate tax loads, these have had a rather minimal effect, although a useful one, on this particular differential that we are talking about.

If you look at the second-last factor, Mr. Chairman, which is "Funds retained by company", it will make the point even more clearly. This is money that is on hand to pay dividends or to revitalize or rebuild the company, and just looking at the averages in the two sets of columns you will see that in this example there is about $5.2 million left in the case of a Canadian company as against about $6.3 million left in the case of a United States company. The United States company has about 20 per cent higher retention of earnings with which to keep the company going.

Hon. Mr. Phillips: The reason I did not pay too much attention to that is, among other things, that the location, capital employed, and other factors would have a bearing on this comparison. Aside from the Fact that there is still an estimate for 1972, it would be much more impressive if this committee were given specific instances so that the comparisons could be made and the opinions of honourable senators could be determined as to whether they are effective or not. Knowing your industry and your representation here, I believe you will give us a fair comparison.

Senator Benidickson: Nonetheless, Mr. Chairman, as it is only a two-page document, I wonder if the committee would entertain a motion that this be made an appendix to our proceedings?

The Chairman: Could I have a motion to adopt this as part of this hearing?

Senator Connolly: At this juncture?

The Chairman: Yes, at this juncture; not as an appendix.

Hon. Senators: Agreed.

Text of document follows on next page.

Senator Connolly: Just scanning this page that we are now discussing, I note that the average rate for the Canadian company is 47 per cent as against 36 per cent in the United States.

Would you say, Mr. Hart, that the difference in the tax rate is due to the general American tax laws, or is it due to specific arrangements made for this industry?

Mr. Hart: The differential arises out of the technical feature that pertains particularly to the forest products industry in the United States. Under the tax laws of the United States a forest products industry is able to classify a substantial portion of its profits into a category that is subject to a capital gains tax rather than to the normal corporate tax levels. What this hypothetical illustration is meant to indicate is the impact of this margin of difference.

Senator Connolly: So it is a matter of a reduced tax on a wasted asset—the return from a wasted asset?

Mr. Hamilton: A renewable asset.

PULP AND PAPER INDUSTRY

COMPARISON OF CANADIAN AND UNITED STATES TAXES ON INCOME—1972
'000 $

	Ontario and Quebec	British Columbia	Washington and Florida	Georgia, Oregon, South Carolina
Provincial Tax—				
Income	12%	10%		
Logging	10%	15%		
State Tax Rate			0%	6%
Sales	$ 100,000	$ 100,000	$ 100,000	$ 100,000
Capital Expenditures	10,000	10,000	10,000	10,000
Income before tax	10,000	10,000	10,000	10,000
Augmented Capital Cost Allowance (5)	225	225		
Income from timber (30%) (3)			3,000	3,000
State Income Tax			0	600
Taxable Income	9,775	9,775		
Income taxable at corporate rate			7,000	6,400
Federal Tax at 46.5%	4,545	4,545		
Federal Tax—48%			3,360	3,072
Less—				
Abatement for Prov. Income Tax	977	977		
Abatement for Prov. Logging Tax	433	433		
Less—Investment Tax Credit (7%)			700	700
			2,660	2,372
Plus—Tax on Timber Income (30%)			900	900
Federal Tax Payable	3,135	3,135	3,560	3,272
Provincial Income Tax	1,173	977		
Less—Abatement for Logging Tax	217	210		
	956	767		
Logging Tax (4)	650	975		
Total Provincial Tax	1,606	1,742		
State Tax			0	600
Total Federal and Provincial Tax	4,741	4,877		
Total Federal and State Tax			3,560	3,872
Funds retained by Company	5,259	5,123		
Funds retained by Company			6,440	6,128
Rate of Tax—				
on Taxable Income	48.5%	49.9%		
on $10,000	47.4%	48.8%		
Rate of Tax on $10,000			35.6%	38.7%

25 October 1971
CPPA

NOTES

1. It is assumed that the company operates entirely within the boundaries of the particular state or province.
2. The federal tax rates are those that will be applicable, according to present information, to public corporations in Canada and to income over $25,000 in the United States. It is assumed that the proposed investment tax credit of 7% will be in force in the United States.
3. Income from timber represents the capital gains treatment (for tax purposes) of the excess of current market value of standing timber over original cost. Wood cut is charged off at current market value in determining income subject to taxation with the excess over original cost taxed as a capital gain. The percentage of total income represented by income from timber ranges from quite low to close to 100%. For purposes of this comparison it is assumed 30 per cent of income is represented by the gain in the value of timber.
4. Income subject to logging tax after processing allowance is assumed to be 65% of income.
5. Capital cost allowance increased by 15 per cent, charged at 15 per cent per year.

Senator Connolly: A renewable asset, perhaps, in your case is a more apt description.

Mr. Hart: The key point, senator, is that the technique does exist, and it is the resultant impact rather than the technique used to get there that is of critical importance.

Senator Connolly: In other words, there is a special tax situation applicable to the forest products industry in the United States which is different from the general tax laws?

Mr. Hart: Yes.

Mr. Hamilton: One of the other features in this calculation is the investment tax credit, but that applies to all industries. The point you just mentioned is unique to the forest industry.

Senator Burchill: Does that hold true with respect to Scandinavian countries too?

Mr. Hart: They have a different approach, sir. They are allowed to set aside, as retained earnings, capital for

future use without paying any tax on it. In other words, the retained earnings part that they do not distribute in dividends does not attract any tax at all; it is deposited into the national bank; it gets interest; they then come forward and request permission to utilize this, which introduces some part of state control, if you like, on the rate of expenditure and when it is spent, but they have that credit which is non-taxed to bring back and spend in their business.

The Chairman: Whatever method is used, the net result is that you turn out to be at a competitive disadvantage.

Mr. Hart: I think this is the point we are trying to establish.

The Chairman: I take it you are not trying to suggest to us that we should recommend the Swedish or the United States system?

Mr. Hart: No.

The Chairman: I take it you have proposals of your own.

Mr. Hart: We do have a proposal. You have come right to the heart of our problem. The competitive disadvantage with respect to tax structures does exist. I might point out again with respect to this example, this may not even be the whole story, because this particular example for 1972 does not take account of any advantage the United States firm may get from the DISC proposal, which they seem about to adopt, which would further widen the differential to the American companies advantage. On the other side, while this statement does include the recently announced 7 per cent reduction in Canada, we must keep in mind that that is only in effect for one year as currently announced. I would say this hypothetical case is a fairly modest statement of the difference.

Senator Burchill: Does what you are saying now apply to other forest products, such as logs, lumber and plywood?

Mr. Hamilton: Yes, sir.

Mr. Hart: Yes. We think, quite frankly, that this differential in the tax burden on the industry in Canada compared with its major competitors is historically the major factor that is applied to the industry today. This has affected our ability to be competitive, to have lots of muscle in export markets and rebuild our plant in this country. Having reached our present situation, which is anything but admirable, we are pretty concerned about the future, because we know that the demand for wood fibre is growing; it has a modest rate of growth. We know that plants will be built somewhere in the world to supply that fibre, and in the present state we are very concerned that these plants will not be built in Canada. We have resources in terms of people and fibre, but so do other people, and with more favourable tax rates they will grow and we will not.

The Chairman: To what extent, if at all, does the 10 per cent United States surcharge affect your operation?

Mr. Hart: It has a very substantial impact on those portions of our operation that supply paperboard, linerboard, fine paper, wrapping paper, the so-called specialty grades of paper.

Senator Connolly: Finished products generally.

Mr. Hamilton: There are only two major classifications of paper products which do not attract the 10 per cent surcharge. One is market pulp and the other is newsprint. All others attract the 10 per cent surcharge.

Mr. Hart: I am sure the point you are most interested in is what we would propose to correct the situation.

The Chairman: That is right.

Mr. Hart: We have recommended as a part of tax reform that the forest products industry be allowed to earn a tax-free investment allowance up to one-third of its income subject to taxation. This is in a proposal made to government very early this year. We propose that it be earned by expenditures in qualifying fields, such as organization, plant improvement, improvement in woodlands operation, pollution abatement, and plant expansion where justified. This is merely our offsetting technique to try to get ourselves on side with the basic corporation tax burden that the Americans and Scandinavians have. They arrive at that lower base by their own methods. We are proposing what we consider a uniquely Canadian approach to it. It is very much a carrot and stick operation, which would force the companies to modernize in order to qualify for income tax reduction. We think it should give us the muscle in the export markets that we so badly need, to modernize.

The Chairman: Is that developed in the brief?

Mr. Hart: It is developed in the brief we submitted earlier in the year and discussed with your committee, I think it was about March of this year. We would be happy to supply additional copies if you would like to have them.

The Chairman: No, I think we have copies.

Mr. Hart: The document I am referring to is called "Corporation taxes and growth in the pulp and paper industry". It was a submission to federal and provincial governments in February, 1971. Mr. Bell is just pointing out to me that there are two statements before you which indicate the means of application of this investment tax allowance.

The Chairman: One has the heading "Logging tax abatement"?

Mr. Hart: No. I am referring to the document headed, "EXample of application of forest industries investment allowance."

Senator Benidickson: Does anybody have the record of the date that was presented? I assume you are talking about your presentation in respect of the White Paper.

Mr. Hart: It was submitted in February 1971, and was discussed with this committee, I believe, in about March.

Senator Desruisseaux: It was discussed with the department?

Mr. Hart: Yes, sir.

Senator Benidickson: It was part of your submission on the White Paper. I am merely pointing out it has already been printed and is available.

Mr. Hart: I perhaps stand corrected, Mr. Chairman. One of my colleagues says we discussed the matter in general terms with this committee, but we did not discuss our submission in March. If I may, I would like, if senators would be willing to receive it, to supply you with copies of the document "Corporation taxes and growth of the pulp and paper industry", which does outline in considerable detail our proposals for correction.

The Chairman: Very well.

Mr. Hart: On the matter of the general rate of corporation tax, we pointed out the need for competitive reasons to have a rate lower than that in the United States. The reduction of 7 per cent for the period July 1, 1971 to December 31, 1972, is a step in the right direction, but it did take a long time to accomplish and it is only a temporary measure.

Senator Benidickson: It applies to all industries.

Mr. Hart: Correct.

Hon. Mr. Phillips: What is the justification for any position that this particular formula should be applicable to the forest industries inclusive of logging, as Senator Burchill mentioned, and not to other industries that engage in the marketing of natural products on world markets?

Do you justify your position specifically because of the nature of your industry, or do we have to make an explanation, if we accept your view, that you should not be assimilated to mining or any other world industry based in Canada that sells on world markets? That is the obvious reaction to any recommendation we may make.

Mr. Hart: We have been asked several times by Department of Finance officials, in making this presentation to them, that if the proposal we have made were granted on behalf of forest products industries would not the department receive similar requests from other industries. I think in all honestly our answer has to be that of course you are likely to. But a government has to govern and has to make decisions to justify the case. I opened my statement by saying the factor we feel is of absolutely critical importance is that industries that sell in international markets must have corporation tax burdens that are competitive with their competitors, unless perhaps in the rare circumstance that we had an industry in Canada that could be so prosperous that it could stand any kind of a tax rate. But in the real world in which we live, I feel that international industries have to have corporate tax burdens which are roughly equitable to those of their competitors.

The Chairman: That is acknowledged in the White Paper. I can recall a statement made in the White Paper that fiscal policies in relation to multinational companies in the foreign field, meeting competition in the foreign field, must be such that there will be no competitive disadvantage vis-à-vis those competitors.

Mr. Hart: I think we had better find that portion of the White Paper.

The Chairman: It is in the White Paper because I turned it up yesterday.

Mr. Hamilton: Unfortunately, it has not been translated into action.

The Chairman: That is why I looked it up.

Senator Desruisseaux: What is the percentage of the total production now?

Mr. Hart: About 75 to 80 per cent, I think.

Mr. Chairman, if I may return to your earlier question, I think we would argue that the differential taxation for different industries, depending on the competition they face in the world markets and the contribution they are likely to be able to make to Canadian economic growth, is a key factor in determining the level of tax burden. We see no justification in setting a level equal for all industries but which will not permit some of them to compete.

Hon. Mr. Phillips: The mining industry and the petroleum industry are not going as far as you go in your brief.

Mr. Hart: Perhaps they do not have as good a case as we have, sir.

Senator Benidickson: The mining industry does have peculiar tax consequences in other ways.

Hon. Mr. Phillips: I am trying to emphasize a point that a request has been made because of the peculiar nature of your industry, as distinguished from other natural resource industries, quite apart from the competitive aspect in Sweden and the United States.

Mr. Hart: We have not based our case on the fact that the mining industry already has preferential tax treatment within the Canadian scene. In other words, we are not "me too-ing".

Senator Connolly: Mr. Hart, at the present time your industry is in a very unfortunate position, I understand. Is that so?

Mr. Hart: I beg your pardon.

Senator Connolly: The Canadian pulp and paper industry is in a very depressed condition, a terribly depressed condition in fact. Now, it was not that way perhaps three or four years ago. Then you were in a very prosperous condition, I gather.

Mr. Hart: I think that is relative, sir. I think we would argue that we have been subject to this trend for something in the area of 10 or 12 years. Perhaps we have been a little slow in realizing what has happened to us.

Senator Connolly: That is what I am coming to, because it seems to me that at one stage, even though you had these excessive rates of taxation, if you want to describe them that way, you were still able to sell your products, because the world demand was very great. But once the world demand falls off in any way, as a result of what you have said earlier, namely, that economic conditions deteriorate abroad, then weaknesses in the tax system put you in an unfair position in competition with other world producers. Is that a fair statement to make?

Mr. Hart: Yes.

Mr. Hamilton: I think what you have said, sir, is fair. I might just go a little further in this. Most of us in the industry would be of the opinion that the trend began to become unfavourable at the beginning of the 1960s, and the devaluation of the Canadian dollar was a good paint job over some cracks. It amassed some of the basic underlying trends such as taxation and the increase in the capacity of the industry, not only in this country but in other parts of the world as well, which have greatly distorted the operating rates in the industry. And this puts a severe strain on the profits. The trend was set back then, but the prime factor was the devaluation of the Canadian dollar. The trend was unfavourable before we ran into the revaluation upwards of the Canadian dollar when it was allowed to float. But this was the single most serious step when the problems began to occur.

Senator Connolly: The change in the valuation of the Canadian dollar is obviously a factor that affected the situation in your industry both positively and negatively; and this is a situation which we have not yet discussed here. I do not know that we really need to, but it is good to have this pointed out to us.

Mr. Hamilton: The industry has to be so structured that it can take this kind of variation in its stride. If it cannot do that, it does not hold a strong position.

The Chairman: I think we should put into the record at this point two examples of applications of Forest Industries Investment Allowance.

Text of Examples follows.

EXAMPLE OF APPLICATION OF FOREST INDUSTRIES INVESTMENT ALLOWANCE

Assumes income of 100, of which 60 is from logging

Current Situation	Tax Rate	Logging Tax Abatement	Net Tax
Federal Tax	40	4	36
Provincial Tax	12	2	10
Logging Tax	6		6
		6	52

Proposed Situation	Tax Rate	Logging Tax Abatement	Earned Reduction	Net Tax
Federal Tax	40	4	13	23
Provincial Tax	12	2	4	6
Logging Tax	6			6
		6	17	35

NOTE: Taxes in the current situation have been calculated on the basis of a pulp and paper company operating in Ontario or Quebec. For such a company operating in British Columbia the net tax would be higher because of higher logging tax. Rate is as given in Reform Bill for 1972.

EXAMPLE OF APPLICATION OF FOREST INDUSTRIES INVESTMENT ALLOWANCE

Assumes income of 100, of which 60 is from logging

Current Situation	Tax Rate	Logging Tax Abatement	Net Tax
Federal Tax	36.5	4	32.5
Provincial Tax	12.0	2	10.0
Logging Tax	6.0		6.0
		6	48.5

Proposed Situation	Tax Rate	Logging Tax Abatement	Earned Reduction	Net Tax
Federal Tax	36.5	4	12.2	20.3
Provincial Tax	12.0	2	4.0	6.0
Logging Tax	6.0			6.0
		6	16.2	32.3

NOTE: Taxes in the current situation have been calculated on the basis of a pulp and paper company operating in Ontario or Quebec. For such a company operating in British Columbia the net tax would be higher because of higher logging tax. The rate of federal tax is that applicable in 1972. For 1973, the 7 per cent reduction would no longer apply and federal rate would be 49 per cent.

The Chairman: This is the substance of the request you are making?

Mr. Hart: That is correct sir.

The Chairman: It will be published. You say that the exchange situation in the devaluation of the Canadian dollar, together with your other operations, distorted the picture regarding the operating profits of the industry?

Mr. Hamilton: Similar to a drastic price increase, in effect.

Mr. Hart: Mr. Chairman, if the suggestion is being made that an upward trend in demand is going to correct this fundamental problem, I think we are misleading ourselves.

Senator Connolly: I did not suggest that. That might result, but you still have the underlying inequity that plagues your industry.

Mr. Hart: Yes, we will not participate in the upward trend in demand unless we have a better base from which to operate.

Hon. Mr. Phillips: Suppose the dollar was pegged at 92½ cents, would you need this relief?

Mr. Hart: Yes, because naturally it would be unrealistic to peg it at 92½ cents.

The Chairman: Tell me, Mr. Hart, is there any way, other than giving tax abatements and reduction in corporate

rates, by which the problems of the industry could be dealt with? In the mining industry, and the oil and gas industries it is dealt with in a variety of ways, by write-offs, by accelerated write-offs, by factors of earned depletion, all of which have the effect of substantially reducing the amount of earnings. Is there anything along that line that would accomplish the result that you are seeking, or which you feel is necessary?

Mr. Hart: Mr. Chairman, we have in effect recommended a procedure which does reduce the volume of earnings that are subject to tax. I am certainly not informed enough to recommend other procedures. We have made one specific proposal which we feel would be a satisfactory solution to the problem. If there is sufficient understanding that the problem does exist, then, it seems to me that man's imagination in this area can be almost limitless, and, to me, the technique is secondary to the recognition of the problem and the intent to correct it.

Senator Gélinas: Have your submission to the Government actually been turned down, or is it just being held in abeyance?

Mr. Hart: It is hard to say, senator. We have not been told that it is going to be adopted. On the other hand, it has not been adopted and it is not mentioned in the Tax Reform Bill, nor has it come up in any hearing. We are still pressing for it.

Senator Benidickson: You say the real presentation was subsequent to the floating of the dollar.

Mr. Hart: It was earlier this year, and our recommendation was that it be adopted either as a measure of tax reform or sooner by other means, if possible.

Mr. T. Bell, President, Abitibi Paper Company: We have had no sympathy from the Department of Finance whatsoever.

Mr. Hamilton: Not that we have been able to detect. If there is sympathy, it is not evident.

Senator Macnaughton: Would you say you have been ignored?

Mr. Hamilton: No, I would not. I do not think that would be fair to the department.

Mr. D. A. Wilson, Director, Canadian Pulp and Paper Association: We have come close to being ignored.

Mr. Hamilton: Let us say we have certainly had the opportunity to meet with them and discuss it with them.

The Chairman: There may be some feeling against granting a favourable reduced tax rate to a particular industry if there is some other way of giving the benefit, by reason of peculiarities in the operation of that industry.

Do you have any suggestions in that regard?

Mr. Hamilton: I gather, Mr. Chairman, you are staying within the tax structure?

The Chairman: Yes. Do you want to move into another area?

Mr. Hamilton: There are many other areas. For example, you run into transportation problems, the combines legislation, the competition act, and so forth. There is a whole range of other areas, all of which in total could have a significant impact on the ability of the pulp and paper industry to be competitive.

The Chairman: The only one that is immediately before us is Bill C-259. We are not proposing to bring before us the so-called "competition bill." It has a long road to move along before it gets to this committee.

Senator Connolly: I hope I am not putting my head or my hand into a hornet's nest here, but what percentage of this industry is Canadian-owned and what percentage is foreign-owned?

Mr. Hamilton: The best guess, senator, is that between 55 and 60 per cent is Canadian owned.

Mr. Hart: That has not changed significantly in the last seven or eight years.

Senator Connolly: Do you sense any feeling that because there is a large percentage of foreign ownership perhaps spcial tax treatment for the industry is not forthcoming?

Mr. Hart: I have not felt that, sir. Quite frankly, I believe the basic road-block is that it may be unrealistic to expect the Department of Finance, which obviously has to take in enough money to pay the Government's bills, to propose a major reduction in its tax revenue. It seems to me the impetus has to come from other areas of the Government which recognize the economic problems and the social problems involved, as well as the opportunities for growth. This is where the pressure on the Department of Finance has to come from.

Senator Connolly: But surely we are not discovering for the first time that the forest is a depleting asset in our country. It is renewable, if you will, but at a cost, and if there are aspects of the tax laws that apply, for example, in the mining industry and the petroleum industry, they should also apply to the forest products industry. Has any suggestion ever been made as to how this could be done?

Mr. Hamilton: I think this point is covered in our original submission on the tax structure.

Senator Connolly: Was this the first time that it had been put before the Government?

Mr. Hamilton: I would say that last year was the first time.

Mr. Bell: That is right.

Senator Connolly: But this is a basic condition which has persisted since the beginning.

Mr. Hamilton: It has persisted for a long time.

Senator Connolly: I wonder why the tax laws did not recognize this fact.

The Chairman: The problem did not become acute.

Mr. Hamilton: I believe you could rightly challenge the industry in that the industry did not in fact make it their business to bring this situation to the attention of the Government.

Senator Benidickson: Were you not inspired to look somewhat more carefully at these matters as a result of the floating dollar?

Mr. Hamilton: We were inspired to look at these matters as the result of a whole series of circumstances, senator.

Senator Connolly: I remember, Mr. Chairman, when we had a committee of this house on land use one of the most important submissions was made by this industry and that was with respect to the replenishment of the forest. This is not new. Surely, at that time the tax implications should have been triggered by the work of the committee and by the submission made by the industry?

The Chairman: It is a pertinent point, senator, but it seems to me that we should not look back at this time.

Senator Connolly: No, Mr. Chairman, but the answer to your question obviously is that this approach has not been made.

The Chairman: When you renew or you have a reforestation program, how would the cost of that be dealt with for tax purposes?

Mr. Hamilton: It varies widely across the country because it is a provincial matter.

The Chairman: But do you write it off as an expense or do you treat it as a capital item?

Mr. Hamilton: It is an expense, to the extent we incur expenses.

The Chairman: It may well be that it is not sufficient to treat it as an expense. It may be that you need something on top of that that might be parallel to earned depletion in the mining, oil and gas industries. Those expenses would also qualify as a deduction from your earnings.

Mr. Hamilton: Yes.

Mr. Hart: This could be an alternative technique that you are proposing.

The Chairman: I am just trying to search and reach out. It seems to me this is the politically-wise preferred area as opposed to a tax reduction.

Mr. Hamilton: We have structured our suggestion here, Mr. Chairman, in a manner which is parallel to the mining industry; but we have based our reasoning for suggesting that consideration be given to it, not on the fact we want to be the same as the mining industry, but as a road to parity in the tax structures, with our competitors.

The Chairman: The overall answer, of course, is that if you are not making money these allowances do not do you any good.

Mr. Hamilton: That is correct, and there would be an onus on the companies to get themselves in a position where they could take advantage. This, we felt, answered the valid criticism that grants and other special types of deals can, in fact, be supportive, but it is not socially or economically desirable for them to do that.

Senator Benidickson: We cannot only concern ourselves with the matter of taxation and the corporate features. You are a tremendously important industry in Canada from the point of view of the number of people you employ. Have you anything to say as to where you stand as an employer of labour in Canada?

Mr. Hamilton: In manufacturing, I believe, we are "number one".

Senator Benidickson: I would think so.

Mr. Hamilton: This, I might add, with the chairman's permission, places a tremendous responsibility on the management of these companies because we are like the mining industry in that, if a mine closes down, the town closes down; if a mill shuts down the area goes down.

Senator Benidickson: In the area I have represented for 20 years the mill is a major source of employment.

Mr. Hamilton: It is a fact that today there are many mills in this country which are running just because of the social responsibilities of the company concerned, but the arithmetic of it says they should be shut down.

Senator Burchill: Do you get any tax relief on account of the money you spend on pollution control?

Mr. Hamilton: Not as yet.

Senator Burchill: That would be a point to hammer home.

Mr. Hamilton: We have been hammering that point home at the federal level and also at the provincial level. Some of the provinces have rescinded in one way or another their sales taxes. Some provinces have kept pollution abatement facilities out of real estate tax rolls, which is an advantage. But in terms of the federal Government we have got a 50 per cent straight line write-off on these facilities, but that is the extent so far.

The Chairman: It may be that something akin to DSIC would be a help, because there on export sales you get really an abatement in your taxes.

Mr. Bell: That is on new facilities for export. We are already in the export business and to add new facilities in an already glutted market does not make sense.

The Chairman: That is why I said "similar to". I was thinking in terms of to the extent of the proportion of your income from export sales to your total income; if that was segregated and treated specially by a reduced corporate rate, there would be lots of justification for that, because Canada to live must have export sales and you cannot have export sales unless you can sell and make money on them. To do that you must be competitive, so you could find justification, I would think, and politically justified considerations at this time, because we certainly have to be export conscious.

Mr. Hart: I detected from a point you mentioned earlier that you are concerned about the acceptability of our tax proposal, which we are going to send you in detail, because I think you characterized it as simply a tax reduction. When you see the detail of the proposal I think it may commend itself to you, because it is in fact an earning process. This is not a reduction in taxes which the companies will come by easily; they will have to earn it through our proposal by expenditures in expansion or modernization or pollution control.

Senator Macnaughton: I am under the impression that under the new Department of the Environment there is a fund that has been set up fairly recently to which you can apply for aid and assistance in the building of pollution control measures or works.

The Chairman: I do not think it is within the scope of what we are looking at now. I was going to suggest that this was a very interesting and provocative discussion; it is not going to resolve anything today, because we are waiting for some more material. We may get some ideas as to an area of approach that would be different from just a straight tax reduction, and maybe you will too, now that you know what our thinking is. Could we move on to the next heading?

Mr. Hart: Turning to the more technical aspects of the bill, we have listed in our submission with respect to Bill C-259, after the general introductory comments about the level of taxation, a number of points with respect to clauses about which we are concerned. My colleagues would be prepared to try to answer any detailed questions you might have on these, but I should point out that we are not sure we have listed all the changes; in fact, we are almost sure we have not listed all the clauses that we will ultimately be concerned about. We think this is one of the very serious problems about this bill, namely, how you get to understand it.

I would like to give three examples that we discussed this morning in preparation for this meeting this afternoon. In our submission to government last February, in this document we are going to send you, we urged that techniques be found through federal-provincial negotiation to provide for full abatement of logging taxes so that the forest products firms would not pay a greater corporation tax than the rate that normally applies to the corporations generally. I do not want to go into the details of the logging tax structure now, but it does have the effect that in certain provinces the abatement for the logging tax is not complete and companies wind up paying a higher rate of corporation tax than companies generally.

At the very least, we have been under the impression from discussions we have had with government officials that the present incomplete abatement would not be reduced. However we now find from a careful reading of Bill C-259 that under certain circumstances the provisions of the bill will in fact reduce the already less than complete offset for that logging tax.

We have prepared a special statement on this point, a copy of which is before you, which is called "Logging tax abatement". I merely mention that to indicate two points. First, we are concerned that logging tax abatement, even though now not complete, has a possibility in certain circumstances of being less complete in the future. Also it illustrates that we are almost shooting at a moving target on this bill, which seems to be moving faster than we can keep up with on the clauses and the changes.

The Chairman: On that point, I would suggest that we print this memorandum, "Logging tax abatement", as part of our proceedings today at this point. Is that agreed?

Hon. Senators: Agreed.

Text of memorandum follows.

LOGGING TAX ABATEMENT

The intention of the present Income Tax Act (Section 41A) was to provide full abatement to the taxpayer for logging taxes imposed by the Provinces, provided the rate of logging tax did not exceed 10% and the Province concerned abated one-third of the logging tax against its Corporation Tax. A measure of logging tax has, however, always been disallowed for Federal tax purposes on technicalities.

Bill C-259 now proposes to ensure that there will be further and potentially serious double taxation due to logging taxes: this will be particularly severe whenever the company as a whole has a tax loss in a year or whenever the non-logging operations suffer a loss. These provisions are particularly harmful as the double taxation arises when the company can least afford it.

Another anomaly occurs as the half of the capital gain on the sale of a timber limit that has to be brought into income is excluded from the taxable income available for a logging tax credit, even though the whole gain may be subject to logging tax.

The most suitable solution to the problem of logging taxes is that proposed for mining taxes in Bill C-259—as proposed in an earlier CPPA Brief.

A sample calculation of the effects of this extra tax is set out in Appendix A.

October 25 1971 C. A. BROOKE.

ILLUSTRATION OF DOUBLE TAXATION
DUE TO SECTION 127 OF BILL C259

Year	Year 1	2	3	4
Logging Income	100	100	(100)	100
Mining Income	100	—	—	100
Half Capital Gain on Sale of Timber Limit (Sec. 129(4))		—	—	100
Other Business Income	100	(50)	(50)	—
Income	300	50	(150)	300
Losses Forward	—	—	—	(150)
Taxable Income	300	50	(150)	150
Logging Tax**	6	6	—	18
Federal Tax Net of Provincial Abatement	120	20	—	60
Less Mining Income Adj.	(15)	—	—	(15)
Logging Tax Adj.	(4)	(3)	—	(3)*
Net Federal Tax	101	17	—	42
Provincial Corporation Tax	36	6	—	18
Less Logging Tax Adj.	(2)	(2)	—	(6)
	34	4	—	12
Provincial Logging Tax	6	6	—	18
Provincial Mining Tax	15	—	—	15
Total Tax	156	27	—	87
Rate	52%	54%	—	54%

*6.2/3% of taxable income less mining income or investment income, i.e., $6.2/3 \times (150-100)/100$.
**Assuming 40% processing allowance and 10% rate.

Mr. Hart: There is a second point I might use by way of example. Clause 192(13) of the bill, dealing with designated surplus, has already been amended in one of the 95 changes, and I understand amended primarily to correct a defect in drafting. It is our view again on what inspection we have been able to make of that clause that it creates an even worse situation than the unamended clause, and that it could give rise to very serious cases of retroactive taxation.

The Chairman: When you say a worse situation, I take it you do not deal specifically with that point in your brief as to what is the worse situation?

Mr. Hart: No, sir. It is not even in our brief.

The Chairman: Then we would like you to point that out to us, because we are all operating in that field, for 95 amendments is a lot of amendments to digest and correlate.

Senator Benidickson: On a 1000-page book.

The Chairman: You, with a special problem, would be looking at that special thing, and therefore would detect the defects maybe a little faster than we would. Would you give us a short memo on that point, then we do not need to take any time in discussing that point now.

Mr. Hart: We will send you a memo.

Hon. Mr. Phillips: In connection with designated surplus, it has been suggested from certain quarters that the bill would be substantially simplified if designated surpluses were eliminated from the statute completely, and that we would be dealing solely with undistributed earned income and capital surpluses. Do you see any particular reason why the statute should be burdened with designated surpluses, in view of the introduction of the capital gains tax?

Mr. Hart: Mr. Chairman, may I ask Mr. Brooke to respond to that, because he can do so much more effectively than I can.

Mr. Colin Brooke, Manager, Tax Division, Domtar Limited: I agree, sir, on the introduction of the capital gains tax. I would have thought this provision on designated surpluses was absolutely redundant.

Hon. Mr. Phillips: I would like to put a halo over your head.

Mr. Hamilton: Don't bother. That would cost us more money.

The Chairman: You may not realize it, but Senator Phillips was riding a pet view of his and now he has your support. Shall we move on?

Mr. Hart: Mr. Chairman, I was trying to give examples of the difficulty of keeping up with this bill. Another one is, of course, that the Minister of Finance has announced still further revisions will be forthcoming. Quite frankly, I do not know quite how we are supposed to keep up with those and make comments on them before the bill is due for enactment.

The Chairman: We will do the best we can.

Mr. Hart: Generally, Bill C-259 introduces considerable rigidity into business operations, in our opinion. We do not support this, primarily because we have been exposed through our competitors to corporate tax structures in other countries which are based on giving corporations as much flexibility as possible. So this is a point about which we are concerned. To give you some examples, the bill goes to great lengths to close some minor loopholes, but in the process it sets up conditions that we feel will just hamper business development. For instance, some corporations will suffer tax penalties in accomplishing much needed reorganizations for purposes of efficiency. It is our belief that tax-free reorganizations should be permitted.

The bill requires payment of corporation taxes very often months before the receipt of the cash upon which those profits—or in our industry hopefully those profits—will be based. We think that the reverse should be true.

In the case of a company making an incorrect election, the penalty imposed in some cases can be confiscatory.

The Chairman: You do not need to develop that at all, because I would think that there is a pretty firm view in the committee on the penalties. If you are out one cent in your calculation of undistributed income, they can invoke the full penalty of the law 100 per cent. Of course, this just does not make sense. We have had submissions on that.

Mr. Hart: I suspect that you are much more knowledgeable in this area than we are, Mr. Chairman. We are really leading up to the point that we believe that the adoption of the reform bill in January, if this is the schedule, does not provide for adequate discussion of the bill. There are a great many things wrong with it. Meanings are obscure. There are punitive sections and there are the 95 amendments. And there is more to come I suspect.

I think a real element of which we can all be concerned here, too, is that there has to be some co-ordination between the federal and provincial governments.

Senator Benidickson: Particularly with respect to a natural resource industry.

Mr. Hart: Precisely.

The Chairman: We are conscious of those things, and we are going to do the best we can.

Mr. Hamilton: I might suggest, Mr. Hart, that if you were just to go down the list of the particular points, the Chairman might indicate which ones he would like to have us amplify. Although most of them are particular to the paper industry, generally they are applicable to the whole of industry.

The Chairman: On some of the points on your list we have already had discussions. For example, your nothings, your consolidated returns and the corporate tax instalments and tax-free reorganizations.

Mr. Hart: No. 6 has been partially taken care of, I believe, in amendment.

The Chairman: So that takes us down to No. 7. I can tell you that on dividends received from foreign affiliates we have had excellent submissions from Massey-Ferguson and from Alcan. We had almost a catechizing from them, and, as they are very knowledgeable in that field, they were very helpful to us in the information we received. Actually, we are doing some writing on this now so that I cannot take it any further than that. With all due respect to your paragraph 7, I do not think it will add anything to our fund of knowledge or will effect a change in the view with which we are approaching the subject at the present time.

You have already spoken about the additional tax on excessive election and you have heard what I had to say about that. I take it there is nothing further you want to add. The question is how a penalty of that kind could possibly be justified, if you make a mistake in the calculation of your undistributed income. Is there anything further you wish to add?

Mr. Hamilton: No, sir. Many of these subjects have been brought up by many others who have appeared before you.

The Chairman: We are always open to hearing anything additional that you wish to say. Now, on the dividend tax credit is there anything special you wanted to add there?

Mr. Hart: Just what is in the statement, Mr. Chairman.

Mr. Hamilton: I do not think there is anything we would add to what is said there, Mr. Chairman.

The Chairman: Now, allowances for automobiles and club dues. This looks pretty much like a policy decision by the Government. I think we did express views on that in our report. Is there anything further you would like to point out?

Mr. Hart: No, Mr. Chairman. We came prepared on these detailed points to respond to questions, if that was your wish, but we have nothing to add to the brief statement we have made on each point.

The Chairman: All right. We now come down to taxation and stock option benefits. We have had some submissions on that. Have you a point that you would like to make? We would certainly like to hear it.

Mr. Hamilton: The only point we make, Mr. Chairman, is that we consider this as a mechanism by means of which we can compete in the North American market for talent in the management ranks of this industry. Some people think we need more talent so this would be one thing that would help us.

The Chairman: Stock option benefits are a well recognized way of competing. This reduces the attraction.

Mr. Hamilton: That is correct.

Mr. Bell: Mr. Chairman, I should like to add one point. In our company, with American operations it is almost impossible to entice an employee of ours working in the United States back to Canada. There is no way we can get him to come back to Canada because of the difference in the tax structure. The employee option is only one way which you can add to this enticement, and there really is no enticement. So far as pulp and paper people talking of stock options is concerned, well, that is pretty redundant.

The Chairman: Right now there is not much attraction.

Mr. Hamilton: It is a good time to get them.

The Chairman: With respect to the deemed disposition on ceasing to be a resident of Canada, we have had some submissions. I think there have been views expressed by some of our members that there are some circumstances in which, at the discretion of the minister, a departure of residents from Canada should not be subject to the penalties that are provided for in the bill; for instance—health reasons, age, change of job. We have looked very seriously at these things. I notice the heading "Capital Gains—Valuation Day" which is found on page 14. Have you anything to say about that?

Mr. Hart: I believe a part of that has been corrected by an amendment, sir.

Mr. R. W. Wilson, Tax Specialist, Consolidated Bathurst Limited: Yes, the area of capital gains respecting fluctuation has been altered to our satisfaction by the amendment; and there has been a minor alteration amending section 2 resulting from the purchase of bonds for sinking fund purposes. But I feel this is very nominal.

The Chairman: You mean, if you go into the market and are able to pick up some of your bonds for redemption

purposes at, let us say, 80, with a resulting capital gain, you would have to pay tax on that gain.

Mr. R. W. Wilson: Yes.

The Chairman: You say they have done something about that situation?

Mr. R. W. Wilson: They have done a little on that.

The Chairman: What do you mean by "a little"?

Mr. R. W. Wilson: A gain of, let us say, 20, in the case you were suggesting, will be treated as capital gain and, if we were to go through a refunding issue and settle the entire debt, I think it would be taxed on the income. I do not know whether that is a correct interpretation, but it is a possibility.

The Chairman: I question the rules, and I think it is a good idea to make that notation in our report. But there are physical problems, I would think, in getting a ruling sooner than that. A ruling is certainly desirable, and there should be rulings available quickly, but how are you going to get them?

Mr. Hart: Our single recommendation, Mr. Chairman, is that whatever provision can be made to enlarge the ruling and to make it more effective and more prompt is the only thing that we can do. There is a need for this to happen.

The Chairman: The answer that has been given is that this will be a question the courts will have to decide, and this is not very satisfactory. It would interfere with the completion of normal business operations.

Mr. Hart: The kind of discussion that you have promoted on this individual clause and the kind of response which we can give, which is at best incomplete, is like taking a shot at a moving target. We are very concerned about the implementation date of this bill. We feel it will not be done until such time as the federal and provincial governments have developed a system that truly and effectively meets our Canadian needs. We feel it would be very dangerous to try to solve some of these basic policy problems.

The Chairman: This is exactly what we said in our report. We thought they were putting the cart before the horse in many ways; and to build a structure with the complexity that we have—and I am not critizing those complexities as such at the present time because a lot of them arose from the fact they were trying to do some very beneficial things, they were trying to write provisions into the bill in relation to small businesses, and so on—you may find yourself going up and down the same street and not recognizing the street, but in most cases they are trying to benefit the situation. There is nothing we can do about this at present, except to draw their attention to as many things as we think need to be

Are there any other points?

Mr. Bell: The main point in our submission is tax relief. Because we are competing in world markets, would it be more appropriate for us to base the main thrust of our request for relief on the export segment of our income?

The Chairman: My own view, having heard many submissions and given careful consideration to it, is that that is an area in which the Governement, the public and everyone is really conscious of the problem. The US 10 per cent surcharge brought that into prominence.

Senator Benidickson: We know they are an important export industry; everyone knows that.

The Chairman: Yes; Canada has to export to live and these exports do bring money to Canada. However, all that will be finished if they are not in a position to compete in those markets and it is important to Canada that they should be in that position.

Mr. Hamilton: This becomes a very complex problem, as I think you gentlement all know, because of the commitments to GATT as to what is permissible.

Hon. Mr. Phillips: Yes, plus the bookkeeping involved to segregate the export segment.

Mr. Hamilton: We all know what is going on in the common market, where because of their value-added taxation principles they are able to rebate the tax on exports, which very neatly solves the problem.

The Chairman: I gather that Mr. Bell is referring to a solution directed to supporting the export industry in some way in the bringing home of its earnings. They operate in other countries, which have tax credits and incentives. The corporate tax rate as a result is much lower, but the benefits received in other countries are then taxed away to the extent of the difference between the rate of tax paid abroad and the Canadian rate. The net result is to create a disadvantage for the exporter and remove a competitive advantage that he may have had under the earlier system, where he could bring these dividends home with a certain percentage of voting shares without paying income tax.

It might not be too difficult to illustrate in a presentation how invaluable that is.

Hon. Mr. Phillips: Mr. Bell's point is interesting; it is good sense, but difficult of application. For example, if a company makes $5 million and, segregating it, over a million of that $5 million is made up of export trade, there you have the justification for a special rate of taxation, because it relates to the competitive features as we discussed them with regard to the United States. The question of treatment of expenses such as interest on funded debt and other items arises. Should they be related to sales, and so forth, and administratively would it work out? I think, with respect Mr. Chairman, that we might consider that, because it is the one basic justification that I have heard today, aside from the broad application of protecting the competition of world markets, that would justify a special rate.

The Chairman: The Chamber of Commerce made a submission the other day and I asked them to rate the priorities in looking at the bill with respect to the order of changes, and they gave us a rating in which they placed foreign source income as number 2. I told Mr. Crawford, who was explaining it, that to our way of thinking the most important item was multinational or foreign income because it cuts across our whole trade.

Mr. Hart: Mr. Chairman, as Mr. Bell suggested, if it could be achieved it is seven-eighths of a loaf, which is considerably better than half a loaf or no loaf at all, but it also defies the principle, if it is an accepted principle, that industries that are competing and subject to international competition should not bear a corporate tax burden higher than their competitors; and there is 20 per cent of our industry where international competition exists right here in Canada.

Senator Benidickson: And that is the first argument you put forth this afternoon.

Mr. Hart: That is right.

The Chairman: If you go back and read a couple of paragraphs in the White Paper, and I suggest you do, you will see that that is enunciated there quite clearly and quite distinctly, and if I were asked to make a presentation as to the value of the export industry and how it should be treated, these are the first quotes I would use.

Mr. Bell: It has not come out in the proposed legislation though, has it?

The Chairman: No. Some inhibiting source came along.

Thank you very much, gentlemen.

The commitee adjourned.

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THIRD SESSION—TWENTY-EIGHTH PARLIAMENT

1970-71

THE SENATE OF CANADA

PROCEEDINGS

OF THE

STANDING SENATE COMMITTEE ON

BANKING, TRADE AND COMMERCE

The Honourable SALTER A. HAYDEN, *Chairman*

No. 46

WEDNESDAY, NOVEMBER 3, 1971

Tenth Proceedings on:

"Summary of 1971 Tax Reform Legislation"

(Witnesses—See Minutes of Proceedings)

24293—1

THE STANDING SENATE COMMITTEE ON BANKING, TRADE AND COMMERCE

The Honourable Salter A. Hayden, *Chairman*

The Honourable Senators,

Aird	Grosart
Beaubien	Haig
Benidickson	Hayden
Blois	Hays
Burchill	Isnor
Carter	Lang
Choquette	Macnaughton
Connolly (*Ottawa West*)	Molson
Cook	Smith
Croll	Sullivan
Desruisseaux	Walker
Everett	Welch
Gélinas	White
Giguère	Willis—(28)

Ex officio members: Lynn and Martin

(Quorum 7)

Order of Reference

Extract from the Minutes of the Proceedings of the Senate, September 14, 1971:

"With leave of the Senate,

The Honourable Senator Hayden moved, seconded by the Honourable Senator Denis, P.C.:

That the Standing Senate Committee on Banking, Trade and Commerce be authorized to examine and consider the Summary of 1971 Tax Reform Legislation, tabled this day, and any bills based on the Budget Resolutions in advance of the said bills coming before the Senate, and any other matters relating thereto; and

That the Committee have power to engage the services of such counsel, staff and technical advisers as may be necessary for the purpose of the said examination.

After debate, and—

The question being put on the motion, it was—

Resolved in the affirmative."

Robert Fortier,

Clerk of the Senate.

24293—1½

Minutes of Proceedings

Wednesday, November 3, 1971.
(58)

Pursuant to adjournment and notice the Standing Senate Committee on Banking, Trade and Commerce met this day at 9:30 a.m. to further examine:

"Summary of 1971 Tax Reform Legislation"

Present: The Honourable Senators Hayden (*Chairman*), Aird, Beaubien, Benidickson, Blois, Burchill, Carter, Connolly (*Ottawa West*), Haig, Hays, Isnor, Macnaughton, Molson, Smith, Sullivan and Welch—(16).

Present, but not of the Committee: The Honourable Senators Heath and Laird—(2).

In attendance: The Honourable Lazarus Phillips, Chief Counsel.

WITNESSES:

Hollinger Mines Limited:

Mr. A. L. Fairley, Jr., President;

Mr. Percy C. Finlay, Q.C., Vice President and General Counsel;

Mr. Wendell F. White, Treasurer, Labrador Mining and Exploration Company Limited.

The Canadian Life Insurance Association:

Mr. A. H. Lemmon, Past President and President, The Canada Life Assurance Company, Toronto;

Mr. Hervé Belzile, Past President and President, Alliance Mutual Life Insurance Company, Montreal;

Mr. T. M. Galt, Chairman, Committee on Taxation and Executive Vice-President, Sun Life Assurance Company of Canada;

Mr. J. A. Tuck, Managing Director;

Mr. F. Kimantas, Tax Officer.

Dominion Foundries and Steel Limited:

Mr. J. Plumpton, Comptroller;

Mr. A. D. Laing, Assistant Comptroller and Assistant to the Executive Vice President—Financial.

At 12:00 o'clock Noon the Committee adjourned.

2:15 p.m.
(59)

At 2:15 p.m. the Committee resumed.

Present: The Honourable Senators Hayden (*Chairman*), Beaubien, Benidickson, Blois, Burchill, Carter, Connolly (*Ottawa West*), Haig, Hays, Isnor, Macnaughton, Molson and Welch—(13).

In attendance: The Honourable Lazarus Phillips, Chief Counsel.

WITNESSES:

The Canadian Institute of Chartered Accountants:

Mr. R. D. Brown, F.C.A., Chairman, Tax Committee;

Mr. Michael Carr, C.A., Member, Tax Committee;

Mr. R. C. White, C.A., Director of Communications.

At 3:35 p.m. the Committee adjourned until 8:00 p.m. this day.

8:00 p.m.
(60)

At 8:00 p.m. the Committee resumed *in camera.*

Present: The Honourable Senators Hayden (*Chairman*), Beaubien, Benidickson, Blois, Carter, Connolly (*Ottawa West*), Cook, Gelinas, Haig, Hays, Isnor, Molson and Smith—(13).

In attendance: The Honourable Lazarus Phillips, Chief Counsel.

The Committee proceeded to the consideration of the Preliminary Report respecting the Summary of 1971 Tax Reform Legislation.

It was Agreed that typographical and other minor revisions and additions be left for the consideration of the Chairman.

At 10:15 p.m. the Committee adjourned until Thursday, November 4, 1971 at 9:30 a.m.

ATTEST:

Frank A. Jackson,

Clerk of the Committee.

The Standing Senate Committee on Banking, Trade and Commerce

Evidence

Ottawa, Wednesday, November 3, 1971

The Standing Senate Committee on Banking, Trade and Commerce met this day at 9.30 a.m. to give consideration to the Summary of 1971 Tax Reform Legislation, and any bills based on the Budget Resolutions in advance of the said bills coming before the Senate, and any other matters relating thereto.

Senator Salter A. Hayden (*Chairman*) in the Chair.

The Chairman: Honourable senators, we have four submissions this morning by: Hollinger Mines Limited; The Canadian Life Insurance Association; The Canadian Institute of Chartered Accountants; and Dominion Foundries and Steel Limited.

The first is Hollinger Mines Limited, represented by: Mr. A. L. Fairley, Jr., President; Mr. Percy C. Finlay, Q.C., Vice-President, Treasurer and General Counsel; and Mr. Wendell F. White, Treasurer, Labrador Mining and Exploration Company Limited. I understand that Mr. Fairley will make the opening statement.

Mr. A. L. Fairley, Jr., President, Hollinger Mines Limited: Mr. Chairman and honourable senators, I would like to express our appreciation for your courtesy in allowing my colleagues and me to appear before you, and to emphasize to you the very serious problems which will confront the mineral industry in Canada generally, and, particularly, two of Hollinger's subsidiary companies—Labrador Mining and Exploration Company Limited and Hollinger North Shore Exploration Company, Limited—if Bill C-259 is enacted in its present form.

I have with me this morning, Mr. P. C. Finlay, Vice-President, Treasurer and General Counsel of Hollinger Mines Limited, and also Mr. Wendell White, Treasurer of Labrador Mining and Exploration Company Limited and Hollinger North Shore Exploration Company, Limited.

We have appeared before your committee previously, when hearings were being held on the White Paper on Taxation, and, at that time, we opposed in principle, with broad philosophical arguments, certain segments of this paper, as they affected the mining and mineral industry. Since that time, certain modifications have been made in this proposed legislation, which would have the effect of somewhat, not nearly enough, but somewhat, mitigating the burden on operating mining companies. Nothing has been done, however, to relieve its onerous impositions on Canadian mineral exploration companies—companies which represent the very basis of the future growth of the mineral industry in Canada. Labrador Mining and Hollinger North Shore are in this category of mineral exploration companies.

Therefore, in the brief we are presenting today, we have addressed ourselves in some detail to two specific points:

(1) That the mineral exploration companies, under the terms of Bill C-259, will not be able to earn any significant depletion, as would a large mine-operating company; and,

(2) Due to the specific wording of the bill, the mineral exploration companies will not even qualify for the federal abatement to the provinces of the additional 15 percentage points, which mine-operating companies would be allowed.

The ultimate result of these two regulations would be that, after 1976, the mineral exploration companies would pay approximately 50 per cent of earnings in taxes. When provincial taxes are taken into account—and they will probably vary from province to province—the total would probably exceed this amount. This means that the mineral exploration companies would be taxed at a substantially higher rate than mine-operating companies and, depending on what the provinces do with their taxes, possibly at a higher rate than general manufacturing companies.

This prospect represents a complete reversal of the laws which have governed mineral exploration in Canada, for many years—a movement from a basis of encouragement of this very necessary industry to one of punitive taxation which would have a most discouraging effect on it.

Furthermore, as we point out in our brief, there is a strong element of retroactivity in Bill C-259, as it affects the mineral exploration companies. Income from contracts and leases which were entered into in good faith by all parties, previous to 1965, under the tax laws then existing, will, under the new law, be subjected to unanticipated taxation, which will seriously penalize those companies which made royalty arrangements at that time or earlier.

This situation bears particularly heavily on Labrador Mining and Hollinger North Shore, and the royalty contracts made between these companies and Iron Ore Company of Canada prior to 1965. It is not practical, and probably impossible, to revise these royalty contracts at this time, because our negotiating position is eroded.

We would, therefore, respectfully urge that this committee either:

(i) recommend the restoration of the capital status of such royalties as they existed prior to 1965; or,

(ii) at least reiterate the recommendation of your committee with reference to the White Paper and which is referred to in our brief, relating to non-operators percentage depletion. You will recall that your committee's recommendation was:

"that paragraph 5.43 White Paper be implemented to eliminate the percentage depletion available to non-operators, but only to the extent that the interests of such non-operators are acquired after the date of the White Paper or commitments to acquire have been made after

such date. Failing this in the opinion of your Committee, such non-operators would be made subject to tax on the proceeds received under existing agreements which were concluded under the present rules of percentage depletion which may have been a factor in the price accepted."

The underlining is ours.

This, we would hope, you would again recommend.

The predicament in which the proposals of Bill C-259 would place Hollinger and its exploration subsidiaries, Labrador Mining and Hollinger North Shore, has been outlined in submissions which we have made in the past, and are reiterated and brought up to date in this present brief. It is hoped that after further study of this situation your committee will recommend to the Government that it take the necessary steps to rectify the serious and injust wrongs which have been and will continue to be imposed on us and our many shareholders as a result of the changes made and proposed in income tax legislation since our commitments to Iron Ore Company of Canada were first made.

Thank you, Mr. Chairman and honourable senators. If there are any questions you wish to ask, either I or my colleagues will attempt to answer them.

The Chairman: Mr. Fairley, I take it that you are familiar with what has been called the proposed regulations which were issued in July of 1971. In your view, do you find that those proposed regulations restrict the plain intent of the minister's letter of August, 1970, or are you satisfied that they follow and do not restrict that intent?

Mr. Fairley: Mr. Chairman, I will ask our general counsel to speak to that. I see what you are getting at, and I will ask Mr. Finlay to reply to that.

Senator Benidickson: Mr. Chairman, has the evidence of Noranda been printed yet and, if so, have these gentlemen read that evidence?

The Chairman: Well, the newspapers have published every word of the briefs that this committee has had submitted to it, along with quite a few headings as well.

Mr. Fairley: I did read the Noranda evidence in one newspaper, but I do not believe it was complete. At any rate, I would ask Mr. Finlay to speak to that.

Mr. Percy C. Finlay, Q.C., Vice-President, Treasurer and General Counsel, Hollinger Mines Limited: Mr. Chairman, I believe you are referring to the regulations in regard to the amount that can be taken for depletion for buildings, and so on.

The Chairman: Yes.

Mr. Finlay: I am quite prepared to speak to that. Incidentally, it has little, if anything, to do with this presentation today because we are speaking particularly on behalf of non-operators. The question you have raised is something that affects a company in which we have a substantial interest: Iron Ore Company of Canada. It would also affect Noranda, in which we have a substantial interest as well.

The real basis of it is that, if they are giving something as a substitution for a fixed depletion, like 33 1/3 per cent, and if the first part of their theory is correct that they should allow it for mine and mill expansion, to which they limit it, then they should allow it completely; but they refer it to one and not to the other.

The other point is that in these mines that are brought out there are many expenditures which are not included, like expenditures for social services or for railroads which are off the property but which nevertheless have to be built. These expenditures are for things that are part of the risk, danger and expense of bringing a mine into production.

The Chairman: There are three elements, really: the capital cost allowance, which is more general in its application; accelerated depreciation; and earned depletion. Those are the three phases of entitlement to new mines and major expansions of existing mines. The mix may not suit very well.

Mr. Finlay: Well, the first two are items which ordinarily you get in due course anyhow.

The Chairman: Except that you may get accelerated depreciation and you may get capital cost allowances, but you may find that in some instances those expenditures do not qualify for earned depletion.

Mr. Finlay: That is right. That is why I say that the first two may be and are quite good for the mining industry. It is always nice to get your money back as fast as you can, dealing with the question of accelerated depreciation. Nevertheless, when you come down to the basic principle of earned depletion, it is not fair to eliminate a great number of items that, in my opinion, are part of the category that should be included in earned depletion. I think that is the basis of the Noranda contention; the earned depletion only went so far. I believe that they understood that the generalities—and I do not know how direct the statements were—were to include these other items to which I have referred.

The Chairman: If the purpose is to encourage exploration and development, it is difficult to understand why there is a limitation. There is a limitation even in time. If your development goes along at a certain rate and then certain things are contracted for, et cetera, before the mine comes into production, you then qualify. If, however, there are delays in delivery of machinery and equipment so that the mine is actually in production, then you lose your entitlement.

Mr. Finlay: Yes.

The Chairman: As an observer with some experience, it strikes me that that is defeating the purpose for which it was originally intended. It certainly is not under the new rulings putting mining companies in the position where they can get back all their money, as the minister said, almost as fast as they spend it. If you put time limitations in and if you deal with it at certain times, fine, you get it. If there are delays—and delays may not be controllable either—you do not qualify.

Senator Molson: Mr. Chairman, as I recall it, when you get to the 60 per cent rate of production you are in. After

that, if there are any deliveries delayed you get no benefit whatsoever.

The Chairman: That is right.

Mr. Fairley: Mr. Chairman, I have tried to pull all of this together in general terms—and it has to be in general terms, because I have not gone into all the details of all the testimony. Speaking of general terms, the first statement of the Minister of Finance which you referred to was quite general, as to what would be allowed as a base for depletion. The second statement was much more specific. It was a disappointment to almost everybody in the mining industry.

Senator Benidickson: Are you referring to the 1970 statements, Mr. Fairley?

Mr. Fairley: I am saying that the last statement was somewhat more restrictive than the first statement.

The Chairman: The 1970 statement was in general, clear language. The 1971 statement is the one that contains the proposed regulations.

Senator Benidickson: That is a distinction I wish to get at. The 1970 statement referred to the White Paper, and the 1971 statement had to do with the regulations which might follow the new Income Tax Act.

Mr. Fairley: They were somewhat more restrictive in what would be allowed as a base for depletion than most of the mining companies had anticipated.

Senator Connolly: Mr. Fairley, what specific exclusions do you think are most damaging?

Mr. Fairley: I would refer that question to Mr. Finlay.

Mr. Finlay: The most damaging one, so far as anything we are associated with is concerned, would be the construction of railroads.

Senator Benidickson: I am not aware whether any official documents were issued to the press as a result of the federal-provincial finance ministers' meetings of the last two days, but the *Globe and Mail* this morning says that as a response, particularly to a request from the finance minister of Quebec, the federal Minister of Finance announced a concession yesterday that, for example, railroad construction expense from prior to the date of the issuing of the White Paper statement would be entitled to earn depletion. I repeat that I do not know what was officially given to the press yesterday at the conclusion of that meeting.

The Chairman: Of course, Senator Benidickson, that may suffer the same attrition as the 1970 statement suffered when we looked at the proposed regulations in 1971. Certainly, we can note it, but it is not in any very official form at the moment.

Senator Connolly: Mr. Chairman, may I pursue what I started a moment ago? I shall not be long. What about infrastructure? You did mention the construction of towns and town sites which included, of course, roads, sewers, water mains and that sort of thing. Is that a big factor?

Mr. Fairley: Yes, it is a factor, particulary in the opening of a brand new operation.

Senator Connolly: We have been told that the mining companies, after the announcement was made in the summer of 1970, at the instance of the provinces who were mainly concerned, originally thought that the cost of such infrastructure would in fact qualify for earned depletion, and then subsequently it was excluded and apparently is to be excluded in the regulations. Have the provinces complained about this refinement?

Mr. Fairley: I would not know what the provincial finance ministers or premiers may have done on this. I honestly do not know the answer to that. But certainly from the original statement that the Minister of Finance made, we felt that the infrastructure, housing, social services and this kind of thing, were included. It was our understanding originally that it was to be included as a base for depletion.

Senator Connolly: Is it not fair to assume that if they do not qualify—and here I do not know about your company, but I am speaking of mining companies generally faced with this kind of problem—they might very well find themselves rapping on the door of the provincial authorities for help in this area? Up to a certain point it may be necessary for a mining company to provide these social services that we talk about, which is more than a service really.

Mr. Fairley: It is a necessity.

Senator Connolly: But surely there is a public responsibility there too, particularly in respect of the province, so would it not be natural for companies to go to the province to ask for help as they do for roads?

Mr. Fairley: This is conceivable. It depends how it works out, of course, but it is conceivable.

Senator Connolly: It seems to me, Mr. Chairman, that the proposal to exclude them from the regulations so that they do not qualify for depletion will probably ultimately come back upon the federal authority's desk, perhaps not through the direct route of the mining companies complaining, but through the provincial authorities who may have to step in to the breech in some cases where, for example, a mine is more or less marginal and the provision of a two site might make the difference. It would then be back on the doorstep of the federal authorities. Why cannot these qualify for depletion?

Senator Benidickson: Mr. Chairman, that is why I made reference to the meetings of the finance ministers. Members will recall that a week or so ago, when we were hearing from members of the Canadian Mining Association, I asked a few questions with respect to the attitude of the provinces, and I think it could be surmised that I was hinting that as a result of representations from the mining industry, or by invitation of this committee, we should perhaps hear from the provincial governments as to their attitude to this tax bill and public press releases respecting prospective regulations thereunder, because there is certainly a dual responsibility in this field of natural resources. I still wonder if this committee should not make known, perhaps, that we would be glad to hear from interested provinces, just as we heard from them when we were examining the White Paper.

Senator Beaubien: Mr. Chairman, I should like to start on a new subject if this one is finished with. Mr. Fairley, if this bill were law now, what difference would it make in the taxes paid by Hollinger Mines Limited?

Mr. Fairley: Well, since Hollinger is a holding company, I should rather take Labrador Mining, for example, because that gets closer to the basis of the thing. Labrador Mining also has some income from sources other than royalties, and has some investment income and some dividend income.

Now, to answer your question, as of this minute, in 1971 our estimated earnings before taxes are going to be somehwere around $13.2 million, with estimated taxes of $4.1 million. The after-tax earnings will be somewhere around $9 million. On the basis of the new law, as we know it now, our taxes will be up $1.1 million and our earnings, instead of being $9.1 million, will be $8 million. Therefore, our taxes this year would be increased by about 25 per cent in one year. Those are more or less exact figures, but we are of course estimating what our earnings will be for the full year, since we do not yet know exactly what they will be.

On page 9 of our brief you will find an example which is really better because it sets the thing up purely on royalty income. This is not diluted or confused in any way with investment income or anything else like that. In that example, if a company was earning $5 million pre-1965 less all the prospectors', grubstake exemptions, and so forth, there would have been no tax on it at all; it was treated as a capital gain. So you would have had after-tax income of $5 million. This is the type of situation we had in mind when we made our deal with the Iron Ore Company back in the early 1950s. There was no tax on royalties, and that is why we made a royalty agreement with them. What we did, as is pointed out in this brief, is that we took royalties and then we took a small interest in the Iron Ore Company. If we had known this was coming of course, we would have foregone the royalties completely and taken everything we were going to take as a shareholder of the Iron Ore Company, because under the new law dividends will still be tax free.

So, we could say we made a mistake, and in fact we did make a mistake if this new law goes into effect. From the early 1950s until 1965 this worked fine and these were the conditions under which we operated, and for 10 or 12 years or so this is the way we operated. Then in the 1965 taxation year the situation changed; it was no longer considered a capital gain; but we still did get a non-operators' depletion allowance of 25 per cent. So, beginning after that period—and let us take, for example, the taxation year of 1970, which is before the White Paper came into effect, we would have had a $5 million income with a non-operative depletion allowance of $1,250,000 which would leave taxable income of $3,750,000. Then allowing for taxes and so forth, we would have ended up with a net income of $3 million instead of $5 million. Now, if the present law goes into effect as it is now worded, we will be subject to a full 49 per cent tax.

The Honourable Lazarus Phillips, Chief Counsel to the Committee: When you say, "if the present law goes into effect," Mr. Fairley, when do you mean?

Mr. Fairley: Right now, the first of the year.

Senator Beaubien: It is effective in 1976.

Mr. Fairley: It is fully effective in 1976, yes. Then our net income will be $2,550,000 or down about half-a-million dollars from what it is now, and down $2½ million from what it was when we originally made our deal. So, without our doing anything one way or the other, good, bad or indifferent, the income of this hypothetical company, which earned $5 million a year, has been cut in half.

The Chairman: Is it possible to re-write your deal?

Mr. Fairley: As I have said in my statement, it is not practical. I will not say it is impossible to re-write it, because you can always re-write a deal. But all our partners and shareholders know the tax situation we are in; and we are in an untenable bargaining position. So we cannot re-write our deal on any kind of practical basis and end up with as much—

Hon. Mr. Phillips: We must consider this from the point of view of making a recommendation which would be simply administrative in nature. We are dealing with a grievous royalty situation. We will come to the abatement problem later, but if we can deal for a moment with the royalty problem; suppose royalties received on agreements entered into prior to the White Paper were deemed to be dividend income, you would, of course, be very happy.

Mr. Fairley: Yes, sir.

Hon. Mr. Phillips: If these royalties received were deemed to be capital gains which were taxable at the 50 per cent rate, would that bring the essential relief which you are seeking without the necessity of seriously restructuring the proposed act?

Mr. Fairley: Yes, sir, give or take a little, it would just about bring the necessary relief.

Senator Connolly: Would Mr. Phillips repeat that, please?

Hon. Mr. Phillips: We must be careful, because we have been dealing with operating mining companies and we must now redirect our minds to this particular brief which deals with a serious problem for exploration companies. In this particular instance, the two basic problems of grave concern to this company are the royalty, which at one time was non-taxable, and the abatement with respect to the provinces, which are contemplated by the proposed new bill.

Confining myself at the present moment to the royalty problem, we took the position on the White Paper that special consideration be given to cases where royalty agreements were entered into prior to the submission of the White Paper. Since that time we have a capital gains tax on our hands. Hollinger Mines Limited are speaking on behalf of operating companies who have royalty moneys coming in from pre-White Paper agreements.

I put the question to Mr. Fairley, and through him to Mr. Finlay, that within the framework of the present law, on the assumption we felt they had a proper case, a solution might be to recommend that royalty income to which an exploration company is entitled, identifying the type of

company, be deemed to be exempt income. That would be a real Christmas gift.

Mr. Fairley: That is one we would like very much.

Hon. Mr. Phillips: Yes, I know, that would be delightful—or, alternatively, that exempt income deemed to be capital gains income would be taxable only to the extent of 50 per cent of the royalties received. I am told by Mr. Fairley that dollar-wise that would essentially give them what they ought to be getting. But you would use the simple formula to bring this about.

Mr. Fairley: Perhaps Mr. Finlay would like to say something further.

Mr. Finlay: The problem with the royalty situation, when you look at it from the ambit of the whole field, is not quite as simple. Dealing with our individual case, while all our agreements preceded 1969, the fact remains that when we look at the wording of your previous recommendation we are not quite certain where we stand. With this $300 million expansion of the Iron Ore Company of Canada we had to make certain concessions with respect to those royalty agreements. They are still considered royalty agreements, but we had to give up additional ore. In the north there was not enough ore to warrant the type of expansion we had done there. We had reserved one-third of that ore, but we had not used it since 1959. That was for a period of three years, and it was not salable. Our agreement dates back from 1951 to 1954 and during that time they have made certain amendments; and one of the amendments was that we had to give additional ore to support this complex which is now being built. There are certain other minor adjustments.

Hon. Mr. Phillips: When you speak of royalty agreements being regarded as exempt income or, alternatively, capital gains income, we do not restrict it to arrangements made prior to the introduction of the White Paper?

Mr. Finlay: Yes, as far as we are concerned.

Hon. Mr. Phillips: Does that cover the point you are making now?

Mr. Finlay: Yes, in respect to dividends, the White Paper originally said that all dividends from Iron Ore Company of Canada to Hollinger Mines Limited were fully taxable. Then Mr. Benson came along and added the words "any company incorporated after 1971." Dealing with the royalty situation, it would seem to me it would have to be after the passing of the bill.

Hon. Mr. Phillips: Let me ask you this question. I am not sufficiently knowledgeable in this area. If you were to get exempt income or, alternatively, capital gains treatment, would you be in a better position than operating companies in the mining industry generally? It is one thing to grant relief and quite another to get an advantage over the operating companies.

Mr. Finlay: I might answer that by saying that historically an exploration company starts with no income and spends all of its money trying to discover something. They have always been in a better position than operating companies. Unless there is some encouragement given, there will never be other exploration companies like Hollinger Mines Limited.

Hon. Mr. Phillips: That is a very helpful answer.

Mr. Fairley: To go one step further: yes, if our royalties were considered tax-exempt as dividends, then we would be better off. However, if they were considered to be capital gains, on which we would pay tax, we would be in just about the same position as the operating company, depending on the company, of course.

Mr. Finlay: They were treated as capital gains prior to 1965.

Hon. Mr. Phillips: Yes, I know; capital gains, but no tax.

Mr. Finlay: Yes.

Senator Hays: Mr. Fairley, I am not very knowledgeable in the mining field, but if your firm were in the United States rather than Canada, with the arithmetic that you have projected would you experience a disadvantage or an advantage?

Mr. Fairley: It would be a very large advantage, very large.

Senator Hays: Have you projected it in dollars?

Mr. Fairley: Yes, I can elaborate on that. Here, even under the present law, we only receive 25 per cent of our profits as depletion allowance. In the United States at the present time, depending on the mineral produced, the allowance is anywhere from 10 to 15 per cent of the gross amount of income, or 50 per cent of profits. Although the lesser figure applies, in 90 per cent of the cases the 50 per cent of profits is the governing figure.

The present law provides for 25 per cent in the case of non-operating and 33 per cent in the case of operating companies, as opposed to 50 per cent in the United States. Under the present law the depletion allowance is going completely by the board. We have to earn whatever depletion we can by taking it on the new money we spend, for which we get one-third of every dollar.

One the basis of depletion, the American law is even today far superior to that of Canada from the standpoint of the mining company. Under the new law it will be eminently more superior than it is today.

You may ask why, if the American law today is so much better than that of Canada, are we in Canadian mines, which is a perfectly logical question. However, the answer is that under the present Canadian law, before the White Paper was introduced, in addition to the 25 or 33 per cent automatic depletion, we had other advantages which the United States does not give such as the three-year exemption on a new mine, which was a great advantage.

The average mining company in Canada under the present law, before the White Paper, in comparison with its counterpart in the United States paid an almost similar tax.

The Chairman: The loss of the tax holiday and automatic depletion will change that.

Mr. Fairley: We will be in a very much poorer position than the equivalent American mining company.

Senator Hays: Have you made a comparison between the United States and Canada in relation to your projection of earnings and tax? I am referring to your figure of $2-½ million, and so on.

Mr. Fairley: I have not done it for the purpose of this brief. We have calculated it many times in specific cases. In the case of $5 million income, 50 per cent being depletion, there would be $2.5 million depletion and tax would be paid only on the $2.5 million, which would cut us well below what we have today in this theoretical case. We will no longer have the three-year exemption and other considerations, which are very important.

Senator Hays: Is it very difficult to project a set of figures to apply exactly to the situation in the United States and to that which will occur new bill?

It would be helpful for this committee to have figures which would illustrate the disadvantages our mining industry faces in comparison with that of the United States.

Mr. Fairley: Yes.

The Chairman: We are pressed for time and would like to receive these figures as soon as possible.

Mr. Fairley: We could do it probably this afternoon and send them up to you. It will be a hypothesis, of course, but we will calculate on the basis of the same income in each case.

The Chairman: For what period would you like the comparison made, Senator Hays? Before and after?

Senator Hays: Before 1965, from 1965 on and under the new bill.

Mr. Fairley: Three periods: before 1965; 1965 to the White Paper; and post-White Paper?

Mr. Hays: Yes.

Mr. Fairley: Then post-1976, of course.

Mr. Finlay: Post-1976 is the important one.

The Chairman: You will have to speculate as to what the allowances and rates will be in the United States.

Mr. Fairley: That is right; we can only calculate on the basis of the present rates and allowances in the United States.

The Chairman: Mr. Finlay, is it possible, under your royalty agreements, that the royalty payments might be regarded as instalment payments for making available certain ore bodies—in other words, the sale of ore?

Mr. Finlay: That has not been possible under our law since 1965.

The Chairman: Disregarding the law, because perhaps the law could be changed more easily than your agreements.

Mr. Finlay: I am sure that we are at a great disadvantage in attempting to change our agreements. I do not like to use the word "force", because everything we do to expand ultimately helps us. However, we had to give up certain rights subsequent to the White Paper, which has altered our royalty agreements.

Senator Connolly: Contractual rights?

Mr. Finlay: Yes. We had to give them up in order to make this expansion possible. A great deal more ore will be used, and it was insisted that certain tonnages be included in the royalty agreements. You will understand that with expansion from 19 million or 20 million to 32 million a great deal more ore must be provided. However, basically our agreements were not changed. Tonnages were changed and the computation was altered to keep up with the times. These changes provided for royalties on pellets, as contrasted to natural ore. When we entered into these agreements there was only royalty on natural ore; there were no such things as pellets. Some time ago they applied with respect to concentrates, then pellets became the main factor.

If any of those changes were made, as far as anyone could estimate it would leave us in the same position, or worse.

The Chairman: Mr. Finlay, have you any language to suggest which would relieve the situation with respect to the matter of royalties as far as you are concerned?

Hon. Mr. Phillips: Lawyers always bear the burden.

Mr. Finlay: The first thing which occurs to me, which is not a good solution for the future, is that it should be the same as dividends, as in 1971 rather than when the White Paper was introduced.

Hon. Mr. Phillips: Or, alternatively, capital gains tax.

Mr. Finlay: Yes. From what I know of it, in the long run I would think that the capital gains would be the easiest one to write. The problem then becomes: When would that come into effect?

Mr. Fairley: I think Mr. Finlay has answered the question. If we are not going to get the royalties handled as capital gain, we would like to have them handled like your committee recommended in the White Paper, except make the effective date not the date of the White Paper but the effective date of the law.

Hon. Mr. Phillips: Would you not have to include the amendments that were made to existing agreements since they are not referred to in that White Paper report?

Mr. Fairley: That is right.

Senator Connolly: Mr. Fairley indicated that in the proposed new bill the tax that the company pays will be substantially higher than it is under the existing law.

Assuming that the Government wants to obtain as much revenue as possible, I suppose the change has been made to increase revenue. If you were operating entirely in Canada, and if the markets for the product that we are concerned with are entirely in Canada, it might not matter

very much. But how much are you depending upon foreign markets, and how much foreign competition are you subject to?

Mr. Fairley: In the case of the iron ore operations which we are talking about, we export something better than 90 per cent of everything that we make, and we will continue to do so. We have at times a maximum of three customers in Canada, and at times we have only one. It varies from year to year. We have never gone below the figure of 90 per cent for exports, and as we go into the future the figure will probably go up, because with our new expansion virtually every ton of ore that we produce will be exported all over the world.

Senator Connolly: Will you be subject to competition that arises from companies operating under more beneficial laws?

Mr. Fairley: Yes, sir, we certainly will. That is a very important point, because there is no shortage of iron ore in the world. Also, there is no shortage of iron ore productive capacity. Right now the mines that are in operation in the world can produce millions of tons more ore every year than they can sell. Of course, this has a depressing effect on the price. Therefore, we are competing with those operators.

Our biggest tonnage moves to the United States, where we are competing mainly with American mines operating in the Lake Superior region. With the ore that we are shipping to sea-coast steel plants in the United States, we are competing with foreign ore producers in Africa, Australia, South America, and many others. With the ore that we ship to Europe—and it is substantial, since we ship to Holland, Belgium, Germany, all of the British Isles, France, Spain and Italy—we are competing directly with local ore industries; and in the case of France that is quite substantial. They produce a large amount of ore in the Alsace-Lorraine region.

Senator Connolly: Under more beneficial tax laws?

Mr. Fairley: Equally as beneficial, and probably more so. But in their case they are right next to the steel plants, and we have to ship the ore nearly 4,000 miles.

With ores which we ship to Japan, we are under very heavy competition from Australia, India and South Africa. Therefore, to answer your question, the great majority of our ore is exported—at least 90 per cent of it, and probably more in most years. We are under very heavy competitive pressure from all producers in the rest of the world.

Senator Connolly: Would you say that the law of diminishing returns could be set up in respect of the tax-take from a company like yours?

Mr. Fairley: It is possible. It makes it less attractive as you go on into the future. The Iron Ore Company of Canada has been well run and is highly successful. One problem is that many of our major customers—and well over 50 per cent of the ore moves to the American steel industry—are partners in the Iron Ore Company of Canada. They have big operations, which they either own or in which they are partners, in the Lake Superior region. So they can go either way to supply their mills; they can expand in Canada or in the United States.

The Chairman: Referring to Hollinger, which is a holding company, and with particular reference to its royalty income, let us look at the direction in which you would apply that money. You would, of course, pay dividends. What about exploration and development? Is some of that royalty income used by Hollinger directly or indirectly for exploration and development?

Mr. Fairley: Yes, sir. About 10 per cent of our net tax income every year is used for exploration; that is, for completely new exploration. It is not development of something which we already have, but it is spent on looking for new mineral deposits. Over the last many years we have spent every bit of this money in Canada, with the exception that in one or two years we spent a little in Ireland.

Senator Connolly: Good for you.

Mr. Fairley: Canada has been good to us, and we think that this country represents just as good an opportunity as any other. Therefore, we have stuck with it. However, if this law comes into effect in its present form, I can assure you that the percentage of exploration in mining which we undertake in Canada will be cut substantially, and the money will be spent in a number of other places, including the United States and Australia. That should answer your question.

The Chairman: Yes; but to the extent that you expend earnings on exploration and development, you do get a write-off, do you not?

Mr. Fairley: That is right.

The Chairman: If you spent 10 per cent of your net royalty income on exploration and development, what part of that would you recover in allowances?

Mr. Fairley: That would depend on what the new law says.

Mr. Finlay: We would be in the same position as we are now.

The Chairman: You would get $1 for every $3 that you spent.

Mr. Finlay: Yes. Let us take a company that has $9 million. Under the present law they would get a $3 million exemption.

The Chairman: I am trying to keep away from operations. I am looking at Hollinger, the holding company, which receives a royalty income.

Mr. Finlay: The money that Hollinger expends, since it does not have any taxable income, goes down the drain. It is no good to us at all. The result is that we have tried to concentrate our exploration work in the two subsidiaries that have royalty income. If they had $9 million-worth of royalty income and spent 10 per cent, which would be $900,000, then you would get $300,000 of non-taxable income.

The Chairman: The answer to my first question, then, may have to be revised. I suggested that Hollinger, the holding company, has royalty income. Is that right?

Mr. Finaly: No.

The Chairman: When you speak of 10 per cent of the net income from royalties you are not talking about Hollinger, the holding company?

Mr. Finlay: It is just a holding company.

The Chairman: Therefore, the only type of income that Hollinger, the holding company, would have would be dividend income. Is that right?

Mr. Finlay: Dividend income and interest income.

The Chairman: In that event the right to write off something would not benefit you because you would not have taxable income against which to use it up.

Mr. Finlay: Yes, and that is why we try to concentrate as much of our exploration as we can in the two subsidiaries.

The Chairman: What, then, are you proposing to us? It would appear that you are asking us to do nothing in relation to Hollinger Mines Limited.

Mr. Finlay: That is right.

The Chairman: Your representations are in relation to Labrador Mining and Exploration Company Limited and Hollinger North Shore.

Mr. Finlay: Yes, with one qualification, and that is to the extent that if, at some time in the future, Hollinger Mines Limited decide to use some of its money, which it has been doing, to form another exploration company or something. We cannot see any point in it. We have two such companies at the present time, and these two companies have no other income except the royalties from the results of their explorations. They are not operating companies. That is where we are really looking for relief right now.

Hon. Mr. Phillips: If you have consolidation in the future, that would more or less answer the Chairman's question.

Mr. Finlay: Yes, but how are you going to consolidate the Labrador Mining and Exploration Company Limited, based in Quebec, and Hollinger North Shore Mining, based in Ontario?

Hon. Mr. Phillips: Well, you have a common sense approach to it.

Senator Beaubien: In so far as Hollinger Mines Limited is concerned, there is not much change in its tax situation as a result of Bill C-259, is that right?

Mr. Finlay: I would just like to say something by way of explanation. The schedule which is attached to this brief was written when integration was before us. I think it presents the picture fairly fully.

In regard to Hollinger itself, we were in serious trouble under the White Paper, but they have now made dividend income from iron ore flowing to us from a company incorporated prior to 1971 tax exempt. Any company incorporated outside Canada after 1971 will be in serious difficulty.

The result is that any royalties from the two subsidiaries will eventually flow tax free because the only way Hollinger North Shore Mining and Labrador Mining and Exploration Company Limited can get money into Hollinger Mines Limited is to declare dividends and those dividends are tax free, as well as dividends from our other share investments, so Hollinger has no taxable income.

Senator Beaubien: And no problem with respect to Bill C-259?

Mr. Finlay: No, except we are going to be in the mining business in the future.

Mr. Fairley: I might say that Hollinger does have one small operation; it is just a stand-off coal mine and it does not make any money, but at least to that extent we do come under this new situation.

The Chairman: I repeat my question again, then, Mr. Fairley: In the light of this development in the evidence—and we will put Hollinger aside for the moment, because it is not really affected in any substantial way by what Bill C-259 says—anything that we might consider doing should be in the direction of Labrador Mining and Hollinger North Shore?

Mr. Fairley Yes.

The Chairman: So what type of language do you suggest would give relief in that area?

Mr. Finlay: What we are saying is with relation to all agreements entered into prior to 1972. In other words, down to the end of 1971.

The Chairman: That was the burden of our report, was it not?

Mr. Finlay: Yes, that is exactly what your recommendation was, Mr. Chairman, except you had 1969.

Hon. Mr. Phillips: And inclusive of amendments thereto.

Mr. Finlay: Yes, inclusive of amendments thereto. Then the other one which has been suggested by your committee, Mr. Chairman, was the question of capital gains. This has a lot of merit, but when you look at it historically, the country did treat those as capital gains up until 1965, and then they were treated as income with a depreciable allowance; but they have never been treated as production income, using the word "production" in the way it is used in this bill.

The Chairman: What you are saying is that if you go back along the chain to the source of this income, its source is production?

Mr. Fairley: That is right.

The Chairman: And then it flows out?

Mr. Finlay: Yes.

Senator Carter: Could I ask a question concerning these royalties, Mr. Chairman?

The Chairman: Yes.

Senator Carter: Are these royalties computed on a common, uniform basis, or do you have different rates for ore concentrates as opposed to, say, processed ore?

Mr. Fairley: They are slightly different. It is a rather complicated formula, but basically they are figured on the basis of the market value of the material loaded into the boats at Seven Islands, Quebec. Regarding what we call direct shipping ore—which is ore that you just take out, crush, screen and ship—7 per cent of the value of it at Seven Islands is the royalty. Regarding concentrates—which is ore we dig out, grind down and concentrate, which is 2.2 tons for every ton of concentrate—that also is 7 per cent of the market value of the ore loaded into the boats at Seven Islands. Pallets, which are a much higher grade product and much more costly, carry a higher price. The royalty is 5 per cent on the market value of the pallets loaded into the boat at Seven Islands.

Senator Carter: Senator Connolly made the point earlier that one of the objectives of Bill C-259 was to encourage revenue, and perhaps to make the mining industry carry a larger share than previously, but I am under the impression that a second objective might be to encourage processing.

Is there anything in Bill C-259 to encourage processing? Are there any incentives towards greater processing or a higher degree of processing of minerals?

Mr. Fairley: I cannot see very much.

Can you, Mr. Finlay?

Mr. Finlay: No, I cannot.

Mr. Fairley: The only thing along those lines might be, when this bill is finally worked out, if they allow processing plants as part of the base for depletion. That would make it look a little better. You would consider processing, but basically the thing that determines processing is the markets around the world—what can we sell?

We have processing and we have steadily increased the amount of processing we are doing in Canada since we started. The first ore we shipped out in 1954 was raw ore. When we finish this present program, there will probably only be three or four tons of raw ore shipped out of a total of 30-odd million tons shipped. We went to processing because we had to meet the markets.

Senator Carter: Is there anything in the bill that would encourage fabrication?

Mr. Fairley: Not to my knowledge.

Mr. Finlay: One thing that must be remembered with respect to fabrication is that this company, alone, with its expansion will produce practically three times the ore that is consumed in Canada, regardless of all the other iron ore companies in Canada. There is just no market except by shipping it out. There is a 10-million or 12-million ton market; it depends whether you are talking about pellets or raw ore, but there is a market. I remember in 1954, when we made these first contracts, Canadian consumption was about four million tons.

The Chairman: Do you regard the production of pellets as being a processing operation?

Mr. Fairley: Yes.

The Chairman: Under the regulations that are supposed to come in under this bill, if the present equipment, plant and so on qualified for earned depletion—and we have had many submissions indicating some restrictions that are difficult to understand, but I will not develop that at the moment—assuming the processing plant and the money spent on that would qualify for earned depletion, the company spending that money would have income that would otherwise be taxable, against which you could write that off?

Mr. Fairley: Yes.

The Chairman: That would be a benefit, and a substantial benefit.

Mr. Fairley: Very much so.

The Chairman: The problem in the example I like to use, which we got the other day, to show how far astray some of these proposed regulations have gone, is this. If I had three small mines in an area some distance apart, having good readily marketable ore, but not in substantial quantities, by constructing a smelter at each mine before it came into production I could earn depletion. The difficulty would be that there would not be enough income, because the smelter costs would be so great. However, if I decided to do custom smelting and located a smelter in an area where it could be fed into from these three mines, I would not be entitled to earned depletion under the proposed regulations.

Mr. Fairley: That is right.

The Chairman: That just does not add up. It makes one wonder what is the purpose of earned depletion if it is not to encourage more production as economically as possible.

Hon. Mr. Phillips: You get depletion in one sense, as the chairman puts it, and you have no income. If you have your income, you get no depletion.

The Chairman: It depends which way you wheel your toe, I guess. Your second point is the abatement. Your difficulty there is that taxable production profits are defined in the regulations as being an amount that would be determined under the basis of the automatic depletion.

Mr. Finlay: That is 33 1/3 per cent.

The Chairman: Now you are not entitled to that as non-operators; you are not entitled presently to that 33 1/3 per cent, and your limitation would be 25 per cent.

Mr. Fairley: That is it.

The Chairman: If this is an obstacle to you, what do you suggest?

Mr. Finlay: The federal 15 per cent, which is the reduction from some 40 to 25, was intended to say to the provinces, "You do what you like." Maybe the theory was that they were presently being allowed by Ottawa to deduct 10

per cent, but they were credited that. The bank was charging 12 per cent; the foundry was charging 13 per cent on those rates. We do not know where they will go.

The Chairman: Just let us stay in the federal field and address ourselves to the abatement proposed under the present legislation. That is 15 per cent. What language would we have to use in order that you might get the benefit of that?

Mr. Finlay: Let us take the 25 per cent as well as the 33 1/3 per cent.

Mr. Fairley: We would like to be included in not just, say, the operating companies; we would like to have the 25 per cent. We would like to have an abatement on our 25 per cent depletion.

The Chairman: So if we add "and in the case of non-operators", this calculation would be on the basis of 25 per cent.

Mr. Fairley: That is exactly right.

The Chairman: I think we understand the problem. Those are the two points you have?

Mr. Fairley: Yes, sir.

The Chairman: Are there any other questions senators wish to ask?

Senator Carter: I would like to put forward an idea. I am not very well versed in the operation of mining companies, but we seem to have a general objective of increasing employment in Canada. Some people have said that perhaps the mining companies are not doing as much as they could in this respect. What kind of incentives would the mining industry require to encourage increased employment rather than, say, increasing dollars earned?

Mr. Fairley: I think I would have to answer that in broad, general terms. The incentives under the present tax laws are quite good, and they have resulted in a massive increase in production and employment in the mining industry since World War II. Those incentives were prospectors' allowances, automatic depletion, percentage depletion, and the three-year exemption. Those three incentives have been most successful. We would like to see the present law continue for the mining industry, as we have said over and over again. However, the Minister of Finance and the Government have indicated that they are going to make certain changes. Any changes they make which reduce the attractiveness of the mining industry in Canada will tend to slow it down rather than speed it up. The proposed law reduces the attractiveness of the mining industry, compared with the present law, so we would be very happy if you keep the law you presently have.

The Chairman: It reduces the attractiveness in Canada for non-resident investors?

Mr. Fairley: Compared with other places.

The Chairman: And non-resident capital.

Mr. Fairley: Yes.

The Chairman: And it makes the road a little heavier in the export market?

Mr. Fairley: That is right.

Mr. Finlay: I would like to say a few words on employment. In the past year we have heard a number of speeches to the effect that the mining industry's employment is not what it should be. There is no point in hiring people you have no use for. I want to draw your attention to how much indirect employment comes from mining through all the supplies and services. Let us consider the iron ore project we have referred to with a 360-mile railroad into the wilderness and all the services and buildings that go with it. The town of Seven Islands, with 15,000 people, has grown up; there is another one half that size or more at Labrador City; another one of about 5,000 or 6,000, Schefferville. Millions of dollars are spent indirectly on employment.

The Chairman: From the two companies for which you are speaking, what would you say would be the sum total of direct employment?

Mr. Fairley: It would be very small. You mean Labrador North Shore?

The Chairman: Yes.

Mr. Fairley: We just have very highly trained exploration crews, who are highly trained experts, geologists and engineers, and we probably would not be employing more than 60 or 70 men. The Iron Ore Company would probably employ 5,000 or 6,000.

The Chairman: We were told the other day by one of the mining companies that, for indirect employment, it takes at least six people to service one employee working in the mines.

Mr. Fairley: That is right; and by the time you consider all of them, about 12 per cent of the working population of Canada is employed, in one way or another, serving the mining industry.

Senator Connolly: Of the entire working force of Canada?

Mr. Fairley: In one way or another. That includes the secondary employees who are building trucks, shovels, railroads, houses.

Senator Connolly: They would not have employment if there were no mining industry?

Mr. Fairley: That is it. Well, excuse me. In all honesty, I would not say quite that, because a company that is building trucks for the mining industry also builds trucks for construction, so they would have some employment there. I would not wish to give a false impression.

Senator Molson: The Iron Ore Company is incorporated in the United States, in Delaware, is that right?

Mr. Fairley: Yes.

Senator Molson: Is it the owner of any of the properties, or are they vested in Labrador Mining, North Shore, and so on?

Mr. Fairley: The mineral properties are all vested in Labrador Mining and North Shore, and they are leased to the Iron Ore Company of Canada.

Senator Molson: What about the pelletising plants and railroads?

Mr. Fairley: Those are owned by the Iron Ore Company or by subsidiaries of the Iron Ore Company. The railroad is a subsidiary. It is a common carrier.

Senator Molson: But these other facilities, grading and so on, are owned by Iron Ore?

Mr. Fairley: That is right.

Senator Molson: Why was it incorporated in Delaware? There must have been a very good reason.

Mr. Fairley: There was a very good reason. Mr. Finlay will explain it.

Mr. Finlay: This was the subject of a number of amendments to the reciprocal arrangements between Canada and the United States of 1951 or 1952. The Americans would not put their money in here unless they got certain arrangements at that time. One of them was that they have an American company, because when dividends go from the Iron Ore Company to their corporate shareholders they are only taxed on the full tax rate on 15 per cent of their income, or roughly 7½ per cent.

Mr. Fairley: When they divide the dividends between American companies, it is taxed at 7½ per cent.

Mr. Finlay: It is a tax rate on 15 per cent. Nevertheless that would be an entirely different situation as far as Canadian dividends to American companies are concerned.

The Chairman: You have the 15 per cent withholding tax?

Mr. Finlay: Yes.

Mr. Fairley: Let me just put this in a few words, Senator Molson. The Americans own the major part of the Iron Ore Company. They have put up most of the money and have taken most of the ore too, by the way, which is the most important part of it, as they are the customer. They would not go into this unless the Iron Ore Company were an American company so that they could get a tax advantage to them on dividends. We, being the only Canadian owners of this company—that is, Hollinger Mines and Labrador Mining—we could not have it as an American company because we got caught up here in the same way, working the other way. So what the Government did, with Mr. Finlay, Mr. Howe, and a whole lot of other people, working on it—

Senator Connolly: And Mr. Humphries.

Mr. Fairley: Yes, he was very much in on it.

Senator Connolly: Mr. Abbott the Minister of Finance.

Mr. Finlay: It was long after that.

Mr. Fairley: They said, "You set up the Iron Ore Company of Canada and make it an American company, but we, in turn,"—and this was all put into the tax treaty, by the way, between the two countries—"we, in turn, in order to make Hollinger and Labrador Mining whole, will, for dividend purposes, consider the Iron Ore Company of Canada a Canadian company, provided it operates only in Canada and provided it pays all of its taxes in Canada."

It has always done this. Even when the Iron Ore Company has short-term investments—six months, or something like that—even though it may be earned in the United States, taxes are paid on it in Canada.

The Chairman: Mr. Fairley, it seems that if, as a matter of law, you can deem an American-owned company to be a Canadian company for certain purposes, it would not be stretching your imagination too far to deem that royalty payments are capital.

Mr. Finlay: It would stretch my imagination.

Senator Connolly: There are other "deems" in the bill, too.

The Chairman: Thank you, Mr. Fairley.

Mr. Fairley: Thank you, gentlemen.

The Chairman: Honourable senators, the next submission is from the Canadian Life Insurance Association. Appearing for the Canadian Life Insurance Association is Mr. Lemmon, the president of the Canada Life Assurance Company.

Mr. J. A. Tuck, Managing Director, The Canadian Life Insurance Association: Mr. Chairman and honourable senators, the president of the association this year is Mr. Hicks, the president of Sun Life Assurance Company of Canada. He asked me to express his regret that a prior engagement has kept him away. Another officer of the association, Mr. Hervé Belzile, president of Alliance Mutual Life Insurance Company, also its immediate past president, is here. We have also with us: Mr. A. H. Lemmon, president of The Canada Life Assurance Company; Mr. T. M. Galt, vice-president, Sun Life Assurance Company; Mr. F. Kimantas, the tax officer; and myself.

The Chairman: And, of course, we all know Mr. Tuck.

Mr. Hervé Belzile, Past President, The Canadian Life Insurance Association, and President, Alliance Mutual Life Insurance Company: Mr. Chairman and honourable senators, on behalf of our association, the Canadian Life Insurance Association, we wish to thank you for the opportunity to appear before this committee on the statutes in question.

We prepared a brief which was sent to the members of this committee, and I would ask a member of our taxation committee, Mr. Lemmon, who is president of Canada Life, to make the presentation and to make some comments to your committee.

Mr. A. H. Lemmon, Past President, The Canadian Life Insurance Association, and President, The Canada Life Assurance Company: Mr. Chairman and honourable senators, I beg the indulgence of this committee. This is really the third time that we have had the privilege of appearing before you.

The point we would like to discuss with you this morning was discussed on each of those previous occasions. About two years ago, in June 1969, we appeared before you to discuss the bill that was introduced in October, 1968, establishing new methods of taxing life insurance companies in Canada. This point was made at that time.

In June, 1970 we again appeared before this committee, subsequent to the publication of the White Paper. At that time it was proposed that a measure of integration be introduced into the income tax law of this country for the first time, which would have seriously aggravated the situation that we would like to discuss with you this morning. That proposal of integration was not proceeded with in the bill introduced this spring, but we are still backing substantially the position that we were in when we appeared a little over two years ago, when the life insurance bill was passed into law.

The matter we would like to discuss with you is the effect of that tax bill on the investment of life insurance companies in Canada in ordinary shares or common stocks in this country. We understand that it is, and has been for some years, Government policy to encourage individuals and Canadian institutions to invest to a greater extent in common stocks in this country, to retain control of some of our major companies in this country and, generally, to provide more equity capital. We suggest, Mr. Chairman, that because of the way in which the Income Tax Act works with regard to Canadian life insurance it does not encourage the investment of those companies' income in stocks, but in fact discourages it.

Prior to the Income Tax Act being introduced in October, 1968, life insurance companies did enjoy a measure of tax advantage. This tax advantage was substantially eliminated by the tax bill of 1969. As a matter of fact, in this particular area, and perhaps in one other area, it has gone over to the other side, to the extent of discriminating against the life insurance industry.

When Mr. Benson appeared before this committee in June, 1969, he recognized that the treatment of common stock dividends in, at that time, the proposed life insurance taxation was different than for other financial institutions such as banks and trust companies. He justified it on the ground that the amount of stocks owned by such banks and trust companies was so small that it did not really make any difference to them. He stated an odd position that, if it did get big enough to make any difference, he would remove the incentive that there was for them to invest in common stocks. This appeared to us a little odd when we believed, and had been led to believe, that it was the object of the Government to encourage investment in Canadian common stocks.

We have carried on negotiations with the officials of the tax department, the Department of National Revenue and the Department of Finance over that period. We have never received a flat turn-down on this particular point. On the other hand, nothing has been done. Certainly, in the bill that has been proposed, or in the amendments that we have seen so far, nothing has been done to correct what we believe is unfair discrimination against life insurance companies investing in common stocks in Canada.

If you like, Mr. Chairman, I would be glad to read the brief, but I believe it was furnished to all the members. I would just like to point out to the members of the committee that Appendix A shows that, in fact, because of the way this tax act works for life insurance companies, and additional $100, or an additional $100,000 or whatever figure you like to take, of dividend income added to the business income of a life insurance company attracts tax of the order of 34 per cent. This is much greater than in the hands of an individual, and, in fact, it attracts no tax in the hands of a bank or trust company. These small institutions happen to be the ones with whom we compete, which makes life a little difficult.

Hon. Mr. Phillips: May I put a question, Mr. Chairman?

The Chairman: Yes.

Hon. Mr. Phillips: Have you collated the sections of the bill which have a direct bearing on the subject matter you are about to discuss, and have you related those sections to the Insurance Act of 1969, so that in the study of this particular question that you are about to go into we could look at the sections of this bill as well as those of the 1969 act?

Mr. Lemmon: I am not sure exactly what you mean, sir. This is not referred to in the new bill at all.

Hon. Mr. Phillips: So you are complaining about your treatment in the 1969 bill.

Mr. Lemmon: That is right.

Hon. Mr. Phillips: And that you are not getting relief under the new bill.

Mr. Lemmon: That is it exactly.

Hon. Mr. Phillips: So it is a negative of my affirmative. What are the sections in the new bill which do not give you the exemptions that are given to others?

Mr. Lemmon: I do not think I can quite answer that question in a direct manner, sir. I feel another section would have to be added to the bill to change the 1969 act.

Hon. Mr. Phillips: Then we have clarified the situation. You are complaining that you do not have affirmative relief in the proposed act.

Mr. Lemmon: That is right.

Hon. Mr. Phillips: You are not complaining of any sections in the proposed act that hurt you.

Mr. Lemmon: We are not, sir.

Hon. Mr. Phillips: On the other hand, you want relief in the proposed act to tie in with your 1969 bill?

Mr. Lemmon: That is right, sir.

The Chairman: Do you want relief because other corporations are getting relief in this bill or because they have always had it?

Mr. Lemmon: Because they have always had it, sir.

The Chairman: That is the question.

Senator Connolly: I take it that the provisions of the 1969 act are repeated in this bill.

Mr. Lemmon: They are carried forward.

Senator Connolly: They are carried forward into the new bill?

Mr. Lemmon: Yes. There is no change arising out of the new bill at all.

Senator Connolly: Quite so. Just for the sake of the record at this point, could you identify the sections?

Mr. F. Kimantas, Tax Officer, The Canadian Life Insurance Association: Yes, sir. In the new bill it is section 138(6). In the present act it is section 68A(6).

Senator Connolly: Is that section 68A(6) of the Income Tax Act as amended in 1969?

Mr. Lemmon: Yes.

The Chairman: Mr. Lemmon, what do you suggest would do what you think should be done?

Mr. Lemmon: To answer that I would have to explain fairly briefly how the act works.

The Chairman: All right.

Mr. Lemmon: When a Canadian life insurance company receives dividends on common shares, as is explained in Appendix B, that income, together with all other interest income is prorated between various sections of the company's activities.

The Chairman: That is internal practice.

Mr. Lemmon: No, this is by requirement of the Income Tax Act.

Senator Connolly: There is a formula in the act to prorate?

Mr. Lemmon: Yes.

Hon. Mr. Phillips: When you speak of "the" act, are you speaking of the Insurance Act?

Mr. Lemmon: I am referring to the amendments to the Income Tax Act that were passed in 1969 and carried forward into the proposed bill now.

Hon. Mr. Phillips: All right.

Mr. Lemmon: The first section that is mentioned in Appendix B is what is known as tax exempt policyholders. These are policyholders who own policies of life companies that are registered under the Department of National Revenue as retirement income vehicles. As such they accumulate interest without paying any tax.

Senator Connolly: In other words, the tax on the money that is in this fund is paid by the beneficiaries when they take their retirement.

Mr. Lemmon: Yes. It is accumulated. The payments that go into it are tax-exempt. The interest accumulation during the accumulation period is tax-exempt.

The Chairman: It is really a deferral.

Mr. Lemmon: Yes, it is a deferral. The taxation arises when the money is paid out.

The second section is known as the company funds. In the case of a mutual company, that is substantially the reserves that the company retains for whatever purposes it sees fit. The third section is the other policyholders. In the case of a mutual life insurance company this is substantially the participating policyholders of the company. Under the second section might also be considered the shareholders of a stock life insurance company, which are in the same position. The effect of allocating to the first section of policyholders a portion of the common stock dividends we receive means that we get no tax relief on those common stock dividends because there is no tax payable in that fund.

Senator Connolly: I am sorry, I just do not follow that. You are talking now about the tax-exempt policyholders?

Mr. Lemmon: We are talking about the tax-exempt policyholders. A certain portion of our common stock dividends are allocated by the Income Tax Department by formula and there should be a tax credit to the people in that fund, but since there is no tax payable, nobody gets it.

Senator Connolly: So you seek a tax credit for those payments?

Mr. Lemmon: No. We suggest that type of policy should be exempt from the prorating formula and that the common stocks owned by a life insurance company should be considered as being owned by the company or by the participating policyholders who can through dividends from the company benefit or otherwise from the common stock investments. In the first type we feel that these are very parallel to the so-called guaranteed funds of trust companies. Trust companies are required by law to segregate their assets and this group of assets, identifiable, is allocated to their guaranteed funds while the other group of assets, identifiable, is allocated as belonging to the company, and the trust companies in fact do not allocate any of their common stock investments to the guaranteed fund account, so that the problem does not arise with them. But the income tax law arbitrarily assigns some of the common stocks that the companies own into this fund where in fact no tax relief can be obtained.

Mr. Tuck: Is it right to say, Mr. Lemmon, that we mean that because of the tax deferral regarding Group I the benefit of the tax-free dividend procedure is lost?

Mr. Lemmon: It is lost.

Mr. Tuck: Therefore none of the company's dividend income should be regarded by the tax act as going in that direction, because if it is so regarded, there is a meaningless result.

Senator Beaubien: Are you saying really that if the company were left to its own devices, it would not buy any common stocks for that portion of the fund deemed to be belonging to tax-exempt policyholders?

Mr. Lemmon: When a life insurance company makes its investment decisions—and here I cannot answer for every company and so I will have to speak very generally on

this—life insurance companies have been accused over the years of not putting a sufficiently high percentage of their assets in common stocks. These particular policyholders cannot benefit from the investment in common stocks. Their rates are guaranteed as are guaranteed investment certificates of trust companies, and in their investment policy generally the companies regard these funds as invested in fixed interest securities, and the rates we offer on them have to be competitive with the rates the trust companies offer or we just do not attract the funds, and they are based substantially on the rates available in the fixed interest market.

Senator Beaubien: So what is wrong really is that the act deems that part of your income accrues to the tax-exempt policyholders and it should not do that.

Mr. Lemmon: That is right, sir.

Mr. T. M. Galt, Chairman, Committee on Taxation, The Canadian Life Insurance Association: If I may confirm that. In our company we definitely do calculate rates assuming entirely that there are no common stocks. The rates are based on fixed interest investments at the current levels. I cannot speak for other companies, but that is the case with us. We assume there are no common stocks in these funds for our purposes.

Senator Beaubien: Could you give us the language then that would amend the right part of the act so that dividend income would not be deemed to accrue to the policyholder?

Mr. Lemmon: I do not know that we are in a position this morning actually to put words in there. The intent of the words would be to exclude from the prorating formula these particular types of policies. We would be very glad to furnish this committee, later today, if you like, with the particular wording. We do not have a lawyer with us this morning who can do this.

Senator Carter: If I remember correctly, Mr. Chairman, the change in the act in 1969 was a deliberate policy movement on the part of the Federal Government. I think it was based on the premise that the funds, the life insurance funds, were invested mainly in blue chips in foreign countries particularly south of the border, and not sufficient funds were available for the capitalization of Canadian companies. I may not be stating it 100 per cent accurately, but that was the broad intent. Now assuming that was the policy objective, how successful has it been? What percentage now of life insurance funds are used to finance Canadian enterprises as compared with pre-1969?

Mr. Lemmon: If I can speak generally to that, without quoting any figures which I do not have with me, I do not think there has been any real change since 1969. Prior to that time the Canadian life insurance industry had more money invested in Canada than its liabilities to Canadian policyholders. That has continued to be the case. A great many Canadian life insurance companies including my own and Mr. Galt's do a substantial amount of business outside of Canada. In our own company our business is divided approximately 50 per cent in Canada and 50 per cent outside. Mr. Galt's company I think would be slightly more than 50 per cent outside.

The Chairman: You operate in the United States?

Mr. Lemmon: We operate in the United States. My own company operates in 35 states of the United States. We also operate in the British Isles.

The Chairman: Well when you talk about 50 per cent investment in Canada and 50 per cent outside, what is the 50 per cent that goes outside? It is 50 per cent of what?

Mr. Lemmon: It is 50 per cent of our total assets. But that is not quite the simple answer. We are required by law in the United States to invest in the United States the liabilities accumulated for our United States policyholders. Our company and I believe most of the companies accumulate in sterling assets payable in sterling sufficient to pay their liabilities to their policyholders in that currency and the same general policy with minor variations is followed by the various companies and has been for years. Now the surplus funds of the company, the excess reserves, may be invested here or there or around and about in the judgment of the management of the companies, but the statement still stands that we have invested in Canada over the years and still do more than our liabilities to Canadian policyholders.

The Chairman: I am interested in that 50 per cent, Mr. Lemmon. If you have 50 per cent invested in Canada and 50 per cent invested outside of Canada, does that result in there being more than 50 per cent invested outside of Canada, when you look at the assets which are held outside of Canada?

Mr. Lemmon: This would vary from company to company, Mr. Chairman. I do not know whether this is of any help to you or not, but I can quote to you some figures as far as our own company is concerned. Approximately 92 or 93 per cent of our assets are held to cover liabilities which are required by the various insurance departments. Approximately 50 per cent of that amount is held in Canada, which would amount to 46 per cent of our total assets. Approximately 46 per cent would also be held outside of Canada. The other 8 per cent of our assets is the company's general surplus held for contingencies of whatever nature. They can be held in one place or the other, and can be changed from time to time at the discretion of the management of the company. A substantial portion of it is always held in Canada. Sometimes the percentage of total assets might be 49 per cent, while in other cases it might be 53 or 54 per cent. This is the area in which it varies. But our liabilities to policyholders in Canada are always covered with a varying percentage of our surplus.

Mr. Tuck: Mr. Chairman, I wonder if I could comment on Senator Carter's question. Mr. Lemmon has described the holdings of Canadian companies outside of Canada as essentially securities, held for business performed outside of Canada. I thought from your question that you might have had this in mind, also the fact that there might have been a desire on the part of the life insurance tax legislation of 1969 to emphasize Canadian life insurance companies purchasing more Canadian corporation shares. If that was the intention, then this pro rata formula negates the intention.

Senator Carter: That was my next question. What has been the net effect of the 1969 change in legislation? Has it affected your earnings, assets, dividends to policyholders?

Mr. Tuck: It may have affected the distribution of our assets as far as the general funds are concerned, but we do not have figures which would indicate this. As far as our total investments in Canadian stocks are concerned, there is a complication here. The investments in Canadian stocks may be up, but this may not be the result of an increase in the investment of our general funds in Canadian common stocks; but perhaps it is because many of the companies have segregated funds that are backing equity-linked products. These are invested in common stocks; so the global figures which we do have may well show an increase, but the reason for the increase may be the segregated funds. Is that right, Mr. Lemmon?

Mr. Lemmon: You are quite right.

The Chairman: You will give us that wording a little later on today?

Mr. Tuck: We will try to do that Mr. Chairman, yes.

Hon. Mr. Phillips: Am I right in saying that the only section to which you have directed yourself is section 138(6), because of the special treatment which is given there, as distinguished from the normal treatment for corporations under section 112? Does it reduce itself to that?

Mr. Kimantas: And also to section 208(2).

Hon. Mr. Phillips: Section 208(2). Will you wait a moment while I take a look at that? Oh yes, I see.

The Chairman: Any material that you will give to us for our consideration in making a recommendation will deal with section 208—

Mr. Lemmon: With both of these sections.

The Chairman: Section 208 and also section 138.

Mr. Lemmon: Both of those sections.

Hon. Mr. Phillips: Section 138(6) and section 208(2). In effect, you are saying that these two sections give you the type of treatment which you prefer over section 112 dealing with exempt income?

Mr. Lemmon: Yes.

Hon. Mr. Phillips: I think we need a new wording here, Mr. Chairman.

The Chairman: While we have experts here, we might as well make use of them. If there is any suggestion that we have missed the point, we can say that we were badly instructed. It could never be said that we makde a mistake!

Mr. Lemmon: Mr. Chairman, we did have an interview with the Minister of Finance prior to the introduction of the bill this spring, and we raised this point with him. He did not say "no"; but nothing was done.

The Chairman: How many dollars would be involved if the change were to be made?

Mr. Lemmon: It is rather difficult to calculate, because as an industry we do not have block figures for exempt funds. If the total amount of pro rating were removed—and we are not suggesting this—it would amount to about $9 million. If the exempt funds were eliminated what would it be, Mr. Kimantas—two-thirds of that amount?

Mr. Kimantas: Oh no, it would be much smaller than that.

Mr. Lemmon: One-half of that?

Mr. Kimantas: I would say less than that.

Mr. Lemmon: It would be around $4 million.

The Chairman: That would be the net result, if what you are seeking today were recognized?

Mr. Lemmon: Yes.

The Chairman: Your reduction would amount to another $4 million?

Mr. Lemmon: Yes, sir.

Hon. Mr. Phillips: You are dealing with non-segregated funds only?

Mr. Lemmon: Yes, we are dealing with non-segregated funds only.

Hon. Mr. Phillips: In effect, you want exempt income similar to that given to investment companies and banks under section 112?

Mr. Lemmon: Yes, sir.

Hon. Mr. Phillips: And the two sections that hurt you are section 138(6) and part of section 208(2).

Mr. Lemmon: We are not suggesting any change in segregated funds. We feel they are reasonable.

The Chairman: Is there anything else you wish to say? I think we have the point you are making.

Mr. Lemmon: No, thank you sir. It has always been a policy of mine that if you have made a sale, stop talking.

The Chairman: There is a variation to that Mr. Lemmon; when you have sold something, wrap it up.

Mr. Lemmon: Thank you very much, sir.

The Chairman: Honourable senators, we have a third brief before us this morning, Dominion Foundries and Steel Limited. They were before us earlier, when we were dealing with the White Paper. Mr. Plumpton, are you going to make the opening remarks?

Mr. J. Plumpton, Comptroller, Dominion Foundries and Steel Limited: Yes sir; and Mr. Laing is with me.

The Chairman: Will you proceed, please?

Senator Beaubien: Mr. Chairman, could we have the names of the witnesses again?

The Chairman: Yes. Mr. J. Plumpton, Comptroller, and Mr. A. D. Laing, Assistant Comptroller and Assistant to the Executive Vice-President (Financial), both of Dofasco.

Mr. J. Plumpton, Comptroller, Dominion Foundries and Steel Limited: Mr. Chairman and honourable senators, may I first express the regrets of our President and Chief Executive Officer, Frank Sherman, for being unable to attend today. I am also requested to express the regrets of John Sheppard, our Executive Vice-President, Financial, who is out of the country. Dominion Foundries and Steel, Limited (Dofasco) is a steel mill and foundry. Our production is about 2,300,000 ingot tons of steel a year—about 19 per cent of Canadian ingot production. There are about 19,000 shareholders and 95 per cent of our shares are held in Canada.

Our steel producing facilities are located at Hamilton, Ontario. We receive all our iron ore from three Canadians mines—at Temagami and Kirkland Lake in Ontario and at Wabush Lake in Labrador.

There are about 8,000 employees in Hamilton. 77 per cent of the employees are members of the Employees' Savings and Profit Sharing Plan. There is a three year waiting period before an employee becomes a member.

The fund began in 1938 and is a pension plan based on profit sharing. In addition, we have a Deferred Profit Sharing Plan which began in 1966 and eligibility for membership in it is the same as for the pension plan.

The assets of the pension plan are about $80 million and of the Deferred Profit Sharing Plan about $2 million. Employees' savings paid into the pension plan were $1,-100,000 in 1970. Total profit sharing paid by the company in that year was $5,600,000 of which $3,400,000 was paid into the pension plan. The income earned by the Fund over and above these payments was $4,600,000. The amount paid out of the pension plan for those who terminated employment in the year was $4,300,000. There were 67 people who terminated employment by retirement at retirement age.

The Chairman: What is the total membership in this plan?

Mr. Plumpton: Over 6,100.

The amounts which each of them received varied from the lowest payment of $20,300 to the highest of $47,600. In addition, there were twenty-four employees who died whose estates or beneficiairies received the full amounts at the credit of each of these employees.

With this background, let me now try to state why we are appearing before you a second time. When we appeared the first time we were concerned about some other matters as well but our main purpose in appearing then was to explain why we, and our employees, think an average rate of tax of Section 36 type on lump sum payments out of pension and deferred profit sharing plans is fair and desirable.

The Chairman: Senators will remember that we have heard submissions on deferred profit-sharing plans, so we do have a familiarity. The deferred profit-sharing plans, as described to us, consist of employers' contributions, under which there is a deferral of tax until the lump sum payment is made, and the contributions of the employees, on which tax is paid.

Mr. Plumpton: That is not so in our case; the employee has a deduction for tax purposes.

The Chairman: Let me continue. Then there are the gains, which are treated as income in the administration.

Mr. A. D. Laing Assistant Comptroller and Assistant to the Executive Vice-President, Financial, Dominion Foundries and Steel Limited: Mr. Chairman, you are describing what I understand to be an employee's profit-sharing plan.

The Chairman: No, I am describing a deferred employee's profit-sharing plan. I am familiar with the employees' profit-sharing plan, such as that of Simpsons-Sears, who pay tax on everything. They wished to have certain considerations. The whole idea of the word "deferred" in the deferred profit-sharing plan is that the tax which might be attracted by the employers' contributions to the plan, which would be income to the employee, is deferred until such withdrawal is made.

Mr. Plumpton: That is correct.

The Chairman: That, I take it, is the deferred feature of your plan?

Mr. Plumpton: Yes.

The Chairman: When the deferral falls in and the tax must be paid, benefit is received under section 36 in the current act or it may be averaged over three years. This bill removes section 36.

Mr. Plumpton: That is right.

The sole reason for our appearing today is to comment on Bill C-259 as it applies to lump sum payments and to state our reasons for requesting retention of section 36 type averaging.

The Chairman: Are there lump sum payments under your pension plan in addition to those under the deferred profit-sharing plan?

Mr. Plumpton: Yes. The passing of Bill C-259 would, in effect, negate one of the very basic rights that Dofasco employees have enjoyed since the introduction of their profit-sharing plan in 1938. The cash withdrawal option is such a vital and important part of the program that its withdrawal would, in our view, practically destroy profit-sharing at Dofasco as an important incentive to harmonious employer-employee relations.

We have had communication with the Prime Minister and with the Minister of Finance. We have talked with the members of Parliament from our area who know some of the people who work at Dofasco, and these members know how important our employees feel the lump sum payment feature of our plan is.

Our brief describes the impact of the type of general averaging proposed in Bill C-259. It in no way compares with the section 36 type of averaging, as you can see from the page on which the results of the tax calculations are summarized.

The brief also describes the ineffective nature of the transitional provisions—that is, first, continuation of the section 36 type averaging for payments received in 1972 and 1973; and, second, continuation of section 36 type averaging indefinitely on the vested portion of the person's 1971 balance. However, once this option is exercised, any

other type of averaging must be sacrified in that year of receipt. This means neither general averaging nor income averaging could be used for pension funds accumulated subsequent to 1971, nor for any other unusual receipts.

The Chairman: Let us consider the case of a person who is a member of the plan when this bill becomes law, and remains in it for ten years. He then withdraws and is entitled to a lump sum withdrawal at that time. However, some accounting has to be carried out, and I understand the bill to provide that the averaging enjoyed under section 36 of the present act would be available for that person in 1980. That is with the proviso that the amount he would have received, had he withdrawn in 1972, is ascertained. His income tax is calculated applying the averaging provision under section 36 to that amount. So he receives a substantial benefit, because the averaging provisions under section 36 are very helpful in lowering the level of tax.

Mr. Plumpton: That is correct.

The Chairman: However, he then has to pay a price for that. He remains in the plan for a further 10 years and is not entitled to any of the benefits of averaging provided in this bill, but is subject to full tax rates. In effect, it would reduce very substantially the lump sum payments.

Mr. Plumpton: Right.

The Chairman: So much so, we have been told, that it would cease to be attractive. The only offer that the bill gives to avoid the impact of taxation is that if you take your lump sum withdrawal and buy an annuity, you do not have to pay the other burden of tax, and your income would be on the income portion of the annuity in each year. But that wipes out completely the lump sum.

We were told that of the employees in the Simpsons-Sears plan, over 99 per cent—which does not give you much room to go further—of those who took lump sum payments, over all the years that the plan had been in operation—that is, for some 50 years—not one had misapplied or lost it. It had been put to a useful purpose. It looks like a sort of paternalism, fearful that the employee, when he gets the lump sum, might not know how to use it. However, the employees had used it well, paying off mortgages and acquiring small businesses after they retired; and they felt that they were entitled to that money. This is what they had built up over the years, and when something has been going for 50 years, it must be good.

Senator Benidickson: Is my recollection correct, that over a fairly substantial number of years your employer-employee relations record, vis-à-vis your competitors, has been quite favourable?

Mr. Plumpton: Yes, it has.

The Chairman: I think you could say "very favourable."

Senator Benidickson: That was my impression. Do you attribute that very fine record, in part, to the type of company plan that you have had in existence?

Mr. Plumpton: Yes, we do. We think it has had a direct bearing on our relationship with our employees.

Senator Connolly: This is not a pension; we are now talking about profit sharing.

Senator Benidickson: I meant profit sharing.

Senator Connolly: Profit sharing is a partnership between management and workers.

Mr. Plumpton: Right.

Senator Connolly: That is the purpose of it.

The Chairman: One way of remedying your situation might be if section 36 of the present act continued to be available up to 1972. If thereafter the general averaging provisions in the bill were available—in other words you did not have that exclusion—that would deal with part of the problem.

Mr. Plumpton: That would partially offset the problem. What we fail to understand is why an employee would be penalized by opting to take the 36-type averaging which he has been entitled to. If he does so, he is, in effect, then penalized by not taking advantage of the new law.

The Chairman: One correction would be to let them keep what the bill gives them for the time period in the bill, and then give him the right, in subsequent years that he is in the plan, to be subject to the general averaging provisions of the plan. Since we have introduced the capital gains tax, do you want the gains in the fund to be treated as gains and therefore subject to the capital gains tax rate of 50 per cent—in other words, 50 per cent of the gains would be subject to income tax? Do you want that as well, as a relief?

Mr. Plumpton: Even if that were applied, with the averaging provisions continued, it would be more favourable than the straight tax rate on a lump sum.

The Chairman: Yes; but I still cannot understand why, if you have a capital gains tax on gains, and you have gains, you pay income tax rates instead of the capital gains tax rate. Perhaps you are right, Senator Hays, when you say that we should eliminate capital gains. It is becoming too complicated.

Senator Hays: That is what it is all about.

Senator Connolly: Regarding profit-sharing plans that are being built up year by year in favour of employees, are employees taxed in that year on the amount that is credited to their account?

Mr. Plumpton: No, they are not. They are free of tax until the payment is made.

Senator Connolly: We have to be practical about the kind of thing that we face. Would it be better if the allocated amount year by year formed part of their income? Can you say whether it would be better in the long run?

Mr. Plumpton: That is an alternative that we have to consider.

Mr. Laing: We have a lot of figures, but we have not evaluated them.

Senator Connolly: It could be said that if you join a profit-sharing plan and receive benefits—and apparently the benefits are very substantial—the beneficiary pays no tax when the amounts are credited to his account, and he would pay no tax when it comes out. It is obviously an advantage that the average taxpayer has.

The Chairman: If you remember, Senator Connolly, when the representatives of Simpsons-Sears and Allstate were here, we were told something of the origin of section 36. I think it developed in 1960 or 1961. Its particular application was then in relation to deferral of tax on the employer's contribution to the fund. The tax on that would fall in only when he withdrew his lump sum and when section 36 averaging applied.

In one of the plans that we had before us, the employee was contributing tax-paid dollars as his share of the contribution to the fund, so he would not run into tax again with a lump sum payment. It would be a refund of his money. We were told that on the earnings and gains of the fund, they were subject to income tax at the normal rate, and that annual payments were made and deducted by the trustee from the employee's income.

Senator Connolly: I did not hear that last sentence.

The Chairman: I said that tax on the annual contribution by the employer was deferred until the man withdraw his money from the plan. At that time his rate of tax was determined under section 36, with averaging. What is it that you want?

Mr. Plumpton: Basically, we would like to see a continuation of lump sum payments, with an averaging provision similar to the section 36 type.

The Chairman: Let us assume you cannot get that. There are averaging provisions in the present bill that are good. If those were available to you and the averaging provisions under section 36 were available to you up to the date the new bill becomes effective, that would remove the risk of retroactivity. Would that not put you in a good position?

Mr. Plumpton: Not that good. We have worked out an example in our brief which shows the proposed averaging, as opposed to the former section 36 type averaging, and there is a tremendous difference in tax.

The Chairman: That is a strong argument for giving you the averaging going forward, and it might also be a strong argument for segregating the capital elements in the fund and saying that they attract capital gains tax only.

How are you dealt with now in that regard? It is on an income basis, is it not?

Mr. Plumpton: Yes.

The Chairman: So that would be a definite advantage. It would cut your taxable income by 50 per cent.

Mr. Plumpton: Yes.

The Chairman: Would you be satisfied if you got all those things?

Mr. Laing: A relatively low portion of our fund is invested in equities. The capital gains portion, we would expect under the present investment policy, is not likely to be a significant portion.

Hon. Mr. Phillips: But on the proposed recommendation you would be talking only to the extent of 50 per cent of the capital gains.

Mr. Laing: Yes. The accumulation in out pension fund over the years represents a relatively small portion in the form of capital gains. This will be the case unless we change our investment policy, which we do not foresee doing.

The Chairman: You do not have the provisions in your plan that other plans have, and that is that a percentage of the fund is invested in company shares?

Mr. Laing: No, we do not have that provision. Our fund is invested in a broad range of investments.

To speak to your proposed suggestion just a moment ago, Mr. Chairman, Mr. Plumpton mentioned that the general averaging available under the new bill, as compared to section 36 averaging, is quite a disadvantage. On the forward averaging, which you may also have been referring to, you do not get your lump sum; and what we are saying here is that the important factor in the minds of our employees is the freedom to have a lump sum if they so choose. If you use forward averaging, you obviously do not have a lump sum.

The Chairman: What if you give them the option to elect to take forward averaging, or go along with the general averaging and get capital gains?

Mr. Plumpton: We have worked out an example of general averaging, and the employees, I am sure, would feel that this is not a great advantage to them.

If you refer to the example, honourable senators, you will see that under the present averaging method, the tax calculation on a lump sum of $45,000 is $6,903.00. Under the tax reform general averaging method, the tax payable on such a lump sum would be $16,792.00, or an additional $9,889.00. I believe that in the eyes of our employees this is a real stumbling block to lump sum benefits.

The Chairman: The answer, then, is you do not want general averaging provisions; you would like to have the right to take forward averaging if you so decided.

Mr. Laing: If it permitted a lump sum to be paid.

The Chairman: Yes, but the essential thing in your presentation is that you want to continue the lump sum withdrawal.

Mr. Laing: Yes.

Mr. Plumpton: I might add, Mr. Chairman, that our experience has been excellent in so far as employees taking lump sums on retirement is concerned.

Senator Connolly: How can you follow that after the employee leaves?

Mr. Plumpton: Our personnel department tries to maintain contact with retirees, and, of course, we have our 25-year club and other associations where the retirees

participate, and there is a general follow-up in that regard. I would not say it is a 100 per cent follow-up.

Senator Connolly: But it is sufficient to allow you to make the statement?

Mr. Plumpton: Yes.

The Chairman: Simpsons-Sears, if you recall, had a complete story on that. They stated that 99 per cent-plus of the employees did not waste their lump sum payment.

Is there anything further you would like to say? Does it appear to you that we understand your problem?

Mr. Plumpton: Yes, sir.

You have asked the delegations preceding us if they wanted to suggest a change in wording. We have looked at the proposed act, and we could make suggestions with respect to some of these provisions.

The Chairman: You may put them on the record.

We have been studying this thing and we may even have gotten to the stage where we have drafted something on this point.

Mr. Plumpton: We would suggest that section 38(2) be eliminated; that is the section that restricts the general averaging and the income averaging annuity subsequent to the option on the section 36 type averaging. We would also suggest that Section 40(1)(c) be amended by eliminating the words "and before 1974". Our third recommendation is in respect of Rule 40(7) of the Income Tax Application Rules which states:

> The provisions of this section are applicable in respect of any payment or payments described in subparagraph (1)(*a*)(i) or (1)(*a*)(iv) made in a taxation year ending after 1973—

We suggest stopping there and eliminating the rest of that paragraph.

Hon. Mr. Phillips: You are now referring to section 40(7)?

Mr. Plumpton: Yes, sir.

Hon. Mr. Phillips: Are you sure it is section 40?

Mr. Laing: It is the application rules, sir.

Senator Connolly: We are not talking about the bill; we are talking about the rules.

Hon. Mr. Phillips: Mr. Chairman, would you allow the repetition of the suggestion?

What are you asking for in that regard?

The Chairman: What do you want done with subsection 7?

Mr. Plumpton: In the third line, after "1973" we suggest a full stop, and omit the rest.

Mr. Laing: That may mean the whole subsection would come out; it might have the effect of taking the whole thing out.

Hon. Mr. Phillips: It is equivalent to taking it out.

The Chairman: If you take out the limitation.

Mr. Laing: I think so.

The Chairman: Is there anything else you want to say?

Mr. Plumpton: Only to thank you very much, Mr. Chairman.

Senator Isnor: Might I put this, just before you go? Your brief is based entirely on a pension scheme?

Mr. Plumpton: There are two parts to our profit sharing: there is the pension part, which is really our profit sharing fund; and a deferred profit sharing plan, which has nothing to do with a pension. Both are amalgamated for the benefit of employees and can be taken out under the present law as lump sum payments, whereby the tax is averaged under section 36.

Senator Isnor: I ask that question because Simpsons-Sears said very definitely that theirs is not a pension scheme.

Mr. Plumpton: That is correct. I understand that theirs is not a pension scheme.

The Chairman: That is right.

Thank you very much.

We have one submission left, which is the brief of the Canadian Institute of Chartered Accountants. It is lengthy and may take a little time to deal with. As it is getting close to 12 o'clock, I suggest that we adjourn now and resume at 2.15 p.m. Is that agreed?

Hon. Senators: Agreed.

The committee adjourned until 2.15 p.m.

Upon resuming at 2.15 p.m.

The Chairman: Honourable senators, this afternoon we have before us the Canadian Institute of Chartered Accountants. To my immediate right is Mr. R. D. Brown, F.C.A., Chairman of the Tax Committee. Immediately next to him is Mr. Michael Carr, C.A., a member of the Tax Committee; and next to Mr. Carr is Mr. R. C. White, C.A., Director of Communications.

Would you care to make your opening statement now, Mr. Brown?

Mr. R. D. Brown, F.C.A., Chairman, Tax Committee, The Canadian Institute of Chartered Accountants: Thank you, Mr. Chairman.

Honourable senators, we welcome the opportunity to present the views of the Canadian Institute of Chartered Accountants—the representative body of 20,000 chartered accountants in Canada—on the tax reform legislation which you are considering.

Chartered accountants have, of course, been deeply involved in tax practice, in completing returns and advising clients, and our profession and the legal profession are the founding bodies of the Canadian Tax Foundation in Canada. As such, the CICA has participated fully in the debate on tax reform which has gone on for the last few years in Canada, making submissions to the Government, to the committee of the House of Commons and to this

committee on this matter. Now that a concrete proposal for tax reform legislation has been advanced, we are confining our submission this time basically to points which deal with technical matters. We are not reiterating some of the more fundamental policy points which we have made in previous submissions.

First of all, I should like to mention two or three main areas of concern which the CICA has with respect to the tax reform legislation, and then I will refer to our submission in which a great many other areas are outlined.

Some of the areas that we feel require the most attention, at least in technical terms, are, first, the area of business mergers and reorganizations. We are concerned that the new law will hamper necessary and desirable restructuring of business. There is a whole combination of factors here: first of all, the lack of roll-overs with respect to capital assets and transfer without imposition of capital gains tax; secondly, the new requirement to transfer depreciable property at fair market value, even between related persons in most circumstances; thirdly, a need to recognize goodwill on the sale or transfer of a business; and, fourthly, a stengthening of the designed surplus provisions which prevent the free-flow of surplus from one corporation to another.

The Chairman: Did you say the strengthening or the deletion?

Mr. Brown: Well, they are much more effective than they ever were before. I think that this factor, in combination with a number of other changes that I have referred to, gives you a total package by which it will be extraordinarily difficult in future to reorganize business enterprises.

The Chairman: I did not mean it from that point of view. I meant the designated surplus idea. Is it needed, with all the other insurance you now have?

Mr. Brown: We seriously question whether it is. One of our recommendations is that a very strong look should be taken at this whole area of designated surplus with the introduction of a tax on capital gains. We question whether as a long-term measure it is necessary to keep the designated surplus provisions in.

The Chairman: And with section 138—

Mr. Brown: That is correct.

Hon. Mr. Phillips: The Canadian Bar Association supports you in that view.

Mr. Brown: Yes.

The Chairman: And Mr. Phillips supports you.

Mr. Brown: Very good. I think the point we would like to make here very strongly is that the various provisions that we have mentioned with respect to reorganizations will not really raise any material amount of tax revenue. The point is that what they will do is force businesses to operate in an inefficient manner and through an inappropriate corporate structure. We seriously question whether in Canada, where there is a need to reorganize and perhaps consolidate our businesses in various areas, this is an appropriate posture. We suggest that there is a need for tax-free provisions for exchanges where there is no tax advantage being secured by any write-up in the value of assets and where there is a continuity of economic interest.

Another area we have some concern about is the international area. Here our concern is primarily with respect to the foreign accrual property income, the so-called passive income.

The Chairman: FAPI.

Mr. Brown: FAPI, yes. That is correct. The fact is that these provisions, in a complex way, will inhibit competitive ability of Canadian companies abroad to operate in competition with the subsidiaries of other countries.

Senator Connolly: Apart altogether from the Competition Act.

Mr. Brown: Yes, sir.

The Chairman: How do we treat that, senator? As an aside?

Senator Connolly: *Obiter dicta.*

Mr. Brown: We have other concerns in the international area, but these are of a more technical sort. Fundamentally, we believe that tax reform has taken a very long time in Canada; it has been a long process, perhaps too long. As an institute, we welcome the conclusion of this process—or its apparent conclusion as it now appears to be—but at the same time we urge that as it proceeds through the other body and through the Senate, the most careful attention be given to the details to make sure that this legislation will be the most efficient and that it will be fair and equitable to all concerned.

In terms of our submission to you, what we have put in front of you is a document which, first of all, under the covering letter, sets out the main areas of concern that we have with respect to Bill C-259. Behind that submission is a much longer document entitled "Points for Discussion". That document was prepared by our committee working a great many hours over the summer, and it summarizes about 150 different points of comment with respect to Bill C-259 as it stood at the end of June. That memorandum was submitted to officials of the Department of Finance at the end of August, and we had a meeting with them at that time to discuss some of the points.

The Chairman: Are you able to indicate to what extent, if at all, any of the points that you have raised have been incorporated in the admendments that have come down?

Mr. Brown: We have just completed the chore of matching up the amendments with our earlier recommendations. Of course, the last set of amendments was not available until last week. I am afraid that all I have with me is one copy, with the points that have been corrected marked off. We would be pleased to leave that with you, or to send you a copy of it.

Hon. Mr. Phillips: What is the "track record" for the institute with the Department of Finance in respect of the August submissions and the amendments as they have come down?

Mr. Brown: It is very difficult to say. I think they have answered about one-third of the points we raised—one-

third at the most. I think some of the others have perhaps become a trifle redundant because of other changes that have taken place in the bill. It gets rather complicated, because if you fix one area then sometimes you fix others at the same time.

The Chairman: Would you say that any of the areas that would appear to have been fixed may require further amendment?

Mr. Brown: Yes, that is true. As a matter of fact, we specifically direct your attention to one point in the amendments that were put down last week. On page 6 of the document entitled "Areas of Major Concern with Respect to Bill C-259," we note that the amendment to clause 192(13) proposed on October 27 would have the effect of accidentally designating the surplus of all corporations which have undergone a statutory amalgamation in the last 25 years.

Hon. Mr. Phillips: Is that October 27 or October 13?

Mr. Brown: This is the amendment of October 13. This is because of a change in the definition of a designated surplus. What they have done is to define "designated surplus" in a controlled corporation as always being the total surplus less, in effect, the control period earnings, and when a corporation has gone through a statutory amalgamation it has no control period earnings and all its surplus is changed, I am sure not intentionally, into designated surplus. We believe that this is a technical point which should be corrected.

Senator Connolly: Do you have a specific recommendation involving the words to amend the given section?

Mr. Brown: In the case of section of 192(13) I do not have words with me, but we would be pleased to drop you a note to comment on them. I think the basic point is that in the case of a statutory amalgamation the control period earnings of the predecessor company should flow through to the new company so that you do not achieve any designation under that type of definition.

The Chairman: You have finished your presentation?

Mr. Brown: Yes, we have finished our presentation.

The Chairman: Is there anything your panel would like to add before we come to any questions we might have?

Mr. Brown: I do not think so, thank you.

Senator Benidickson: Mr. Chairman, referring to the introduction to this presentation today, there was a brief given to each member of the committee which is not by any means in the exact language given by Mr. Brown this afternoon. While it has been our policy not to print in full the entire submissions, as we did in the case of the White Paper hearings, I wonder if the first two pages of the submission could be printed as an appendix to our proceedings this afternoon. There it is explained very clearly what the Institute of Chartered Accountants is prepared to comment upon, and what it has not been able to comment upon because of some recent amendments.

Then, again, it makes it very clear, inasmuch as the institute previously expressed its views on the subject of tax reform in a general way which would include, perhaps, comments and suggestions concerning that policy. They did so both to this committee and to the House of Commons committee when they studied the White Paper, and they made their representations to the Government. Today they have confined themselves simply to technical revisions to the bill as presented in June. I think that should be clear.

The Chairman: Well, Mr. Brown has said that. Do you feel that the first two pages of this letter should be printed?

Senator Benidickson: I am saying why I think it should form part of the evidence today.

The Chairman: Is it the wish of the committee to print it as part of Mr. Brown's evidence right in the record of our proceedings rather than as an appendix, because then you get a continuity of reading? Is that agreed, honourable senators?

Hon. Senators: Agreed.

Hon. Mr. Phillips: May I suggest that we give it today's date and that we include all ten pages at this point in the record?

Mr. Brown: It really speaks as of today.

Hon. Senators: Agreed.

Text of document follows:

November 3, 1971.

Honourable Sirs:

INCOME TAX REFORM—BILL C-259

The Canadian Institute of Chartered Accountants is pleased to have this opportunity of presenting its views on tax reform legislation—Bill C-259—to your Committee. This presentation is being made on behalf of the Institute by its Taxation Committee which acts as the representative body of chartered accountants of Canada on taxation matters. The members of our Committee, in common with all of the members of our profession, have been deeply involved over the past few months with a review and consideration of the income tax legislation introduced into the House of Commons last June by Finance Minister Benson, and we hope our comments on this proposed legislation will be of use to your Committee.

To prepare our profession and the business community for the likely implications of this new legislation, the CICA has been active in disseminating information on the tax reform proposals. Toward this end, the Institute has prepared a special two day course on the tax reform legislation, which has been attended by over 3,500 chartered accountants and other businessmen across Canada; we expect another 1,500 to participate in this course by the end of the year. A special series of articles on tax reform has appeared in our journal, *Canadian Chartered Accountant*, and we have published an analysis of Bill C-259, "Tomorrow's Taxes".

In addition to these information programmes relating to the new legislation, the Taxation Committee met earlier in the summer on a number of occasions to review the technical aspects of Bill C-259, and was materially assisted by

submissions received from a number of the Taxation Committees of the provincial Institutes of Chartered Accountants. Because of the short time available to the CICA Committee for a review of this detailed and highly complex legislation, it did not follow its normal practice of making a formal, detailed submission to the Department of Finance on the new tax legislation. Instead, the Committee prepared a memorandum entitled "Points for Discussion on Bill C-259" which set out in summary fashion, the comments and recommendations of the Committee on the Bill as it then stood. This memorandum was reviewed with officials of the Department of Finance on August 27, and copies of this memorandum were subsequently distributed to various other interested parties.

These "Points for Discussion", a copy of which is annexed to this submission, dealt with the provisions of Bill C-259 as introduced into the House of Commons on June 30, 1971 only; it does not, regretfully, refer to the list of approximately 100 amendments to Clause 1 of this bill which the Minister of Finance tabled in the House of Commons on October 13, nor with the substantial number of additional amendments tabled on October 28. (Due to the complex nature of these amendments and the short time available between their introduction and our meeting with you, it was not possible for our Committee to revise its earlier submission to take these changes into account.) However, Mr. M. Carr and I, as representatives of the CICA Taxation Committee, are prepared to discuss informally with your Committee certain of the implications of these amendments.

To assist your Committee in evaluating the main thrust of the recommendations and comments of the CICA Taxation Committee on Bill C-259, we have also prepared, and enclose, a separate brief submission which highlights our major concerns with the tax reform legislation. This memorandum, which also of necessity had to be prepared in a relatively brief length of time, does take into account, to a degree, the amendments to Bill C-259 which were introduced on October 13, but not those contained in the amendments of October 28. In this supplementary submission, we have attempted to highlight a number of technical areas which we feel requires further consideration, of which perhaps the general lack of provisions for effective tax free business reorganizations and the adverse implications of certain proposals in the international area are amongst the most important.

We would like to emphasize that all of the comments in the attached submission and in our original "Points for Discussion on Bill C-259" are directed towards the technical implications of the new legislation, and are not concerned with the policy implications of the legislation. The CICA has previously made submissions to the Carter Commission, the Department of Finance, the Finance Committee of the House of Commons, and to this Committee of the Senate on certain of the broader aspects of tax policy and we now feel that it is appropriate to confine our remarks solely to the more technical implications of the legislation, although of necessity our comments will, in some areas, touch on policy matters. All of our comments are, however, directed towards tax reform in the context as set out in the legislation introduced by the Minister of Finance, and our observations are designed to make the legislation both more equitable and easier to administer.

If there are any areas of the legislation where you believe the particular expertise and experience of chartered accountants could assist the Committee in its study and deliberations on Bill C-259, we will endeavour to do so if you let us know.

Respectfully submitted,

R. D. Brown,

Chairman, Taxation Committee.

THE CANADIAN INSTITUTE OF CHARTERED ACCOUNTANTS TAXATION COMMITTEE

R. D. Brown, FCA, Toronto Chairman; J. M. Belanger, St. John's; F. J. Mair, FCA, Calgary; P. Walton, Vancouver; D. R. Huggett, Montreal Vice-chairman; M. Carr, Toronto: D. K. McNair, FCA, London: W. K. McIntyre, Toronto Secretary.

THE CANADIAN INSTITUTE OF CHARTERED ACCOUNTANTS

Areas of Major Concern with Respect to Bill C-259

This memorandum is provided as a supplement to "Points for Discussion on Bill C-259" which was prepared by the Committee in August 1971; a copy of this memorandum is attached, and is intended to summarize a number of the major areas of concern to the CICA Taxation Committee. It deals with the provisions of Bill C-259 as they stood, after giving effect to the amendments to Clause 1 of the Bill tabled by the Minister of Finance in the House of Commons on October 13, but does not take into account (due to the shortness of available time) the proposed amendments submitted to the House on October 28.

CAPITAL GAINS

Valuation of Liabilities

No provision exists in the legislation for the valuation of debts (except foreign currency) owing by taxpayers at the commencement of the new system. As presently drafted, the legislation would include the entire amount of any "gain" realized by taxpayers on the repayment of a debt, etc., after January 1, 1972 as giving rise to a taxable gain.

We recommend that the taxation of gains realized by taxpayers on the repayment or settlement of debts existing at the end of 1971 should not extend the amount of any "gain" which may then have accrued, having regard to the market value of debts then outstanding, at least when such debt is in marketable form. We, therefore, recommend that a taxpayer should have an "adjusted cost base" of existing debts owing by him as at December 31, 1971 equal to

—original par value (or issue price, if lower)

—fair value of debt at "valuation day"

Subsequent "gains" on the settlement of liabilities should be measured from the lower of the above two values while losses would be measured from the higher of these two amounts. These rules will be consistent with the provisions for the valuation of assets for capital gains purposes.

We also recommend that a similar recognition be given to the fair value of options outstanding at the end of 1971 so that the value of such options be included in the adjusted cost basis of property subsequently acquired through the exercise of such options.

Disallowance of Non-arm's Length Losses

There are a number of sections of the Bill dealing with the disallowance in a variety of circumstances of capital losses sustained in non-arm's length transactions. While recognizing the need to protect the revenue against artificial losses which may be created in non-arm's length transactions, we question whether severe and general restrictions of the nature of those in the present bill are necessary or desirable. In addition, we note that these provisions will have different application to a variety of different circumstances, and are unable to appreciate the reason for different treatment afforded different types of such losses.

We suggest that, in *every* case where a loss is disallowed, or a gain increased in a non-arm's situation, a corresponding carryover for adjustment of base to the non-arm's length party acquiring the asset to be provided for—the disallowance of losses in non-arm's length transactions carried out at par value should be limited to certain clearly defined circumstances where the taxpayer may be regarded as not severing his economic interest in the asset.

Re-investment of Proceeds

We are concerned that a number of provisions dealing with expropriations or other forced realizations of property do not afford adequate time for the taxpayer to reinvest the proceeds to avoid being subject to capital gains on an involuntary conversion.

Charitable Donations

We are concerned that the provisions requiring a recognition of gain or loss on the disposition of property by way of gift or bequest will have an adverse effect on the donations of appreciated property to charities. Such gifts or bequests may cause the donor a substantial tax liability in circumstances where he may not be able to utilize the deductibility of the full charitable donations. We recommend that where property has been given or bequeathed to a charity it may be valued at the option of the donor or his estate at any amount not greater than fair market value, or less than cost (except where cost exceeds fair value).

Carryback of Unabsorbed Losses

If a deceased person has unabsorbed capital losses remaining after the carryback provisions now in the Income Tax Act, we recommend that such unabsorbed losses should either be carried back to earlier taxable capital gains realized by the same taxpayer, or possibly added to the adjusted cost base of such properties tramsmitted in the deceased's will.

MINING AND RESOURCE INDUSTRIES

The provisions regarding the recognition of gains or losses on the transference of mineral properties will, in our view, have an extremely detrimental effect on the development and financing of new mineral resources in Canada. Under the Bill, as it presently stands, any transfer of mineral properties (except in the limited circumstances of a transfer from a wholly owned subsidiary to a parent) must be made at fair market value.

This will create immense problems in a number of common situations where it is essential that mineral properties be transferred from one corporation or individual to another in order to facilitate the development and financing of such properties. It will create difficulties where properties are transferred in consideration of exploration work to be done by others.

We recommend that mineral properties should be freely transferrable in non arm's length transactions at adjusted cost base, and furthermore that undeveloped mineral properties might be transferred at adjusted cost basis to a new company in circumstances where the only consideration taken back is the shares of the stock of the company in question.

We also believe that the exclusion of social capital and certain other items from the "earned depletion base" may be unfortunate.

INTERNATIONAL

Departure Tax

We have observed that many Canadian citizens, and non-residents temporarily employed in Canada, are extremely concerned with the implications of the "deemed realization" provisions with respect to the capital assets of persons giving up Canadian residency. This happens frequently on the transfer of executive and technical personnel from Canada. The provisions, as presently drafted, would appear to impose a substantially higher tax burden on individuals who, because of their position or occupation, are required to take up and give up Canadian residency during their careers, than on individuals who remain resident in Canada.

We strongly recommend that the provisions in this regard be re-examined and have made a number of particular recommendations in our "Points for Discussion".

Foreign Accrual Property Income

The provisions respecting this concept as now drafted would appear to have extremely adverse effects on Canadian based multinational corporations operating abroad and will subject them to tax on many types of income which cannot be regarded as having been artificially diverted from Canada. These provisions will hamper Canadian companies operating abroad from achieving the best financial and tax position, and will place such companies at a disadvantage relative to those of other jurisdictions. The proposals appear not only unfair but also technically deficient in some areas. We also note that they would adversely affect Canadian beneficiaries of non-resident inter-vivos trusts. We strongly recommend this whole concept be thoroughly reviewed and have advanced a number of concrete suggestions in our more detailed memoranda.

Dividends from Foreign Affiliates

We have a number of technical observations and questions with respect to the provisions regarding the taxation of dividends from foreign affiliates. Though these provi-

sions will not be fully effective for some time, we recommend that the government clarify certain of these difficulties at the earliest possible date so that the affected taxpayers may plan their foreign operations.

Reorganization of Foreign Affiliate

Provisions should be introduced allowing tax free reorganizations and regroupings of foreign affiliates.

Foreign Competition

We believe that the taxation system should enable Canadian exporters to effectively compete with exporters of other countries. In this regard, we believe that the government should take into consideration proposals now before the United States Congress, as well as current trends in Europe and elsewhere, in deciding on an appropriate tax system for Canada in respect of international income.

CORPORATIONS AND SHAREHOLDERS

Reorganizations

One of the principal concerns in this area, and in the related area of capital gains on business assets, is the absence of any effective provisions allowing tax free reorganizations in a number of defined circumstances. We are particularly concerned that:

—the strengthened and expanded provisions dealing with "designated surplus"

—the requirement that depreciable property be transferred at fair market value in many non-arm's length situations

—the requirement that capital property and goodwill be transferred at fair market value in many situations

will combine to unduly hamper and impede the necessary reorganizations and consolidations of Canadian business enterprises.

The provisions, as now drafted, would impose a substantial tax cost on even the most simple consolidation of a group of enterprises under more or less common control in a number of cases, and would impose virtually intolerable complexities and costs on the reformation or reorganization of a corporate group following a major acquisition. We question whether the provisions now in the Act in this regard serve the long-run interests of Canada to obtain an efficient business community.

We are convinced that the elaborate structure built into the bill to require recognition of gains or losses on business acquisitions, and to tax the distribution of acquired ("designated") surplus will not raise significant revenues for the government. Instead, what these provisions will do is hamper the needed consolidation and regrouping of Canadian business, and force industry and commerce into inefficient operating procedures.

Accordingly, we recommend that all of the following transactions be considered as "tax free" rollovers (transactions which do not generally give rise to taxable gain or loss):

1. All statutory mergers.

2. The acquisition by one company of the majority of the shares of another company in exchange for voting, participating shares.

3. The sale of all of the properties of one company to another in exchange for voting, participating stock.

4. Any transfer of assets between any members of a group of companies with at least 50% ultimate common ownership.

5. Any recapitalization, change in identity or place of incorporation, etc., which does not involve a capitalization of surplus or distribution of assets.

As an interim measure, we suggest that certain of the above transactions might be permitted "tax free" rollover status only in circumstances where an advance ruling had been obtained. Such a ruling might only be available in circumstances where the applicant had a continuity of economic interest in the asset; and where there was no intent to improperly avoid tax.

We also recommend that the provisions with respect to designated surplus be completely reviewed. We believe that with the advent of a tax on capital gains, the justification of a substantial tax on the distribution (or even more seriously, an artificially deemed distribution) of acquired surplus requires re-examination.

We also note that the amendment to Section 192(13) tabled by the Finance Minister on October 13 will apparently have the effect of accidentally "designating" the surplus of perhaps hundreds of Canadian corporations which have undergone statutory amalgamation in the last few years. This arises because the section, as proposed to be amended, provides that the "designated surplus" of all controlled corporations is to be computed as their current undistributed income, less their earnings in the control period: a corporation emerging from a statutory amalgamation has no earnings in the control period carried over, and hence its surplus at that time will become designated. This technical anomaly should be corrected.

INDIVIDUALS

Income Averaging

We recommend individuals should be permitted to use both "general averaging" and the transitional specific averaging rules for pension, stock option, and other lump sum benefits in the same year.

PARTNERSHIPS

We have expressed a general concern over the complexity of the provisions respecting the taxation of partnerships. We are concerned that many taxpayers who use this common form of business organization, may not be able to interpret the provisions of the new legislation, and that the Department of National Revenue will have difficulty in administering these new provisions. We recognize that in the context of the tax system proposed by Bill C-259 (including the taxation of capital gains and the amortization of goodwill) any proposals for the taxation of partnerships and their income must be somewhat complex but we believe that the provisions as drafted will prove difficult to have application in a number of circumstances. Some of our particular concerns with the taxation of partnerships are set out in the memorandum "Points for Discussion on Bill C-259".

We urge that specific provisions be inserted in the legislation clarifying the right of a partnership to make deduct-

ible payments to retired partners and their spouses and dependants, with such payments being taxed as ordinary income to the recipients.

Senator Benidickson: In connection with that letter, Mr. Brown has indicated that since the Income Tax Reform Bill C-259 was introduced the institute has prepared a special two-day course on the tax reform legislation, and my understanding is that this is a course that consists of a travelling panel made available not only to members of your institute across the country, but also to concerned individuals who are not members of your institute but who have chosen to take advantage of the availability of this travelling panel.

Mr. Brown: That is correct. We hope to have this presentation shown to over 5,000 persons in Canada before the end of the year. As a matter of fact, a condensed version of that presentation will be given here tomorrow, and will be open to all members of the Senate and the House of Commons interested in attending.

Senator Benidickson: That is what I wanted to come to. I was at another meeting this morning and heard the Chairman of the Finance Committee of the House of Commons who referred to your making it available. I take it that, since it is a one-day sitting, you are condensing what you are doing elsewhere in two days, but I just wanted to make sure that senators have been invited as well as members of the House of Commons.

Senator Carter: Will the proceedings of tomorrow be printed?

Mr. White: The proceedings tomorrow will not be printed. There is a book which we have published entitled *Tomorrow's Taxes*, and this will be given to all those attending the presentation tomorrow. To the best of my knowledge, arrangements have been made by the Commons Finance Committee.

Senator Connolly: Could you circulate a copy of *Tomorrow's Taxes*?

Senator Benidickson: We have received it. That is referred to also in the letter which is being made part of our proceedings today. At a one of the recent sittings a witness did raise a book of which the title was the same. The colour was different, but, as I say, the title was the same—*Tomorrow's Taxes*—and it was attributed to your Institute, but the copies which were circulated to this committee say it was "prepared for the clients and staff of Clarkson, Gordon & Company." Is it the same document?

Mr. White: It is the same document. Clarkson, Gordon made the text of the study available to the Institute, and we published it for general distribution to the business community and our members.

Senator Benidickson: Basically, what will be made available in this seminar tomorrow to members of the House of Commons and of the Senate who are invited—except, I should mention, we will have some difficulty in that we will be having a meeting tomorrow—is basically contained in this fairly substantial booklet called *Tomorrow's Taxes*?

Mr. White: I would think so, but Mr. Brown might be better prepared or qualified to comment on it than I. I understand that the method to be used tomorrow will be to try to get a bird's-eye view of the full tax reform legislation as it now stands. *Tomorrow's Taxes* is a much more detailed examination of it, but I think the two complement each other very well.

Senator Benidickson: It is unfortunate that the House of Commons does not have a standing committee dealing with the bill itself, as it did with respect to the White Paper. We have a committee which is examining the bill itself. We are sitting tomorrow and probably cannot take advantage of this seminar.

Mr. Brown: We regret this very much. We were attempting to organize it at a time available to everyone, but it appeared that there was no such time.

Senator Benidickson: I understand you have made it more attractive in that, unlike the travelling panel where a fee was charged, you have made it available free of charge to parliamentarians?

Mr. Brown: That is correct. I might mention that the two-day course on the abbreviated version will be presented tomorrow. Our effort is to present what is a very complex subject in terms which can be understood by accountants and businessmen. It basically consists of visual presentations and a great many overhead slides of examples where the impacts of the changes have been worked out. Therefore, while it deals with the same material as the book entitled *Tomorrow's Taxes*, it is in a somewhat different format.

The Chairman: Let us get down to business, Mr. Brown. I note in the introductory part of your brief that your submission is addressed to technical changes and not to matters of principle.

Mr. Brown: Yes, these distinctions, of course, cannot be clean-cut. What I mean to say is that in all cases we have confined our comments to agreements or disagreements on the proposals in the bill. We have not attempted, in effect, to bring about a different approach to the problem. We have attempted to deal with the particular approach the Government has chosen to deal with and to suggest modifications which would make it work more effectively.

The Chairman: On that basis, where do you want to begin?

Mr. Brown: Perhaps it might be better if we went over the main areas of concern, such as the treatment of individuals, of capital gains, and so on. In our shorter seven-page memorandum, at the beginning of the material—

The Chairman: Yes, we have had a fair amount of background on this. There are certain items which you have indicated as areas of major concern which, quite frankly, it is our view also that they are major concerns.

Mr. Brown: I would like to make a correction before you go on, sir. The areas of major concern begin with capital gains, and the first area of concern is the valuation of liabilities. This was written last week, but we find that the amendments submitted to the House of Commons on

October 27 deal substantially with the problem mentioned under that heading. Therefore, I feel that our comments under that particular heading are perhaps not necessary. All of the other comments in our report remain unchanged.

The Chairman: Yes. Then moving on to mining and resource industries, we have had substantial submissions from major companies, and we feel that we understand their problems. Is there anything particularly that you want to direct our attention to, recognizing that your approach is one of technicalities?

Mr. Brown: Yes, without speaking to the burden of the total taxation on the mining industry, the first of the two points I would like to make is, that the restriction on the transferability of mining property, that is oil and gas properties, mining rights, in the particular circumstances will have a crippling impact on the establishment of new mining ventures where frequently the transfer of such assets is required in order to place them in a vehicle which can be financed and where stocks can be issued to the public. But if you have to make a transfer at the fair market value, you will have to pay a substantial amount of tax at a time when the funds available to pay the tax are not available.

The second point is the unfortunate effect of the exclusion of what might be called social capital from the earned depletion base; that is, expenditures by mining companies for townsites, transportation facilities, et cetera. These are only important in remote areas; but they are expenditures of critical importance.

The Chairman: You would agree that the provision in the bill relating to earned depletion appears to be too narrow?

Mr. Brown: Yes, were concerned about that.

Senator Connolly: It might be that the industry will require the provinces to contribute materially to the development of social capital in new or remote areas. It may very well increase the financial load that the provinces will have to carry.

Mr. Brown: That is correct. I think one other point that should be brought out is that both the federal and provincial governments are evidently prepared to subsidize other developments in remote areas, such as a number of pulp and paper projects, some of which have turned out rather unfortunately. On grounds of basic social policy there should be some question as to whether these types of mining expenditures should not not be included.

Senator Connolly: Might I add this point, Mr. Chairman? Perhaps you are in the same position as I am being a member of the profession you cannot judge the situation. Would you think, generally in dealing with the provision of social capital, the infrastructure can be done more efficiently and more economically by the private sector rather than by the public sector, particularly as would seem to be the case in the provinces?

Mr. Brown: That is a very difficult question to answer because it depends so much on the circumstances. In a number of areas I think mining companies have done quite well in the past in providing this type of structure. But in one recent case, for example, the Sherritt Gordon development in Manitoba, they arranged to have the province do all the work, even though Sherritt Gordon later agreed to finance the project. As long as you can avoid building what used to be called company towns, the undertaking of the necessary infrastructure by the corporation has substantial advantages because you can definitely fix the responsibility for financing the work.

Senator Connolly: What specific objection do you wish to put on record about "company towns"?

Mr. Brown: In dealing with company towns I was speaking of the situation where the company owns the stores and the recreational facilities and, in effect, runs everything from the top down. For example, if you were to take a town such as Thompson, Manitoba, in effect it was organized and planned by the International Nickel Company; but all the stores and recreational facilities are independently owned and operated. In that way I think they have avoided the curse of a company town where, in effect, everything is run by one company-appointed manager.

The Chairman: I think you would find the same situation in Elliot Lake.

Mr. Brown: That is correct.

Senator Benidickson: And, of course, they have changed their form and their political participation quite substantially from the time of construction of the community.

Mr. Brown: That is correct.

The Chairman: We certainly agree with you with respect to the areas for concern. We have put something on paper as regards FAPI and dividends from foreign affiliates.

Have you made any comment in your brief on the situation with respect to exempt income under the new bill, and particularly with respect to the fact that the determining factor as to whether income from an active business operation abroad is exempt or not is based on whether the Government has been able to make a treaty with the country concerned? Why should there be a penalty to the company if the Government is not able to make a treaty?

Mr. Brown: That is the point, I believe, we made in our earlier policy submission to this committee and to the committee of the House of Commons. At that time our committee was convinced that there should be no distinction in this area, and we are still of that view, but as it is a basic policy matter it is not included in our brief at this time.

The Chairman: It is a rather odd situation. Whether or not you have exempt income depends on whether there is a treaty between Canada and the country involved. The company has nothing to do with that, and the qualifications for exempt income are all otherwise met by the dividends coming forth from the active business operation.

Mr. Brown: The implications of this are particularly severe in the case of Canadian mining companies, utilities, and insurance companies operating abroad due to the particular tax laws that affect these enterprises.

Hon. Mr. Phillips: So-called multinational corporations.

Mr. Brown: Yes. You will find in the proposals with respect to the dividend income received by manufacturing companies from abroad that there are a good many alleviating provisions. For example, in the case of dividends which would otherwise be taxable there is an election to credit such dividends against the adjusted cost base of the shares to pick up a disproportionate amount of foreign tax, and so forth. These provisions will mitigate the effect in a number of cases but not in others. In other words, I feel the change will fall rather unevenly on Canadian multinational corporations, some being virtually unaffected and others being very substantially affected.

The Chairman: Yes, but there would not be any difficulty, or it would be quite negligible, in relation to exempt income if you did not have that artificial tax treaty or not treaty.

Mr. Brown: We agree with that point.

Senator Macnaughton: Under the heading on page 4, "Foreign Accrual Property Income," you are quite definite in some of your wording. You state in that paragraph:

> The proposals appear not only unfair but also technically deficient in some areas. We also note that they would adversely affect Canadian beneficiaries of non-resident inter-vivos trusts. We strongly recommend this whole concept be thoroughly reviewed and have advanced a number of concrete suggestions in our more detailed memoranda.

Do you care to say a few words on that?

Mr. Brown: Yes. The basic idea of foreign accrual property income is that Canadian individuals or corporations who have foreign affiliates will be required to include in their income immediately the passive income of such foreign affiliates as it has earned. "Passive income," for this purpose, is defined as any inactive business income together with all income from property.

The provisions are somehwat indefinite, because, as I believe you are all aware, the question of what is income from property and what is income from a business, let alone an active business, is a little imprecise. In addition to that, there are a number of technical problems. There are situations, for example, where a Canadian taxpayer could be required to include in his income, let us say, 150 per cent of the foreign passive income of a foreign affiliate simply because of the technical deficiencies in the wording. The provision that deals with the percentage of foreign income that you have to include in your income has no limiting income on it. It is the sum of a number of factors, and these factors could easily add up to more than 100 per cent. In addition, and I believe this is the clearest cut example, where you have a Canadian who has both income and is a capital beneficiary of a foreign trust, that individual could well be required to include 200 per cent of the income of the foreign trust in his income under the provisions as they now stand.

Senator Macnaughton: If that is true, it certainly justifies your remarks.

Senator Connolly: In the document we have before us, have you a suggestion for an amendment to a clause of the bill?

Mr. Brown: Yes. If you turn to the more detailed part of our submission, which is the memorandum of August 27—

Hon. Mr. Phillips: May I have a word before we go on?

Senator Connolly: Yes, certainly.

Hon. Mr. Phillips: We have detailed representations with respect to charitable donations, mining and resource industries, international companies, FAPI, dividends from foreign affiliates and reorganization of foreign affiliates, foreign competition, corporations, shareholders and partnerships.

There are two items that you have included in the highlights which I do not think the committee has had the benefit of hearing interested parties on. They are to be found on page 2, the first and second paragraphs, and at page 7, the short paragraph on income averaging. That short paragraph, to my mind, is quite pregnant to the substance, and I am wondering whether honourable senators will allow you to deal with these two items. We would then have a complete record of the highlights before we get to the details.

Mr. Michael Carr, C.A., Member, Tax Committee, Canadian Institute of Chartered Accountants: Mr. Chairman, perhaps I could speak to these two items. The first one is at page 2 and deals with the disallowance of non-arm's length losses. I believe this is one of the situations in the bill where, in attempting to close possible future loop-holes, there is a certain degree of over-killing, and certain situations which should not be penalized are, in fact, being penalized.

The general rule in the new bill is that when you have a non-arm's length disposition of an asset, in those circumstances, any capital loss on the transaction will not be recognized for tax purposes. This, of course, is to avoid the situation where people might artificially create capital losses for deduction against other income by disposing of assets on a non-arm's length basis. What is proposed is to put a general prohibition in the legislation preventing a deduction of capital losses in those circumstances where it is a non-arm's length disposition.

However, we feel that there are two problems here. In the first place, we feel that the general prohibition should be cut back very substantially, and that the prohibition against the deduction of capital losses should only apply when it is clear that it is not a bona fide transaction or when it is clear that some type of tax advantage is being obtained or being sought to be obtained.

In circumstances where the non-arm's length loss is prohibited because it is perfectly reasonable to do so because of the aim of the tax minimization, we feel that the amount of the loss should, in effect, always be added to the cost base of the person who acquires the asset on a non-arm's length basis. In some circumstances in the bill there are provisions for the adding of this disallowed amount to the cost base. I think it is in the superficial loss area, for example. You do get the addition to your cost base in this situation. However, this is not the case in all of the non-arm's length disposal situations, and we feel that in any

situation where you have a non-arm's length disposition which gives rise to a non-deductible capital loss, that non-deductible capital loss should be added to the cost base of the person who acquires the asset.

Hon. Mr. Phillips: I wonder if the Chairman and honourable senators will have patience with me on this point. The Canadian Bar Association, with you, represents the Canadian Tax Foundation, and I am obviously proud of that foundation for historic reasons. Well, the Canadian Bar Association went into this matter at greater length than you have here, and the question was put to them as to whether the greater part of the problem, or the problem itself, might be mitigated in its adverse effects if we had consolidation. We have had consolidation previously, and it had been recommended some time back by the Bar as well as by the chartered accountants. What is your view on that point?

Mr. Carr: I am appreciative that you asked the question, Mr. Phillips. I think we are definitely in favour of some provisions allowing for the preparation of consolidated tax returns. They certainly would mitigate a great many problems. They would not merely mitigate the one we are discussing now but others as well. However, I do not think they provide a complete solution to this particular type of problem.

Hon. Mr. Phillips: I said "mitigate."

Mr. Carr: Yes, they would mitigate it. They would not completely resolve it.

Hon. Mr. Phillips: In other words, you are still of the view that consolidated tax returns would mitigate the problem covered by this paragraph?

Mr. Carr: In certain intercompany transactions, and in other situations not even covered by this paragraph, it would definitely be an advantage.

Hon. Mr. Phillips: Do you think consolidated tax returns are relevant to the problems we are now facing?

Mr. Carr: Yes, I do.

Senator Connolly: Are we to understand that under the bill as it is now a consolidated tax return is prohibited?

Hon. Mr. Phillips: Yes, of course. It was eliminated some years ago, and it was not reintroduced in this bill.

Senator Connolly: With respect to a parent company and all of its affiliates and subsidiaries, then each one of them has to make a tax return separately.

Hon. Mr. Phillips: Yes.

Mr. Carr: Quite so.

Mr. Brown: That is correct. I should like to make the point that the new provisions make this even much more difficult than the present provisions, because in the past the existence of separate corporations and their adverse tax consequences could sometimes be avoided through the sales of assets or businesses between the companies involved. Under the new provisions this will be extraordinarily difficult in some cases.

Hon. Mr. Phillips: Because of the capital gains tax. Excuse me, Mr. Brown, for interrupting, but I just want to point out to Senator Connolly that the movement of capital assets between parents and subsidiaries becomes all the more complicated because of the introduction of the capital gains tax. I am sorry I interrupted you. Will you continue your thought, Mr. Brown? I was rude there.

Mr. Brown: Not at all. I think that was the basic point. We have always felt the lack of consolidated returns and we feel it much more under the bill's new provisions. There are a number of ways, of course, to effect consolidated returns. The most efficient is simply to allow consolidated returns. Another alternative is to go to the type of subvention payment available in the united Kingdom, where one company in a group can make a payment to another company in the same group. The payment will be deductible by the first company and taxable to the second. It has the effect of transferring the loss from the one to the other when both are members of the same group.

Senator Benidickson: What does that do to tax revenues?

Mr. Brown: I think in the long run it does not adversely affect them. The point is that if you have a corporation which carries on business with two subsidiaries, for example, and one of those subsidiaries has a profit and the other has a loss, then you have to pay taxes on the profit in the one and you do not get any deduction for the loss on the other.

I can give you one glaring example. One of my clients went into the fast food business in Canada, selling hamburgers. He was so ill advised as to have a separately incorporated company created for every stand. He wound up with 130 corporations, a good many of which had losses, although some had profits. Overall, consolidated, he had a profit before taxes, but his tax provision was 400 per cent of his net profit before taxes because he could not offset the losses in some companies against the profits in others.

The Chairman: Well, he was loyal to this advice, anyway.

Mr. Brown: It was not mine!

Hon. Mr. Phillips: If I may be permitted to say so, Senator Benidickson, anything that interferes with the normal, common-sense, routine operation of business, according to sound business principles, in the final analysis affects the revenue adversely.

Senator Connolly: That is very true.

Senator Benidickson: That is good philosophy.

Senator Connolly: Your man here may have been able to make fast foods, but he could not make a fast buck; in fact, he could not even make a buck.

Mr. Carr: Mr. Chairman, we were also asked to deal with an item on page 7, income averaging. This matter was mentioned this morning in the Dominion Foundries and Steel presentation. As the situation stands now, the existing section 36, and certain other provisions allowing averaging, are going to be carried forward for a year or two or three under the new act. If a taxpayer in the next two or three years, in the transitional period, elects to use the old

law, he will not at the same time be entitled to the benefit of the averaging rules which are contained in the new legislation.

The Chairman: I may have read incorrectly, but my understanding there is that the individual who is entitled to a lump sum withdrawal can wait until the withdrawal date and then he can make his own elections.

Mr. Carr: Yes, but by that time I take it that these transitional rules, Mr. Chairman, might be over, and he would no longer have the opportunity of using the old section.

The Chairman: I am talking about what the bill provides.

Mr. Carr: I think the bill merely provides for the use of these old provisions for the next two or three years.

Mr. Brown: It is for two years. There is the provision in the transitional amendments, however, which would allow the use indefinitely of this section 36 averaging, but only with respect to the amount of benefit accrued to the end of 1971. The basic point here is that to prevent individuals who want to take advantage of these transitional section 36 rules to the extent that they are available—and after 1973 they will not be available with respect to the whole payment—to prevent them, when they take advantage of those, from using the other averaging elections results in a very unfortunate incidence of tax.

Mr. Carr: Really, what we are looking for is a somewhat more liberal set of provisions in that respect.

The Chairman: Well, you heard the discussion here this morning. There were some suggestions—that perhaps the Chairman was rash enough to make—to the effect that if they had the best of all worlds they could have their election up to the end of 1971 and get the section 36 averaging. That would require changes in the bill, but the language of bills has been changed before, and they could be given the benefit for any obligations after 1971; they could be given the benefit of the general and forwarding averaging and the capital gain character to the gains.

Mr. Carr: Right.

The Chairman: And their position, they say, would be slightly better than it is now.

Mr. Carr: Oh, really? I did not catch that, but they said that, did they?

The Chairman: Yes. And that would appear to be fair treatment. Is that your view?

Mr. Carr: I think it is a reasonable compromise anyway.

Senator Connolly: I am going to have to read that passage because I did not hear it, but it was a summary of this morning's argument and the witnesses this afternoon agree with it.

The Chairman: Did I interrupt your flow, Mr. Carr?

Mr. Carr: I think I am finished, Mr. Chairman, on the specific matters raised by Mr. Phillips.

The Chairman: In some of these areas of concern we have already moved along pretty far, always looking for additional supporting ideas.

Senator Carter: Mr. Chairman, did not Senator Connolly request some suggestions as to draft legislation?

Mr. Brown: Senator Connolly asked for the provisions or more specific comments with respect to the foreign accrual property income.

Senator Connolly: Do you have some form of words that you would like to suggest?

Mr. Brown: We always like to leave that to the lawyers. I think our comments are made more specifically, if I can find them, on foreign accrual property income and are set out essentially on pages 12 and 13 of our longer brief. I am sorry for the confusion of documents, but that is the longer submission entitled, "Topics for Discussion on Bill C-259" attached at the end of the main document. On pages 12 and 13 we make some specific comments about foreign accrual property income, and make very definite recommendations as to how an approach might be made to get something which would still be within the framework of the Government's intention but which would not work too much hardship on Canadian companies.

The Chairman: You speak about exercising effective control?

Mr. Brown: That is correct.

The Chairman: Is that another way of saying that if the foreign affiliate is a control corporation, then it might be all right?

Mr. Brown: First of all, we say that the foreign accrual property income provisions should be confined to companies which are controlled from Canada, where somebody from Canada has the right to influence the activities of the foreign corporation. Secondly, they should not apply to any type of income which is related to any type of business activity carried on abroad. In some instances this might include rents and royalties and other types of income which, in a technical sense, might be considered property income. Thirdly, we look for some minimum exclusion of this type of income. We do not think the law should reach down to get the last dollar of this type of income, and should only be concerned when it exceeds a certain amount or percentage of active business income.

The Chairman: We have had a suggestion here—and I think it is in the U.S. law—that we should establish a permissible base, and if this type of income does not exceed that base,—and I think it is 30 per cent—it just is not looked at, but if it does exceed the 30 per cent, then you are stuck with the provisions.

Mr. Carr: I think it would be an excellent suggestion. That would avoid the coming into effect of these foreign income property rules in certain cases.

The Chairman: If you read the White Paper, you will find that time after time where the department is speaking, they assimilate passive income and diverted income, and

diverted income has the connotation of tax avoidance. I think the word "passive" income is switched about and the meaning becomes confused, and I think if we stuck to "diverted" income we might be operating in a better area.

Mr. Carr: At the present time, Mr. Chairman, the proposed legislation draws no distinction at all between the incorporated pocketbook in the Bahamas, which is really accumulating investment income which perhaps should be in Canada, on the one hand, and the situation, on the other hand, where for perfectly valid business reasons royalty income is being accumulated offshore from Canada. I think there should be a distinction, and I think it could be done by a definition of active business income which is more liberal than the one we have at the present time.

Hon. Mr. Phillips: We have struggled with a definition of active business income just as, no doubt, you have, and we have more or less ended up by saying that everything is active business income related to active business unless it is diverted income.

Mr. Carr: It might be well to do it that way and then to exclude certain things like dividends, certain forms of interest, and so on.

Mr. Brown: I think the approach followed in the language of some international tax treaties these days is to deal with income which is effectively connected with an active business. This picks up all types of capital gains from the sale of business assets, royalties from the use of business information, and so on, and puts it into business income and not into passive income.

The Chairman: Well, if you have a couple of affiliates abroad and one of them is owned by another subsidiary, and the first is carrying on an active business and the second is more or less a holding company, do you have a flow-through in those circumstances or is the income, when it moves from the second subsidiary over to Canada, investment income?

Mr. Brown: Under the provisions of the bill, the income retains its character if the bottom company is generating active business income. When that company pays its dividend to another affiliate, it retains its character as active business income. However, if the active business income was earned in a non-treaty country after 1976, the mere payment of the inter-affiliate dividend triggers another clause of the bill dealing with inter-affiliate dividends, and that becomes taxable income to the Canadian parent, but not under the passive income rules.

Hon. Mr. Phillips: I think that on page 13 you get a direct answer to your question on the more detailed analysis of passive income, Senator Connolly.

Senator Benidickson: While we are on this exercise of relating the seven-page summary to the longer document, and back to the reference in the summary to charitable donations, I wonder if Mr. Carr could direct my attention to the page in the long basic recommendations that relates to charitable donations. I am referring to page 2 of the summary, and I want to know on what pages of the big document can I find a cross-reference.

Mr. Brown: I invite you to look at page 4 of the long document, under section 69(1)(*b*). We are quite concerned that that provision, over a period of time, will lead wealthy people to be extremely reluctant to leave their works of art, and so forth, to museums and to charities on their death.

Senator Benidickson: Mr. Carr was invited to comment on the section in the summary respecting charitable donations, and then we got on to something else. I do not know whether or not he had anything to add to what was contained in the summary.

Mr. Carr: Thank you, I do not think I can add anything to Mr. Brown's comments.

The Chairman: Then we move along—

Senator Hays: Mr. Chairman, before we leave this point, Mr. Brown suggested that wealthy people upon their death would be reluctant to give away their works of art and so on. I wonder what he thinks they might do with them.

The Chairman: They might sit back and contemplate them.

Senator Connolly: You cannot take it with you.

Mr. Brown: I think the point is that they will be reluctant to leave them to charities if they know that the gift, in effect, is going to be subject to tax which will have to come out of the revenue of the estate. If the beneficiaries have to pay tax, there could be an argument that they might as well have the paintings too, in order to have the assets on which the tax has to be paid.

Mr. Carr: This might be even more of a problem during a person's lifetime, because he would realize that in giving a painting away it has led to taxes of so many thousands of dollars; and I think he would be very reluctant to do this.

Senator Hays: What about the capital gains in this situation?

Senator Connolly: This is a case where capital gains would arise.

The Chairman: I think he would be better off if he sold the painting, and then at least out of the realized proceeds he would have some money to pay capital gains tax. If he gives it away and then has to find the money to pay taxes on it, it is not going to encourage giving things away.

Hon. Mr. Phillips: Mr. Chairman and honourable senators, two important charitable organizations that appeared before us made suggestions other than the ones you are now making. Instead of there being an election, the suggestion is that there be a roll-over similar to a complete exemption on the basis of the gifts that are given, and *inter vivos*, at death a roll-over to the charitable organization, and a deduction in respect of 20 per cent of the taxable income would be confined to the cost of the depreciable assets. I am merely giving you the alternative approach.

Mr. Carr: Yes, with respect, Mr. Chairman, I am not too convinced that there is very much difference between us. Our suggestion is that in these circumstances, where a gift

has been bequeathed to a charity, we suggest that it be valued, at the option of the donor, at any amount not greater than the fair market value and not less than cost. In these circumstances I would imagine the donor would deem the disposition to be the cost. I think this is essentially what the charitable organizations are looking for.

Mr. Brown: The point is if you are talking about an asset with perhaps not a great deal of value, especially with someone in the lower tax bracket, I think they would rather have it at fair market cost because the value of the charitable donation might be worth more to them than the small amount of capital gains tax that they would have to pay on it.

Senator Connolly: I am afraid that I did not follow that very well. Will you give us an example?

Mr. Brown: Let us take a situation where you have an individual who has a painting which he acquired for $1,000, and it increases in value and is now worth $11,000. If he were to give that painting to a charitable organization or a museum he would be deemed to have a realized capital gain of $10,000, on which he would have to pay tax. A tax of 50 or 60 per cent of half of it would amount to $3,000. He would be allowed a charitable donation of $11,000, but whether he could take advantage of that depends on his total income. If his total income is $22,000 his maximum charitable donation is only $4,000. The savings which he would realize through claiming that donation might be around $1,800 or $2,000. The point is that he is then out of pocket because he has made the gift. A person probably would not mind this deemed realization if he had a very substantial income in relation to the value of the gift. He might as well pay the capital gains tax and get the charitable deduction at the fair value. But in circumstances where you are giving away very valuable property in relation to your annual income, the gift will cost you tax dollars.

Senator Hays: How did we treat that, Mr. Phillips, when we were dealing with the example of giving away a summer home?

Hon. Mr. Phillips: The people who appeared before us requested, in effect, a roll-over provision where there would be no deemed capital gain realization on the transfer. In effect, it would simply mean that the donor would then be getting a deduction from his taxable income within the framework of 10 to 20 per cent, only to the extent of the cost on the gift which was given at death. This is instead of the election as provided for on page 4 of the detailed recommendations. Does that answer your question?

Senator Hays: Yes.

The Chairman: Can we move along now? I was wondering what your thoughts were, Mr. Brown, in connection with the points for discussion. Around one-third of these points have been dealt with in some way by the amendments. They may have been badly dealt with by the amendments. But for our purposes, if we assume that there is something less than all these sections that you have referred to that we need to look at, if you have an eliminator, you might proceed to do the eliminating.

Mr. Brown: Yes, this is a long document. I have one copy here, and we have gone through it and have eliminated all the points which we feel have been dealt with by the Government. I would not wish to read all of this at the moment because it would take some time, but I would be very happy to leave this copy with you.

The Chairman: Would you do that?

Mr. Brown: Certainly. As I have said, the Government has dealt with perhaps one-third or less of the points in our detailed memorandum. Some of the other points have probably become obsolete due to other changes. In one or two cases, quite frankly, we were so rushed into making our comments that the comments themselves were perhaps in error. But we have stroked off all the points which have been dealt with in one way or another. And there remain a very substantial number of technical areas which we think should warrant further consideration. I think some of these points may appear to be relatively technical. We are very much concerned that under a self-assessment system, that depends on taxpayer morality, the taxpayers must be convinced that the system is fair, and they must be convinced that the Government is anxious to see that the system is fair. Even an anomaly which would affect only a relatively few people should be looked into and corrected.

Hon. Mr. Phillips: Mr. Chairman, could I suggest that Mr. Brown send to you, as chairman of this committee, a revised copy of the items which are still outstanding, in other words, eliminating one-third of the points which have been dealt with? Then the chairman, at his discretion, can deal with that material with this committee.

Mr. Brown: We would be more than pleased to do so. I apologize for not having had an opportunity to do that before this meeting but, as you realize, a number of the amendments were just out last week and they are of such a technical nature that one would require several days to ponder them in order to appreciate their implications.

The Chairman: I also understand that the document we have before us is already in the hands of the Department of Finance. Is that correct?

Mr. Brown: That is correct; it has been in their hands since August 27.

The Chairman: In other words, they are aware of all of these items.

We have been giving some thought as to whether we should not have one preliminary report which would deal with the technical changes, in the same way as you have started here and, having done that, we could very well say, "Attached hereto is a list prepared by the Canadian Institute of Chartered Accountants, a copy of which has been in your possession for some months".

Senator Benidickson: Since a specific date.

The Chairman: Yes. With these technical changes we are not likely to say that it should read differently from what you say.

Mr. Brown: As I say, Mr. Chairman, on further sober reflection, we have discarded some of them, but, I would say at least half of them remain outstanding at the present time.

The Chairman: That is the list I want.

Mr. Brown: We will see that you have it within a short time.

The Chairman: Yes, because we only have a short time.

Senator Macnaughton: That will be made an appendix, will it?

The Chairman: No. It will be filed with us, and the purpose I had in mind, subject to what the committee may say, was that we would have one report which would deal with the technical changes and we would attach this document that we get, disclosing the authors of it and drawing to the attention of the Department of Finance the fact that they have had it in their possession for some months and we recommend it quite strongly as requiring some correction.

Senator Benidickson: Not necessarily approving it holus-bolus.

The Chairman: No. I feel we can recommend it. If the Canadian Institute of Chartered Accountants makes recommendations on the technical language, I am prepared to assume that there is merit in the recommendations.

Senator Benidickson: I would agree with you.

The Chairman: That does not mean I am prepared to assume that what they have suggested is the correct and only way to deal with a specific problem, but I feel it does raise a point for them to look at.

Senator Benidickson: And the fact that it has been in their hands since August 27 with the result that only about 50 per cent have been subject to either amendment by the minister or have been discarded upon further reflection by the institute, raises, I feel justifiably on our part, a query as to what was wrong with the other 50 per cent.

The Chairman: It is also subject to the assumption by us, and justifiably so, that they did not simply pick and choose from this list; they must have gone through the list and seized on the ones that they were ready to accept and put into these amendments, so obviously they have been studying it.

Senator Macnaughton: We are printing the pages on areas of major discussion?

The Chairman: Yes, we will be printing the seven pages.

Senator Macnaughton: And in due course the institute will file revised points for discussion with the committee?

The Chairman: Yes, and if honourable senators would like to have copies of it, we will see they are distributed.

Senator Macnaughton: I feel we should.

The Chairman: We may add a great deal to the sum total as a result of this.

Mr. Brown: I would like to make it clear that because we proposed approximately 150 amendments to the tax legislation, we should not sssume that the institute was omniscient. I feel there are probably additional areas which we did not pick up and which other associations, such as the Bar Association and the Canadian Chamber of Commerce, may have recognized and your committee in its work has recognized. Furthermore, we cannot guarantee that all the points we did pick up were correctly dealt with, but these points were arrived at as a result of considerable discussion by groups of chartered accountants across Canada. What we would like to see happen is that these points do receive some consideration and review in order to determine whether these is any merit to them.

The Chairman: We can recommend that this be done. We just do not have the time to take each one of these and relate it to the section of the bill and make a decision as to whether it should go one way or the other.

This is our first run before the bill comes to us. We are just looking at the subject matter. We will have a second run when the bill is before us, and we will see what they have done to that point. If they have not heeded some of the recommendations we have made, there may be some firm discussion, because there is no question about the authority that we have; it is a question of our using it.

Are there any other points you would specifically like to deal with at this time, Mr. Brown?

Mr. Carr: I think not, Mr. Chairman, speaking for myself, because if we start going through the detailed 31-page memorandum with which you are going to be provided, it would be difficult to know where to draw the line.

The Chairman: You do not feel that we are shutting off or snuffing out some information in relation to some of the sections of the bill that we should particularly look at in a way other than the way we are proposing to do it?

Mr. Brown: I do not believe so. I feel the bill is an enormously technical document, and once you get into the particular sections of it and their implications the discussion does become one where, perhaps, one would like to sit down all by one's self and go through it until one understands the language rather than having a committee meeting on it.

What we are concerned with, and we emphasize this again, is that we hope, that by bringing forward constructive ideas, in as disinterested a way as we possibly can, we can improve the tax legislation. We are concerned that it has been brought forward in something of a hurry, and we believe that there were a number of technical deficiencies of almost staggering proportions in the bill when it was first introduced in June. A good many of these, of course, have been corrected, but some remain.

Senator Benidickson: I am glad to hear that, because I have heard some comments that the amendments were of little significance, except in, shall I say, narrow areas.

Mr. Brown: The amendments the Government has introduced to date have solved a number of important problems. For example, one that was put in just last week gives professional people—lawyers and accountants—who have an interest in a partnership, for the first time under this provision, a cost base for capital gains tax purposes equal to what they paid for the partnership asset. That, I feel, is of great significance to some of our members, and we are very glad to welcome that change in the tax law.

What we are essentially concerned with are the technical matters. For example, to bring home something directly to the point, you will not find in our representations any comments about the accrual basis of taking up income for professional practice. We had a great many words to say about that when it was a policy issue, but now that the issue has been decided in the legislation before Parliament, we are silent on the matter. We are simply concerned with the technical implications.

Senator Benidickson: But you have not changed your views?

Mr Brown: No, we have not.

The Chairman: Is there anything further?

Mr. Brown: No, I do not believe there is, Mr. Chairman. We will see that this document is in your hands within two days.

The Chairman: Thank you very much, gentlemen.

The committee adjourned.

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THIRD SESSION—TWENTY-EIGHTH PARLIAMENT

1970-71

THE SENATE OF CANADA

STANDING SENATE COMMITTEE ON

Banking, Trade and Commerce

The Honourable SALTER A. HAYDEN, *Chairman*

No. 47

THURSDAY, NOVEMBER 4, 1971

Preliminary Report

on

The Summary of 1971 Tax Reform Legislation

24295—1

MEMBERSHIP OF THE COMMITTEE

THE STANDING SENATE COMMITTEE ON BANKING, TRADE AND COMMERCE

The Honourable Salter A. Hayden, *Chairman,* and

The Honourable Senators:

Aird	Grosart
Beaubien	Haig
Benidickson	Hays
Blois	Isnor
Burchill	Lang
Carter	Macnaughton
Choquette	Molson
Connolly (*Ottawa West*)	Smith
Cook	Sullivan
Croll	Walker
Desruisseaux	Welch
Everett	White
Gelinas	Willis
Giguere	

Ex officio members: Flynn and Martin

(Quorum 7)

Order of Reference

Extract from the Minutes of the Proceedings of the Senate, September 14, 1971:

"With leave of the Senate,

The Honourable Senator Hayden moved, seconded by the Honourable Senator Denis, P.C.:

That the Standing Senate Committee on Banking, Trade and Commerce be authorized to examine and consider the Summary of 1971 Tax Reform Legislation, tabled this day, and any bills based on the Budget Resolutions in advance of the said bills coming before the Senate, and any other matters relating thereto; and

That the Committee have power to engage the services of such counsel, staff and technical advisers as may be necessary for the purpose of the said examination.

After debate, and—

The question being put on the motion, it was—

Resolved in the affirmative."

Robert Fortier,

Clerk of the Senate.

24295—2

Thursday, November 4, 1971

INTRODUCTION

On September 14, 1971 there was tabled in the House a document entitled "Summary of 1971 Tax Reform Legislation" and on the same date, by resolution of the Senate, consideration of same was referred to the Standing Senate Committee on Banking, Trade and Commerce.

For the purposes of brevity and identification, the "Summary of 1971 Tax Reform Legislation" will be referred to in this report as the "proposed legislation" and the Standing Senate Committee on Banking, Trade and Commerce will be referred to as "your Committee" or "the Committee".

The Committee would like to take the opportunity at this time to commend the Government in respect of many of its proposals pertaining to individuals, in particular for the reduction in taxes, the increased personal exemptions for both single and married taxpayers and for taxpayers aged 65 and over, the allowance of a deduction for child care expenses, the deduction for moving expenses occasioned by a job change and the increased deductions for pensions and charitable contributions. Your Committee also notes with approval the allowance of a deduction by corporations of interest paid on money borrowed to acquire shares of other corporations. W would further commend the Government for modifying many of the proposals put forward in the "White Paper Proposals for Tax Reform" in response to the many representations made in respect of same.

Pursuant to the order of reference dated September 14, 1971, your Committee has heard a number of representations and has received a number of written submissions on the proposed legislation. Having studied the various representations which have been heard or received up to and including the 27th day of October 1971, your Committee has concluded that it is desirable to submit to the Minister of Finance, as expeditiously as possible, a number of recommendations in respect of the proposed legislation which is presently being considered by Committee of the Whole in the other House. It is the hope that, upon the receipt by the Minister of Finance of these recommendations, the same will be accepted by him as being pertinent and relevant, and to the extent so regarded, that appropriate amendments will be submitted by him to the other House while the said proposed legislation is being considered in the Committee stage.

Having regard to the urgency of the matter and the problem of time, your Committee is submitting for your approval at this time a limited number of recommendations but it is hoped that the Committee will still be in the position to make further recommendations before the proposed legislation reaches this House. Alternatively, the Committee will submit these further recommendations when the said proposed legislation reaches this House after having passed the other House.

The proposed recommendations are hereinafter submitted in seriatim form.

IMPACT ON THE CONTINUING VIABILITY OF CANADIAN MULTINATIONAL CORPORATIONS—THEIR DOMESTIC AND FOREIGN OPERATIONS THROUGH FOREIGN AFFILIATES, THEIR NEED FOR SUCH FOREIGN OUTLETS TO MAINTAIN HIGHER LEVELS OF EMPLOYMENT IN CANADA, THEIR CAPITAL NEEDS IN CANADA AND ABROAD AND THEIR COMPETITIVE POSITION IN WORLD MARKETS

Your Committee is deeply concerned with the possible effect of the proposed legislation on the competitive position of Canada's international corporations in world markets. To the extent that Canada's world trading position is adversely affected, it follows that our economic growth as a whole must likewise suffer.

A. Passive Income

One of the areas which gives rise to this concern is that relating to the treatment of income earned abroad by Canadian residents and their foreign affiliates. The principal purpose of these provisions is to prevent Canadian residents from avoiding or unduly deferring Canadian income tax on passive income such as dividends, interest, rents, royalties and certain types of capital gains by diverting such income to a non-resident corporation or trust and allowing the non-resident corporation or trust to accumulate such income abroad instead of repatriating it to Canada.

To prevent any possible abuse in this regard, it is proposed that Canadian residents (both corporate and individual) will be obliged to include in income their "participating percentage" of any diverted income earned by a non-resident corporation or trust which is "affiliated" (as defined) with the Canadian taxpayer. This income must be taken into account each year by the Canadian resident whether or not received in the year from the foreign affiliate.

Most certainly, the objective of attempting to thwart tax avoidance is a valid one. However, the anti-avoidance rules relating to diverted income are extended in such an indiscriminate manner as to encompass not only diverted income but also all passive income of foreign affiliates even though the affiliates are established for bona fide business purposes and are not established or used for the purpose of diverting passive income abroad in order to avoid or unduly defer Canadian income tax.

This is particularly unfortunate in the light of the fact that the proposed legislation does not define what income is to be excluded from the diverted income rules as being "active business income". Because of this, there is a serious danger that income such as interest received by a foreign affiliate on short term deposits or on trade receivables and royalties received by such an affiliate in respect of patents or know-how developed by it abroad in the course of its active business operations (to name but a few) may be taxed currently in the hands of the Canadian shareholder as diverted income even though such income is in fact directly attributable to the foreign affiliate's active business. Such income is not diverted income.

Further, it has been noted that international corporations are not infrequently obliged by the laws of a foreign country to carry on their business operations in that country through a foreign affiliate which is controlled by residents of that country. In circumstances such as these, the fact that the foreign affiliate earns passive income is often a matter which is beyond the control of the Canadian international corporation and is therefore not motivated by tax avoidance considerations. Nevertheless, in the absence of adequate de minimis relieving provisions in the proposed legislation, the Canadian international corporation will be subject to Canadian income tax on its "participating percentage" of such passive income.

This indiscriminate extension of the diverted income rules to include all passive income of foreign affiliates is further aggravated by the following:

1. Because of the manner in which the term "participating percentage" is defined, the amount taxable in a Canadian shareholder's hands under the passive income rules may, in some instances, be greater than the portion of the foreign affiliate's passive income that actually accrues to his benefit; this could occur where the foreign affiliate is not wholly-owned by one Canadian taxpayer and there is more than one class of shares of capital stock outstanding (treating certain income debentures as capital stock for this purpose).

2. No provision has been made in the proposed legislation to allow a taxpayer to apply losses sustained in one year in respect of a passive income source against passive income "earned" in other years under a loss carry-over provision.

Even if the assimilation of passive income with diverted income could be justified, the above-described defects should be rectified.

B. Dividends received from foreign affiliates

Your Committee is also concerned with one other matter that is inherent in the proposals relating to international income. It is intended that the treatment to be accorded to dividends received from foreign affiliates will differ according to whether the foreign affiliate is, or is not, located in a country with which Canada has a tax treaty.

Your Committee has difficulty in appreciating the reason for this difference in treatment. Until such treaties are negotiated, uncertainty will prevail. This can only have an unsettling effect on our trading and business operations abroad. Quite apart from this, it offends your Committee that business decisions should be influenced by the government's success, or lack of success, in negotiating tax treaties. Our international trading position should not be either jeopardized or used as a means of bargaining between governments.

In this connection, while the Committee is aware of the Government's intention to provide tax-sparing relief with respect to operations established in developing countries pursuant to commitments entered into prior to 1976, nevertheless, we cannot agree with the taxing of dividends from affiliates operating in non-treaty countries. Many of these countries are developing nations which offer tax incentives to foreign corporations. Canada should not tax away these incentives and reduce their value to Canadian corporations.

C. Other considerations

As a result of the foregoing proposals, the after-tax return to Canadian international corporations from foreign business operations will be reduced and their competitive standing in world markets will be prejudiced. If this occurs, the effect may be to discourage foreign business operations and, having regard to Canada's dependency on world trade, the curtailment of these operations can only have an adverse effect on our own economic growth. Further, any such restriction on foreign business will reduce the support for marketing and research facilities in Canada, which again will worsen our competitive position abroad. Needless to say, the demand for technical skills and other employment opportunities will be reduced, compounding our present unemployment position.

In voicing its concern about the impact of these proposals on employment opportunities in Canada, your Committee is not unmindful of the fact that two of Canada's largest international corporations who appeared before the Committee and who stated that they would be adversely affected by those proposals are understood to employ approximately 25,000 Canadians. As is well known, any loss of employment in a particular sector of the economy such as this has a ripple effect on the economy as a whole and must inevitably lead to further unemployment. Copies of the briefs submitted to your Committee by the two above-mentioned corporations were forwarded to the Department of Finance at its request.

It is imperative that we, as a nation, do not lose sight of the fact that Canada is one of the major trading countries of the world and that the encouragement of Canada's international corporations in their efforts to expand world markets is of the greatest national importance and the highest priority. Any measures such as those contained in the proposed legislation which inhibit these efforts are to be deplored, particularly in view of the fact that these proposals run counter to the patterns being set by other developed nations. For example, the effect of the proposals recently put forward by the United States government with respect to domestic international sales organizations (commonly referred to as the DISC proposals) would be to defer payment of U.S. income tax until dividends are distributed.

Indeed, the Government in its original approach to the taxation of foreign source income, as outlined in its White Paper Proposals for Tax Reform (1969), conceded that Canadian international corporations should not be placed at a competitive tax disadvantage. At page 72 (paragraph 6.9) of the White Paper it is stated:

"On the other hand, Canadian business is often required to go abroad to seek foreign sources of supply and to develop foreign markets. Going international is frequently necessary to enable Canadian companies to achieve the economies of scale which are otherwise denied to them by the relatively small size of the Canadian domestic market. Such companies would find it hard to compete on the international scene if they were sub-

ject to more onerous taxes than those which apply to their competitors."

In addition to all of the foregoing, recent comments of the Minister of Finance indicate that the Government is also aware of difficulties that may be encountered when he stated as follows:

"We have already received a number of representations relating to the passive income provisions and it seems clear that some changes to the law as necessary should be made before the provisions take effect. However, we have concluded that it would be premature to introduce changes at this time before all representations have been received and given the study they require."

YOUR COMMITTEE RECOMMENDS the following:

I A. Foreign accrual property income (passive income)

That the Government give renewed consideration to the "foreign accrual property income" (FAPI) rules with a view to making at least the following changes:

(*a*) that the definition of the term "foreign accrual property income" be amended to exclude from the category of income which is subject to the foreign affiliate rules any income or capital gains from property that may reasonably be regarded as having been used for the purpose of gaining or producing income from an active business; or, that the term be redefined in such other manner as to ensure that the overall thrust of the foreign accrual property income provisions will be restricted so that the income subject to these rules will include only diverted income; in the result, that income such as interest on short-term deposits, interest on trade receivables, gains on the disposition of capital property used in a bona fide business operation and other like items will not be classed as foreign accrual property income.

(*b*) that the de minimis rule contained in the proposed legislation be broadened to the effect that the passive income rules will not apply to any foreign affiliate whose passive income does not exceed a specified percentage of its total gross revenue (such as the 30 per cent rule in the United States); alternatively, the de minimis rule may be expressed as a percentage of the foreign affiliate's gross assets.

(*c*) that the term "foreign affiliate" be re-defined for purposes of the foreign accrual property income rules to include with respect to foreign corporations only those corporations which are controlled directly or indirectly in Canada.

B. Dividends received from foreign affiliates

That the proposed differentiation in treatment of dividends received from foreign affiliates, depending on whether the foreign affiliate is located in a treaty country or non-treaty country, be eliminated and that all dividends received by resident corporations from foreign affiliates be exempt from tax. In any event, your Committee can find no valid reason for the failure to provide a tax credit in respect of foreign withholding taxes on dividends from non-treaty countries.

II. That the Government announce any changes in these provisions at the earliest opportunity and, pending same, that the effective date of the passive income rules which are to commence with respect to passive income earned in taxation years commencing after December 31, 1972 be deferred in their implementation for a period of at least one further year to December 31, 1973.

In conclusion, your Committee feels constrained to reiterate the views expressed by it in its Report on The White Paper Proposals for Tax Reform condemning the implications inherent in the Government's proposals that vast tax avoidance schemes exist through the use of foreign entities. As stated in its Report, the Committee believes that tax avoidance of this kind can be effectively blocked under existing legislation and failure to block such abuses (if they exist) is due more to lack of enforcement of existing law than to lack of legislation.

FARMERS

A. Basic herds

At the present time, farmers who maintain a permanent herd of animals for the purpose of producing livestock or livestock products for sale are construed as having a capital asset in the form of a "basic herd". This treatment has been sanctioned by the Department of National Revenue in its "Farmer's & Fisherman's Tax Guide" which sets out rules for establishing and enlarging basic herds. In other words, the brood animals forming part of the basic herd are analagous to other capital assets of the farmer such as land and orchards and to the fixed capital assets of any other business.

Under the proposed legislation, it is intended to abolish the concept of the basic herd and to treat such herds as inventory or stock-in-trade. Under the transitional rules, basic herds which have already been established will continue to be treated as capital assets to the extent that gains accrued at the commencement of the new system will not be subject to tax. However, gains accruing thereafter will be treated in the same manner as profits on the sale of inventory.

Your Committee is not aware of any reason for not continuing to recognize a permanent herd for what it is, namely, a capital asset.

YOUR COMMITTEE RECOMMENDS that provision be made in the proposed legislation for the continued recognition of a farmer's permanent herd as a "basic herd" and, therefore, as a capital asset.

B. Capital gains and farm land

Your Committee is of the view that farmers occupy a special position in the economic structure of this country. Over the years, this sector of the economy has become increasingly subjected to pressures which have led to a profound change in the nature and use of farm lands. Your Committee is concerned by this trend and believes that measures should be taken to reverse it.

YOUR COMMITTEE RECOMMENDS that consideration be given to extending the rollover provisions to permit land together with any other capital property which is used by an individual in a farming activity to be transferred, either during lifetime or on death, to lineal ascendants or descendants without being subject to capital gains treatment under the deemed realization provisions. This exemption should only be available in those circumstances where the transferee or transferees continue to carry on the farming activities.

EMPLOYEES PROFIT SHARING PLANS

Under present law, an employee who is a beneficiary under an employees profit sharing plan is taxed in the same manner as an employee who receives a profit sharing bonus directly from his employer and invests the money received. In summary, the employee's position is as follows:

1. the employee is taxed annually on any amount which his employer contributes to the plan on his behalf in the same manner as he would have been if he had received a bonus of an equivalent amount directly;

2. the employee is not allowed a deduction in respect of any contributions which he himself may pay into the plan;

3. the employee's share of the income earned each year by the plan is taxed annually in his hands; and

4. amounts received by the employee out of the plan (whether on retirement or otherwise) are, in general, non-taxable since these amounts will normally have been taxed previously.

Under the proposed legislation, the same general rules will apply. However, with the taxation of capital gains, the employee will also be taxed annually on his proportionate share of one-half of the net capital gains realized by the trust in each year (excluding any protion accrued prior to January 1, 1972) as well as on his share of the income earned by the trust in the year. In addition, provision is made in the proposed legislation with respect to the taxation of any unrealized gain on capital property distributed in specie to an employee on his withdrawal from the plan. Under these provisions, the employee is subject to tax in the year of his withdrawal on any accrued gain in respect of the property received from the trust (excluding any portion accrued prior to January 1, 1972) but it would appear from the proposed legislation that such accrued gains will be treated as ordinary income rather than as capital gain.

Quite evidently, these accrued gains should at least receive capital gain treatment and this should be clearly stated in the proposed legislation. However, even this treatment is unsatisfactory inasmuch as it places a member employee at a severe disadvantage vis-à-vis an employee who invests after-tax earnings directly. In the opinion of your Committee, capital property which is in substance the employee's property should not be considered as having been realized at fair market value on distribution to the employee. The deferral of gain would be consistent with the treatment to be accorded to a capital beneficiary of an ordinary trust.

YOUR COMMITTEE RECOMMENDS the following:

1. that where property is distributed in specie to an employee by the trustee of an employees profit sharing plan, the trustee should be deemed to have disposed of the property for proceeds equal to its cost amount (as defined) to the trust;

2. that the employee should be deemed to have acquired the property at the cost amount to the trust; and

3. that the employee should not be taxed until he ultimately disposes of property, at which time any gain should be subject to capital gains treatment.

DEFERRED PROFIT SHARING PLANS

The tax treatment of deferred profit sharing plans differs from the treatment accorded employees profit sharing plans. The provisions of the present law relating to deferred plans are, in summary, as follows:

1. the employee is not taxed currently on any amounts which his employer may contribute to the plan on his behalf nor on the income earned in the year by the plan; and

2. instead, the employee is subject to tax on the full amount received on his withdrawal from the plan minus any portion representing a refund of contributions paid by the employee into the plan; the exclusion of the employee's contributions follows from the fact that the employee is not allowed a deduction for contributions but is obliged to make these payments out of tax-paid dollars.

It is significant to note that the amount taxable as income in the employee's hands represents not only his share of (*a*) the employer's contributions, and (*b*) the income earned by the plan, but also (c) his share of any net capital gains of the trust. This treatment has been acceptable to member employees partly because of the tax deferral feature inherent in these plans but also in large measure because the employee has the right to avail himself of the special tax averaging provisions of Section 36 of the present Income Tax Act in respect of a lump sum payment received on his withdrawal from the plan.

Under the proposed legislation, the lump sum distribution from the plan will continue to be treated as ordinary income whether the distribution is made from employer contributions, income accumulated by the trust, capital gains realized by the trust or unrealized gains in respect of property distributed in specie to the employee.

However, the tax averaging provisions of Section 36 of the present Act are not carried forward into the proposed legislation in respect of amounts accumulated by the trust after 1971. Instead, these provisions are to be replaced by averaging provisions which, for purposes of members of deferred profit sharing plans, appear to be quite inadequate. In this regard transitional provisions are to be introduced to permit employees to take advantage of an averaging provision equivalent to Section 36 of the present Act in respect of amounts accumulated in the trust up to December 31, 1971. However, if such an election be made by an employee, he cannot avail himself of either of the

proposed averaging provisions (general or forward) in respect of that portion of the amount accumulated in the trust after December 31, 1971. Also, in future years, the transitional rule will be of diminishing benefit.

The general and forward averaging provisions available under the proposed legislation are not only much less generous than the elective provision under section 36 of the present Act, but the requirement to purchase an income averaging annuity in order to obtain forward averaging in effect removes the basic purpose of a deferred profit sharing plan, i.e. the accumulation of a lump sum on retirement.

In the opinion of your Committee, the effect of the proposed legislation will be to legislate these plans out of existence. Relief should be granted; the most appropriate means of achieving this relief is by the application of capital gain rules to the property of the trust.

YOUR COMMITTEE RECOMMENDS the following:

1. that any amount distributed by the trustee of a deferred profit sharing trust out of capital gains realized by the trust should qualify for capital gains treatment in the employee's hands;

2. that where property is distributed in specie to an employee by the trustee, the trustee should be deemed to have disposed of the property for proceeds equal to its "cost amount" (as defined) to the trust;

3. that the employee should be deemed to have acquired the property at the "cost amount" to the trust; and

4. that the employee should not be taxed until he ultimately disposes of the property, at which time any gain should be accorded capital gain treatment.

DEEMED DISPOSITION ON CEASING TO BE A RESIDENT OF CANADA

One of the provisions of the proposed legislation which has occasioned widespread concern is the Government's proposal that taxpayers who emigrate from Canada will be deemed for capital gains purposes to have disposed of all of their capital assets (other than "taxable Canadian property") for an amount equal to the fair market value of the property at the date of their departure. Any taxable capital gain (or allowable capital loss) determined by reference to such fair market value must then be taken into account in computing the emigrant's income for tax purposes for the year in which he ceases to be a resident.

One of the effects of these provisions is that a taxpayer who leaves Canada to take up residence abroad will often be subject to double taxation—first in Canada in the year in which he ceases to be a resident and secondly in his new country of residence in the year in which he ultimately disposes of the property. This will occur if the foreign country imposes tax on capital gains (but does not have a provision similar to that contained in the proposed legislation to the effect that there is a deemed acquisition on becoming a resident) and if the tax payable in one country is not available as a credit against the tax payable in the other. The only possible relief in such a situation would be by way of tax treaty and, in your Committee's opinion, this type of relief is unlikely as we know of no other country which uses an accrual basis of accounting for capital gains upon entering or leaving the country. Failure to provide adequate relief runs counter to the principle in our law that doulbe taxation is to be avoided.

The proposed legislation does provide an alternative to the foregoing. Instead of paying tax on his deemed gains as aforesaid, the taxpayer may elect to defer taxation until the year in which the gains are actually realized. However, if such an election is made, the taxpayer will be subject to Canadian income tax in the year of realization on his world income for that year (and not simply on the capital gain) to the same extent as if he were still a resident in Canada. This alternative will often prove unduly harsh insofar as it applies to persons who are not in fact resident in Canada when the gain is realized. For example, a taxpayer who has ceased to be a resident of Canada may find himself in the position of having to pay a substantial amount of Canadian income tax under these provisions in the year in which such a gain is realized even though the amount of the gain be nominal.

Your Committee notes that the problem alluded to in the preceding paragraph only arises in respect of property other than "taxable Canadian property". It is important to realize that a taxpayer who leaves Canada and who has assets consisting of "taxable Canadian property" is not subject to the aforementioned rule. When he subsequently becomes a non-resident, he may dispose of his "taxable Canadian property" and, although subject to tax, the tax is calculated on the basis that he has no income other than his gain on the disposition of his "taxable Canadian property". Unless the taxpayer is otherwise deemed to be a resident of Canada, it is obvious that this rule has quite different tax effects from those which would apply is the same taxpayer also had property other than "taxable Canadian property". In the latter situation, the taxpayer will be subject to Canadian income tax in the year of realization on his world income. Your Committee does not appreciate the necessity for such a difference in tax treatment.

There are other anomolies such as the lack of carry-forward provisions in the event of capital losses.

Your Committee also considers it unfortunate that no allowance has been made in these provisions for the many exceptional circumstances which are bound to occur; for example, where the taxpayer is forced to leave Canada for health reasons or by reason of a transfer abroad at the request of his employer.

YOUR COMMITTEE RECOMMENDS:

1. that provision should be made to enable the Minister of National Revenue to grant relief if, in his opinion, hardship will result and the departure is occasioned

(*a*) by reason of illness;

(*b*) by reason of the transfer of an employee at the direction of the employer; or

(*c*) by any other reason which the Minister considers deserving of relief.

2. that when a taxpayer ceases to be a resident of Canada he should be deemed to have disposed of all his capital assets, wherever situate, for an amount equal to fair market value and that a fixed rate of tax, say of 20 per cent, be levied on any gains at that time; and

3. that if the taxpayer elects to defer payment of tax as provided for in the proposed legislation, he should not be obliged to pay Canadian income tax on his world income if he is not in fact resident in Canada in the year of realization; instead, all of the capital property owned by the taxpayer at the date of his departure should be deemed to be "taxable Canadian property" and the taxpayer should be subject to tax on any taxable capital gains realized in respect thereof in the same manner as other non-residents.

GIFTS, BEQUESTS AND DEVISES TO CHARITIES—DEEMED REALIZATION

The proposed legislation provides that all capital property (other than depreciable assets) owned by a taxpayer at the date of his death will be deemed to have been realized at its then fair market value and any capital gain or loss shall be included in income for that taxation year. In the case of depreciable property, there will be a deemed realization at midway between fair market value and undepreciated capital cost. A similar rule is proposed in respect of gifts inter vivos. There is an exception to the general rule where assets are transferred on death or by way of inter vivos gift to a spouse or to certain trusts in favour of a spouse. In the latter circumstances, the transferee is considered to have acquired the property at an amount equal to the "cost amount" of the property to the transferor.

Your Committee is concerned that no exception has been made in respect of gifts, bequests or devises to registered charitable organizations or to other similar tax-exempt organizations. By way of contrast, gifts, bequests and devises to such organizations are not subject to tax under the present Estate Tax Act nor under the provincial succession duty Acts. Your Committee therefore considers it unreasonable that a taxpayer should be subject to an income tax on a deemed realization when making a gift, bequest or devise to a charitable organization or to other similar tax-exempt organizations.

Your Committee appreciates that, in some circumstances, it may be more beneficial from an income tax point of view to accept a deemed realization of an amount equal to the fair market value of the subject matter of a gift and claim a deduction for the full market value thereof. On balance, however, your Committee believes that the legislation should be neutral in respect of any tax benefits resulting from the making of a charitable gift (except as otherwise provided).

YOUR COMMITTEE RECOMMENDS that the proposed legislation be amended to provide that, where capital property is transferred to a charitable organization or other similar tax-exempt organization by way of gift, bequest or devise, the taxpayer will be considered to have disposed of the property for an amount equal to the "cost amount" thereof to him.

MINING AND PETROLEUM

Since the majority of provisions of the proposed legislation affecting the resource industries are to be implemented by amendments to the Income Tax Regulations, most of the comments which follow refer to the news release of the Department of Finance dated July 6, 1971. That document outlines the regulations proposed to apply to the mining and petroleum industries.

A. Earned Depletion

The proposed legislation will remove the automatic 33 1/3 *percent depletion presently permitted under the Income Tax Act; it is to be phased out gradually over the next 5 years. Automatic depletion will be replaced by the concept that depletion must be earned by incurring exploration and development expenditures. The formula adopted will be that for every $3 of eligible expenditures made after November 7, 1969 a taxpayer would earn the right to deduct $1 of depletion in computing his taxable income after 1976, subject to a maximum of 33 1/3* percent of net production profits.

The proposed regulations define expenditures which will be eligible to earn depletion as including the following:

(*a*) Canadian exploration and developments expenses, except for:

(i) the acquisition cost of Canadian resource properties,

(ii) costs in respect of such community and transportation facilities as houses, schools, hospitals, sidewalks, roads, sewers, sewage disposal plants, airports, docks and similar property (other than a railroad not situated on the mine property) acquired to establish community and transportation facilities necessary for the operation of the mine,

(iii) Canadian exploration and development expenses in the vicinity of the mine after it came into production, and

(iv) interest on funds required to finance exploration, prospecting and development.

(*b*) New depreciable mine assets (ie. a building except an office building that is not situated on the mine property; mining machinery and equipment; and electrical plant set forth in Class 10 of Schedule B by virtue of subsection 1102 (9) of the Income Tax Regulations in connection with a new mine or a major expansion of an existing mine), and

(*c*) Expenditures on new buildings and machinery, to the extent that they are to be used to process ore from Canadian mineral resources beyond the stage to which they were previously processed in Canada, up to but not beyond the prime metal stage or its equivalent.

Expenditures for the acquisition of Canadian resource properties should, in the opinion on your Committee, qualify to earn depletion. The acquisition of such properties is an integral part of exploration and development expenditures: indeed it is the first step in any exploration or development program. Your Committee recognizes, however, that the inclusion of the cost of Canadian

resource properties as expenditures which would be eligible to earn depletion would require that safeguards be inserted into the proposed legislation to prevent the buying and selling of such properties between related taxpayers to artificially earn depletion. One suggestion would be to deduct $1 of the transferor's earned depletion for each $3 of proceeds of disposition. If the transferor had no earned depletion capable of the reduction, it could be subject to recapture of depletion previously allowed.

Following the publication of the White Paper on Tax Reform, the Department of Finance issued a news release dated August 26, 1970 which contained a letter from the Minister of Finance to the provincial ministers of finance and treasurers. That document stated that the government was "prepared to propose three further important changes affecting the taxation of the mining industry".

The first two changes were to widen the definition of expenditures which would qualify for "earned depletion" to include

(1) "the costs of new facilities located in Canada to process mineral ores to the prime metal stage or its equivalent"; and

(2) expenditures "for mine buildings, and machinery and equipment acquired in connection with a major expansion of an existing Canadian mine. This extension would put the major expansion of an existing mine on a roughly comparable tax footing with the opening of a new mine."

Your Committee heard evidence of expenditures of the type set forth in that letter which were incurred by reason of the acceptance by mining companies of the above-proposed changes. In your Committee's view, the mining industry was entitled to accept the government's proposals at their face value, namely as being "further important changes affecting taxation of the mining industry". In effect the government represented that the changes proposed in its news release of August 26, 1970 would be implemented in legislation and Regulations so that the mining industry might more immediately undertake the opening of new mines and the major expansion of existing mines in the interest of expanding employment and the national economy. One witness stated that his company had incurred expenditures of $120 million in expanding its production facilities, $30 million of which were spent on major smelter and refinery expansions. The Company made public its reliance on the August 1970 changes to the White Paper when it announced that expansion. The government did not at that time contradict what was apparently the clear intention of its news release.

However in the proposed regulations released on July 6, 1971 there appears the statement that "expenditures on *new* buildings and machinery, to the extent they are to be used to process ore from Canadian mineral resources beyond the prime metal stage or its equivalent" would be eligible to earn depletion. The restriction to "new" buildings and machinery appears to contradict directly the government's August 26, 1970 proposal to permit expenditures for "mine buildings and machinery and equipment acquired in connection with a major expansion of an existing Canadian mine" to earn depletion.

Your Committee heard evidence that officials in the Department of Finance have stated that their interpretation of the proposed regulations would render ineligible for earning depletion, expenditures on a major expansion of existing facilities. Their alleged interpretation will require eligible buildings to be new from the ground up. However since your Committee has not yet heard any witnesses from the Department of Finance, it has set out the facts in connection with

(1) the news release by the Minister of Finance on August 26, 1970 proposing additional changes to widen the definition of expenditures that can qualify for earned depletion;

(2) the proposed Regulations released on July 6th, 1971 by which such proposed changes would be administered;

(3) the interpretation allegedly put upon the language of the Minister's proposal of August 26th, 1970 substantially limiting its scope; and

(4) evidence submitted that it was only following the Minister's widening of the proposed scope of the definition of earned depletion that projects involving substantial expenditures became feasible.

YOUR COMMITTEE RECOMMENDS that serious consideration be given to the situation presented by this set of facts.

In any event, your Committee believes that if the government's intention be to encourage additional processing in Canada, all expenditures on structures and machinery incurred to increase Canadian processing facilities should qualify to earn depletion. Companies which cannot afford to construct elaborate smelting and refining facilities as part of their initial investment should not be penalized if subsequently they expand their existing processing facilities. Nor should the construction of custom smelters and refineries be denied this incentive to the extent that they process foreign ores.

In the White Paper on Tax Reform, at page 67, the Department of Finance proposed that expenditures "on exploration for or development of mineral deposits in Canada" be eligible to earn depletion. The August 26, 1970 News Release reiterated the White Paper proposals in this regard. However the proposed regulations issued July 6, 1971 exclude the four above-noted categories of Canadian exploration and development expenses which will be eligible to earn depletion. Your Committee heard numerous submissions urging that these exclusions be eliminated.

The company engaged in the $120 million expansion programme referred to above incurred $10 million of expenditures on development of an existing open pit mine by stripping waste rock, only to discover that expenditures eligible to earn depletion are now to exclude "Canadian exploration and development expenses in the vicinity of a mine after it came into production".

Other witnesses stated that such an exclusion would penalize small mines that have insufficient capital to enable them to complete their total exploration before bringing a property into production. Your Committee feels that this particular exclusion is not warranted. The gov-

ernment may be concerned with the difficulty of determining whether an open pit or underground operation is exploration or actual mining. YOUR COMMITTEE CONSIDERS that to be a question of fact to be decided in each case, and does not consider that problem to be sufficiently burdensome to warrant excluding any *bona fide* exploration from being eligible to earn depletion.

Your Committee is of the opinion that the risks of the oil and gas industries are of sufficient magnitude to require that depreciable property such as production equipment and natural gas plants be eligible to earn depletion in the same manner as mining machinery and equipment are treated in the case of new mines and major expansions of existing mines. At a time when the cost of production equipment (such as drilling and production platforms) required for the development of off-shore and far-north petroleum and gas properties will be enormous (likely double and triple present costs), YOUR COMMITTEE RECOMMENDS that those and similar expenditures qualify to earn depletion.

In order to encourage the development of remote areas of Canada, YOUR COMMITTEE RECOMMENDS that the cost of social capital and transportation facilities be eligible to earn depletion. Those expenditures, when incurred in remote regions, can form a major portion of total exploration and development costs and are essential to the operation of a mine. Without such expenditures there could be no development of the property.

The exclusion from eligibility to earn depletion of interest on funds required to finance exploration projects can only penalize smaller companies with limited capital. YOUR COMMITTEE THEREFORE RECOMMENDS that the cost of borrowing money to be used to finance exploration qualify to earn depletion.

In summary YOUR COMMITTEE RECOMMENDS that all "Canadian exploration and development expenses" as defined in the proposed legislation should earn depletion, as should depreciable mine assets (whether new or used), depreciable production equipment and natural gas plants in the petroleum and natural gas industries, and expenditures on new buildings and machinery as well as on expanded buildings and machinery, to the extent that they are to be used to process ore from any mineral resources beyond the stage to which they were previously processed in Canada, up to but not beyond the prime metal stage or its equivalent. Therefore any expenditure which is required to reduce the profit from which depletion may be deducted should qualify as an eligible expenditure.

In the event that your Committee's recommendation in this regard be not adopted, an alternative (but less satisfactory) treatment would be to permit the expenditures enumerated above to be deducted from income by resource companies for purposes of computing their taxable income, but to stipulate that such expenditures would not reduce their production profits from which earned depletion is deductible. In other words if the expenditures in question are not to be permitted to earn depletion, they ought not to reduce the base on which depletion is calculated; however they should remain deductible in computing taxable income.

YOUR COMMITTEE RECOMMENDS that the transitional period required to convert from automatic depletion to earned depletion be extended to 1980. Alternatively, companies should be permitted to "bank" eligible expenditures whenever incurred (that is, including expenditures incurred prior to November 7, 1969) after deducting from such "bank" all depletion previously allowed. Expenditures made prior to November 7, 1969, (which is the date prescribed by the proposed regulations as being the date after which companies can accumulate expenditures which will qualify to earn depletion) were incurred on the basis that automatic depletion would be available. Accordingly those expenditures should at least be included in the computation of earned depletion.

B. Accelerated Capital Cost Allowance

The three-year exemption from tax of profits derived from the operation of a new mine is to be withdrawn on December 31, 1973. It will be replaced by an accelerated write-off of specified capital equipment and facilities. The proposed regulations provide that the following types of *new* depreciable assets acquired before a new mine comes into production and for the purpose of gaining or producing income from the mine (including income from the processing of mineral ores up to the prime metal stage or its equivalent) will qualify for accelerated capital cost allowance:

1. a building (except an office building that is not situated on the mine property),

2. mining machinery and equipment,

3. electrical plant that would otherwise be included in Class 10 of Schedule B by virtue of sub-section 1102 (9) of the Income Tax Regulations, and

4. houses, schools, hospitals, sidewalks, roads, sewers, sewage disposal plants, airports, docks and similar property (other than a railroad not situated on the mine property) acquired to establish community transportation facilities necessary for the operation of the mine.

Depreciable property of the type listed in clauses (1), (2), and (3), will also qualify for the accelerated capital cost allowance where it is acquired in the course of the major expansion of an existing mine and before the commencement of production at the higher level of capacity. For this purpose a major expansion will be considered to have taken place if the productive capacity of the *mine mill* is increased by at least 25 per cent.

The proposed regulations will enable both new mines and existing mines engaged in major expansion programmes to claim accelerated capital cost allowance on specified types of "new depreciable assets", provided they be acquired before the mine came into production (or, in the case of major expansions, before production at the increased capacity commences). The purpose of this incentive appears to be to promote increased development of new and expanded mines, rather than to encourage the purchase of new assets instead of used assets. YOUR COMMITTEE CONSIDERS that if a company decides that it should, for economic and business reasons, pur-

chase used assets rather than new ones, the cost thereof should be eligible for the accelerated capital cost allowance.

In addition your Committee sees no reason to limit this incentive to assets acquired *before* production begins. That restriction places at a severe disadvantage those mines with insufficient financing to defer the commencement of production until after all of the qualifying assets have been acquired.

Similarly many "new" mines cannot afford to build a smelter or a refinery immediately. If a smelter or refinery were added after a mine had established itself, the addition would not appear to qualify as a "major expansion", since that term is defined in the proposed regulations to mean an increase by 25 per cent in the productive capacity of the "mine mill". Your Committee is of the opinion that new or used smelting and refining assets, whenever acquired, should be eligible for accelerated capital cost allowance. This will help to promote increased processing of minerals in Canada.

Your Committee also wishes to draw attention to the following items which, although technical, do merit serious consideration:

(*a*) an expenditure which the proposed regulations describe as a "building (except an office building that is not situated on the mine property)" should be amended to include other "structures" to make it clear that dams, conveyor trussels, tanks and sub-structures will qualify for accelerated capital cost allowance;

(*b*) the phrase "mining machinery and equipment" should be amended to read "mining and processing machinery and equipment" to accord with the preamble to the proposed regulations. The preamble states that various assets acquired for the purpose of producing income from the mine, "including income from the processing of mineral ores up to the prime metal stage or its equivalent" would be eligible for fast write-off;

(*c*) the definition of the social capital transportation costs which will qualify for accelerated capital cost allowance should be re-phrased by stating the general categories of expenditures which are to qualify. That general principle should be followed by an enumeration of particular items which would not restrict the generality of the guiding principle. As presently worded, the proposed regulations would appear to exclude dams, lighting installations and water lines, for example;

(*d*) social capital and transportation costs incurred on a major expansion of an existing mine logically should qualify for fast write-off to the same extent as buildings, machinery and equipment; and

(*e*) the definition of "major expansion of an existing mine" should be revised to include a 25 per cent increase in the productive capacity of a mine or mill. On occasion the output of a mine could increase by 25 per cent without a corresponding increase in mill capacity (for example, where ore is custom milled). It is seldom that ore is custom milled outside Canada.

C. Transfers of Resource Properties

Under present law, mining properties and royalty interests are treated as capital assets. That is, their acquisition cost is not deductible and proceeds on their sale are not taxable. However, since 1962 the acquisition cost of oil and natural gas rights have been deductible as exploration and development expenses, and proceeds on their disposal have been fully taxable.

The proposed legislation will, following an eight-year transitional period, require the inclusion in income of the entire proceeds of sale of all Canadian resource properties. Correspondingly, the cost of acquiring such properties will be deductible from income.

YOUR COMMITTEE RECOMMENDS that the transfer of Canadian resource properties between related companies should be permitted to occur without incidence of tax.

DEFERRED RECOGNITION OF CAPITAL GAINS (ROLLOVERS)

With the introduction of taxation of capital gains in Canada, provisions must be made for the deferring of tax in appropriate circumstances such as where there is no change in economic interest. The proposed legislation duly recognizes this and contains a number of provisions to defer the tax on gains. The principal ones are:

1. Involuntary dispositions where property has been destroyed or expropriated and the compensation received is used before the end of the following taxation year to replace the property.

2. The conversion of convertible bonds, debentures and notes for shares of the same corporation or bonds for bonds from the same debtor.

3. The transfer of assets to a corporation if the tranferor (which may include a partnership) owned at least 80 per cent of each class of the corporation's capital stock immediately following the transfer. This deferral is subject to a number of limitations and restrictions.

4. The transfer of capital property to a spouse or to specified classes of trusts for the benefit of a spouse.

5. The transfer of property by a partner of a Canadian partnership to the partnership. This deferral is also subject to certain restrictions and limitations.

6. The transfer of partnership property to a member of the partnership provided that the transferee subsequently carries on the business formerly carried on by the partnership.

7. The liquidation of a wholly-owned Canadian subsidiary into its Canadian parent corporation.

8. The disposition of shares on the reorganization of a corporation's share capital to the extent that any money or property (other than shares of the corporation) received by the shareholder does not exceed the adjusted cost base of the shares disposed of in the course of the reorganization.

9. The disposition of shares upon the amalgamation of two or more corporations provided that

(*a*) where preferred shares are disposed of, the shares of the successor corporation which the share-

holder receives in exchange therefor have substantially similar rights and conditions as the preferred shares which were exchanged, and

(*b*) where common shares are disposed of, the shareholders of the predecessor corporation receive in total at least 25 per cent of the issued common shares of the successor corporation.

Your Committee is of the opinion that the aforementioned rules which provide for deferred recognition of capital gains (rollovers) are of assistance but are not adequate. A tax system should not impede transfers of properties in bona fide legitimate business transactions. Sound management decisions often dictate that transfers of capital property be made between related groups of corporations for example, transfers of unused equipment from one subsidiary to another which could employ it more efficiently. Unfortunately the proposed legislation imposes a barrier to such transactions unless the corporation is willing to pay the tax on a deemed gain or is willing to assume a non-allowable capital loss. There is no valid reason for imposing penalties in circumstances such as this especially when appropriate safeguards have been incorporated in the proposed legislation to disallow superficial losses and to block artificial transactions and tax avoidance.

Your Committee fails to understand why the Government has departed from the ground rules it laid down in its own White Paper on Tax Reform, which read on page 42, paragraph 3.43:

"The government believes that there are some situations in which it would be unfair to collect a capital gains tax even though the taxpayer has sold or otherwise disposed of an asset at a profit. These situations fall into two broad classifications—those where there is a forced realization and those where there has been no change of underlying ownership even though there has been a sale."

Provided that there is no change in economic interest, no deemed realization should occur in any circumstances where, for example,

(*a*) there is a forced transfer,

(*b*) corporate reorganizations occur,

(*c*) property is transferred to a corporation by its "incorporators"—the proposed legislation restricts deferral to those situations where the transferor (which may include a partnership) transfers property to an 80 per cent controlled corporation,

(*d*) there is a transfer of assets to a business trust.

The Committee believes that there are other transactions which are as equally entitled to a deferral as those specified in the proposed legislation and suggested above. It is not possible for your Committee to envisage all of the transactions which should be accorded deferred gain treatment, therefore:

YOUR COMMITTEE RECOMMENDS that the tax-free deferral provisions be broadened to the greatest extent possible to include all situations where underlying ownership remains the same. Because it is impossible to foresee all of the situations in which deferrals should be permitted, it may be appropriate to authorize the Minister of National Revenue to expand the deferral provisions by way of Regulation as the need for such provisions becomes apparent, perhaps requiring prior approval as a condition of obtaining the benefit of a tax-free deferral.

DESIGNATED SURPLUS

Your Committee has noted that the concept of "designated surplus" is to be retained in the proposed legislation. This concept was originally introduced into the present Act in 1950 to prevent taxpayers from being able to distribute their corporate surplus free of tax. Prior to the enactment of these provisions, it was possible to arrange to receive a corporation's undistributed income in the form of a non-taxable capital gain through the relatively simple expedient of selling the shares of a surplus-laden corporation to another corporation which could then distribute the surplus of the first corporation free from income tax.

In order to offset any advantage to this kind of transaction, provisions were enacted to the effect that, where one corporation acquired control of another, the surplus or retained earnings on hand in the controlled corporation at the end of the taxation year immediately before control was acquired was designated and any dividends paid out of such surplus became taxable to the receiving corporation.

As events have shown the designation of corporate surplus was not entirely satisfactory and in 1963 a further provision was enacted known as Section 138A, whereby the receipt of amounts by a vendor of shares should be construed as a dividend and could be taxable as such in his hands. With the introduction of Section 138A it might have appeared that the designation of corporate surplus was no longer necessary, but it was nevertheless retained.

In considering the need for retaining the designated surplus provisions, your Committee notes that the tax savings that might be achieved under present law in the absence of designated surplus provisions could be as great as 60 per cent of the surplus involved (i.e., tax at the 80 per cent maximum rate of personal income tax less the 20 per cent dividend tax credit). The proposed inclusion of one-half of capital gains in ordinary income combined with the proposed reduction in the maximum rate of personal income tax and the change in the dividend tax credit system will substantially reduce the amount of tax saving which could be achieved by converting corporate surplus into a capital gain. Therefore, there is not the same need for the designated surplus provisions under the proposed legislation as there is under the present Act.

Despite this, various amendments have been made to these provisions which will effectively deter many valid corporate reorganizations. An example of this tightening of the designated surplus provisions is the deeming of a dividend to have been paid out of designated surplus in the event of a vertical amalgamation, e.g. the amalgamation of a parent and its subsidiary.

Having regard to the reduced need for the designated surplus provisions and the obstacles which these provisions place in the way of bona fide corporate reorganizations, these provisions should be eliminated; particularly in view of the fact that Sections 137(2) and 138A(1) of the present Income Tax Act, with which the Department of National Revenue has successfully attacked dividend stripping arrangements, are to be carried forward into the proposed legislation. It would also appear desirable for the purpose of simplification that your Committee give consideration to the abandonment of designated surplus, particularly when the proposed legislation is introducing so many new types of surpluses.

It might also be relevant to note that since the deemed dividend provisions of the proposed legislation do not apply to foreign corporations, Canadians who control such corporations will be able to convert corporate surplus into a taxable gain. There is therefore some precedent in the proposed legislation for eliminating the designated surplus concept. However their counterpart Canadian corporations will be refused such a treatment.

YOUR COMMITTEE RECOMMENDS that the special taxes which are to be levied on dividends paid or received out of a corporation's designated surplus be withdrawn.

It is recognized that the elimination of tax on dividends paid out of designated surplus will presumably require amendments to the proposed legislation to provide that these dividends will reduce the cost base of shares for eventual capital gains purposes. It may also be necessary to provide that a corporation which wishes to make a distribution of pre-1972 designated surplus will be required to "tax pay" amounts distributed from such surplus by paying the special 15 per cent tax relating to 1971 undistributed income.

Recent amendments to the proposed legislation were tabled pertaining to the definition of designated surplus. One of the effects of these amendments would be to designate the undistributed income on hand of a corporation the control of which changed prior to the end of its 1972 taxation year. This would appear to mean that an amalgamation which was effected before 1972 would result in the designation of the entire surplus of each of the amalgamating corporations. Such designation of surplus would carry over into the amalgamated corporation.

Your Committee considers that such a result could not have been intended, and it desires to voice its disapproval of designated surplus in general and this amendment in particular.

CONSOLIDATED RETURNS OF INCOME

The question of consolidated returns of income by related corporations is not a new one, having been raised many times in the past. In point of fact this concept was part of our taxation law for some 20 years, between the periods of 1932 and 1952. The apparent reason for its introduction into the law during that period, was the absence of business loss carry forward provisions and as a result, qualified corporate groups were permitted to consolidate their incomes and thus absorb their losses on a current basis. In effect, these corporations were prepared to be associated for income tax purposes as if they were a single entity.

In 1952, with the introduction of provisions allowing taxpayers to a business loss carry-over, it was believed that there was a reduced need for consolidated returns of income by corporate groups and the concept was therefore abandoned. There is also some suggestion that the decision was dictated by administrative convenience.

In appreciating this matter it is noted that for some period of time we have also had in our law the concept known as associated corporations. In order to assist small business corporations, provision was made in the income tax law for a dual rate of corporate tax. That is, the corporation was subject to tax at one rate on a defined amount of taxable income and at a higher rate on any taxable income in excess of this amount. However, it was decided that corporations which formed part of a related group (as defined) should be considered to be associated and that one corporation in the group should be entitled to the lower rate of tax or, alternatively, that the amount eligible for the lower rate should be allocated amongst the group. These associated corporation rules were for the purpose of determining the applicable tax rate and did not permit the application of current losses from one corporation to another within the group.

Throughout the years, extensive rules have been enacted for the purpose of deeming corporations to be associated. Under the present provisions, the Minister of National Revenue is also entitled, in his discretion, to treat corporations as associated. The effect of these provisions is to associate corporations who would not otherwise wish to be associated.

In the opinion of your Committee it appears somewhat incongruous that there exist situations wherein some related corporations wish to be associated, and other related corporations do not. To this end, the concept of the consolidated return of income provided a vehicle for the former while the concept of the associated corporation provided the vehicle for the Minister of National Revenue in respect of the latter. The difficulty is that upon the abandonment of consolidated return of income provisions, the former group continue to be associated corporations without the ability to apply current losses from one corporation to another.

Your Committee recognizes the fact that separate corporations must often be created for various commercial purposes. In some cases, provincial or federal laws will require separate corporations to be established. These corporations are nevertheless in substance part of the same corporate family and their financial consolidation should therefore be duly recognized.

While the loss carry-over provisions permit application by each corporation of current losses to other taxation years, nevertheless, the immediate application of such losses to the income of other corporate members of the group is a more realistic view of the situation. Your Committee recognizes the basic principle that profits of one member of a group should be used to reduce the losses of another member of the group. This principle has been duly recognized in the United States.

Because of the restricted number of rollover provisions in the proposed legislation and the resulting difficulty which will be encountered in merging the operations of a related corporate group, your Committee believes that it is essential that corporations should be permitted to file consolidated returns of income, if they so elect.

The Committee has made this suggestion on previous occasions. This view has been reinforced by other notable committees, commissions and professional bodies, including the House of Commons Committee on Finance, Trade and Economic Affairs, the Royal Commission on Taxation (Carter), the Canadian Bar Association and the Canadian Institute of Chartered Accountants.

YOUR COMMITTEE RECOMMENDS that provision be made in the proposed legislation to permit corporations which are members of a qualifying group to elect to file on a consolidated return of income basis. If it is found that such a provision is impractical; YOUR COMMITTEE RECOMMENDS that consideration be given to the introduction of a scheme of subvention payments similar to that formerly used in the United Kingdom.

CONSTRUCTION INDUSTRY

Your Committee has studied the representations made by this industry and has come to the conclusion that two major points should be modified in the proposed legislation.

The first one relates to the reporting of income and arises from the fact that it is extremely difficult to determine the annual income from contracts such as stipulated sum contracts of more than one year's duration. For this reason, the construction industry has historically reported income on the completed contract method of under two years' duration. This method has been approved by the Minister of National Revenue as a matter of administrative practice. However, there is no statutory authority for this method of reporting income and the taxpayer has accordingly no right of appeal if the Minister refuses in any given situation to accept this method of reporting.

The second problem raised relates to the fact that the description of assets falling within class 12(*h*) and class 22 of Schedule B to the present income tax regulations is unduly restrictive in respect of the conditions referred to therein. It is the view of your Committee that the conditions set forth in these classes do not reflect present-day prices for the purpose of class 12(*h*) and that a more extended definition should be provided for the equipment to be included in class 22.

YOUR COMMITTEE RECOMMENDS

1. That the completed contract method on fixed sum contracts of under two years' duration should be incorporated in the proposed legislation as an accepted method to determine a construction business' taxable income for a year.

2. That special attention be given in regulations to be issued concerning capital cost allowance related to the construction industry in order to remove unnecessary restrictions and to expand its application.

CAISSES POPULAIRES AND CREDIT UNIONS

Under the proposed legislation, caisses populaires and credit unions will no longer be exempt from tax. Instead, it is proposed that these organizations will be taxed in substantially the same manner as other private corporations. As such, they will be entitled to take advantage of the small business deduction to the extent allowable to other private corporations.

One of the defects of the proposals originally put forward by the Government was that the provisions relating to the small business deduction failed to give recognition to the constraints that are placed upon caisses populaires and credit unions by their governing legislation. These organizations are required by law to set aside an annual mandatory reserve, no part of which may at any time be distributed amongst the organization's members. In addition, they may set aside such additional reserve as they consider necessary to assure their financial stability. Like the mandatory statutory reserves, these voluntary reserves cannot be distributed to members.

In considering the effect of the original tax proposals on these organizations it should be recognized that amounts set aside as reserves annually pursuant to the relevant governing legislation are not allowed as a deduction in computing income for tax purposes. These reserves should not be confused with the allowances which caisses populaires and credit unions will be allowed to claim as a deduction under the proposed legislation in respect of their outstanding loans and investments.

In view of such statutory restrictions, these organizations are unable to distribute all of their after-tax income by way of dividend and are therefore unable to perpetuate the small business deduction in the same manner as other private corporations. Having duly considered the representations submitted by these organizations, your Committee concluded that the following recommendation should be put forward:

That caisses populaires and credit unions should not be required to include in their "cumulative deduction account" (for purposes of determining the available balance of their total business limit of $400,000) such portion of their taxable income as is set aside in the year as a reserve to the extent that such reserve is not available for distribution to members. This should be subject to the further limitation that no recognition be given to any such reserve to the extent that the total amount set aside does not exceed, say, 5 per cent of the organization's total deposits and share capital at the commencement of the year.

The effect of the amendments which the Government recently tabled in this regard is to alleviate, at least in part, some of the problems which confronted these organizations under the original proposals. We commend the Government for introducing these amendments. However, as the effect of these amendments differs somewhat from the afore-mentioned recommendation, YOUR COMMITTEE RECOMMENDS that this matter be given further consideration by the Government.

ADMINISTRATION AND ENFORCEMENT

Your Committee has had referred to it several provisions of the proposed legislation relating to enforcement. Your Committee concurs with attempts to protect the rights of taxpayers whose affairs are under investigation. The Committee is concerned however, that these attempts have not gone far enough, and furthermore, that other existing defects have not been dealt with.

Under the proposed legislation the power of holding an inquiry pursuant to the Inquiries Act is continued. Nevertheless, the changes proposed permit:

(*a*) the hearing officer to be appointed by the Tax Review Board upon the application of the Minister of National Revenue,

(*b*) the person whose affairs are being investigated is entitled to be present, and to be represented by counsel, and

(*c*) the hearing officer may, upon application by the Minister, exclude the person whose affairs are being investigated, and his counsel, if their presence would prejudice the conduct of the inquiry.

Your Committee has also noted that in matters of evasion, if the Minister of National Revenue has elected to proceed by way of a criminal prosecution, no liability for any ministerial penalty may be levied *unless* such penalty was assessed *prior* to the laying of the information or complaint.

Finally, the saving provision relating to the prevention of double ministerial penalties as found in Section 56, ss 3 of the present legislation, is omitted from the proposed legislation.

YOUR COMMITTEE RECOMMENDS the following:

1. that in respect of inquiries into the affairs of a taxpayer under the proposed legislation:

(*a*) the appointed hearing officer should not be an official of the Department of National Revenue,

(*b*) the taxpayer whose affairs are being investigated should be entitled either personally or through counsel, to cross-examine all witnesses and should also be entitled to receive a copy of the transcript of all evidence taken at such inquiry, and

(*c*) any order excluding from an inquiry the taxpayer whose affairs are being investigated, or his counsel, should be subject to immediate review by a judge of the Federal Court of Canada;

2. that the double jeopardy provision should be expanded so that if the Minister of National Revenue elects to proceed against a taxpayer by way of information or complaint, the Minister cannot as well levy a ministerial penalty; or, conversely, if the Minister elects to proceed against a taxpayer by way of ministerial penalty, the Minister cannot as well commence criminal proceedings by way of information or complaint; and

3, that the saving provision contained in Section 56, ss 3 of the present Act be introduced into the proposed legislation.

VALUATION DAY

With the introduction of a capital gains tax in Canada, it is essential that such a tax should not apply to any portion of ultimate proceeds of disposition which represent simply a recovery of original cost. This was the error of the White Paper when it originally proposed that capital property should generally be valued at fair market value at Valuation Day.

To some extent the foregoing error has been corrected by the introduction of the concept popularly referred to as the "tax-free zone". Gains will be included for taxation purposes only to the extent that the proceeds exceed the higher of actual cost and Valuation Day value, and losses will be deductible only to the extent that the proceeds are less than the lower of actual cost and Valuation Day value.

Your Committee commends the Government for introducing this concept in the proposed legislation. However, the Committee regrets that the Government did not see fit to provide that property acquired by a taxpayer prior to June 18, 1971 by way of gift, bequest or devise should be deemed to have been acquired at a cost equal to the fair market value of the property at date of acquisition. Such a provision would be inconsistent with the proposed treatment of property so acquired after December 31, 1971.

YOUR COMMITTEE RECOMMENDS that provision be made in the new law to the effect that property acquired by way of gift, bequest or devise prior to June 18, 1971 be deemed to have been acquired at an amount equal to its fair market value at date of acquisition for the purpose of calculating any taxable gain but not for the purpose of calculating any allowable loss.

EPILOGUE

The foregoing sets forth the observations, opinions and recommendations of your Committee on the briefs presented and witnesses heard up to and including the 27th day of October, 1971. It is therefore of a preliminary nature only.

Your Committee intends to present a second report after the termination of its hearings covering submissions made subsequent to October 27, 1971.

Some of the topics with which your Committee intends to deal in its second report are:

1. professional income on an accrual basis,

2. new rules applicable to partnerships and to trusts and their beneficiaries,

3. the treatment of mutual funds, investment corporations and clubs,

4. investment income of private corporations,

5. Canadian income of non-residents such as withholding tax, branch tax, non-resident owned investment corporations, capital gains of non-residents,

6. corporate distributions,

7. natural resources (other than those already dealt with) for example the pulp and paper industry,

8. mutual funds (registered retirement savings plan),

9. treatment of income of insurance companies

10. the ability of recipients of all forms of lump sum payments to avail themselves of general and forward averaging even though they elect the equivalent of section 36 averaging in respect of the pre-1972 portion of such payments.

11. Tax incentives for fixed income securities.

Your Committee finally notes with approval that the proposed legislation has been the subject of discussion at the recent conference between the Minister of Finance and his counterparts in each of the provincial governments. It is to be hoped that these will be continuing discussions. The Committee's views as to the need for these consultations in order to develop a unified tax system are adequately expressed in its Report on The White Paper Proposals for Tax Reform where it was stated:

> "Your Committee, however, wishes to again express its appreciation of the Government's desire to work closely with the provinces in an attempt to evolve with the passage of time a symmetrical taxation system, and it urges the Government to continue its quest for the attainment of this highly desirable goal."

Respectfully submitted,

Salter A. Hayden,
Chairman.

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THIRD SESSION—TWENTY-EIGHTH PARLIAMENT

1970-71

THE SENATE OF CANADA

PROCEEDINGS

OF THE

STANDING SENATE COMMITTEE ON

BANKING, TRADE AND COMMERCE

The Honourable JOHN J. CONNOLLY, *Acting Chairman*

No. 48

THURSDAY, NOVEMBER 4, 1971

Eleventh Proceedings on:

"Summary of 1971 Tax Reform Legislation"

(Witnesses:—See Minutes of Proceedings)

THE STANDING SENATE COMMITTEE ON BANKING, TRADE AND COMMERCE

The Honourable Salter A. Hayden, *Chairman*

The Honourable Senators,

Aird	Grosart
Beaubien	Haig
Benidickson	Hayden
Blois	Hays
Burchill	Isnor
Carter	Lang
Choquette	Macnaughton
Connolly (*Ottawa West*)	Molson
Cook	Smith
Croll	Sullivan
Desruisseaux	Walker
Everett	Welch
Gélinas	White
Giguère	Willis—(28)

Ex officio members: Flynn and Martin

(Quorum 7)

Order of Reference

Extract from the Minutes of the Proceedings of the Senate, September 14, 1971:

"With leave of the Senate,

The Honourable Senator Hayden moved, seconded by the Honourable Senator Denis, P.C.:

That the Standing Senate Committee on Banking, Trade and Commerce be authorized to examine and consider the Summary of 1971 Tax Reform Legislation, tabled this day, and any bills based on the Budget Resolutions in advance of the said bills coming before the Senate, and any other matters relating thereto; and

That the Committee have power to engage the services of such counsel, staff and technical advisers as may be necessary for the purpose of the said examination.

After debate, and—

The question being put on the motion, it was—

Resolved in the affirmative."

Robert Fortier,

Clerk of the Senate.

Minutes of Proceedings

Thursday, November 4, 1971.
(61)

Pursuant to adjournment and notice the Standing Senate Committee on Banking, Trade and Commerce met this day at 9:30 a.m. to further examine:

"Summary of 1971 Tax Reform Legislation"

Present: The Honourable Senators Connolly (*Acting Chairman*), Beaubien, Benidickson, Blois, Burchill, Carter, Cook, Croll, Desruisseaux, Gélinas, Haig, Hays, Isnor, Molson, Smith and Welch—(16).

Present, but not of the Committee: The Honourable Senator Laird—(1).

The Chairman being occupied with revisions to the Preliminary Report and upon motion duly put it was Resolved that the Honourable Senator Connolly (*Ottawa West*) be elected Acting Chairman.

In attendance: The Honourable Lazarus Phillips, Chief Counsel.

WITNESSES:

Elgistan Management Limited:

Mr. J. D. H. Mackenzie, President;

Mr. George P. Keeping, C.A., partner, Clarkson & Gordon Co.;

Mr. A. M. Minnion, Q.C., of law firm of McMaster, Meighen, Minnion & Co.

Loram Ltd.:

Mr. Fred P. Mannix, President;

Mr. W. G. Gray, Controller;

Mr. D. W. McClement.

Anglo-American Corporation of Canada Limited:

Mr. J. David Taylor, Q.C., Director, and partner Toronto law firm of Fasken & Calvin;

Mr. Gerald J. Risby, Vice President-Treasurer and Director.

At 12:00 o'clock Noon the Committee adjourned to the call of the Chairman.

ATTEST:

Frank A. Jackson,
Clerk of the Committee.

The Standing Senate Committee on Banking, Trade and Commerce

Evidence

Ottawa, Thursday, November 4, 1971

The Standing Senate Committee on Banking, Trade and Commerce met this day at 9.30 a.m. to give consideration to the Summary of 1971 Tax Reform Legislation, and any bills based on the Budget Resolutions in advance of the said bills coming before the Senate, and any other matters relating thereto.

Senator John J. Connolly *(Acting Chairman)* in the Chair.

The Acting Chairman: Honourable senators, we are going to hear three submissions this morning, from: Elgistan Management Limited; Loram Ltd.; and Anglo American Corporation of Canada Limited. If it is satisfactory to the committee, we will hear Elgistan Management Limited first.

Hon. Senators: Agreed.

The Acting Chairman: Representing Elgistan Management Limited are: Mr. J. D. H. Mackenzie, President; Mr. George P. Keeping, of Clarkson, Gordon & Co.; and Mr. A.M. Minnion, Q.C., of the law firm of McMaster, Meighen, Minnion & Co., of Toronto.

I understand you are going to make the opening statement, Mr. Mackenzie. Would you care to proceed with that?

Mr. J. D. H. Mackenzie, President, Elgistan Management Limited: Thank you, Mr. Chairman. Honourable senators, before giving a short introduction to the written submission of Elgistan Management Limited, copies of which are already in your hands, I should like to introduce Mr. Keeping of Messrs. Clarkson, Gordon & Co. and Mr. Minnion of Messrs. McMaster, Meighen, Minnion & Co. Mr. Keeping and Mr. Minnion are, respectively, partners in firms of accountants and lawyers which act for our company and provide us with tax advice. They had much to do with the preparation of the submission.

As representatives of Elgistan Management Limited we were privileged to appear before you in April, 1970, when the Government's White Paper entitled "Proposals for Tax Reform" was being considered by your committee. You have now kindly given us the opportunity to present our views on tax reform Bill C-259 in so far as the bill and its amendments affect the non-resident interests under our company's management.

In our submission on the White Paper we provided an outline of the manner in which our non-resident investors held their interests in Canada. There has been no material change in these arrangements in the intervening time. Briefly, the non-residents continue to hold their investments through the medium of non-resident earned investment corporations, which we will refer to as NROs, and, for ease of management, each NRO's marketable securities are held through units in a unit trust fund. In addition, the NROs hold shares in several private companies.

In our submission on Bill C-259 we attempt to show how the tax reform proposals affect the interests under our company's management, and why the existing corporate and trust structure could not be suitable for these interests beyond 1971. We have tried to be objective and have confined most of our observations to technical points.

I must mention, however, that an examination of these technical aspects naturally led to a consideration of matters of principle. We came to the inescapable conclusion that after 1971 the NRO could play only a very limited role in the marshalling of a non-residents' capital, and a Canadian unit trust fund owned either directly or indirectly by non-residents would be penalized to such an extent, and for no good reason that is apparent to us, that it would have to be terminated and the assets transferred to another country.

I think the implications of this for Canada are worth considering. If a sizable pool of capital, largely invested in Canadian marketable securities, were to be moved out of the country, it seems unlikely to us that the managers of a foreign unit trust which would take the place of the Canadian trust would have the same inclination to buy Canadian securities as their predecessors. Canada's security markets suffer from a lack of liquidity now, and we envisage the situation deteriorating as serious foreign investors with long-term objectives not inimical to Canada are discouraged by an inhospitable tax climate.

While we live in hope that the Government will introduce relieving amendments, the uncertainties engendered by tax reform must make even the staunchest non-resident investor wonder whether continued involvement in this confusing process makes good business sense.

Mr. Chairman, that is basically our stand. We have tried to outline this in our submission, and I and my colleagues will be pleased to answer any questions your committee may wish to put.

The Acting Chairman: Thank you, Mr. Mackenzie. For the record, perhaps it would be helpful at this stage were you to give us a specific example of how your company operates, even though we went through it on the White Paper submissions. You talk about non-resident owned investment corporations, and perhaps you would tell us precisely what you do and whether you are actually managing other companies in which non-residents have investments.

Mr. Mackenzie: Well, our company, Elgistan Management Limited, is a management company and it has been

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formed to act for non-resident investors who, for the most part, reside in the United Kingdom and in the Republic of Ireland.

The Acting Chairman: Corporate and individual?

Mr. Mackenzie: Basically they are individual investors, private investors. The management company manages a number of non-resident owned investment companies, NRO's as we call them, for the benefit of these individuals. Typically, an individual would probably have a non-resident owned investment corporation. The non-resident owned investment corporation will hold assets in three main classes of security: shares of other private companies, which I might term operating companies; units of a unit trust into which, for ease of management, we have grouped all our marketable securities; and bonds held directly by the NRO's themselves. The reason for these, and the usefulness of the NRO, has been that you have a corporate entity in the country in which you are operating.

The Acting Chairman: Your company is organized and incorporated in Canada?

Mr. Mackenzie: Yes.

The Acting Chairman: Federally?

Mr. Mackenzie: Yes.

Senator Molson: Do your principals have any similar companies or investments in other jurisdictions or in other countries?

Mr. Mackenzie: Yes, indeed they have.

Senator Molson: Where?

Mr. Mackenzie: In Europe.

Senator Molson: Are there any in the United States?

Mr. Mackenzie: We do not have any in the United States.

The Acting Chairman: Would you care to say anything about the magnitude or size of your portfolios?

Mr. Mackenzie: We did reveal this when we made our submissions on the White Paper, and the whole was put at $100 million.

The Acting Chairman: This is foreign capital which would otherwise presumably not be here in Canada for investment?

Mr. Mackenzie: Again, if you go back to our White Paper discussions over a year ago, I pointed out that one of the main reasons we were in Canada was the very hospitable tax climate. This is the reason, I think, the capital was here in the first place vis-à-vis the United States.

The Acting Chairman: What are the principal features? I do not want to monopolize this questioning . . .

Senator Hays: May I pursue Senator Molson's questioning? You said you had investments in Europe. In what countries in Europe do you have investments?

Mr. Mackenzie: In Holland, Italy, France and Germany.

Senator Hays: Can you tell us what sort of treatment you receive from these countries as compared to Canada?

Mr. Mackenzie: It varies.

Senator Hays: I think it is important that we should have this type of information, if available, so that we can see whether you are being treated less favourably in Canada than in Holland or Germany.

Mr. Mackenzie: Holland has a fairly agreeable tax climate, I understand, but you are really directing your question to somebody who is not au fait with tax arrangements for all these countries.

Senator Hays: But much of your investment in Canada is in the way of real estate, buildings and that sort of thing?

Mr. Mackenzie: We have a real estate company, yes.

Senator Hays: Do you have buildings in Holland and France?

Mr. Mackenzie: Yes.

Senator Hays: You are making these investments continually?

Mr. Mackenzie: Yes.

Senator Hays: And you cannot tell this committee exactly how they are treated in each of these countries?

Mr. Mackenzie: Well, it is a very complex question to answer. I mean, you are asking me to explain the taxing arrangements of these European countries.

Senator Hays: Well, would you just identify one country?

Mr. Mackenzie: Since June I have been trying to understand what this country's taxing arrangements are going to be.

Senator Beaubien: Mr. Mackenzie, from what you understand about this tax bill, what is the difference going to be between what you pay now and what you would pay under Bill C-259 if it becomes law?

Mr. Mackenzie: Well, the foremost is a capital gains tax. Most countries in the world do not levy a capital gains tax on non-residents unless the non-residents hold real property, direct business assets or partnership assets in the country in question. Now Canada is seeking to tax non-residents on the gains they make on disposal of taxable Canadian property, which is a list defined in clause 115 of the bill. This includes shares of all private companies, which would include our non-resident owned investment corporation.

Senator Beaubien: Mr. Mackenzie, in the United States are shares in that sort of thing held by non-residents not taxed, and the profits made and capital gains?

Mr. Mackenzie: I understand not, because Canadian capital gains are not taxed by the United States Treasury if those gains are made in U.S. stocks.

The Honourable Lazarus Phillips, Chief Counsel to the Committee: This is the result of a treaty which we have.

Mr. Mackenzie: Yes.

Senator Beaubien: Mr. Phillips, do we have a treaty with England?

Hon. Mr. Phillips: Yes.

Senator Beaubien: Would they not be covered by the treaty?

Mr. Mackenzie: Yes, where the treaty exists non-residents will be protected. But Canada is seeking to re-negotiate these treaties to make section 115 applicable. But it can be applied immediately to non-residents living in non-treaty countries.

Senator Beaubien: Would that affect you?

Mr. Mackenzie: Canada does not have a treaty with the Republic of Ireland. It has a treaty with the United Kingdom. As of January 1, 1972, non-resident-owned investment corporations, although entirely owned by non-residents, will immediately have their gains taxed on taxable Canadian property. This is one of the arguments in our submission.

Mr. George P. Keeping, of Clarkson, Gordon & Co.: I think that I am right in saying that this committee, in its report on the White Paper, recommended, along with the Commons committee, that NRO's be taxed similarly to non-residents. In other words, if a non-resident investor sought to invest his portfolio in Canada through a non-resident investment corporation, he would be in no worse position than if he invested directly in Canada. I think Mr. Mackenzie pointed out the advantage of having a corporation in Canada to help facilitate the management of the portfolio investments.

Hon. Mr. Phillips: The recommendations made were that residents in Canada functioning through an NRO would be in no better or no worse position.

Mr. Keeping: Yes, that is right. This has not been implemented in Bill C-259. By the amendments some changes have been made which have alleviated inequities between the taxation of a non-resident holding his investments directly and the taxation of a non-resident investing through an NRO. There are still major areas where an investor who invests through an NRO is at a distinct disadvantage as compared to a non-resident with a direct investment. These areas are as follows: first of all, a number of non-resident-owned investment portfolios in Canada are not confined entirely to Canadian investments. Mr. Mackenzie has already said that his company does not operate in the United States. However, they do have some American investments in their portfolio. As the amended law now stands, capital gains made on foreign investments will not be taxable. This is in line with the non-resident investor who owns foreign investments directly. Naturally, Canada would not enter into the picture at all. When a person makes a capital gain on a foreign investment in Canada, he cannot distribute it to the NROs without suffering a withholding tax. The capital gains merge into the income stream with the rest of the revenue, and he can only get them out by way of an ordinary dividend. In many countries when a dividend is received it is classified as income. This is the case in the United Kingdom. You can imagine the difference in the United Kingdom between taxation of income and taxation of capital gains.

The second point is that on the sale of non-resident-owned investment corporation shares Bill C-259 imposes a tax on a non-resident shareholder's gain on the disposal of his NRO shares. Very frequently in these instances, in dealing with an NRO investment there are large portfolios of Canadian marketable securities which are not subject to capital gains tax if held by a non-resident. However, if a non-resident were to dispose of his NRO shares to a member of his family, the unrealized gains on the marketable securities would become taxable. Under the recent amendment he could get his gains on the marketable securities out tax-free by way of a capital gains dividend. However, he could not get the unrealized gains out. The unrealized gains enter into the valuation of the shares of the NRO and, therefore, help to determine the gain or loss which he would make on disposal of his NRO shares. This is a ridiculous situation. If he were to sell his whole portfolio on the day before he disposes of his shares and then buy them back again, he would realize all the gains. This would be very good for the stockbrokers.

Hon. Mr. Phillips: Please do not prejudice the tribunal!

Mr. Keeping: The third point is that at present there is a tax treaty with the United Kingdom which precludes Canada from taxing gains made by non-residents on the sale of Canadian securities and, vice versa, the United Kingdom from taxing Canadians on disposal of United Kingdom investments. However, under the proposed legislation, as of January 1, 1972 gains on taxable Canadian property in a non-resident-owned investment corporation become immediately taxable. If the investor held his investments directly he would be protected by the treaty. However, if he has invested through an NRO his gains on taxable Canadian property are immediately subject to tax.

Hon. Mr. Phillips: But is this not the complication, that when a non-resident investor decides to invest in a company which is, after all, incorporated under our law—I am playing the devil's advocate against you on this point—you are saying that the NRO which is organized under our laws should, for taxation purposes, be assimilated to a non-resident? Is that your basic premise?

Mr. Keeping: That is the way the law has been in the past; and the Commons committee has recommended that it be treated this way in the future.

Hon. Mr. Phillips: Yes, but if I may, I am trying to help this committee understand your basic legal point, that non-residents investing in Canada, obviously if they have a permanent establishment, place of business, or purchase real estate and so on, get one type of treatment. If they purchase securities generally they receive another type of treatment. For purposes of convenience, non-residents group themselves together, in effect, and agree to take their investment position through the medium of an NRO company. In the process this NRO company, if organized under the laws of Canada, immediately subjects itself to all the pressures resulting from that and the fact that it is a resident in Canada. Because of the circumstance that it is an NRO company, your point is that it should not be

assimilated, in effect, to an ordinary organized Canadian company. You apply that to even an organized company for holdings of securities, et cetera, legally owned business establishments, because of the circumstance that the ownership is vested in individuals outside of the country.

Mr. Keeping: That is right.

The Acting Chairman: I wonder if we could pursue it one step further. I understood Mr. Mackenzie to say that one of the categories of investment managed is that held by this company, Elgistan Management.

Mr. Mackenzie: No, it does not hold anything; it is just a management company.

The Acting Chairman: In any event, there are non-residents who have direct investments in Canada. I take it that your company acts as trustee for those investments. Is that so?

Mr. Mackenzie: As manager.

The Acting Chairman: Well, in that case I take it that the dire tax consequences described by Mr. Keeping, and commented upon by Mr. Phillips, would not apply.

Mr. Mackenzie: They would not apply to the management company. They will apply to the interests of the non-residents we are managing; that is, they will apply to the non-resident investment corporation.

Hon. Mr. Phillips: May I, with your approval Mr. Chairman, draw to the attention of honourable senators the following: We have spent some weeks recently dealing with the subject matter of international income generally. We have confined ourselves thus far to briefing, studies and recommendations, which presumably will continue today, with respect to foreign income moving to Canadian residents. This is the first brief we have heard with respect to the other side of the coin in connection with the new bill. It deals with international income generally and covers what is now being discussed in part, the movement the other way, from Canada, so far as the interests of non-residents are concerned.

We are moving into new terrain, which heretofore has not been covered. This will now become, presumably, the subject matter of further consideration as reflected in what was described last evening as the epilogue of further matters to be considered.

In other words, we are not too late to consider the representations which are being made today having regard to our deliberations to date. I wish to explain that, because we have a time limit in respect of certain representations which have been made to date and which will be dealt with, possibly, today. Therefore I wish to make it clear that there will be no time to deal with this subject matter in our up-to-date discussions, but this will go forward for further consideration.

Senator Carter: I have trouble distinguishing between the company itself, which does the managing, and the investors whose investments they are managing. Your plea is not on behalf of your company, which is an incorporated company, but, as I understand it, is on behalf of those who invest in it. They receive different treatment because they happen to group together through your company to do their investing, rather than managing it themselves.

Mr. Mackenzie: That is broadly correct. Our submission is on behalf of our non-resident principals. That is possibly a better word.

Senator Carter: As a Canadian company, incorporated under Canadian law, are you treated differently from other Canadian companies?

Mr. Mackenzie: Elgistan Management is not, but we are really referring to the NRO companies we manage, of which there are several. They are non-resident investors who invest through non-resident owned investment corporations.

The Acting Chairman: Could I take Senator Carter's question a step further: I understand that you manage for at least two classes of non-residents. Some buy and own shares in Canadian incorporated non-resident corporations?

Mr. Mackenzie: That is correct.

The Acting Chairman: In addition to that, you also have a portfolio of investments for individuals who are domiciled and resident abroad, which you manage in trust for them—is that so?

Mr. Mackenzie: Yes, but the units of that portfolio investment are in the main owned by the NROs. There are exceptional cases in which the units are owned directly by non-resident investors.

Mr. Keeping: Elgistan Management Limited is a purely management organization; it does not itself own investments. It derives its income from the fees of managing its principals' investments through their non-resident owned investment corporations. Elgistan Management is not a group of the funds of certain non-residents, but purely a management corporation. The actual investments are held in the larger part by the marketable securities in the trust. The trust has units which the non-resident owned investment companies hold. The non-resident owned investment companies are owned by individual non-residents.

Senator Carter: As a management company you are not an investment company, but you must have income or you would not be in business.

Mr. Keeping: Elgistan Management Limited derives its income from the fees of management and is taxed as an ordinary corporation.

Senator Carter: You are no different from any other corporation?

Mr. Keeping: No, not at all.

Senator Carter: So you are only concerned with the interests of the companies who use your services.

The Acting Chairman: This brief is presented only on behalf of the NRO companies managed by Elgistan.

Senator Beaubien: As far as Elgistan is concerned, your tax problem does not change.

Mr. Keeping: That is true.

Senator Beaubien: You have no problem there at all.

Mr. Keeping: No.

Senator Cook: When the ordinary private non-resident in the United Kingdom makes capital gains through holding a Canadian security does he pay capital gains tax there?

Mr. Mackenzie: Yes.

Senator Cook: Is the holder of NRO shares any better off? If he is exempt from paying capital gains tax in Canada on the profits made by the NRO, does he also escape capital gains tax in England?

Mr. Mackenzie: Not when he comes to dispose of the shares in that company.

Hon. Mr. Phillips: Mr. Chairman and honourable senators, I think that the background of this and the difficulty involved could probably be explained. It is the other side of the coin resulting from diverted income from Canadians which is reflected in the new bill in the famous FAPI or passive income, which, in the attempt to reach diverted income, went further and reached legitimate non-Canadian income of multinational Canadian corporations, even though it was not diverted income.

What we are facing here is the broad problem in a series of highly technical amendments recommended in this brief, which even tax lawyers would have to study carefully. It is the fundamental problem about which these gentlemen are complaining, that an NRO compny is, in effect, a non-resident even though it is organized under Canadian law and was given certain privileges under Canadian law to come here in order to attract foreign capital during a period when the climate seemed to indicate that it was desirable for Canada to provide a haven for foreign capital coming into the country, to help our balance of payments and to do many other things. The climate has changed, but historically that is behind the organization of the NRO's.

Under the new act we have moved towards the conception that if a foreign investor comes here and avails himself of a Canadian corporate medium for his investments, that NRO company, as much as possible, is assimilated to a Canadian resident in every way, with all the consequences resulting therefrom. In effect, the basic point is—and it is something that we discussed in the White Paper some time ago: Are we in favour of penalizing NRO companies and taking the position, "Thank you for nothing in coming here with your foreign capital"; or being a new, developing country, do we say, "We love you, or at least like you. Come up here with your money and help us in using your funds for the expansion of our country, in investments and the like."?

The Acting Chairman: "And we will give you an attractive tax position."

Hon. Mr. Phillips: Yes;—"And this will not be considered as a tax haven," and we so recommended. The Commons committee did not recommend it in quite the same way. Mr. Keeping said that the Commons committee took the same position as the Senate committee. It did to the extent that the NRO company was used as an instrument for Canadian residents. That is a modification, and you say so in your own brief. The Commons committee did not go as far as we did in that respect.

Mr. Keeping: May I quote from the Commons committee report?

The Acting Chairman: Yes.

Mr. Keeping: The Commons committee recommended:

> To the extent possible the NRO be treated as a non-resident for all purposes including tax on capital gains.

Hon. Mr. Phillips: But did you not say that there was some reasoning in the Commons report, that to the extent that it was used as an instrument of tax avoidance by residents it was not to be given that privilege?

Mr. Keeping: That is right. The Commons committee recommended that non-residents be subject to Tax on what is now called taxable Canadian property, largely on the ground that if that tax were not imposed it would leave a loophole whereby Canadian residents could avoid tax.

Hon. Mr. Phillips: Through the medium of the NRO. In other words, to the extent that an NRO—

Mr. Keeping: Not necessarily through the medium of the NRO. For instance, let us take an ordinary private company which owns an apartment house and the shares are held directly by a non-resident. I think the Commons committee felt that if there was not a tax imposed on any gain on disposal of the shares of that company on a non-resident, there would be a loophole whereby a Canadian resident could avoid the capital gains tax.

Hon. Mr. Phillips: Or deemed to be a loophole because the location of the capital asset was deemed to be a permanent establishment, or something of that nature, and should be taxed. Broadly speaking, your fundamental complaint is that the non-resident using the mechanism of an NRO should not be placed in a worse position than the individual himself.

Mr. Keeping: That is the fundamental point.

The Acting Chairman: I understood that from the beginning. I thought you had the two categories of investment to manage, that in one case you got preferential treatment, namely for the individual who had the direct investment here, while if he did it through the NRO he did not get the preferential treatment.

Mr. Mackenzie: I think that is also right. If treaties are re-negotiated so that section 115 comes in and taxes also come in, I think a non-resident of Canada will find himself in a worse position investing in Canada than, say, in Australia or the United States. This is an important point.

Senator Hays: That is the point I was trying to get across, namely, what other countries receive a better deal.

Mr. Mackenzie: If Mr. "X" in London owned more than 25 per cent of a public corporation and he sold those shares, in Canada he would be taxed on the gain.

The Acting Chairman: If he owns those shares in a public corporation in Canada and is a resident of Canada?

Mr. Mackenzie: Yes. He would be taxed on that gain. He would also be taxed on that gain in the United Kingdom.

Senator Beaubien: Could he offset?

Mr. Mackenzie: I imagine he could. Take somebody who is in the Republic of Ireland. There would be no offset, because there is no capital gains tax in Ireland.

Senator Hays: The countries that you have mentioned would be more desirable for investment, namely, Australia and Ireland. You also mentioned another country.

Mr. Mackenzie: I am not sure whether if you owned more than 25 per cent of a public corporation in the United States the capital gains tax would apply to a non-resident.

Senator Cook: I can see the point that a non-resident who invests in a non-resident owned corporation would be no worse off than a non-resident who invests privately. On the other side of the coin, is an investor who owns a non-resident investment corporation any better off than a private investor?

Mr. Keeping: He is worse off.

Senator Cook: Is he any better off?

The Acting Chairman: You mean under the present law?

Senator Cook: No. I was thinking in terms of the amendment. Would he be better off if the amendment goes through than if he were a private investor in the UK?

Mr. Mackenzie: Ultimately, he would suffer capital gains on the disposal of the NRO shares in the United Kingdom.

Senator Cook: But there is a deferral of the capital gains tax?

Mr. Mackenzie: There is a deferral, yes.

Senator Cook: For how long?

Mr. Mackenzie: Until he realizes his shares. You could argue that this would be the same for a non-resident direct investor in marketable securities; he could just postpone the selling of his stock.

Senator Cook: Yes, but that would take place in Canada.

Senator Molson: Mr. Chairman, is not one of the problems the matter of the principle of the new legislation that incorporates capital gains into income, creating, in effect, a penalty for the non-resident in many jurisdictions? if it had been a straight capital gains tax this might not have applied.

Hon. Mr. Phillips: This is one aspect.

Senator Molson: It is one aspect. The gain becomes income in the hands of the foreign recipient and he is penalized.

Hon. Mr. Phillips: Honourable senators, there is a summary of the recommendations here. You will find them at pages 10 and 11 of the brief. There is quite a sophisticated set of recommendations which clearly call for a careful study by your committee and your advisers. I would suggest, if I may, Mr. Chairman, that all this committee may be seized of in the presentation today are the fundamental aspects involved in the treatment and the determination of the basic point as to whether Canada should remain a respectful haven for bona fide investments by non-residents. We have to be concerned as to whether, with the imposition of the capital gains tax, we will introduce such a number of road blocks of one type or another as to invite foreign capital to leave us, or, at least, inhibit foreign capital from coming in. That is what it really amounts to.

The Acting Chairman: Yes.

Hon. Mr. Phillips: In the process you have the philosophy that Canadians are here and, willy-nilly, we are subject to the laws. But the foreigner is not here willy-nilly; he can either come or not come, as he sees fit. To the extent that he is here, he may be caught by the proposed laws.

There aretwo aspects to the proposed legislation. One is that of those who are here, like the gentlemen who are making submissions today. The other, and it is probably a more serious question—I do not wish to appear cynical—is with respect to those who are not here but who otherwise might come if the conditions were fair and reasonable.

Senator Molson: Those who are not here and probably will not come.

Hon. Mr. Phillips: Yes, in all likelihood.

When I ws on the other side of the table, I was strongly in favour of regarding Canada people and one of the great trading nations of the world. I believe it is absurd to take the position that through normal savings, bearing in mind thehigh tax rates and the social content of our legislation, we could ever build up the necessary reserve of capital to bring about the normal expansion of our country; and I took the position then, as I do now, that surely this country requires the NRO companies. I strongly supported the philosophy behind that, many of my colleagues felt the same way, and the Senate generally supported the conclusions arrived at by this committee. We are now facing legislation that says the contrary.

Senator Cook: Would the provisions of the tax treaty affect the reciprocal arrangements?

Hon. Mr. Phillips: Yes; that is another aspect, Senator Cook. We took the position in the report on the White Paper that we were putting the cart before the horse in the treatment of this whole business of international income. There are phasing-out aspects in one sense, crystallization of the legal position from 1976 onwards, and, presumably, on parallel lines we are supposed to work out treaties.

The position taken by the Senate was, "For heaven's sake, work out your treaties first, before you strike in this area in order to determine to what extent you can work out a set of orderly treaties; and when you have worked out a set of orderly treaties with the great nations of the world, then condition the legislation to conform so that we know exactly what our position is." The idea was to take ten or twelve of the leading trading nations—the United Kingdom, the United States, Germany, Belgium, Holland, and so forth—and work out a series of treaties.

We have a situation of an increased imposition of withholding tax here, and we do not even know whether there is a distinction to be drawn between treaty and non-treaty countries. In its effect it becomes a matter of hopeless complexity. The failure to accept the concept that the treaty should precede the treatment of foreign income has created this impasse. If you are dealing with a company based in Ireland or if you are dealing with major shareholders in a non-treaty country, you have one consequence. If you have a revision of a treaty with a treaty country, you have another consequence. You cannot balance out the whole situation in terms of recommendations unless that is known. This committee is faced with a matter of domestic policy preceding the treaties. That is our problem.

Senator Molson: It may be difficult to write these treaties after committing ourselves to a policy in that regard.

Hon. Mr. Phillips: We thought we were rational in our approach. After all, normally the history of locomotion is that the horse does precede the cart, if you want to move forward.

Senator Hays: We did not properly define capital gains either.

Hon. Mr. Phillips: The only proper definition of course, would be negative in its withdrawal, as is proven by the complexities that have arisen.

The Acting Chairman: You say your portfolio is worth approximately $100 million?

Mr. Mackenzie: No, I said the total assets were worth $100 million.

The Acting Chairman: Yes, your total assets. What percentage of that is invested in Canada?

Mr. Mackenzie: I would say 85 per cent.

The Acting Chairman: And how long has this process been going on?

Mr. Mackenzie: Since 1930.

The Acting Chairman: So it is an operation that has been in being for the benefit of Canadian investment for 41 years. Are there other organizations similar to yours that operate in this area?

Senator Hays: Yes, there are a good many.

The Acting Chairman: I just want this on the record. In other words, what we want to get at here is some idea of the magnitude of the problem.

Mr. Keeping: The figure I have heard bandied about would indicate that the amount involved is probably in the vicinity of $800 million to $1 billion.

Mr. A. M. Minnion, Q.C., McMaster, Meighen, Minnion & Co.: I have one group of European clients who have, I would say, an interest of $200 million. I cannot name them at the moment because it is confidential.

The Acting Chairman: And you are just one practising lawyer interested in this field.

Mr. Minnion: Yes.

The Acting Chairman: Senator Molson, do you have a question?

Senator Molson: I merely wanted to query that figure, as to whether it was the amount invested.

Mr. Mackenzie: I think Mr. Keeping was just answering the amount that probably came in via the NRO.

Senator Carter: Are there any major differences between the recommendations in the summary on pages 10 and 11 and the ones in the Senate report on the White Paper?

Hon. Mr. Phillips: The Senate report on the White Paper dealt with the broad principles of non-taxation of non-residents other than in respect of withholding taxes, as moneys moved out of the country for the benefit of the non-resident investor or beneficiary. We never went into detail to the extent that we have here, because at that time, although there was talk of a capital gains tax, it would have been utterly impossible to follow through on the treatment on a mere hypothesis or assumption of a capital gains tax.

For instance, in the Senate report we suggested a capital gains tax of 25 per cent flat not to be included in income. Here again, rationality gave way to something else, in my humble opinion. Although we deserve, I would think, some credit for having annihilated the whole concept of integration, we lost out when capital gains tax came into play, because 50 per cent of it was included in income. Our recommendation was that we supported a capital gains tax, but consistent with our strong views against integration—which, thank God, were accepted in part—we said that if there is to be a capital gains tax, and that was inevitable, there should be a flat rate of taxation thereon. Where there is a flat rate of taxation thereon, the treatment of NRO's under the law now, which calls for remedies in the opinion of these gentlemen, could not possibly have been in the minds of this committee when we considered the White Paper.

The Acting Chairman: Are there any other questions?

Hon. Mr. Phillips: I should like to put forward one thought, if I may. I am looking at page 10 of the brief, which is the series of recommendations. This is getting to be technical, and I will not take too much time over it. As I said a little while ago, real property is being assimilated to part of the operations of an establishment in Canada. What bothers me is "B". A shareholder of an NRO company can sell the shares, make a full capital gain thereon even though there are unrealized gains on Canadian marketable securities in foreign investments. Notwithstanding that, you want to deduct it from the sale price of the shares. In other words, a shareholder of an NRO company may sell at pretty much true worth, even though there is unrealized capital gain on domestic securities and foreign securities, and still you would want to deduct it from the purchase price.

Mr. Keeping: The reason for that is that, when realized, those gains would not be taxable under the bill. The gains on foreign investments and the gains on Canadian marketable securities would not be taxable. However, if one were

selling the shares of an NRO in which there were unrealized gains on those two types of investments, they would be taxable because, as you say, it would be the real value, which would include the unrealized gain. As I said, if an individual who owned an NRO was disposing of certain of his interests, perhaps settling them on his children in his NRO, he could avoid this by selling out his whole portfolio and buying it back the next day, and therefore realize the unrealized gains, and there would be no tax, if his whole portfolio were made up of foreign investments and investments in Canadian marketable securities. Surely, that is an absurdity which would cause a person to sell out his whole portfolio and buy it back the next day?

Hon. Mr. Phillips: The first one, "A," I can see, but suppose that broadly speaking the conception was accepted that the NRO was to be assimilated to an individual, would you not simplify the problem by accepting the suggestion that on the sale of securities there is a flat withholding tax applicable, and that therefore becomes available for the NRO shareholders?

Mr. Keeping: That is what we have advocated here. On Canadian taxable property we have advocated that the non-resident be treated in a similar manner to the resident. In other words, if a resident is a resident of a treaty country providing for a 15 per cent withholding rate on income, we suggest that the capital gains that are taxable, gains on Canadian taxable property, be treated in the same way as they would be treated in the hands of a Canadian resident; that is to say, one-half of the gain would be taxed at the income rate. In other words, if it was a 15 per cent withholding tax rate, he makes $100 capital gain, 50 per cent of that, or $50, would be taxable at the 15 per cent rate, and you therefore preserve the same relationship between the taxation of residents and the taxation of non-residents, the same relationship between the taxation of income and taxation of capital gains.

Hon. Mr. Phillips: Of course, if you took the position that the NRO should not be assimilated to the Canadian taxpayer, you would simplify matters by having a flat rate of taxation applicable to the NRO companies, and that flat rate of taxation would be equivalent to withholding tax before the movement of the proceeds to the NRO shareholder. Where you get yourself in a box here is the movement, as Senator Molson said, of the capital gains into income.

Hon. Mr. Molson: That is the trouble.

Mr. Keeping: To some extent this has been provided for now in the law by the amendments of October 13. They now provide that a special capital gains dividend may be paid out of gains from Canadian marketable securities, and from gains from Canadian taxable property after the 25 per cent tax. There has been some movement in order to identify the capital gains going out from an NRO, and I think that will be of some assistance to the residents of the other countries, who will be able to identify their capital gains. Prior to that amendment of October 13 it all went into the income stream, and it would have made life absolutely intolerable for the non-resident of a country such as the United Kingdom.

Hon. Mr. Phillips: Mr. Chairman and honourable senators, my suggestion is that I do not think we can do much more with this brief, other than send it back to the technical advisers for careful study, and inculde it in our subsequent deliberations.

The Acting Chairman: Is that agreed?

Hon. Senators: Agreed.

The Acting Chairman: Thank you very much, gentlemen.

The Acting Chairman: Honourable senators, next is Loram Ltd., represented by: Mr. Fred P. Mannix, Jr., the President; Mr. D. W. McClement; and Mr. W. G. Gray, Controller. Mr. Mannix will make a preliminary statement.

Mr. Fred P. Mannix, President, Loram Ltd.: Mr. Chairman and honourable senators, first of all I should like to thank you very much for the opportunity to appear before you again. It was a year and a half ago that we were here.

I might remind you that we are involved in major ways in three basic industries: we mine about 37 per cent of the coal in Canada; we are one of the major construction interests in Canada; and we also have a more than minor part in the oil and gas industry, inasmuch as we have the controlling interest in Pembina Pipelines.

There are set out in the brief three basic points which we feel quite strongly on, more on a technical than a philosophical basis.

The point on joint ventures, to do with construction, is on page 12 of the brief. In the construction industry, as you know, a joint venture is very common because of the magnitude of the projects and the associated risks. Partnerships, which we call joint ventures in construction, are very common, not only within Canada but also in the international sphere. We feel that the legislation which is presently operating is much more simple and that the proposed legislation under the new tax law is unnecessarily complex.

The basic point is that these operations are merely extensions in specific areas on a pool basis to reduce exposure because of the very great financial commitments, and it would seem only reasonable for each participant to reflect only its applicable share. Really, we cannot understand the problem, as the legislation is set up, that the minister must feel, because of the great complexity of the law, as he has suggested.

Hon. Mr. Phillips: Mr. Chairman, may I interrupt here again, and draw the attention of the committee to the following. We heard from the construction industry generally. We heard the Canadian Construction Association, and one of the points they raised was the question of the method of treatment of profit and loss in respect of long-term construction contracts and the like. Their representations in that respect are being dealt with in the preliminary report. The construction people also raised the question that Mr. Mannix is raising now, with respect to the subject matter of partnerships, which is a special section under the bill.

Honourable senators will recall that strong opinion has been expressed in some quarters in Canada that the whole section is unnecessary, complex, and not sufficiently important to have been introduced at all, and that, if it were introduced, in any event a distinction should be drawn between partnerships, as such, in the normal sense of the term—all of us here understand in general terms the meaning of a partnership—and a joint venture where A, B, C and D, retain their so-called economic and business sovereignty and contribute their resources, know-how and assets in such a way as to bring about a joint venture. This does not result in a partnership, which is a new legal entity. There is a fundamental distinction between a joint venture, broadly speaking, and a partnership. If A, B, C, and D go together into something that creates a new entity, that is really a partnership. A, B, C and D agreeing to go together . . .

Senator Isnor: For the time being.

Hon. Mr. Phillips: . . . in a common, single undertaking of some kind would more or less constitute a joint venture. All I wish to say is that this subject matter is included for study already in the epilogue material which is presently being considered by your technical staff, and you need not pause any further on that with Mr. Mannix. We know the problem and it is the subject of study.

Mr. Mannix: The main concern is that it would make Canadian construction companies non-competitive in the international sphere and would certainly impose problems within Canada as well. We already have problems in dealing with competitors from other countries, and this would unnecessarily complicate our position in dealing with international matters.

Hon. Mr. Phillips: In other words, what you are telling the committee is that you could live with this act without the whole section dealing with partnerships being there; and that, to the extent that it is there, it hurts you rather than helps you?

Mr. Mannix: That is right.

The Acting Chairman: I take it that when you talk about joint ventures with reference to the construction industry you are not confining your remarks to the construction industry. I gather from your opening statement that you are involved in areas of the economy other than construction where joint ventures do in fact get established.

Mr. Mannix: That is correct.

The Acting Chairman: Is there any other branch?

Mr. W. G. Gray, Controller, Loram Ltd.: It is very much so also in the oil and gas undertakings.

The Acting Chairman: And you are familiar with that?

Mr. Gray: Yes.

The Acting Chairman: And your remarks would apply to the oil and gas industry just as they do to the construction industry?

Mr. Gray: Yes, that is correct.

The Acting Chairman: That is your first point.

Mr. Mannix: The second point really starts on page 7, stating that, "The new provisions taxing proceeds on sale of mineral rights results in gross retroactive taxation of capital."

The proposed legislation says that the cost of mineral properties incurred after 1971 will be allowed as a deduction in determining taxable income, and the proceeds from the sale of mineral rights will be included in income, even though the properties may have been acquired prior to 1971 and no deduction has been allowed for their cost. We basically run into a point where, if you have acquired a property before 1971 and then you sell it, you have no deduction for the comparable cost, and this is retroactive taxation.

We feel this is unnecessarily harsh and retroactive and that anybody who is in a position of already assembling properties, coal properties, for example, and then subsequent to this taxation sells that property will be taxed on 100 per cent of the proceeds, with no deduction for the cost of assembling that property.

Hon. Mr. Phillips: Is that dealt with specifically in respect of mineral rights?

Mr. Gray: Yes, sir. It is phased in.

Hon. Mr. Phillips: Have you the section where that appears?

Senator Beaubien: Mr. Mannix, surely there will be some value for that property on valuation day?

Mr. Mannix: They are not allowing that as a deduction, sir, as I understand the act.

Hon. Mr. Phillips: Have you a section in the act that supports that statement, because that comes as a surprise to us?

Mr. Gray: I will get that section for you, sir.

Hon. Mr. Phillips: Then shall we suspend that, Mr. Chairman, and proceed to the next point?

The Acting Chairman: Yes. Perhaps you could take the third point, Mr. Mannix.

Mr. Mannix: The third point is depletion, and we refer to that on page 8. It is proposed that the present depletion allowances be replaced by a concept of earned depletion. This proposal is unfair to taxpayers with a mine in production at the present time, or when the legislation was announced, because they may not be required to expend further moneys on exploration, which would contribute to a depletion bank. As a result of that, where they have based the economics on the present ten-cents-a-ton depletion, for example, and they have based the economics of a mine on the existing circumstances beyond the phasing-in period, they will lose the depletion if they are not in a position to or do not spend the money to earn the depletion in a bank.

Hon. Mr. Phillips: Mr. Chairman, I should like to direct myself to Mr. Mannix on that point. Mr. Mannix you are

addressing a group of gentlemen who have been through this business for the last month, roughly. We have heard from a number of very important companies both in the mining industry, as such, and in exploration and development, as such, as distinguished from active mining operations, and we have heard from the oil and gas industries. Conclusions have already been arrived at with respect to the whole subject matter of depletion, to the extent that I do not think you have dealt with any items that are not already covered at some length by us. I do not want to shorten your presentation, but I want you to know that we have gone into practically every element you have raised in your submission with respect to depletion. Before the end of the day you may be reading about it. Certainly, before the end of the week you will. It is not likely that we have overlooked any items you have referred to in your depletion study.

The Acting Chairman: In other words, Mr. Phillips is saying that you are pretty good because you agree with us.

Mr. Mannix: Thank you, sir. There is just one other point I might mention. In the coal industry we have to compete with the coal industry of Australia, for example, and of various other countries. We find that in the coal industry if we have an earned depletion bank concept we are in a much more difficult competitive situation vis-à-vis countries that have depletion on an earned income basis. In other words, it is a percentage of income.

The Acting Chairman: Particularly where you have established mines.

Mr. Mannix: Precisely.

The Acting Chairman: And I take it that in Alberta you do have extensively established mines.

Mr. Mannix: That is our position at the present time. We have six established mines which we are operating. For an established miner this is unduly harsh, we feel.

Hon. Mr. Phillips: If you were a member of this committee, we might be able to go into the section in more detail, but I do not think we can do so with you now, Mr. Mannix. I think you had better leave depletion alone, because it is completely dealt with by this committee already and there is no use in stating to you that which is covered and that which is not covered, because that is for the Senate to consider. I would suggest that all you can do is leave your brief here and let us see, in due course, whether or not we have met you on it.

The Acting Chairman: I wonder if Mr. Gray has come up with that section.

Mr. Gray: Yes, it is section 59(3) and (4).

The Acting Chairman: That deals with the disposition of resource property acquired before 1972. I note that it is a long section, but perhaps it would be as well to read it into the record.

Senator Beaubien: It does seem to be an important point. I think you should read it.

Hon. Mr. Phillips: Yes, Mr. Chairman, I think you should.

The Acting Chairman: Section 59, subsection (3) of Bill C-259 reads as follows:

> 59. (3) Where a taxpayer has made a disposition after 1971 of property owned by him on December 31, 1971 that
>
> (*a*) is property described in any of subparagraphs 66(15)(*c*)(i) to (vi) and is not property described in paragraph (1)(*c*), or
>
> (*b*) would be property in subparagraphs 66(15)(*c*) to (vi) if the references therein to "in Canada" were read as references to "outside Canada",
>
> the following rules apply:
>
> (*c*) the relevant percentage of the amount receivable by the taxpayer as consideration for the disposition thereof shall be included in computing his income for his taxation year in which the disposition was made, notwithstanding that the amount or any part thereof may not be received until a subsequent taxation year; and
>
> (*d*) where the taxpayer and the person who acquired the property were not dealing with each other at arm's length, for the purposes of this section, section 64 and section 66
>
> (i) the cost to that person of the property shall be deemed to be the amount included in the taxpayer's income by virtue of paragraph (*c*) in respect of the disposition by the taxpayer of the property, and
>
> (ii) when that person subsequently disposes of the property of any right or interest therein, the amount receivable by that person as consideration for the disposition shall be deemed to be the relevant percentage of the amount actually receivable by that person as consideration therefor.

I am sure we are all greatly enlightened by that.

Then section 59(4) reads as follows:

> (4) For the purposes of paragraphs (3)(*c*) and (*d*), the "relevant percentage" of any amount receivable as consideration for the disposition of property is 60% plus the percentage (not exceeding 40%) obtained when 5% is multiplied by the number of full calendar years in the period commencing at the end of 1972 and ending with the end of the calendar year in which the disposition was made.

Hon. Mr. Phillips: I think, Mr. Chairman, that honourable senators would like to include in the record their appreciation of the precision, clarity and phraseology of the section.

Senator Beaubien: Now, you tell us what it means.

Hon. Mr. Phillips: I am not going to attempt to do so. Having recorded our appreciation, I think that here also we can only take cognizance of it and have it really studied, because you have a series of references, as you can see, to other sections which involve exclusions.

The Acting Chairman: For the purposes of the record it might be helpful if our witnesses here were to give us their interpretation of it.

Hon. Mr. Phillips: And possibly some guidance, Mr. Chairman, as to why, if your interpretation is right, it is there at all. Usually there is some motivation behind the introduction of a section which would seem to exclude from capital gain the deduction of the cost or valuation, whichever is higher, because that is what you are saying, is it not?

Mr. D. W. McClement, Loram Ltd.: It seems very inconsistent with the rest of the features where they allow you a capital base at the start of the act.

Hon. Mr. Phillips: Do you have any clue on that?

The Acting Chairman: Just a moment. Mr. McClement, would you mind repeating your comment, because it is rather important and we have a reporter here who has to take it down. So would you mind repeating what you said, and not too quickly, please, because we want to get it on the record.

Mr. McClement: It seems very inconsistent with the rest of the features of the act which start out taxing capital subsequent to the implementation of the capital gains tax on January 1, 1972, presumably, because this section taxes all capital right from initiation. Say it went back to 1800, it would tax the whole process. Now, of course, it is scaled down a little because in the first year it only taxes 60 per cent, and then it escalates up 5 per cent a year, so after 10 years it taxes 100 per cent of the proceeds, even on a property that may have been acquired in 1800, which is gross retroactive taxation and hard to comprehend.

Senator Burchill: Has this been brought to the attention of the officials of the department?

Mr. McClement: Through the Coalmine Operators Association, yes. They presented a brief pointing this out.

The Acting Chairman: When was that brief presented?

Mr. McClement: About three weeks ago.

The Acting Chairman: Do you know if any part of the representations have been reflected in the amendments that have been laid before the House of Commons?

Mr. McClement: Not, we understand, to date.

Hon. Mr. Phillips: But we will still put the question, Mr. Chairman, with your approval. There usually is a reason—and in many instances the reasons are not good, and the reasoning may not be sound—but why this unusual section applicable to mineral rights?

Mr. Mannix: We do not know why. It is inconsistent from the point that it does not value the mineral rights at a time, and the only reason I can see is perhaps the very great difficulty in valuing a mineral property, say, one that was completely unexplored at the start of the act, and this would be the only reason that we can see that they would say, "We do not take a value as of January 1, 1972," and for that reason they have phased in a progressive tax.

Senator Beaubien: But, Mr. Mannix, if you sold the property just after January 1, 1972, and got $10,000 for it, that would give you a pretty good idea of the value it had on December 31, 1971.

Mr. Mannix: That is correct, but that would not be allowed as a deduction.

Senator Beaubien: But if you have something that you can sell in January, 1972 for a price, surely that gives a good idea of the value of it two or three weeks before that?

Mr. Mannix: That is correct, but historically many properties are held for a long period of time. We have properties, for example, that were picked up in the early 1950's and which may not come into development for another 10 or 15 years. How do you value that as of January 1, 1972, if you have not had, for example, some sort of appraisal mechanism; and the difficulty of the appraisal mechanism is the only reason that I can suggest for this section of the act.

Hon. Mr. Phillips: Well, what do you suggest to overcome that difficulty?

Senator Beaubien: But that cannot be a good reason, Mr. Phillips, because if somebody owns the property and dies, then somebody makes a valuation.

Mr. Mannix: That is correct, and we suggest that the property should be valued at the start of the new system, and that from then on any increase in value be taxed accordingly as a capital gain. This section is inconsistent with the rest of the legislation from the point of view that it does not take a start value, if you want to call it that, at the start of the new system. With everything else a value is taken, but with regard to mineral properties the legislation is not written in that way.

The Acting Chairman: An arbitrary valuation is provided.

Mr. Mannix: That is right, and through the actual section there is not one provided as a cost, and instead of taxing it as a normal capital gain, they have phased in something that retroactively taxes any value accumulated to the date of the start of the system.

Senator Cook: Even if the owners had evidence to say it was worth $1 million, they would not be heard.

Mr. Mannix: That is correct.

Senator Beaubien: It does not make any sense.

The Acting Chairman: It might very well be that the committee would want to hear evidence from the officials of the department on this point.

Hon. Mr. Phillips: I do not think, Mr. Chairman and honourable senators, that we can do more than take cognizance of this point for study.

The Acting Chairman: Are there any other questions, honourable senators?

Are there any other points you would like to make, Mr. Mannix and gentlemen?

Mr. McClement: I just gather it is too late for a capital gains tax at this point. That is accepted. I think we feel that we are still a pretty young country for that point.

The Acting Chairman: It is too late for a separate capital gains tax rather than one whereby the capital gain is added to income.

Senator Molson: He is of our team, Mr. Chairman, but I am afraid his help has come a little late.

Hon. Mr. PHillips: We made that recommendation, as you know, in the Senate report and we failed on that.

Mr. Mannix: I would like to thank you very much Mr. Chairman and honourable senators.

The Acting Chairman: Thank you very much indeed.

The Acting Chairman: The last brief is being presented on behalf of Anglo American Corporation of Canada Limited. Those appearing are: Mr. J. David Taylor, Q. C., Director, and partner in the law firm of Fasken & Calvin; and Mr. Gerald J. Risby, Vice-President-Treasurer and Director, Anglo American Corporation of Canada Limited. Mr. Taylor will make a preliminary statement.

Mr. J. David Taylor, Q. C., Director, Anglo American Corporation of Canada Limited: Mr. Chairman and honourable senators, we appreciate the opportunity of appearing before you once again in connection with your hearings on tax reform. We have filed our brief with you, which contains a certain amount of background material, and part of this will be familiar to you from our earlier appearance. In essence, it shows that the Anglo American Corporation of Canada Limited is the investment arm in Canada of what is probably the largest mining finance group in the world. This company has assets in Canada of $127 million. As the brief indicates, we have a policy of re-investing the earnings from these Canadian investments, subject to what would be considered a modest return by way of dividends repatriated abroad. The principal investments of this group are in the resource industry. You have received a great many submissions from such groups.

One of our potential investments is in Baffin Island, where the total investment, if you include financing cost, would be in the order of $300 million. This investment has been very adversely affected by Bill C-259.

Senator Cook: About which project are you speaking?

Mr. Taylor: The Baffin Island project, on page 2. It is an immense iron ore deposit which is very pure; and because of its remoteness it is a very expensive project to develop.

Senator Benidickson: Is this the property in which Madsen Gold Mines Limited have an interest?

Mr. Gerald J. Risby, Vice-President-Treasurer and Director, Anglo American Corporation of Canada Limited: Yes, it is the same property.

Senator Cook: It does not appear on your chart.

Mr. Taylor: No, we do not show anything on our chart but wholly-owned subsidiaries. This is a potential development in which, when it commences, this group would have the controlling interest.

In our submission to you we will not be elaborating with respect to depletion and other matters in connection with the resource industries. However, I did want to point out that so far as the new earned depletion rules are concerned there would be contained within this $300 million figure almost $8 million for townsite, $34 million for a railroad and bridge, and $46 million for dock and harbour facilities, none of which would be eligible for earned depletion.

The Acting Chairman: Was there a change made at the recent Meeting of Ministers of Finance with respect to railroads? I do not think there was an amendment, but I thought some change was made.

Mr. Taylor: I have not been made aware of any changes.

Senator Benidickson: Mr. Chairman, I made that assertion yesterday after reading the Toronto *Globe and Mail.* I read it again this morning, and it does not appear to be in as positive language as it was yesterday. It indicated this morning that the Minister of Finance had simply told the Quebec treasurer that in relation to earned depletion he would give very careful consideration to the inclusion of railroads under the new proposal.

Senator Molson: There is nothing mentioned about infrastructure?

Senator Benidickson: No, there is nothing mentioned about social infrastructure.

Mr. Taylor: I was aware that you had representations made to you on this matter; and I simply wanted to make the point that there is at least $30 million invested in a railroad and bridge on this project.

The Acting Chairman: Mr. Taylor, I wonder if we could return to the Baffin Island investment project. You spoke briefly about this aspect of it. Is the fact that infrastructure social capital investments do not earn depletion the main problem in connection with the Baffin Island project?

Mr. Taylor: No, our brief sets out in detail the fact that, in our judgment, the change in concept from percentage depletion to earned depletion makes this, as any other project, inherently less attractive to us. We consider the earned depletion concept to be stingy in the areas it contains. It is a combination, in fact, with the loss of the three-year tax holiday and other aspects. I do not think any of them can be quantified, but we can say that all of them, taken as a whole, make this project, which is risky and speculative, far less attractive.

Senator Benidickson: What is your opinion of its relationship to investment in other countries, where taxation might be more attractive or less onerous?

Mr. Taylor: Simply with regard to that aspect, we consider that investments in Australia or Ireland are now inherently much more attractive to the group as a whole. One of the points made in the brief is that the Canadian company, for which we are particularly speaking this morning, will now perhaps be told by the greater group that its resources will be devoted to Australia and Ireland in preference to Canada.

Senator Cook: This is a remote area, is it not?

Mr. Taylor: Very remote.

The Acting Chairman: It could not be more remote.

Senator Cook: Did we not recommend in our report on the White Paper that mines in remote areas should reveice special consideration?

Hon. Mr. Phillips: Yes, we did, and to the extent we have dealt with this subject matter it will be reflected in today's report.

Senator Burchill: Do you measure the life of an ore body such as that in the Baffin Island project when making your investment?

Mr. Taylor: We can only say at the moment that there is such an immense quantity of ore there that sufficient to ensure the financing of a project of this type. It is believed, without being able to demonstrate it, as would be necessary for public financing, that the reserves are incredibly large.

Senator Burchill: How will you calculate the life of the railroad for purposes of write-off?

Mr. Taylor: It will be needed for at least 30 years, sir, by which time there will probably be a different type of transportation.

The Acting Chairman: Your company is not an NRO company.

Mr. Taylor: No, I wish to make the point that this company has not come in as an NRO, which I regard as a company which attempts to remove all dividends from this country, subject ot whatever withholding taxes may be applied.

This company has followed a deliberate policy of reinvesting the major portion of its earned income here. The effect of the treatment it will receive under the new bill will force a change of that situation.

We know you have had many submissions with regard to depletion; we do not know if you have had any with respect to this point. The cardinal problem facing this company is that it is not a public company under the provisions of the new bill. It is a private company and, despite the size of these investments which in Hudson Bay Mining, for example, amount to $60 million, they are still not controlling interests, but portfolio investments.

Here we stand, a private company with portfolio investments, which under the bill will be taxed by a special refundable tax of 33-1/3 per cent. This applies to a private company regardless of size. The consequence of that is that if it is wished to recover that tax, dividends must be paid. Examination of the chain of companies shown in the chart contained in the brief will illustrate that to recover the 33-1/3 per cent tax, dividends must eventually be paid abroad and a 15 per cent withholding tax paid for non-residents. It becomes a simple question of whether it is desired to pay a tax of 33-1/3 or 15 per cent.

Hon. Mr. Phillips: I do not usually do this, but I wish to compliment the author of this brief. It is very important, and I would suggest that the senators read it carefully.

We included at the top of the list in our so-called epilogue the subject matter of private companies. In my opinion, the distinction drawn between private and public companies in this respect is one of the most unwise aspects of the bill.

I was amazed by the distinction, which is as follows. The phrase "private corporation" is distinguished from "public corporation" in the sense of the public corporation being listed on stock exchanges, and so forth. If such a corporation has investments in Canadian companies, the dividend income from one Canadian company to another Canadian company is tax-exempt. That has been moved over from the present law. The dividend forms part of the undistributed earned income and is distributable at any time in the form of a public dividend. It is only then that the matter of taxability to the local shareholder, resident or non-resident applies. The non-resident pays withholding tax, and the resident in accordance with his tax rate.

A private company such as that referred to by Mr. Taylor, having all its investments in Canadian companies, is subjected to a 33-1/3 per cent tax.

Senator Beaubien: Which it would not pay if it were a public company.

Hon. Mr. Phillips: That is correct, and it is refundable only when the tax-exempt income brought in is paid out as dividends to shareholders. The result of this, as Mr. Taylor points out, is that an important Canadian company which has thus far, as indicated in the brief, received 3 per cent average income on its investment, will pay a 33-1/3 per cent tax. On moving into the hinterland of Canada, taking long-term views as to what it should do with its accumulated income, as is proven by its investments in these major companies, in wanting to reach into such places as Baffin Bay and the like, it is subject to a 33 1/3 per cent tax immediately, if it does not declare the dividend out. If it declares a dividend out, to the extent that you have non-resident shareholders, those non-resident shareholders are subject to what is now a 15 per cent withholding tax. What will it be under the new law? Whether it will be 15 per cent or in excess thereof depends on whether it is a treaty or a non-treaty country.

I may say that after 50 years in tax practice I found that to be the most amazing aspect of the entire legislation. The rest is complex but, at least, if you had the patience, you could work the thing out. I could never understand why bona fide companies such as these people who are building up capital and using the money for further investment, and all the rest of it, should be forced to declare it out.

In effect, what we are doing in respect of all private companies is putting a freeze on the accumulated savings of our country to the extent that it is in corporate form in private companies. What is the net result? Moving over to the Canadian field, of Canadian companies controlled in Canada, it is another way of inviting foreign capital.

To the extent that we are in bondage to non-resident shareholders—legitimate bondage, because we welcome

the money here, and I say that with all due respect, but nevertheless it is servitude and bondage economically—we are saying to private companies in Canada, "You are subject to a 33 1/3 per cent tax if you want to build up your further reserves of investment. You owe it now, and you can get it back only if you declare your dividends out." It is another way of saying that we are penalizing thrift and savings which, in my day and in that of all honourable senators, was considered a virtue rather than a vice. In effect, what we are now saying is that it is vicious to be thrifty.

Senator Cook: "Invest your money in Canada,"—

Hon. Mr. Phillips: "... and we will tax you." A classic example is that of a company with a 3 per cent yield historically on investments that will now be forced to pay 33 1/3 per cent on its income or, alternatively, will be subject to withholding tax, and will not have the further reserves of capital for expansion. This is a subject matter which we hope to deal with in what we call the second bite of the cherry. It has not been dealt with by honourable senators in the presentations we have had to date, but it is top on our list if we can get to it in time. I think, Mr. Taylor, you have made a superlative case here because of your record.

Senator Benidickson: Does that apply to a private company, whether it is controlled by Canadians or whether in this case it is controlled by people outside Canada?

Hon. Mr. Phillips: There is no difference.

Senator Benidickson: If it is controlled outside Canada and they want to pay dividends, there is a 15 per cent withholding tax.

Hon. Mr. Phillips: For non-treaty ones I think it goes up to 25 per cent.

The Acting Chairman: Would you agree, Senator Phillips, that it is not only a penalty on thrift, but it is also a road-block to further development in Canada?

Hon. Mr. Phillips: Yes. That is what I mean. It is a very serious thing; it penalizes thrift.

Senator Cook: And it forces money out of the country.

Hon. Mr. Phillips: If you are going to be subjected to a withholding tax, or alternatively a 33 1/3 per cent corporate tax, it does not make any sense.

Mr. Taylor: You have no option but to distribute.

The Acting Chairman: You will go from Baffin Bay to Bantry Bay.

Mr. Taylor: That is right. There will be a loss to our group in this country of $1,300,000 a year from its dividend flow. It will go either to our Government in tax, or it will just go out of the country and will not come back.

Senator Cook: What is the rationale of that? What is behind it?

Hon. Mr. Phillips: It is the philosophy against accumulation of savings without declaring dividends out. There is merit to the conception that with moneys accumulated by way of exempt income there should be some method of getting it out within a reasonable period. Further, the philosophy behind the exemption is that public companies are under pressure of shareholders. They have a public board of directors subject to dividend pressures. The market place determines the policy of public companies. Presumably the retention of the exempt income will be related to dividends required plus corporate needs, and the shareholders will be instrumental in bringing pressure to bear on the directors to cause a distribution of dividends. Therefore, under the new bill, they said to public companies, "Keep your exempt income". But when it came to private companies, there is no such pressure, and therefore they said there must be some way of preventing undue accumulation of wealth.

Anticipating that, we took the position in the Senate, when dealing with the White Paper, notwithstanding the views in certain quarters that we were allegedly representing vested interests, we were the only ones to take a concrete position on this—compared to that of the committee in the other place, which is supposed to be the portector of the small man—and said that if at the end of five years—we drew no distinction between public and private companies—exempt income is not declared out as a dividend, then at the end of the fifth year from the date of its receipt a penalty tax of 15 per cent should be payable by the corporation to the revenue of the country.

That 15 per cent paid by the corporation would not be a credit on any dividend subsequently declared to the shareholders; in other words, it could be an appropriation of a surplus. When a divident was declared out of $100 and the 15 per cent penalty was paid, the shareholders would be taxed on the $100 and not on the $85.

This Senate committee recommended that, and we were the only ones in the study of the bill that insisted that exempt income be taxed. What we said was that there were reasons why companies might not be able to pay out exempt income immediately; there may be indebtedness to banks or attractive investments and that type of thing, and, therefore, we said, "We will give the recipient of exempt income five years to get rid of that dividend. If the corporation does not get rid of it within five years by declaring it out to the shareholders, then the revenue of Canada will receive a windfall of 15 per cent of that undistributed income."

Now, what have they done? We get quite the contrary. We get the public corporations still exempt and the private corporations subject to a rate of 33 1/3 per cent, refundable only if the corporation declares the dividend out.

Senator Burchill: Does the entire dividend have to be declared out?

Hon. Mr. Phillips: Yes, the entire dividend must be declared out in order to get the refund.

I believe, Mr. Taylor, you can prorate it; in other words, if you declare half of it out you get half of your 33 1/3 per cent, but you do not get your whole 33 1/3 per cent unless you pay out the whole dividend.

Senator Gélinas: Mr. Taylor, have you made direct recommendations to the Department of Finance?

Mr. Taylor: No, we have not. We were invited to re-attend here by this committee before we got that far, and we though this was the best forum we could find.

Our suggestion for curing this is a simple one; it is not complex. In fact, we have three suggestions, one of which could work, but we do not think it is sufficiently attractive.

I would like to deal with each one, if I may, Mr. Chairman.

The Acting Chairman: Yes, please do.

Mr. Taylor: It is obvious that our problem is that we are being treated as a non-public corporation when, in fact, we have all the postures of a public corporation as far as this country is concerned. That is the real source of our difficulty. We are looking for means that would enable us, as a matter of right rather than regulation, if that is possible, to elect to be taxed as a public corporation. There are regulations proposed for companies which list on stock exchanges, but there has never been a hint of forthcoming regulations with respect to a company like ours, which at the moment, for reasons which we set out in the brief—whatever its long term intentions may be—does not list on the Toronto Stock Exchange or any other stock exchange in Canada. We suggest, in order to avoid this outflow of money from Canada, that non-resident corporations be entitled to elect to be taxed as public companies. In this sense they would lose some advantages, but, in our eyes, the opportunity to retain the dividend income in this country is worth while and we will give up the other advantages to get this one.

Senator Cook: What advantages would you give up?

Mr. Taylor: The ability to make certain capital repayments which public corporations cannot do and private corporations can do. I hesitate to venture further than that, because I find the rules governing private corporations so incredibly complex that I am sure I will make a wrong statement.

Our second suggestion would be that if the Government is concerned that if it does grant overall exemption of this type to a non-resident corporation, such an overall exemption might lead to tax abuse, then limit it to non-resident corporations of a limited size.

In paragraph 305 of our brief, at page 79, honourable senators, we suggest a simple test. This test is clearly understood in Canada because it is the same test that is in the Canada Corporations Act in order to determine whether or not a company must make its financial statements public. It would be a simple matter to say that any company which is obliged, under the provisions of the Canada Corporations Act, to make its financial statements public, is entitled to elect to be taxed as a public company under this proposed act.

Senator Beaubien: That sounds like a sensible solution.

Senator Molson: It is a small step.

Senator Benidickson: But those private companies that are not obliged to make public their financial statements are relatively small private companies.

Mr. Taylor: That is right.

Senator Benidickson: Would you still qualify? You spoke earlier of an investment in one property of $300 million. I believe a company with over $10 million . . .

Mr. Taylor: It would be an easy test for us; we are well above either side of the test.

The virtue, if you can call it that—I do not necessarily say it is—of putting an absolute size in as the test is that it would allow the Government, if it chose, to perpetuate the business of forcing income out of the smaller private investment companies.

We believe that one of the purposes of enacting this legislation with respect to private companies, as Mr. Phillips has said, is to force dividends out of a company—which are taxed in the company, say, at 50 per cent—to a shareholder who is so well off that he is going to be paying 60 per cent on the income he gets. This is the reason for insisting on this refundable tax on portfolio investments. If that is a virtue, and I do not say it is, it could be avoided by making the test one where we could only elect to be taxed as a public company if we had assets in excess of $5 million and revenue over $10 million.

Senator Cook: Do any of these corporations have revenue of over $10 million?

Mr. Taylor: I cannot imagine there being too many of them.

Senator Hays: They are putting the private companies on the same basis for tax as an individual?

Mr. Taylor: That is their intention.

Senator Hays: The private individual pays his tax on this basis. It is just a matter of degree. If he has no income and he is worth $20 million or $30 million he is taxed on that basis. It appears to me a private company would be taxed on the same basis as an individual.

Hon. Mr. Phillips: That is correct.

Mr. Taylor: We just feel it is inappropriate to treat us as a Canadian individual citizen in terms of what we are and what we are trying to do. We should be able to elect as a matter of right and not regulation to be taxed as a public company.

Senator Hays: You want deferral until such time as it is realized?

Mr. Taylor: This cures the problem of maintaining our existing posture. We are not asking for favoured treatment with respect to other Canadian companies.

Senator Cook: The proposals are not economic; they would be forcing money out of the economy.

The Acting Chairman: As regards the background of this company, that is eminently true.

Hon. Mr. Phillips: Senator Hays put his finger on it. There is a fundamental question of policy as to whether a distinction should be drawn between private companies, who can get exempt income, and individuals, who are immediately subject to a tax rate. The answer is related to the higher issue of economics and expansion, and whether it is desirable to build up within reason a legitimate amount of investment pool.

Senator Hays: Reserve money.

Hon. Mr. Phillips: Reserve money for investment. If an individual gets it, one of the big arguments is that even though he is paying his tax thereon the rest is purchasing power and is lost; the average individual does not save it; probably he will buy a gift for his wife or do something, and it peters out. Whereas, if you get it into pools of capital in corporate private companies, it is available. Obviously that can be done; all you do is make the rich richer by having a pool.

Senator Hays: Accumulation.

Hon. Mr. Phillips: Our idea in the Senate was that it must go out. If it does not go out, then, by heavens, the revenue is entitled to a penalty on windfall income. We suggested 15 per cent. It could even be more than 15 per cent after a reasonable period; even 20 or 25 per cent—so as to avoid the social abuse of undue accumulation of capital in private companies.

Senator Hays: He might redirect his whole operation to a different form of investment as well, saying, "I am now looking for depreciation, and that sort of thing, to invest those moneys that are not used." Would that be right?

Mr. Taylor: It is a possibility.

Senator Cook: Would not this be a better alternative, a better idea?

Hon. Mr. Phillips: The difficulty with this idea is that, first of all, Mr. Taylor's point covers relief for the bigger companies and not for the small ones. Secondly, it would give relief to non-resident shareholders of this type of company rather than to Canadian shareholders. It is an alternative approach. For a company with such a good working record as this company, it seems to be desirable. I think at this stage we have covered this point. I personally think it is one of the most important items in the bill, which deserves the attention of this committee.

Senator Beaubien: Would it be possible to have a special act of Parliament to make this company a public company?

Hon. Mr. Phillips: You do not have to do that. Mr. Taylor gave reasons why the company does not wish to go public. There are all sorts of reasons.

The Acting Chairman: They are in the brief too.

Hon. Mr. Phillips: Today a company such as Mr. Taylor's company could go ahead and create a preferred stock if it has not got one; it could sell it to the public between now and December 31 and, bingo, you are a public company.

The Acting Chairman: With all the advantages.

Hon. Mr. Phillips: You get your exempt income. All he has to do is to create a class of stock.

Senator Hays: Pay your lawyer and go to Miami!

Hon. Mr. Phillips: Get it sufficiently attractive as to rate. I am not counsel for the company, and Mr. Taylor and his clients must have reasons why they do not want to go public. But it does not mitigate or reduce the merits of the case simply to say, "Why don't you go public?"

Senator Beaubien: They may have to.

Hon. Mr. Phillips: If they do not get relief they probably will.

Mr. Taylor: May I speak on this point? Even if we had a very good bland stock market and our pre-investment in Hudson Bay had not had this very long strike, and copper prices were up, so that Anglo American itself would find it a very good time to go public, sooner or later this will happen. Even if that happens, you still do not solve the problem for a non-resident investor in terms of re-investment. If you look at the chart at the back of our brief, our shareholders in An-Can itself are to a certain extent private Canadian companies. We have mentioned Interlink Investments as a specific example. This is a Canadian company incorporated in this country. It has $27 million worth of net assets at the moment. It cannot elect to be taxed as a public company; this company will never be listed. If Interlink is not allowed to elect to be treated as a public company—I do not know that is much of a favour, but that is what they would like—that company's net assets will be repatriated, and there is a substantial loss to the economy, $27 million worth of assets, and the presence of those in Canada as opposed to outside of Canada is gone. There is just no economic choice here; you either pay the 33 1/3 per cent tax or say, "We will take it abroad. We will only pay 15 per cent." Who can expect a non-resident to suffer that?

Senator Cook: Maybe have a combination of both, two tests.

Hon. Mr. Phillips: I think, Mr. Chairman, we are thoroughly seized of this aspect of the brief.

Senator Hays: We get the point.

Mr. Taylor: It is our cardinal point. The others, as I say, we are concerned about, such as the treatment of resource industries, which you have heard about from other people; we are equally concerned.

The Acting Chairman: The material in your brief will be very carefully screened.

Hon. Mr. Phillips: Might I ask Mr. Taylor to repeat the three alternatives, the three suggestions? I think you jumped from one to the other, but I do not think you gave them in seriatim order. Which do you like most? What is the order?

The Acting Chairman: Give them in the order of priority in which you prefer them.

Mr. Taylor: The first priority is to allow a non-resident company, which meets the tests presently set out in the Canada Corporations Act, to elect to be treated as a public company.

The Acting Chairman: For the purposes of the Income Tax Act.

Mr. Taylor: For the purposes of the Income Tax Act. That would let a company which is large in its own right, or large because of its affiliates, have that treatment.

The second—which is a very much simpler approach but not, I think, necessarily as desirable, because it might lend itself to abuse, or the fear of abuse by Canadians—is just to let any non-resident corporation elect to be treated and to be taxed as a public company.

Senator Hays: Would you say that again?

Mr. Taylor: Our first test is the one of absolute size, so that you are dealing only with substantial investors. The second one is to say that any non-resident corporation, even if it has only $100 in it, can take this treatment if it wants to. It has been suggested to us, when discussing this concept, that it might lend itself to some form of tax abuse. I do not quite understand how, but if there is that concern, then I am suggesting the first alternative, that you must have a company of a certain size to get this right to elect.

Our third suggestion is to recognize that there has been in this company, and a great many others, a very substantial investment made in this country under the old tax rules, and we should say, "Fine, we will have two pools of investment. We will have pre-1972 investments and post-1972 investments." The non-resident who comes in tomorrow knows that he gets the new treatment, and if he choses to suffer that it is his affair. On the investments presently in the country, you would account for them separately and say that dividends from existing investments are entitled to this exempt status.

Hon. Mr. Phillips: Including replacement if you sold?

Mr. Taylor: We have tried to be modest in our proposal. We thought it should be the dividends on the stocks, if you like, that we now hold.

Hon. Mr. Phillips: The freeze.

Mr. Taylor: The freeze. You look at those and say that if you had something you could convert into those stocks, convertible bonds, they would be included if you now own those bonds or options. All those rights would be included. If Hudson's Bay amalgamated with another company, for instance, the securities that came out on that amalgamation would continue to be given this treatment. We do not think this is attractive, because we think it is complex and the act is far too complex as it is.

Hon. Mr. Phillips: Mr. Taylor, I think that if I were a minister of the Crown I would eliminate No. 2 because it is a privilege for non-residents as against Canadians. It would not be a particularly attractive suggestion, because we would be putting the non-resident in a somewhat privileged position. I think we are down realistically to No. 1, under the Canada Corporations Act, or No. 3, a freeze of the present assets and their replacement.

Senator Carter: Do you not think that No. 3 is politically more attractive? It is more complex, but there are two disadvantages in No. 2.

Hon. Mr. Phillips: I think No. 3 is obviously politically the least troublesome because it is not retroactive in its effects, whereas No. 1 might be regarded as something in favour of bigness, in terms of $10 million of gross revenue and $5 million of assets under the Canada Corporations Act. However, we understand it, sir.

Senator Molson: By law, you have made some requirements of these companies, because of their bigness. It could be argued—I do not know how well—that all you are doing now is carrying that a small step further, because, as the Canada Corporations Act demands, you are giving them similar treatment under the Income Tax Act.

Hon. Mr. Phillips: One might say that although No. 1 has certain limitations, they can elect and even reduce, for purposes of the exemption under No. 1, gross revenue and the amount of assets, so that bigness does not have the attraction of the exemption. But at least No. 1 and No. 3 Mr. Chairman, are worthy of careful study.

I think, Mr. Chairman and honourable senators, you would want us to tell Mr. Taylor and Mr. Risby that the whole question of depletion and the treating of financial resource industries has been exhaustive studied. Do you agree? So you have lost nothing by not dealing with it now.

Senator Benidickson: In referring to non-resident ownership, I notice on the chart a reference to something called investors groups. Is this what we know as the Winnipeg based investors group?

Mr. Taylor: That is correct, sir.

Senator Benidickson: From the chart, approximately 10 per cent is referred to. Does that mean that the investors group owns 10 per cent of Anglo American, or vice versa?

Mr. Taylor: They own 10 per cent of Anglo American.

Senator Benidickson: That is a distinct Canadian organization that has a fairly substantial interest in Anglo American. I probably think of that one because it is near where I come from.

Mr. Taylor: They have been investors for several years.

The Acting Chairman: Are there any other questions? Have you any further points you would like to make, Mr. Taylor?

Mr. Taylor: We obviously are, and must be, concerned about the intention to tax non-residents in certain areas which are not now taxed, which are not provided for by the treaties. I think it will be very difficult to have these included in our treaties.

Hon. Mr. Phillips: The whole question of treatment of non-residents is expected to be the subject of a study by

this committee. We are seized of all, or a good many, of the difficulties.

Mr. Taylor: The one thing that is perhaps peculiar to this group is that it has the habit of sending its executives here and to other countries on limited tours, three-year or five-year tours, or something of that sort. The Canadian proposal to tax someone who is here for that limited period of time, on gains abroad which are not realized, we find most awkward. It is just the sort of thing that it is almost impossible to police. There are obvious opportunities for evasion.

Hon. Mr. Phillips: Are you discussing the exist provisions?

Mr. Taylor: Yes.

Hon. Mr. Phillips: I think that is worthwhile, if the Chair and honourable senators would take five minutes on that. Let us take that up and take five minutes on it.

Mr. Taylor: It is page 18, paragraph 7. I think the points we want to make are the points you have in front of you. It could create incredible problems about enforcement, because it lends itself to a man deciding he is never going to tell this country what his foreign assets are when he comes here. In any event, if he is honest and says there is an unrealized gain of $5 million or $1 million on his investments in South Africa or England, and he pays the tax here, he gets no help at home. It is not going to be recognized in most of these jurisdictions for a foreign tax credit. So you are really asking the man to become a saint in his own lifetime.

The Acting Chairman: Or a criminal.

Mr. Taylor: Yes. He has incredible opportunities.

The Acting Chairman: What about the capital gains on Canadian investments that he would make while he was in Canada?

Mr. Taylor: We are not opposing that sort of thing. We think that if a man is here and is earning income here, he should pay tax here just as any other individual.

Hon. Mr. Phillips: He is a resident.

Mr. Taylor: We just say that we should perhaps ignore this, because you cannot catch what happens to his assets abroad. Let us forget about those and look to what happens to him while he is in this economy. If he makes capital gains while he is here, then tax him in the same way as you tax any other Canadian resident.

Hon. Mr. Phillips: Would you approach this from the point of view of citizenship?

Mr. Taylor: I do not think that is possible. We would take the residence approach.

Hon. Mr. Phillips: The suggestion is that if you have a representative or official of an international company, who retains his citizenship of another country, say the U.K., and is only here for, say, five years and he is technically a resident of Canada but he clearly retains his characteristic of a transient—

Senator Beaubien: As an American does?

Hon. Mr. Phillips: —that in those cases the exist rule should not apply, as Mr. Taylor says in the brief:

> 7.03. We can appreciate the Government's concern with respect to people who have enjoyed the economic benefits of Canadian residence and then removed their assets tax free from Canada.

We touched on that, and not too lightly, last evening, when dealing with our report.

> However, if an individual is a citizen of a foreign state—

That is why I picked it up on Senator Connolly's point.

> —and is only resident in Canada for a short period of time, it is unrealistic to tax him on accrued gains on foreign property, where these relate to property owned by him prior to entry into Canada.

The Acting Chairman: Mr. Taylor, would it be possible for you to give us a form of words which might constitute an amendment? It occurs to me that this one might well be the subject matter of a draft of a short amendment. I do not think it would be a complicated one. I do not think the other would be complicated, either. If you would give us both, we would be grateful.

Senator Hays: Would they not deal with the fact that this is temporary in the regulation? Would that not be dealt with there?

Senator Benidickson: No one likes to invest $100 million based on a change in the regulation.

The Acting Chairman: We do not want to see it in the regulations.

Senator Hays: Would that not be the way the Government would manage it?

Mr. Taylor: Not necessarily.

Hon. Mr. Phillips: I do not think so. Are you speaking of the exit problem or are you speaking of the private corporations? I think the exit problem goes to the hard core of the matter. It is a substantive matter, senator.

The Acting Chairman: It is dealt with in the act now.

Hon. Mr. Phillips: As you know, senator, we have made some recommendations.

Senator Cook: This is only a small point, Mr. Chairman, but should it not say where these relate to property owned by him prior to entry into Canada? He might get foreign property after he comes into Canada.

Mr. Taylor: Again we were trying to take the modest approach to this. If, for example, senator, he buys property with his Canadian-earned income . . .

Senator Cook: But he might be left property.

Mr. Taylor: Well, I think something acquired by gift or bequest should be exempted.

Senator Cook: It is only a small point.

Hon. Mr. Phillips: I would suggest, Mr. Chairman, that we ask Mr. Taylor to prepared an amendment on the exit

problem, and also one with respect to private corporations. It is purely a personal suggestion, but I think you should deal with election under the Corporations Act, and you alternative No. 3 and leave out No. 2.

Senator Carter: Does the Income Tax Act classify taxpayers other than as residents and non-residents? Do they have temporary residents and that sort of thing?

Hon. Mr. Phillips: No. Either you are a resident or you are not a resident.

Senator Carter: Is there any merit in creating a third category, then?

Hon. Mr. Phillips: Well, this is a suggested amendment for those who are here who are citizens of another country and are here for a period not exceeding five years. The suggestion in respect of their non-resident capital assets is that there would be no deemed-to-be capital gain on departure. The direct answer to your question is that you are either a resident or you are not.

The Acting Chairman: It is something very peculiar to the Canadian economy because of not only the need for foreign capital but the need for foreign technology, know-how, skills and that sort of thing.

Are there any further questions, honourable senators? I thank both witnesses very much indeed.

The committee adjourned.

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Hon. Mr. Phillips: —that in those cases the exist rule problem, and also some with respect to private corporations. It is purely a personal suggestion, but I think you should deal with section under the Corporations Act, and you alternative No. 3 and leave out No. 2.

Senator Cheffins: Does the Income Tax Act already take care of those who are not residents and that sort of thing?

Hon. Mr. Phillips: No. Either you are a resident or you are not a resident.

Senator Cheffins: Is there any merit in creating a third category which would be suggested somewhere for those who are visitors or another country

The Acting Chairman: Mr. Taylor, would it be possible for you to give us a form of words which might constitute an amendment under section 3 or the Senate by Canada

the subject matter of a draft of a short amendment. I do not think it would be a complicated one. I do not think the other would be complicated, either. If you would give us both, we would be grateful.

Senator Hays: Would they not deal with the fact that this is temporary in the regulation? Would that not be dealt with there?

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THIRD SESSION—TWENTY-EIGHTH PARLIAMENT

1970-71

THE SENATE OF CANADA

PROCEEDINGS

OF THE

STANDING SENATE COMMITTEE ON

BANKING, TRADE AND COMMERCE

The Honourable SALTER A. HAYDEN, *Chairman*

No. 49

WEDNESDAY, NOVEMBER 10, 1971

Twelfth Proceedings on:

"Summary of 1971 Tax Reform Legislation"

(Witnesses—See Minutes of Proceedings)

24313—1

THE STANDING SENATE COMMITTEE ON BANKING, TRADE AND COMMERCE

The Honourable Salter A. Hayden, *Chairman*

The Honourable Senators,

Aird	Grosart
Beaubien	Haig
Benidickson	Hayden
Blois	Hays
Burchill	Isnor
Carter	Lang
Choquette	Macnaughton
Connolly (*Ottawa West*)	Molson
Cook	Smith
Croll	Sullivan
Desruisseaux	Walker
Everett	Welch
Gélinas	White
Giguère	Willis—(28)

Ex officio members: Flynn and Martin

(Quorum 7)

Order of Reference

Extract from the Minutes of the Proceedings of the Senate, September 14, 1971:

"With leave of the Senate,

The Honourable Senator Hayden moved, seconded by the Honourable Senator Denis, P.C.:

That the Standing Senate Committee on Banking, Trade and Commerce be authorized to examine and consider the Summary of 1971 Tax Reform Legislation, tabled this day, and any bills based on the Budget Resolutions in advance of the said bills coming before the Senate, and any other matters relating thereto; and

That the Committee have power to engage the services of such counsel, staff and technical advisers as may be necessary for the purpose of the said examination.

After debate, and—

The question being put on the motion, it was—

Resolved in the affirmative."

Robert Fortier,
Clerk of the Senate.

24313—1½

Minutes of Proceedings

November 10, 1971
(62)

Pursuant to adjournment and notice the Standing Senate Committee on Banking, Trade and Commerce met this day at 9:30 a.m. to further examine:

"Summary of 1971 Tax Reform Legislation"

Present: The Honourable Senators Hayden (*Chairman*), Connolly (*Ottawa West*) (*Acting Chairman*), Beaubien, Blois, Carter, Cook, Everett, Flynn, Gélinas, Isnor, Macnaughton, Martin, Molson and Walker—(14).

The Chairman being occupied with other business of this Committee and upon motion duly put, it was Resolved that the Honourable Senator Connolly (*Ottawa West*) be elected Acting Chairman.

In attendance: The Honourable Lazarus Phillips, Chief Counsel.

WITNESSES:

Institute of Profit Sharing:

Mr. R. A. Campbell, Chairman, Director and Vice-Chairman, Wheelabrator Corporation of Canada Ltd., and President, Metal Laundry Ltd.;

Mr. H. M. Cunningham, Treasurer; Assistant Treasurer, Canada Packers Ltd.;

Mr. B. A. Diekman, Executive Director;

Mr. H. A. King, Vice-Chairman; Vice-President, Personnel, Simpsons-Sears Ltd.;

Mr. N. P. Ovenden, Director-Treasurer, Procter & Gamble Company of Canada Ltd.;

Mr. M. G. Welch, Tax Supervisor, Allstate Insurance Company of Canada;

Mr. Edward Hall, Simpsons Limited;

Mr. T. van Zuiden, Dominion Foundries and Steel Limited.

Insurance Bureau of Canada:

Mr. H. Norman Hanly, Chairman, Federal Legislation and Liaison Committee and President, Dominion of Canada General Insurance Co.;

Mr. David H. Atkins, Consultant and Partner, MacDonald, Currie & Co.;

Mr. E. H. S. Piper, Q.C., General Counsel.

At 11:00 a.m. the Chairman having arrived, the Honourable Senator Connolly (*Ottawa West*) took his seat among the Members.

The Royal Architectural Institute of Canada:

Mr. Jean-Louis Lalonde, President, F.R.A.I.C.:

Mr. C. F. T. Rounthwaite, Vice-President, F.R.A.I.C.:

Mr. Wilson A. Salter, Director of Professional Services, F.R.A.I.C.:

Mr. Keith Sandford, Special Consultant.

The Teachers' Insurance and Annuity Association of America:

Mr. John T. DesBrisay, Q.C., Counsel;

Mr. Wilfred Wilson, General Counsel.

At 12:30 p.m. the Committee adjourned to the call of the Chairman.

ATTEST:

Frank A. Jackson,
Clerk of the Committee.

The Standing Senate Committee on Banking, Trade and Commerce

Evidence

Ottawa, Wednesday, November 10, 1971

The Standing Senate Committee on Banking, Trade and Commerce met this day at 9.30 a.m. to give consideration to the Summary of 1971 Tax Reform Legislation, and any bills based on the Budget Resolutions in advance of the said bills coming before the Senate, and any other matters relating thereto.

Senator John J. Connolly (*Acting Chairman*) in the Chair.

The Acting Chairman: Honourable senators, Senator Hayden will not be here for about an hour. We are going to hear four presentations this morning: the Institute of Profit Sharing; the Insurance Bureau of Canada; The Royal Architectural Institute of Canada; and The Teachers' Insurance and Annuity Association of America.

Is it your wish, honourable senators, to take these representations in the order in which I have read them?

Hon. Senators: Agreed.

The Acting Chairman: Then we will call first on the Institute of Profit Sharing. Mr. Campbell, would you like to come forward with your colleagues?

Mr. R. A. Campbell, Chairman, Institute of Profit Sharing: Mr. Chairman and honourable senators, on behalf of the members I would first like to thank you for allowing us to appear before you today, and I should like to introduce to you my colleagues. In alphabetical order, they are: Mr. H. M. Cunningham, Treasurer, from Canada Packers; Mr. E. Hall of Simpsons Limited; Mr. H. A. King of Simpsons-Sears Ltd.; Mr. N. P. Ovenden of Procter & Gamble; Mr. M. G. Welch of Allstate Insurance; Mr. T. van Zuiden of Dominion Foundries and Steel Limited; and last but not least, our President and Executive Director, Mr. B. A. Diekman.

All these gentlemen are here with me to try to answer any questions you may care to raise in connection with the brief we have submitted to you. None of them is here on behalf of his own company. We are here to represent the well over 50,000 employees covered by the profit-sharing plans of our 70-odd members. In last Friday's *Globe and Mail* I saw that Senator Hayden, as chairman of your committee, had already presented preliminary recommendations which, if accepted, would have the effect of eliminating some of the serious inequities in connection with employees' profit-sharing plans which we brought to your attention. So serious were these inequities that we simply did not believe them to be intentional, and we said so in the brief before you. On behalf of all our members who operate profit-sharing plans, we are indeed grateful for your recommendations.

The Acting Chairman: Of course, you are aware that our recommendation is no guarantee of success?

Mr. Campbell: We realize that, but we do appreciate the fact that you have taken such a great interest in our cause, because we think it is a very good and worthy one.

There are two items outstanding at this time regarding employees' profit sharing plans. Lump sum averaging should continue to be available to members of employee profit sharing plans. As Bill C-259 now stands, section 36 disappears and there is nothing adequate to take its place. The second point is only a technical variation on a recommendation that Senator Hayden has already made, and that is that capital gains should be taxed as capital gains. If a member of the employees' profit sharing fund withdraws his holdings in cash, the portion of that cash that represents unrealized capital gains of the fund should be taxed as capital gains in the hands of the employees.

The Acting Chairman: At the time of his retirement.

Mr. Campbell: Let us deal now with deferred profit sharing plans. We contend that if the proposed tax reform bill goes through without a change, it will, for all intents and purposes, kill deferred profit sharing plans. The Government is not making deferred profit sharing plans illegal; but it proposes to penalize a member of a deferred profit sharing plan with heavy taxes and the member has virtually no choice but to take his benefit in the form of an annuity. There is nothing basically wrong with an annuity, but by far the majority of employees who are members of a deferred profit sharing plan have traditionally preferred to take their benefits in a lump sum. The desires, hopes and aspirations of thousands of employee members have been built up over the years on the expectation that they would receive a lump sum on retirement. At this moment a member of a deferred profit sharing plan who takes his benefit in a lump sum can take advantage of a tax rate averaging facility under the existing section 36. Under the proposed tax reform that facility will be taken away from him and it will be replaced by an averaging system that has but a minimum effect. Section 36 becomes the cornerstone of a perfectly legitimate and widely beneficial activity of an employer sharing with his employees the profits which their skill, enthusiasm and labour have produced. Remove that cornerstone and the whole structure comes tumbling down. Is it not a specious breaking of faith with the public to permit a perfectly legitimate practice to flourish and expand for many years and then, suddenly, for no reason that we have been able to ascertain, abrogate the law and so destroy the whole foundation of deferred profit sharing?

Mr. Chairman, as one who has practised profit sharing for many years, I could talk endlessly on this subject, but I will not take up your valuable time by doing so. Let me conclude by saying that profit sharing does not only benefit the small employee who, without it, might never have a chance to build capital of his own which could make him secure and independent in his retirement years. Not only that, but having some capital behind him he remains a far greater tax revenue producer than if he were forced to live on a fixed annuity.

The Acting Chairman: Would you like to explain that point briefly?

Mr. Campbell: For example, if you were on a fixed annuity and you worked hard all your life, as many labour people have to, to pay off a mortgage on their little house, or to put a boy or girl through college, this takes just about everything they have accumulated in their lifetime. If they need an additional sum to take a trip to see Aunt Minnie in Great Britain, or to pay off their mortgage, or to send a third child to college, how are they going to do this on a fixed annuity pension? It is most difficult.

The Acting Chairman: We have had evidence on earlier occasions that very often these lump sum payments are re-invested in businesses by people who are able to run a new business after retiring from their original business.

Mr. Campbell: Thank you senator, I was going to come to that. This is true. I think you will agree that at present the norm is to retire at 60 or even 55. People with great amounts of capital set up thriving businesses and pay great corporation taxes to our government. In our own company we have a case where a young engineer started with us after graduating, around the age of 22, and in 15 or 20 years he has a large sum of capital. The only way he can get this capital out is to leave the company. They get this lovely little lump sum of $25,000 or $35,000 and they start a business which is relatively adequately financed and not completely dependent on bank loans. As you know, the bank interest rates have been rather high.

Senator Macnaughton: Would $20,000 to $35,000 be an average amount on retirement?

Mr. Campbell: We began our plan in Canada in 1961; and in 1970 our average employee, with a $500 maximum contribution, would have around $24,000 to $25,000 to his credit. This is in 10 years.

Senator Isnor: What proportion of that amount was paid by the company?

Mr. Campbell: As I have said, the maximum amount paid by the employee was $500 a year, so for 10 years it would be $5,000 total. The company's contribution would be $15,000.

The Acting Chairman: That is taxed on the employee's hands, as it came into his hands?

Mr. Campbell: His own contribution, yes. He has paid tax on the $5,000; but the company's contribution, which varies as you well know, is limited to $1,500 per employee. This will be changed under the new act. He pays tax on this amount when he takes it out.

The Acting Chairman: Under section 36?

Mr. Campbell: Yes.

The Acting Chairman: I would like to ask one very general question. I am sure honourable senators have other questions to ask, but you have said that in your organization you have 70 member companies with 50,000 employees who are entitled to benefit. Would you like to hazard a guess as to how many other companies and their employees might be involved in similar deferred profit sharing plans that are not members of your organization?

Mr. Campbell: I certainly would, because part of my job as Chairman of the Institute is to run down these figures. I would say there are in excess of 100,000 working employees directly involved in profit sharing plans. As you know, the plans vary but they are basically the same. What so many people do not realize is that profit sharing plans are not a substitute for poor wages; they are over and above the normal going rate of wages.

Senator Isnor: Mr. Campbell, do all of the colleagues who are with you today use the same profit sharing plan?

Mr. Campbell: No, senator, the plans vary. In principle they are similar, but there are many different types of profit sharing plan, some being combined with pension, some being cash, as you know. I would like to have Mr. Welch answer that question because he is one of the tax experts, of Mr. King.

Mr. M. G. Welch, Tax Supervisor, Allstate Insurance Company of Canada: There is one point which was brought up by Senator Isnor regarding whether these were executive or non-executive employees.

Senator Isnor: No, I made the observation that this would apply mostly to executives because of the large amount involved, as mentioned by Mr. Campbell.

Mr. Welsh: We have a case of a girl in Vancouver who works in our service and claims department. She is a service representative; she is not a manager or supervisor. She has been in the plan for 15 years and has contributed $3,600. The company has contributed $6,600. She now has to her credit $22,000 after 15 years.

Senator Isnor: That is an exceptional case is it not?

Mr. Campbell: Oh no, it is not an exceptional case.

Mr. Welch: I have a whole list before me. If she stays with the plan another 15 years she will have at least four times that amount, and probably more. She will have at least $88,000 and probably $60,000 will be capital gain. She would be taxed on $30,000 capital gains. We feel that the retention of the lump sum averaging principle is so important. If this person wishes to go into a business or wishes to use it for some other purpose on retirement, with the lump sum averaging principle removed it will be impossible for her to do this. This is very significant to people right down the line. This particular person makes around $7,200 a year. She is not in the high income bracket, and she is not an exception.

Mr. T. van Zuiden, Dominion Foundries and Steel Limited: Mr. Chairman, may I make a comment? I think we should

understand that in all of the plans that we have been talking about this applies equally to all employees in all companies.

Mr. Campbell: Right from the chairman of the board to the men who sweep out the back shop. This plan is for all employees; it is underlined four times. The only difference is the amount contributed. If one cannot afford to contribute $100 or the maximum of $500, he still shares in the profits.

The Acting Chairman: Would you care to comment on what you think might be the reason for the requirement in the bill that an annuity be purchased, rather than a lump sum payment taken?

Mr. H. A. King, Vice-Chairman, Institute of Profit Sharing: We have had many discussions with representatives of the Department of Finance regarding this forcing employees literally, by high taxation on a lump sum, to buy annuities. Although they have never actually said this in so many words, one reason is that it might be more socially acceptable and would ensure that the individual at the age of 65 would not squander the lump sum.

The Acting Chairman: Did the officials of the department tell you that this was their reason?

Mr. King: No one actually said that. When asked the reason for doing this, no one ever says that they are afraid that a lump sum in the hands of a retiring employee will be spent in a prodigal way. However, having attempted to ascertain the reason, we can only conclude by what they do not say that that must be it.

In our particular company, Simpsons-Sears, approximately 99 per cent of our employees withdraw the lump sum. None has ever, to my knowledge, become a money waster or a welfare burden in the community.

Senator Isnor: 99 per cent are individuals of that type?

Mr. King: Most of them take their shares of the company and keep that as an investment. That will represent approximately half of what they have. In that way they continue their identification with the company and have a hedge against inflation. Most of our employees have been shareholders and have held their shares until retirement.

The Honourable Lazarus Phillips, Chief Counsel to the Committee: I am sure you will appreciate from the interim report, which you saw last week, that this committee has given serious consideration to this whole problem.

Mr. King: Yes.

Hon. Mr. Phillips: As I understand the situation, generally you are happy with our suggested treatment with respect to capital gains. That is more particularly so in the case of companies in which part of the deferred profit is reflected in the shares of the company employer. Am I correct in that?

Mr. Campbell: We think that is very equitable.

Hon. Mr. Phillips: So the committee need not be seized further with that particular aspect.

Mr. Campbell: That is correct.

Hon. Mr. Phillips: Are we really down to the point where this committee did not go as far as suggested in the Simpsons-Sears brief? I forget whether Allstate took the same position, but it was the transposition of the current section 36 into the new bill. Without that transposition, because the committee did not go that far, you still feel that it will be difficult to live under the new bill, on the assumption that our representations are reflected in amendment?

Mr. Campbell: Yes, we must have this averaging bcecause otherwise, particularly in deferred profit-sharing plans, the whole system collapses.

The Acting Chairman: Would you point out to the committee the averaging in section 36 which is most helpful to you?

Mr. Campbell: I think it is fair to everyone. The last three years prior to retirement is averaged, which in most cases is the most highly productive and highest paid period. There might be the odd exception, but most people then are at their highest remuneration level.

Hon. Mr. Phillips: Honourable senators will find that at page 2 of the brief, under the heading "Proposed Section 147, 'Deferred Profit-Sharing plans'". The reference to section 36, saying that it is crucial, which is basically your case, appears in the second paragraph on page 3.

The Acting Chairman: Mr. Phillips, would you care simply to put before the committee the averaging permitted under section 36, and the proposed general averaging formula which the brief indicates has only a minimal effect?

Hon. Mr. Phillips: I suggest that the witnesses draw the distinction based upon a certain defined income.

Mr. Campbell: Would you please tell us what you wish us to discuss?

The Acting Chairman: The committee might be interested to know the difference between the averaging permitted by section 36 of the present act and the proposed general averaging formula provided in the bill, which your brief describes as having only a minimal effect.

Mr. van Zuiden: The general averaging, as provided in the bill, gives the member retiring from our Dofasco plant probably not more than a 10 per cent reduction from the tax that he would pay if he were taking his withdrawal as a lump sum and paying the marginal rate. It is actually a useless provision in so far as it applies to our plant and possibly to some of the others.

The Acting Chairman: What is the formula for general averaging which the bill provides and to which you object?

Mr. van Zuiden: I do not object to the formula, but I think it has more application for those with a very high income, such as actors, in a short span of years.

Mr. Welch: It is more important to deferred profit-sharing plans, but it is also important to employee profit-sharing plans. Almost every member who stays in for 30 years

will be faced with the problem of having a large sum of money taxed at a given time.

The Acting Chairman: At marginal rates, or a little better.

Mr. Welch: Yes. We are considering two types of averaging. One is the old section 36, which is lump sum averaging. I do not consider that this has been carried forward into the new legislation at all.

General averaging is something entirely different, with a different purpose. Lump sum averaging under section 36 was for specific cases of employees or individual taxpayers receiving large sums of money at the end of their working life.

Hon. Mr. Phillips: I know the answer and the definition, but I think it should come from the witnesses themselves. We are all clear that under section 36 the last three years prior to the profit-sharing plan coming into effect are taken. I believe the Chairman desires further clarification for the senators of the situation involving the last three years with, presumably, the highest compensation, which is different from ordinary averaging, as you say, such as that for actors, athletes and others.

Mr. Welch: It is not the average of his prior marginal rates. It is the average of the total tax paid, as related to his total income. Some people in the 35 or 40 per cent marginal tax rate bracket would end up with perhaps a 20 per cent average, when comparing his total tax paid to his total income before deductions. This is the way it is done equitably. He is being taxed on the large lump sum in relation to total taxes paid, and total income over three years.

The Acting Chairman: That is under section 36.

Mr. Welch: Yes. The general averaging is for the purpose of smoothing out incomes of all taxpayers, mass application, and is in no way comparable to lump sum averaging under section 36.

Basically, an over-simplification of how it works is that if in a given year you have an income which is 10 per cent higher than the previous year and 20 per cent higher than the last four years, that income is considered to be your base. On that base you pay at your normal marginal rate. Let us assume that somebody receives $8,000, $9,000, $10,000 or $11,000 over four years, and in the last year he gets $30,000. We take the average—

The Acting Chairman: The $30,000 is paid out of the deferred profit-sharing plan?

Hon. Mr. Phillips: No. We are talking about general averaging, as distinct from section 36.

The Acting Chairman: Mr. Welch, for the record, we want to be clear on what you are saying.

Mr. Welch: Forget the figures I have just mentioned. Take it that in the fifth year he has an income which is 10 per cent higher than his prior year and 20 per cent higher than his average for the past four years. The higher of those two amounts is taken as his base, and he pays normal income tax on that. The figure may reach the 40 per cent bracket. Anything beyond that base goes up from his marginal rate, but in steps that are made five times larger. In other words, if, from his base, he was in a 37 per cent bracket, and he receives another $2,000, he would then be in the 39 per cent bracket. It takes $10,000 to reach the 39 per cent bracket. Basically, he is building on his marginal rate. There is no real averaging of that lump sum. It is averaging of income over the years.

Hon. Mr. Phillips: It is similar to situations where actors may be unemployed for a number of years and then strike a hit. They receive a contract, and that contract may include a percentage of the profits. That is the type of general averating we are talking about.

Mr. Edward Hall, Simpsons Limited: You pay tax on marginal rates up to the threshold. The problem is much more equitable for the lower income employee getting a lump sum, because he is taxed at the marginal rate up to the threshold, before the averaging begins. Part of the problem is that it hits the lower-income employee much more than the higher-income employee.

Hon. Mr. Phillips: Would you not agree that in cases where your profit-sharing plan suffers from the acquisition of shares of the employer company, your averaging problem under section 36, which has been taken away from you, is less serious than in the case of a company which does not have that type of return on a deferred profit-sharing plan? Roughly speaking, do we have more profit-sharing plans which include share-acquisition in the employer company than those who do not? We may probably have been affected by the presentation of Simpsons-Sears, which emphasized the acquisition of shares in the company.

Mr. King: I am from Simpsons-Sears. I would say that so far as we are concerned section 36 could disappear if what the committee has recommended is accepted.

Mr. Campbell: I would say that 65 per cent do not have shares in our companies.

Hon. Mr. Phillips: I do not think the committee was seized of the vital importance of the transposition of section 36 in the new act. The question of lump sum averaging was considered, but the capital gain aspect and roll-over provision received more attention, as you saw from the committee's recommendation. You have used rather strong language in your brief. You say that it is crucial that section 36 be retained in its present form.

Mr. Campbell: I would say so.

Hon. Mr. Phillips: Is there any suggestion of a modified form which would involve less than that which section 36 gives, and more than that which has been taken away? I believe in compromise. If you ask for a return of something which has been taken away, you present a good case in asking for its return, but the likelihood is that you will not get it. Has any one of you given consideration to a mid-way point rather than the transposition of section 36?

Mr. van Zuiden: In our case there is very little that you can gain from having the capital gains treatment on withdrawals, and it is vital for our plan that section 36 be retained, if at all possible.

On the question of compromise, I believe, as Mr. King pointed out, that there has been no statement from Government officials on the philosophy behind the ligislation. I assume that they would take the profit-sharing plans right out of the picture. I do not think there could be a compromise as a substitute for what appears to us to be a philosophy against lump sum payment.

Hon. Mr. Phillips: Philosophy is one thing; but you are taking the position that there is no alternative to section 36. That is an unusual conclusion, because there is always room for compromise.

Mr. van Zuiden: The tax paid under the section 36 treatment is roughly equivalent to that which would be levied if a retired person took out an annuity.

The Acting Chairman: You are saying that the tax to be collected under section 36, if it remains in the bill, would be approximately the same as that which would result form the purchase of an annuity and the annuity were taxed?

Mr. King: It depends on the individual's personal income. It is true to a degree, but generally speaking the tax paid under section 36 will exceed that pid by anyone using that amount of money to purchase an annuity.

Mr. Campbell: Most of these plans are for the common man, the little people, for whom we, as an institute, are here.

The Acting Chairman: The annuity requirement, then, has the effect of reducing the tax revenue.

Mr. King: Yes, and I would think by a great amount.

Senator Beaubien: Mr. Chairman, could we have some examples? It is quite difficult to follow.

Hon. Mr. Phillips: First of all, honourable senators, if you turn to page 5 of the brief you will find the highlights of the subject matter we were discussing a few moments ago. The chairman asked me to deal with this, but I think it should be left to those interested to deal with. It concerns the approach of lum-sum averaging and general averaging, and it explains that general averaging is for mass application to "smooth out" year-to-year irregularities in ordinary income.

The Acting Chairman: As might be the case with an actor.

Hon. Mr. Phillips: Yes, or sometimes even a salesman on commission who gets a bonanza order. In such cases as these you get peaks and valleys, and the aim is to reach something of a plateau.

The Acting Chairman: The farmers and fishermen have this too.

Hon. Mr. Phillips: You get a plateau instead of a mountain peak or a valley.

We are dealing with an entirely different point here, and that is in respect of a deferred profit given, presumably, at the time of retirement, with the right to average it out having regard to the last three years' compensation. That is roughly the difference. We are told there is no alternative to section 36, and the Crown thus far in the new bill has simply deleted section 36.

Senator Cook: Mr. Chairman, I would like to get some clarification with respect to the social benefits. If an employee retires and he receives, say, $25,000 or $30,000 in a lump sum and he dies within a year, can what is left of that amount be passed on to his family? What happens if he is forced to purchase an annuity in the amount of $25,000 or $30,000 and then dies within a year? Does it cease, or does his estate get a return of capital?

Mr. Campbell: He would get some return of capital.

Our plan is only ten years old, but our American company's plan has been in force since 1947. In our own Canadian company, and our employees are very high earners, just about every employee has taken out only 60 to 65 per cent of any lump sum payment and put it in an annuity so that they would know they would have something.

The Acting Chairman: And I suppose a good deal would depend, Senator Cook, on the provisions of the annuity contract.

Mr. B. A. Diekman, Executive Director, Institute of Profit Sharing: It depends on how the annuity is elected. If the annuity dies with the beneficiary, then, that will be the end of it. But, for instance, my own annuity does not die with me; it continues to my wife if she survives me.

Senator Cook: But it is common in an annuity contract that there is some guarantee of a return of the sum, is it not?

Mr. Campbell: So many equal payments.

The Acting Chairman: Or for life, or for a term of years, so that if there are survivors the survivors will benefit. In the case of a person, for example, who is a widower or a bachelor, let us say, perhaps he will have it for a term of years and if he does not survive, then his estate is entitled to a certain benefit.

Hon. Mr. Phillips: Mr. Chairman, may I put a question? Is there a record in the institute of the number of employees who choose lump sum payments as distinguished from those who choose annuities?

Mr. Campbell: Not in the institute. We were a branch of the American Council of Profit-Sharing Industries until two years ago, and, as you well know, the tax laws are so vastly different in the United States that we chose to form our own group. We are still closely connected with our American company and they help us a great deal, but we do not have such figures. We do have some figures from our own company and, as I said, the plan is only ten years old. We have moved our plant from Toronto to Oakville, and we have lost employees, and virtually all elected the lump sum payment.

The Acting Chairman: That is in your company only?

Mr. Campbell: Yes.

Mr. King: In the case of the Robert Simpson Company, the last complete year we have records for, there were 459 people who retired and only four chose to take the annuity. That is less than one per cent.

Senator Cook: The general question is this: The compulsion, if you like, to take the option of an annuity does entail a sacrifice on the part of the purchaser of the annuity, apart from the fact that he will not have the lump sum. In other words, if he invested it he would not get back as much as he put in.

Mr. Campbell: I do not believe he will.

Mr. Welch: I would not agree with that. He could purchase an annuity, and if he lives a long time he may take out more in the long run. He can get a guarantee for five, ten or twenty years and slightly less annual income as a result of asking for a 20-year guarantee; but if he dies after ten years his estate receives the benefits for the next ten years. There is no way you can say that he might not do as well. He might do much better. The big thing that affects people is that they want the lump sum to give them the independence of a capital amount so that they can make some choice in their years of retirement and become a vital human being. The person who retires today does not want to go to his room in the corner of some garret and live on a monthly stipend. He is an interested, active human being, who wants to be part of society; he wants to play his part in society. He wants to go out and get another job to renew his interest in life. He may buy a small business of some kind. We have an electrician who retired last year and he has now put himself into a small servicing and repairs business. This was made possible with the benefits from his profit-sharing plan.

Hon. Mr. Phillips: As I see it, going back to this committee's report of last week, your group is working on the principle that gratitude is the lively sense of favours to be received. Is that it? You are thankful for the recommendations made to date?

Mr. Campbell: Yes, very thankful.

Hon. Mr. Phillips: Nevertheless, that is in the past. Gratitude is the lively sense of favours to be received, not including those we have already recommended, and you are insisting that section 36 is absolutely vital?

Mr. Campbell: We sincerely believe so, sir.

Hon. Mr. Phillips: And you are asking this committee to reconsider its position on this point and supplement its recommendations.

Senator Beaubien: Mr. Chairman, have we looked into what appears to me to be the retroactive effect of this legislation? For example, supposing I had bought a farm expecting that I would receive, say, $30,000 in two years' time, as a result of Bill C-259, if passed, would I not get a much smaller amount? If I had been working for 28 years and had two years to go, would this bill not be retroactive, resulting in my paying a larger portion of tax?

The Acting Chairman: Certainly, this bill changes the rules before the end of the game.

Senator Beaubien: Should we not insist then, with respect to contracts which have been entered into with employees, that those employees should get the same amount after taxes?

The Acting Chairman: I do not believe the company is at fault; it is the change in the tax rules.

Senator Beaubien: No, the company is not changing anything.

The Acting Chairman: That is right.

Senator Cook: Just along the same lines, Mr. Chairman, if we did not have section 36, the great majority of cases would have to elect to purchase annuities.

Mr. Welch: That is right.

Senator Cook: And if we do have section 36, would anyone care to hazard a guess as to whether or not it is going to cost the country very much in the way of lost tax revenue?

Mr. Campbell: I think you will get more revenue.

Mr. Welch: The retention of section 36 will provide greater revenue than will the deletion of section 36.

Senator Flynn: There is no doubt this bill will create more revenue for the Government, despite the statements made by Mr. Benson.

Mr. Hall: Mr. King distributed this table of comparisons of income tax payable. Column 1 is the tax payable under section 36 of the present act, and column 3 is a rough comparison of the tax revenue received if the person elects to take an annuity guaranteed for ten years.

The Acting Chairman: Would you identify the document you are reading from, please?

Mr. King: I will identify it as being some eight or ten cases from our profit-sharing records. These are actual employees.

The Acting Chairman: What does it purport to show?

Mr. King: It purports to show for employee "A", who has been in the fund for 24 years, that his earnings in the last year of employment were $5,125, that he has a taxable portion in his profit-sharing fund of $14,841. Under section 36 he would pay a tax of $1,509. Under Bill C-259, the new averaging formula, he would pay a tax of $3,573. If he buys a 10-year annuity certain, as far as we know he will pay no tax because his total income will be below what is required to pay tax. If he takes it out as a lump sum under the proposal on capital gains, which is the last column, he will pay tax of $888.

The Acting Chairman: That example does show that the retention of section 36 is more beneficial to the Treasury.

Mr. King: Absolutely.

The Acting Chairman: By some $600 or $700.

Mr. King: Here is a low-wage earner who, by Bill C-259, will be paying more than twice as much tax on his lump sum than he would have paid under section 36, so he has no alternative but to buy an annuity.

The Acting Chairman: Honourable senators, you all have a copy of this table before you. Do you think it would be useful to include it in the record at this point?

Hon. Senators: Agreed.

COMPARISON OF INCOME TAX PAYABLE ON WITHDRAWALS

SIMPSONS-SEARS PROFIT SHARING RETIREMENT FUND

				(1)	(2)	(3)	(4)
				Tax on Withdrawal			
Employee	Years in Fund	Earnings Last Year of Employment	Taxable Portion of Withdrawal	Lump Sum under Section 36	Lump Sum Under Bill C-259	10 Year Annuity Certain	Lump Sum under Proposal
A	24	5,125	14,841	1,509	3,573	Nil	888
B	23	6,840	14,050	1,580	3,525	Nil	965
C	19	7,155	12,911	1,829	3,219	Nil	971
D	26	7,626	18,304	2,549	5,405	Nil	1,661
E	24	8,919	18,447	2,899	5,488	280	1,733
F	20	9,839	18,637	3,223	5,943	2,050	2,208
G	19	12,750	21,096	4,241	7,624	5,050	2,762
H	23	15,000	19,159	4,122	7,225	4,770	2,268
J	22	16,400	22,928	5,654	9,378	6,050	3,179
K	20	20,000	20,180	5,431	8,322	5,570	3,038

NOTE: 1. All examples calculated assuming exemption for married—no dependents, standard deduction of $100 and additional exemption for age 65.
2. Income after retirement calculated on basis of Company's retirement formula and employee's social security benefits.
3. Tax in column (3) calculated on capital portion only of 10 year annuity certain.
4. Tax in column (4) is tax payable in year of withdrawal if 50% of realized capital gains, and 100% of unrealized capital gains on securities withdrawn in kind, are excluded from taxable portion of withdrawal. There could be further tax payable on capital gains as and when securities withdrawn in kind are sold.

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Senator Molson: Colum 4 should be identified as what the proposal means.

Mr. King: It shows at the very bottom:

> Tax in column (4) is tax payable in year of withdrawal if 50% of realized capital gains, and 100% of unrealized capital gains on securities withdrawn in kind, are excluded from taxable portion of withdrawal. There could be further tax payable on capital gains.

This is if they were rolled-over and tax was paid on them when he sold them; it would be treated as a capital gain in the lump sum he took out, exactly as the Senate committee had recommended.

Senator Flynn: It is on the basis that he would have no other income that year.

Mr. King: It is on the basis that he would have the income of retirement security, the Canada Pension Plan.

Senator Flynn: And nothing else.

Mr. King: Perhaps nothing else.

Senator Flynn: But if he has something else?

The Acting Chairman: Who can say?

Senator Flynn: The amount may be much higher.

Mr. King: It will be higher.

Senator Flynn: Much higher. It is a minimum in all cases.

Mr. King: Yes. Most people in this bracket do not have anything else.

Mr. van Zuiden: May I speak on the subject of retroactivity?

The Acting Chairman: Certainly.

Mr. van Zuiden: I think it should be made clear that there has been provision, of a fashion, made—

Senator Beaubien: Provision by whom? Who has made provision?

Mr. van Zuiden: The provisions of the bill. This provides that accumulations of profit-sharing plans, as they will stand at the end of this year, will remain subject to the provisions of section 36, but credits that will arise after the end of this year will not be. Our objection on this point is that if a member withdraws, let us say, in ten years from the plan and takes advantage of section 36 on his accumulations to the end of 1971, he is denied the right to use any of the other averaging provisions provided in the new bill. Mr. Phillips asked what might be suggested in the way of a compromise. It seems to me that one thing we could look at in terms of a compromise is to have the accumulations to the end of 1971 and the interest that will be earned on this accumulation in the future continue to be subject to the section 36 treatment, to provide that credits after the end of this year be entitled to the new provisions, but that the member withdrawing cannot be denied the right to use both, as he currently is.

Senator Cook: Why not give the officials of the Department of Finance the right to have a lump-sum withdrawal?

Senator Molson: Then they would be in favour of this.

Mr. King: There is no doubt about that.

The Acting Chairman: You mean under the superannuation fund?

Senator Cook: I do not care how you do it.

The Acting Chairman: Are there any other questions?

Hon. Mr. Phillips: I would think on that compromise, if we go that far, the simplest procedure is to go back to the original request for continuance of section 36.

Senator Flynn: Leave the option?

Hon. Mr. Phillips: Yes.

Senator Molson: Perhaps we should hear the officials from the department and find out just what this philosophy is. This new tax reform is supposed to bring equity in our lives, and it seems to me that we are running into a good many occasions when it does not appear on the surface that there is any equity at all; it seems to be removing equity.

Senator Cook: "If I can't have it, you can't have it!"

The Acting Chairman: At the expense of the Treasury too, in this case.

Senator Molson: In this case it appears that way.

Senator Flynn: You said it is supposed to bring equity; you used the word "supposed".

Senator Molson: I did; I said that it is supposed to.

Hon. Mr. Phillips: I have double-checked, honourable senators, and I see we dealt with the question of capital gains at some length, and the roll-over, but we did not insist, nor did we recommend that section 36 be continued. We more or less relied on the general averaging provisions.

The Acting Chairman: Yes, but I think we have now considered the problem a little more in depth, particularly with the examples in the table that has been provided. Perhaps we now have something to work on further on this point.

Senator Flynn: The lump sum under section 36 would in all cases be a maximum. Whatever is the taxable income, it would be a maximum.

Hon. Mr. Phillips: Average over the previous three years.

Senator Flynn: Then it is not a maximum.

Hon. Mr. Phillips: No, it is an average of the three years.

Senator Flynn: If the taxpayer has other income, these amounts may not be true at all.

Mr. King: That is true.

Senator Flynn: They would vary in the same proportion as will the figures given in column 4.

Mr. Hall: Roughly speaking.

Senator Flynn: On the same basis that if you have other income it goes up.

Mr. Hall: Yes.

Senator Flynn: It is not a maximum.

Mr. King: No.

Mr. Hall: This is just considered as employees' income.

Mr. Campbell: Perhaps I could suggest that this would pertain to virtually all top management people, because presumably they have been getting more than an ordinary workman in salary and have other investments, so the government gets much more revenue.

Senator Flynn: I always thought that was the hidden purpose, if not the admitted purpose, of the tax reform proposals; but that is something else, I suppose.

The Acting Chairman: Are there any other questions?

Hon. Mr. Phillips: I think we have got the point, gentlemen.

The Acting Chairman: Gentlemen, we thank you very much indeed. This has been most informative and very helpful.

Mr. Campbell: We certainly thank you, Mr. Chairman.

Mr. Diekman: Mr. Chairman, instead of relying on what other people who have been before you have been asked to do, we have ourselves committed to paper a method by which the proposed act might be changed.

The Acting Chairman: Do you mean that you have drafted some amendments?

Mr. Diekman: Yes.

The Acting Chairman: Could you leave them with us?

Mr. Diekman: That is what we propose to do, with your permission.

The Acting Chairman: Thank you.

The Acting Chairman: Honourable senators, the next brief will be presented by the Insurance Bureau of Canada. We have as witnesses Mr. Hanly, Mr. Atkins and Mr. Piper. Mr. Hanly is chairman of the Federal Legislation and Liaison Committee, and President, Dominion of Canada General Insurance Company.

Mr. H. Norman Hanly, Chairman, Federal Legislation and Liaison Committee, Insurance Bureau of Canada: Mr. Chairman and honourable senators, perhaps I should put it this way: I am the President of the Dominion of Canada General Insurance Company; but, in addition, I am chairman of the Federal Legislation and Liaison Committee of the Insurance Bureau of Canada.

The Insurance Bureau of Canada is an organization of all the major general insurance companies in Canada, totalling 193 groups of companies or 90 per cent of the general insurance business in Canada.

The Acting Chairman: For the record, may I say that we had a representation here last week from the Canadian Life Insurance Association. Now you are representing the general insurance companies?

Mr. Hanly: Yes. We are perhaps the counterpart of the delegation which represented the life insurance companies, but our activities are confined to general insurance. About 10 per cent of the general insurance companies are not represented by the Insurance Bureau of Canada, and it is possible that one or more of those purely independent companies will be presenting briefs of their own or making recommendations.

The Acting Chairman: That is unlikely. This is likely to be the last public hearing, so you will have the floor and you will be making the presentation.

Mr. Hanly: Honourable senators, I have with me: Mr. David H. Atkins of MacDonald, Currie & Co., who is Tax Consultant for the Insurance Bureau of Canada; and Mr. E. H. S. Piper, Q.C., the General Counsel for the Insurance Bureau of Canada.

Our brief was forwarded to you about ten days ago. I do not know whether you would like us to read the various points we have raised, which are few in number, or whether there are any questions you would like to ask us regarding some of the clauses contained in our brief.

The Acting Chairman: Mr. Hanly, would you like to make a general statement summarizing the brief?

Hon. Mr. Phillips: With your approval, Mr. Chairman, I would like to make a suggestion. In the reading of the brief, I find that there are certain items which have been dealt with already in the interim report presented by the Chairman of this committee in the Senate last week. Some of the important items in your brief are: firstly consolidated tax returns—which item has been dealt with at length by this committee in its report.

The Acting Chairman: Have you read the report on consolidated tax returns?

Mr. Hanly: No, we have not.

Hon. Mr. Phillips: I would like to draw your attention to that. You have: firstly, consolidated tax returns; secondly designated surpluses—which you also dealt with . . .

The Acting Chairman: And which the report dealt with.

Hon. Mr. Phillips: Yes, which has been dealt with at length in this committee's report; and, thirdly, the roll-over provisions. These are three major items which were included in this committee's report last week. I suppose it is my fault. I should have been in touch with you, for it might have been desirable for you to read the report, to make certain whether there is anything you wish to say under these three headings that we have not already included in our report. We will study what you have to say under these headings, although it will be rather difficult to go back and deal with the same subject matter in a supplementary report. It would appear to me that if these three were eliminated you might wish to highlight some of the items in your presentations that have not already been dealt with.

Mr. E. H. S. Piper, Q.C., General Counsel, Insurance Bureau of Canada: Mr. Chairman, with respect to the consolidated tax returns, I have seen the interim report of the Senate committee. It has not yet been formally brought to the attention of the directors of the Insurance Bureau of Canada. I know that my personal recommendation will be that we endorse it completely.

The Acting Chairman: Then that eliminates that point.

Mr. Piper: In regard to designated surplus, I did not have a chance to go into it in sufficient depth to determine whether or not we had anything further to say, and I would not want to close the door on that point.

Hon. Mr. Phillips: Then, on roll-overs, on page 4.

Mr. Piper: On roll-overs, I think we are in complete accord with the interim report.

The Acting Chairman: It seems to me, Mr. Hanly, that what you have said in your brief about designated surplus does not touch any point that was not considered by the committee and perhaps dealt with in the interim report.

Mr. Hanly: We could waive designated surplus, under those circumstances.

Hon. Mr. Phillips: I would think so, and we might get better dividends out of the remainder of the brief and cover things not already studied and dealt with.

The Acting Chairman: Would you agree to proceed along those lines?

Hon. Senators: Agreed.

Mr. Hanly: In the matter of the regulations, the Insurance Bureau of Canada and its member companies are somewhat confused as to whether there will be a change in the regulations affecting the tax position of the companies. Of course, the regulations are the guiding factor. Therefore, we are in a position where we do not know whether the existing regulations will be perpetuated or whether there will be changes in them.

The first point we have to refer to is the question of business losses and carry-overs. Might I be permitted to have Mr. Atkins speak on that point? It is item number 2 on page 1.

Mr. David H. Atkins, Tax Consultant, Insurance Bureau of Canada: Mr. Chairman and honourable senators, the general insurance industry is one in which, in my view, one cannot adequately recognize the results of an entity within one year, in all cases. For example, catastrophes can occur, let us say, at intervals of some ten to twenty years, and in the intervening period profits may occur and reserves be set aside to meet future catastrophes.

I think it is true to say that the insurance cycle is somewhere in the region of six to eight years, being the valleys and peaks of the insurance industry. It could happen, and in some cases has happened, that an insurance company would incur a loss for tax purposes but, because of the time limitations under the existing Income Tax Act and the limitations under the tax reform bill, it would be unable to recover the benefit of those losses.

I think it was the Royal Commission on Taxation that recommended carrying forward losses to extinction.

The Acting Chairman: Yes.

Mr. Atkins: The Insurance Bureau of Canada, I believe, subscribed to that view. In a brief submitted to this committee on the White Paper on tax reform it was recommended by the Insurance Bureau of Canada that losses be carried forward for some ten years, because we recognized that there might be some administrative difficulties in keeping records longer, and we still press for a recognition of losses for a period longer than five years. Our brief does contain an optional treatment, a compromise, if you like, and this compromise is one which is akin to that accorded insurance agents and brokers, whereby the insurance company is given the option of claiming a deduction for its policy reserves.

Senator Isnor: How much longer than five years would you expect?

Mr. Atkins: We did ask for ten years.

Senator Isnor: It is a costly procedure, is it not, to carry a bad debt over the five-year period?

Mr. Atkins: It is, indeed, but I think that the fear of the insurance companies is that a major loss might have occurred at a point in time, and it would be extremely difficult to recoup that loss in the form of income tax savings over the ensuing five years. It would take some time longer than this five years to recover or to have profits to match that particular loss.

The Acting Chairman: You have made that point well, Mr. Atkins, and I think it is clear to the committee. On page 2 you have an alternative to the indefinite carry-forward, and that is the one you have just mentioned, that policy reserves be deductible by general companies in full or in part for any taxation year.

Mr. Atkins: That is correct.

The Acting Chairman: Are there any questions on that point?

Hon. Mr. Phillips: Mr. Chairman, I should like to make the further suggestion that this whole question of reserves and so forth, as indicated in the earlier part of the presentation, will relate itself to the income tax regulations. It is difficult to come to grips with it until the regulations come through. It is difficult to make recommendations. As a matter of fact, it is impossible. There are three items in this brief, however, that are new and that should give honourable senators food for thought.

The Acting Chairman: Senator Phillips, if I may just interject one point here, although we do not have the regulations, it seems to me to be useful that this committee should have remarks of witnesses, such as those present, in order to make them available to those who are going to write the regulations, so that they can take account of the recommendations that have been made.

Hon. Mr. Phillips: My understanding of the matter, and I think it was so reported, Mr. Chairman, is that the Department of Finance has asked this committee to forward to the department all briefs that have been submitted to the committee. You will remember that the committee, in order to save printing costs, agreed that briefs would not form part of the record. The department does receive the evidence and the discussions, because they are printed, but in addition all the briefs that have been presented to date, including the ones now being heard, will go to the Department of Finance.

Now, I would like to refer to the three interesting points that have been raised in this brief. The one of major importance, to my mind, is that which appears on page 4 of the brief. I refer to "Refundable Dividend Tax on Hand." It is a short statement, item No. 6, and I should like to discuss it with honourable senators for a minute.

The basic point here is that the Senate, in its report on the White Paper, took the position that there should be no difference between public companies and private companies, but its recommendation was not accepted, and we end up in the bill with exempt income from one Canadian company to another in so far as dividends are concerned, subject to a 33 1/3 per cent tax refundable when the exempt income is declared out by way of dividend.

The gentlemen before us have taken the position that it might suit their purpose to pay the tax, have the refundable credit and not pay out the dividends. They, therefore, recommend that the refundable dividend tax be regarded as an asset of the corporation in its declaration to the Superintendent of Insurance. I believe that is what you are asking, Mr. Atkins. Will you develop that, because that relates itself to your particular industry?

Mr. Atkins: We are not seeking that dividends be not paid out. The insurance industry, generally speaking, under the federal insurance acts, is limited as to the amount of dividends it may pay out. One good example is, I believe, section 103 of the Canadian and British Insurance Companies Act which prohibits a federal Canadian insurance company declaring dividends in excess of 75 per cent of the average profits of the three preceding years. Consequently, given these limitations, it is extremely difficult to recoup the taxes paid and placed in the tax refundable account. One law conflicts with the other.

Hon. Mr. Phillips: I think that is an important point. You find yourself in a position where you have a refundable asset, but you are not able to get it out because, under the statute law, you cannot declare the dividends out to get it back.

Mr. Atkins: That is right.

Mr. Hanly: That section of the insurance act, Mr. Chairman, is section 105. Section 103 is also affected.

Hon. Mr. Phillips: What is the section, please?

Mr. Atkins: Section 105 of the Canadian and British Insurance Companies Act is the 75 per cent rule. Section 103 is a further solvency limitation provision of that act. Therefore, we are bound by law as to dividends.

Hon. Mr. Phillips: You did not say that in your brief, did you?

Mr. Atkins: No. It is an innuendo contained in the last sentence of that paragraph.

Hon. Mr. Phillips: But this committee does not deal in innuendoes. It is much too important a committee for that. It is prohibited by law beyond 75 per cent. Thank you.

Mr. Atkins: Given these tests contained in the insurance acts which look to assets which are deemed to be admitted, a downward spiral might occur if the refundable tax account were not to be regarded as admitted assets, because that is the very instrument which enables an insurance company to pay a dividend.

Hon. Mr. Phillips: It is a simple point, but a very important one.

The Acting Chairman: It may be very simple, but I think it would be useful to have a practical example on the record to illustrate the points made in paragraph (6) "Refundable Dividend Tax on Hand." In fact, honourable senators, it might be useful were we to incorporate that particular paragraph at this stage. Is it agreed, honourable senators?

Hon. Senators: Agreed.

The paragraph reads as follows:

(6) *Refundable Dividend Tax on Hand*

It is very likely that many insurers will have as an asset "refundable dividend tax on hand". This asset will become significant over the years as a result of the investment income from the substantial investment portfolio that the general insurers are required to maintain. It is recommended that this asset be accepted by the Superintendent of Insurance as an admitted asset. If this refundable tax is not admitted the solvency of insurers will be adversely affected. In addition, since dividend payments are by law tied to solvency, the very instrument required to recoup this refundable tax will be restricted.

Senator Beaubien: Mr. Chairman, should we not have a suggestion as to what should be done about it?

The Acting Chairman: Do you think, Senator Beaubien, that it would be helpful for us to have a practical example from Mr. Atkins illustrating this point, and then we can come to yours?

Senator Beaubien: All right.

Mr. Atkins: In this example we are dealing with a Canadian private corporation.

Hon. Mr. Phillips: Take the sum of $75,000 because then, when using 33 1/3 per cent tax, you will have nice round figures.

Mr. Atkins: A Canadian private corporation is a general insurance company incorporated under the federal Insurance Act. Let us assume that this company has broken even on its underwriting account. Now let us assume that it has received $75,000 of dividend income, and let us also assume that under the tests of section 103 of the Canadian and British Insurance Companies Act its assets are $115,000 and its liabilities $100,000.

If I may just in two sentences explain section 103, an insurance company must maintain at all times assets of 115 per cent of its liabilities at 100 per cent. Therefore, this particular company is at the minimum solvency limit. The company, having received the $75,000 dividend income, pays the one-third tax, or $25,000. Now let us assume that that $25,000 is not to be regarded as an admitted asset.

Senator Isnor: How would you treat that $25,000?

Mr. Atkins: From an accounting standpoint it would be treated as an asset, but from an Insurance Act standpoint we do not know, and I am assuming the worst—that under the insurance regulations it may not be regarded as an admitted asset.

Senator Flynn: But the $25,000 is paid out as a tax?

Mr. Atkins: It is paid to the government as a refundable tax.

Hon. Mr. Phillips: Senator Isnor, it is a little easier to understand if you keep in mind that an asset is really an asset if it has no strings attached to it. But if it is a conditional asset, in the sense that you have to pay out dividends in order to get it back, it is hardly an asset in the ordinary sense of the term.

Senator Flynn: It is an eventual asset.

Hon. Mr. Phillips: It is not even an eventual asset, because it may not be possible to declare dividends.

The Acting Chairman: In any event, as the example unfolds, I think this will become clear. I think Senator Isnor will be helped by the completion of the explanation.

Mr. Atkins: The Board of Directors would meet to determine whether they should declare a dividend, and would receive, I hope, tax consultant advice in view of the tax reform bill. They would also naturally wish to recover as much tax existing in the tax refundable account as possible. Under insurance law the directors would be unable to declare a dividend of more than $50,000 if insurance law does not regard the $25,000 paid in the refundable account

as being an admitted asset. If the $25,000 were treated as an admitted asset, then the directors would be able to pay a dividend of $75,000 and to recoup the full amount included under the tax refundable account.

The point of paragraph 6 of our brief is that we would very much like to have any amounts contained under the tax refundable account as admitted assets and therefore forming part of the solvency tests which condition the payment of dividends.

Senator Isnor: The purpose of that would be to permit you to pay a larger dividend?

Mr. Atkins: Exactly, to permit the industry to recover taxes paid on dividends which it is entitled to recover under the tax reform bill.

Senator Cook: Would you care to express an opinion about the solvency tests? Do you think section 103 or section 105 could be further relaxed, or do you think they are at their minimum now?

Mr. Hanly: I would doubt if the Department of Insurance would be agreeable to any relaxation, as they are vitally concerned with the solvency of companies and any relaxation might create difficulties.

Senator Beaubien: Mr. Atkins, taking the figures that you have given us, what happens now before Bill C-259 goes through? How do you stand at the moment? Say you get $75,000 in dividends, how does that work out so far as tax is concerned now?

Mr. Atkins: If the dividends are received from taxable Canadian corporations, the dividends would come in tax free and the pay-out to the shareholders would also be tax free. It would flow right through.

Hon. Mr. Phillips: We are back to the question where this Senate committee took the position that it would be most unfair and inequitable to draw a distinction between public and private companies. We discussed that last week and the week before. We are back now to the position where private companies are discriminated against in the terms of imposition of tax at 33 1/3 per cent, even if it is refundable, as against public corporations who get the exempt income and have no problems at all. It is aggravated for insurance companies because, by law, they are limited in their treatment of their asset position and of their dividend policy. Here they are facing the position of a 33 1/3 per cent tax refundable, conditional upon the payment out of the entire exempt dividends, which they cannot do because they may not meet the 115 per cent test on solvency in relation to 100 per cent liabilities; and they are caught also because they are not able to declare the entire exempt dividend because the Insurance Act prevents their doing so.

Senator Cook: There is a clear conflict between the two acts.

Hon. Mr. Phillips: Yes, so this is a very important item that has to be dealt with.

Senator Flynn: Inasmuch as our recommendation has not been accepted by the government, is the solution here or in the Insurance Act?

Hon. Mr. Phillips: I was thinking, whether it is relevant or not, that it would appear to me that reference should be made here in the report, because it does come under the revenue statute and the problem arises out of the revenue statute, and we cannot very well suggest an amendment in the revenue statute as related to the Insurance Act.

Senator Flynn: There is no sense in repeating our views on that subject.

Hon. Mr. Phillips: Yes, and then to indicate how inequitably it works out and how impossible the application of it is in instances such as this. We suggest consideration of appropriate remedies to meet this type of situation. We cannot very well take jurisdiction over the Insurance Act.

The Acting Chairman: Are there any other questions on that point, honourable senators?

Hon. Mr. Phillips: The other point is one which we thought had considerable merit, and the investment dealers dealt with it at the time of the White Paper. That is the suggestion regarding withholding taxes on certain types of bonds, whether they are Government bonds or not. You will find this on page 3. This question has always intrigued our committee, and it goes to the debatable area as to whether or not we want foreign investments coming into this country.

At the time of our discussion on the White Paper, we took the position that we should be encouraging foreign capital to come into our country, provided it comes in the form of a foreign debt, on the theory that if you have a debt you pay it back. I had the honour of being vice-chairman at the time of the White Paper; and I pointed out that in the nineteenth century the Americans were lucky that the British used to lend money to the United States which was paid back. The Americans used the profits to develop their own resources and came up here and were smart enough to buy equity stock rather than bonds. This nineteenth century debt has created part of the problem in our country—the twentieth century equity from America to Canada. This has been our economic problem in the last 150 years. One of the suggestions we made was that in order to attract foreign capital to Canada bonds could be purchased rather than equity stock; and we could eliminate the withholding tax on the interest to non-residents with respect to funded debts of Canadian debtor companies. This would be helpful to investors who live in countries where there are no tax treaties, or where there are particular benign forms of tax legislation. You have the flow of capital here in the form of a debt, you lose the withholding tax, but at the same time you stop the flow of equity money coming to Canada and you put out a teaser by saying, "If you want to buy our bonds and debentures, you are most welcome and there will be no withholding tax." Then the feeling was that we ought to do this only up to a certain amount, on the theory that we do not want to become Santa Clauses regarding new sums coming into Canada. The feeling was that there might be a ceiling on the amount.

Senator Flynn: These views were not accepted by the Government.

Hon. Mr. Phillips: No, they were not accepted at all. But this brief gives us the opportunity, if we desire, to deal with it again.

The Acting Chairman: I wonder if one of the witnesses would explain the statement on page 3, at the end of paragraph 4, which states:

At present the "withholding tax exempt" bond—

Would you give an example of a withholding tax exempt bond?

Senator Beaubien: Mr. Chairman, when Churchill Falls was built $500 million was raised in bonds by a special act and they were made tax-exempt bonds.

Senator Molson: You are speaking about withholding tax?

Senator Beaubien: Yes. Is this a good example?

Mr. Keith Sandford, Special Consultant, the Royal Architectural Institute of Canada: Yes, that is a good example. These were Government of Canada bonds.

The Acting Chairman: Government of Canada bonds which were designated as withholding tax—

Senator Molson: No, these were Churchill Falls bonds.

Hon. Mr. Phillips: These were allowed by a special statute.

Senator Flynn: Only the federal Government can do that.

The Acting Chairman: A special statute exempted these bonds from the normal provisions of the Income Tax Act.

Senator Flynn: This would be under federal legislation only?

The Acting Chairman: Yes.

Hon. Mr. Phillips: The question arises as to whether this committee feels that the principle of inviting foreign debt money should be accepted and that a withholding tax, up to a reasonable amount, be considered highly desirable. I do not think that this committee can name a certain figure, and we certainly cannot apply it to a particular industry.

Senator Flynn: Will you refresh my memory on the principle that there should be a ceiling?

Hon. Mr. Phillips: The feeling was that if we had large sums of money coming into Canada and finding a haven in terms of a yield, if Canada did not get something out of it, this would be undesirable. It was probably more a reaction of not wanting to be a haven for large sums of money coming into Canada, getting their yield from Canadian corporations, which yield is deductible as an expense to Canadian companies because it was an interest payment to a non-resident, without having some revenue go to the Crown.

Senator Flynn: You mean a ceiling for each venture?

Hon. Mr. Phillips: No, a ceiling for each debtor company.

Senator Flynn: —or for each venture?

The Acting Chairman: This would not be easy to draft.

Hon. Mr. Phillips: No.

Senator Flynn: For instance, let us take the James Bay project as an example. If you had to borrow $1 billion or $2 billion, they would want a ceiling in such a case.

Hon. Mr. Phillips: At this stage I would say that it would be highly desirable for this committee to accept and reiterate this principle, because there is much to be said in favour of the concept of eliminating a withholding tax on a funded debt owned by a non-resident.

Senator Flynn: I agree with you. I was just wondering whether the principle of a ceiling should be reiterated.

Hon. Mr. Phillips: No, I feel that we should just deal with the principle of inviting foreign capital into Canada in the form of an acquisition of a Canadian funded debt. In that way it would probably slow down investments in Canadian equity participation and give Canadians, through their savings, a greater chance to acquire equity.

The Acting Chairman: The conclusion of the section which is on page 3 is that the witnesses strongly recommend that withholding taxes levied on dividends and branch profits be retained at their present level of 15 per cent, and that the issuance of withholding tax exempt bonds be maintained.

Senator Flynn: But this would not be selective. You do not mean that this should be a privilege granted to certain classes of bonds?

Mr. Atkins: The existing section 106, subsection 1, clause (*b*) lists the various types of bonds which a non-resident may purchase and upon which there is no withholding tax.

Senator Flynn: Do you not think it would be better to apply it as a general rule, as we have already suggested?

The Acting Chairman: Across the board.

Senator Flynn: Yes, not selective, in order to attract all possible investments in this form.

Senator Cook: Care must be taken not to give the best of both worlds. In the situation of a project that will cost $10 million, with $250,000 wholly-owned shares and $9,750,000-worth of tax exempt bonds, the exemption on the withholding tax would be received and after the debt is paid the concern would be owned anyhow.

Hon. Mr. Phillips: You are quite right. In relation to the equity it may be a $50-million investment owned entirely by the non-resident with no Canadian participation. It must be dealt with on the principle that the importation of foreign money, following the exemption on funded debt in a Canadian company, be related to the encouragement to be given to Canadians to acquire equity.

Senator Flynn: Not tied to the equity investment.

Hon. Mr. Phillips: That is right.

Senator Molson: The transfer of the equity investment would have to take place the day after the bond deal was closed.

Senator Beaubien: Could it be left to the discretion of the minister?

Hon. Mr. Phillips: This brief presents an opportunity for us to bring back into consideration the point we previously made.

The Acting Chairman: Is that agreed?

Hon. Senators: Agreed.

Mr. Atkins: With regard to these particular types of bonds, I think the industry recognizes that where they are deployed in the Canadian business then, of course, normal income tax rates would apply. When I say "excess bonds," I refer to those which, in order to do business in Canada, one is required by insurance law to place on deposit with the federal Government. Those bonds may not necessarily be used in the day-to-day business of the Canadian operations.

Hon. Mr. Phillips: Frankly, I feel that that phase comes closer to the insurance act, as opposed to this legislation.

Senator Gélinas: Would that include convertible bonds?

Mr. Atkins: I think so, but there are limitations on equities for an insurance company. Upon conversion, the insurance company may find itself offside. That is my immediate reaction.

Hon. Mr. Phillips: The third point was with respect to ineligible investments. That is mentioned at page 5 of the brief.

Mr. Atkins: Under section 63 of the Canadian and British Insurance Companies Act, and similar sections of the provincial insurance companies acts, an insurance company is obliged to invest in certain types of securities, in the main long-term bonds, Government bonds and similar instruments. There are limitations as to the amount of equity that may be held.

A reading of the benefits, so-called, given to small business under the Tax Reform bill, reveals that where profits in a small business are re-invested in the business in the form of certain types of securities, there is a limitation on the small business incentive. Insurance companies, being obliged by law to invest in securities normally of a duration of over one year, will find themselves investing in ineligible investments under the small business section of the act and therefore unable to avail themselves of the small business deductions.

Hon. Mr. Phillips: This is another aspect of the point which we discussed with respect to the refundable tax. That which is eligible under the insurance laws becomes ineligible under the small business section of the Revenue Act.

In a nutshell the recommendation is at the end of the paragraph, honourable senators: "We recommend that investments which are allowed under the various Insurance Acts be regarded as eligible investments for small Canadian insurers."

Under the small business section certain of these investments would be ineligible.

The Acting Chairman: Because of the term of the investment.

Hon. Mr. Phillips: Yes; it falls under the same heading as the refundable asset we discussed. We can draw the attention of the Minister of Finance to the inconsistency.

The Acting Chairman: There is a conflict between the insurance act and the tax act.

Gentlemen, have you any other points to make, or conclusions to submit to the committee?

Senator Flynn: Does this apply to all insurance companies, including life insurance companies?

The Acting Chairman: At the outset, Senator Flynn, the witnesses stated that they were speaking exclusively to the problems of general, rather than life insurance. You will remember that last week representatives of the Canadian Life Insurance Assscіation appeared before the committee.

Gentlemen, thank you very much indeed.

The Acting Chairman: The next submission is by The Royal Architectural Institute of Canada. Messrs. Lalonde, Rounthwaite, Salter and Sandford are here.

Mr. Lalonde, would you care to introduce your colleagues and make an opening statement?

Mr. Jean-Louis Lalonde, President, The Royal Architectural Institute of Canada: Thank you, Mr. Chairman. The Institute represents 3,200 architects throughout the country. Mr. Rounthwaite is its Vice-President; Mr. Salter is Director of Professional Services at the Institute headquarters; and Mr. Keith Sandford is our Tax Consultant.

The architects of this country are quite impressed by the work of this committee. This is mostly due to the fact that last year, when we presented our brief, it was well received and of the many points brought up quite a few are reflected in the text of the bill.

The Acting Chairman: Your brief indicates that of eight, five were dealt with.

Mr. Lalonde: That is right. We are thankful for that.

Hon. Mr. Phillips: Your track record is better than ours!

Mr. Lalonde: As architects, we feel that we fulfill an important role in society, a role which has been recognized, either in our professional capacity or as businesses. We have commented on what we understand the tax law will do to us, and there are two or three points with which we are not quite happy.

The Acting Chairman: Perhaps one of them is that you think the act should not be brought into force at the end of 1971, but that it should be delayed for one year.

Mr. Lalonde: Yes. I will go into that in more detail.

The Acting Chairman: Would you deal with that now, please?

Mr. Lalonde: Yes. We suggest that there should be more time to study and discuss the bill. We hope, with more time, to be in a better position to win our points and to understand and advise our members on how the new law will affect them. Mr. Sandford is better able to speak on the tax law dealing with the new partnership provisions. My contribution is that of a citizen rather than an architect. We approve of the basic intentions of distributing the load in a more just way, but we do not understand exactly how it is proposed to be done. As citizens we are not completely convinced that it is being done properly. When society needs 700 pages of text in connection with a particular law, and loads of literature to go with it to determine the method of imposing tax, something is wrong with our society.

Senator Walker: Or with the Government.

Mr. Lalonde: Some of you will remember that when we were in school we learned "Ce qui se conçoit clairement, les mots pour le dire viennent aisément." I do not know if there is an equivalent in English; it is difficult to translate. However, it does not seem to be a fact in relation to this law.

The Acting Chairman: We have complained time after time about that to tax experts and the draftsman. The last time we complained to them during the sittings of this committee they told us that the complications resulted from the interpretation of benefits to taxpayers. After sitting here for a month and a half listening to various groups, I am sure that it is very difficult for the general public to understand the bill. However, that is a fact of life.

Senator Flynn: Except that, the benefit to the taxpayer, if the bill is enacted, will be transferred mostly to trust companies and lawyers, because no one will be able to prepare his own income tax return.

Mr. Lalonde: There must be incentives in some part of our economy. I cannot avoid feeling that we have here the result of a tremendous effort on the part of technical people, but there is probably a lack of leadership in being able to present the material in an untechnical way, in a simple way, to enable citizens to understand it. I am trying that to our request for a delay in the enactment of the bill so that we might have more time to study and understand it, and so that the Government might have time to redraft it in a way that it can communicate properly with citizens. We are really offering the Government more time to make the bill more efficient.

Senator Flynn: In that you are joined with some provincial treasurers.

The Acting Chairman: To reach an Utopia we should have a tax act which could be comprehended by the majority of citizens.

Mr. Lalonde: Yes, but that would be stretching it too far.

Senator Cook: It would also be unfair to tax consultants!

Mr. Lalonde: Architects relate themselves to human values and social considerations. Mr. Chairman, that is the only contribution that I can make. I will now ask my confreres to continue.

Senator Salter A. Hayden *(Chairman)* in the Chair.

Mr. Lalonde: Mr. Chairman, I do not know how you would like us to proceed. Our brief is short, simple and straightforward.

Senator Connolly: I suggest, Mr. Chairman, that the main point appears to be the problem of dealing with partnerships. Perhaps the witnesses could direct their attention to that point.

Mr. Sandford: I propose to deal with the partnership requirements in conjunction with the new requirements regarding professional income. The provisions are complex, and solicitors and auditors who have been giving advice have been unable to advise architectural firms on what action they should take to accommodate the proposed tax law. There are certain retroactive features, there are inequities, depending upon what point in time the tax year ends, and we have to tie this in with the new partnership requirements and the adjusted cost basis. In determining all these things there a little time for preparation. In addition, there are corporations in the architectural profession that are subject to these very complex rules in regard to Canadian-owned private corporations.

There are certain idiosyncrasies of the profession in the way income flow is related to construction. There are variations in projects and payment procedures affecting various clients. Mr. Rounthwaite will be able to give you a good example of the complications that arise.

Senator Connolly: Are you familiar with the submissions we have had from the construction industry?

Mr. Sandford: Yes, I was present when the Canadian Construction Association appeared before your committee.

Senator Connolly: So you are aware of the fact that we have had considerable evidence in that regard?

Mr. Sandford: Yes, but the construction industry is usually incorporated; they do not have partnerships.

Senator Connolly: Yes. Perhaps you also should be made aware of the fact that this committee, in its interim report, proposed to deal with professional incomes on an accrual basis in a subsequent report. This is something you might direct your attention to.

Mr. Chairman, I do not want to continue in the Chair, but, in my view, it will help the flow of discussion if that is made clear.

The Chairman: Yes.

Mr. C. F. T. Rounthwaite, Vice-president, Royal Architectural Institute of Canada: Mr. Chairman, I would like to illustrate two practical points. Once a tax law is enacted then there are regulations under the act, and in our own instance, we had one partner die a number of years ago and it was agreed with the taxation people that no goodwill would be attached to his estate. This estate, by the way, was in the six figures. Some time later another partner, who had a far lesser portion of the partnership, died and the same ruling was investigated, the decision then being that goodwill did apply. It is difficult to conduct our affairs with a variation of this sort.

I would like to go further with respect to the question of accruals. One of the valves that the Government likes to manipulate with respect to speeding up or cooling off the economy is marked "construction industry". For example, many projects depend upon federal and provincial supporting funds for their on-going course. In this regard, two years ago we, in good faith, embarked upon a large hospital project. We are normally paid our fees in proportion to an agreed amount of work being done. For example, when the preliminary work is completed, you get your money, and so forth. In the case of the hospital project, we billed the client for some $60,000, and the client said that their project had been arbitrarily put back three years so they did not have $60,000. Under this new law it would appear that our firm had receivables of $60,000. We doubt if we will see this money for another two or three years, and yet we would have to pay tax on it.

Senator Everett: Would you not be able to reserve your receivables if you really thought the account was in jeopardy for that length of time?

Mr. Rounthwaite: We did not know this.

Senator Everett: Did your clients not report to you that they had no money?

Mr. Rounthwaite: Only after the bill was received.

Senator Walker: Could you not withdraw it and say it was a mistake?

Senator Flynn: It is not a bad debt.

Senator Everett: I am not saying it is a bad debt. I am asking whether or not, in your judgment, you could have reserved the debt—not written it off, but reserved it. It is an entirely different accounting procedure.

Mr. Rounthwaite: We have not written it off at all.

Senator Everett: I realize that, but I am asking you whether you thought you could have reserved the debt.

Mr. Rounthwaite: By what action?

Senator Everett: By debiting receivables and crediting the reserve for bad debts.

Senator Flynn: If the department would accept it.

Mr. Rounthwaite: I am not prepared to call it a bad debt.

Senator Everett: You are not prepared to call it that and yet you are in jeopardy? I am not suggesting that you write it off; you are merely reserving it because you are concerned about whether you will get it. This is a normal business practice.

Senator Connolly: The account was rendered and it immediately became a taxation item?

Mr. Rounthwaite: That is correct, and the client says that when he gets his money we will be paid. Now, the expenses incurred in the production of that work have. been dealth with on a previous occasion.

The Chairman: What do you suggest as a remedy?

Mr. Rounthwaite: Because we are in this rather special type of work, where we are subject to these fluctuations beyond our control, some provision must be made so that these difficulties can be avoided. On the old cash basis you paid when you received your money.

The Chairman: Let us forget the cash basis. What do you propose should be done to deal with your problem?

Mr. Routhwaite: I feel we should have some provision whereby we can put such a reserve in abeyance until the transaction is completed and the money is paid. In other words, you simply say, "There it is, and when we get paid we will pay the tax".

Senator Connolly: You are not arguing about the accrual as against the tax propositions?

Mr. Rounthwaite: No.

The Chairman: For instance, Senator Connolly, if you render an account and you are told that your client is unable to pay it because the project has been deferred for two or three years, the question is: What is the value of the account at that time? I suppose one method of approach, which would help to some extent, would be to value the account at that time.

Mr. Rounthwaite: Mr. Chairman, our interpretation of the value of an account at that time would relate to the salaries that we paid in order to produce the work, but we have projects . . .

Senator Everett: May I ask you a question befor eyou go on? Did you, in fact, pay tax on that amount?

Mr. Rounthwaite: No. We were on a cash basis.

Senator Everett: I would suggest to you that with respect to the particular instance you gave us, even if you were on an accrual basis, you could have reserved that account.

Senator Flynn: I doubt it.

Hon. Mr. Phillips: It all depends on when the bill is sent out. For example, supposing the end of the fiscal year is the calendar year and you send out your bill, say, at the end of 1971, not knowing whether it will be paid or not, if you are on a cash basis you have no problem if the debtor cannot pay because you can subsequently write it off as a bad dept or put it into reserve; one way or the other. On the other hand, if at the end of 1972 you send out that bill, again not knowing the status of the debtor, if you are on an accrual basis you are not taking the reserve because you have not been in touch with your debtor.

Senator Everett: I think we agree on that, but what I am saying is that in the particular case brought forward they would have been in a position to put the account in reserve.

Hon. Mr. Phillips: If, during the course of the year, you send the bill out and you know you will not be paid by the end of the year, then you are quite right in suggesting that you would settle for a reserve as against writing it off; but then you have the question, whether you write it off or whether you provide a reserve; as to whether the department will allow you to do so. It becomes a matter of

opinion on the reasonableness of the reserve or the legitimateness of the write-off as a bad debt.

Senator Everett: And that is the same position business is in.

Hon. Mr. Phillips: You immediately create a debatable area by an accrual system of this type, whereas if you were on a cash basis these two areas of dissent between the taxpayer and the tax collector will not arise with respect to professional people such as architects, lawyers, and so forth. If you are on a cash basis, you have no problem.

Senator Flynn: We recommended to retain the cash basis for professional people, did we not, in the report?

Hon. Mr. Phillips: Yes, we did. We were against the accrual basis. We did not come to it in relationship to this bill.

Senator Connolly: No, but we did with respect to the White Paper.

Hon. Mr. Phillips: The real problem of the accrual system is that professional people are not in the same position as are merchants in determining the credit standing of people where debit and credit situations arise. Professional men do their work and bill the client. Another problem with the professional people is with respect to whether or not the debtor will accept the amount as being the correct amount owing.

Senator Connolly: That is right. The bill does not necessarily represent the return.

Hon. Mr. Phillips: We raised that question. Sending out the bill does not create a debit and credit situation, but apparently we do not seem to be able to transmit elementary law in certain directions. The sending out of the bill, which will now be an account receivable for professional people, does not create a debit and credit relationship. It is an expression of view by the professional man that his client owes him that amount of money. Therefore, we said that it should not apply to professional people, because there is no debit and credit relationship on a legal basis.

Senator Connolly: I think this is a fairly important point, because it is basic to the law, and we should insist upon it.

Hon. Mr. Phillips: Then we said, firstly, that it is wrong because it does not comply with the law, to have an accrual system for professional people. Secondly, we said the point I am making now, that once you send out a bill on an accrual basis professional people are not competent enough to deal with the determination of the issue of whether they should have a reserve against it, leaving aside the question even if it is admitted. You are therefore taxable in the year in which you take it in as an account receivable, and you may later on be able to write it off as a bad debt, or set up your reserves. Then you get into a situation that you do not know in what particular year you may be caught; you may be caught in a high tax year professionally and you may get a credit in a low year and lose money.

Senator Connolly: Would you indicate how a professional man can set up a reserve of the type you describe?

Hon. Mr. Phillips: Oh yes. In the course of a year you send out a bill and you know your client's economic strength is weakening, he is dribbling along. You send him a bill for $5,000, and he sends you a series of post-dated cheques for $1,000 during the course of a year. You know he owes you $4,000 at the end of the year and, having sent it out, it becomes an account receivable. I am speaking of 1972. Then you set up a reserve. Let us assume the debtor has admitted he owes you the $4,000. Then you get into that delightful area between the tax collector and the taxpayer, where you take a $2,000 reserve against the $4,000 and you are asked, "What prompted you to regard that account receivable as worth only $2,000 instead of $4,000?" You cannot give the answer, other than that the dribble of small cheques has come in, that when you see the man he says business is bad, and so on. As soon as you have an accrual system for professional people, you immediately have a debatable area.

Senator Flynn: It is more difficult with the example given by the witnesses, because this is not a question of insolvency or doubting that you will be paid. In this example you will be paid; you are sure it is a corporation which will pay eventually, although it may be in three years' time. Of course, you could very well discount the amount by the interest—

The Chairman: I thought you were going to suggest the opposite, that he might endorse the cheque and hand it over to the National Revenue on account of his taxes.

Senator Flynn: Endorse the account?

The Chairman: Yes.

Senator Flynn: If they want to accept that. Some have tried that before. In estates tax, for instance, they have offered to turn over the assets, and the minister would not take them.

Senator Connolly: With respect, Mr. Phillips, could I suggest that in fact you are not describing the setting up of a reserve? What you are describing is a revaluation of an account rendered but not paid.

Hon. Mr. Phillips: That is right, but at the end of the year in one particular year, as I was mentioning to Senator Everett, you do not know whether you have to set up a reserve, so you will pay your tax in respect of your billings. For instance, take law firms. Leaving aside retainers where fiscal years are not calendar years, in the case of my firm 80 per cent is done at the end of the fiscal period; you send out your bills on an annual basis. If it is on a cash basis it makes no difference. But if your accounts receivable come into income, you do not know when you send them out whether you will get 100 per cent or not, and you are not justified in setting up a reserve because you do not know the facts. You owe the money based upon the accounts receivable position, and you only know that in a subsequent year, for better or worse, depending on tax rates applicable to individuals, and whether you are in a peak or a valley situation, whether you have made or lost money, depending upon your rate of taxation. I predict that this will go to the courts on the basic issue of whether with respect to professional people, certainly with respect to lawyers, doctors and dentists—I am not 100 per cent

sure about architects and the like, because they may have contractually bound arrangements as to the amount to which they are entitled—

Mr. Lalonde: In some cases.

Hon. Mr. Phillips: Generally speaking, for professional people it is not an account receivable at the time of billing, and the issue will be raised—

Senator Cook: It may not be admitted by the debtor.

Senator Walker: They can have the bill taxed.

Hon. Mr. Phillips: If there is no debit and credit relationship, it is not an account receivable.

Senator Cook: It is only your estimate of what he owes you, and he may say, "I don't owe that".

Hon. Mr. Phillips: Somebody will raise that issue.

Mr. Rounthwaite: There is a further complicating factor. It might interest you to know that we generally employ a fairly large proportion of highly paid people. For this reason it is most important, as far as your banker is concerned, to be able to show an encouraging set of accounts receivable. You see the dilemma one is in. You want to convince these sponsors that you are indeed in business and in good shape. You get it both ways. You may have to finance large salaries for a long period of time. Some jobs that we are still to be paid for were commissioned out in 1961. It is a long drawn-out sort of thing. The tax year run on a 12-month cycle. These programs move without any regard for a 12-month cycle; they can be on a 36-month cycle, a 5-year cycle or a 10-year cycle. With a big hospital it could be 10 years from the time you are commissioned until the client has the key.

There are many factors here. One fact is that staff, once you are committed to the mobilization of staff who will carry through that large hospital job, will insist upon being paid, so you have to work in between these difficulties. On top of that, if there is a fluctuating economy, a start-stop situation, it is extremely difficult. But you cannot say that responsible university clients, responsible hospitals who have been in being for hundreds of years, and so on, are not going to pay. They will eventually.

The Chairman: When we were conducting hearings on the White Paper we went through this, and as a result we recommended the rejection of the accrual basis in its entirety. Notwithstanding that—i do not know whether they were hard of hearing on the other side, or what it was—we have it in the bill. We know the problem. The question is whether we can, and if we can, how we deal with it. I should say at this stage to the committee that I have literally a heap of letters on my desk from doctors, mainly in general practice, all across Canada, raising this same issue, pointing out the difficulties, and the time lag between when a general practitioner sends out a bill and, if he gets paid, when he is going to get paid. The moment he sends out a bill, all this becomes an account receivable.

Senator Flynn: That would not apply so much in the case of a doctor's fee, since all the bills are insured now, under Medicare.

The Chairman: I will send you some of these letters.

Senator Flynn: They will find out after some time that their position is much better than in any other profession.

The Chairman: There is no Medicare for the architects or the lawyers.

Senator Cook: Would it be fair to say that no one has been able to give us a good reason why the change should be brought about? No one has been able to tell us what the advantages are.

The Chairman: The White Paper offered a reason for making the change. They said that there was no reason why professional income should not be on the same basis as inventory.

Mr. Wilson A. Salter, Director of Professional Services, the Royal Architectural Institute of Canada: Mr. Chairman, there is a point here which is very important. There is a vast difference between a professional man with respect to his client, and a man going out and buying a hundred bales of hay. It is quite a different situation.

The Chairman: Of course, we agree with you.

Senator Flynn: I have a solution for this, Mr. Chairman. We could get around the law very easily by never sending out a bill, unless you are sure you are going to be paid right away. As far as lawyers and architects are concerned, it is very simple: you ask your client for an advance before sending him a bill, you ask him for exactly the amount of the bill that you intend to send him. Once you have received it, you send him a receipted account.

Mr. Lalonde: Except that, as Mr. Rounthwaite was trying to say, we lose.

Senator Flynn: That is the way it works out.

Mr. Lalonde: Sometimes we need these bills or receivables in order to finance our operations through the bank.

Senator Flynn: That is where my solution comes in. You ask your client.

Hon. Mr. Phillips: It is an honest statement for the bank to get credit and an equally honest statement from a man to his executors, who can produce a statement to the executory authorities, which is quite dissimilar.

The Chairman: Is there any other point? I am not stopping you, but we seem to be like a cat chasing its tail. We have not caught up with the real problem and the answer to it yet. Apparently, just to say that we are against this method of accounting for professional income in its entirety, was not enough the last time. We have to find something more. Instead of expressing an opinion, it may be that we have to go into a factual situation.

Hon. Mr. Phillips: Mr. Chairman, may I make a suggestion?

The Chairman: Yes.

Hon. Mr. Phillips: There is only one thing that might work. Because of the special circumstances applicable to professional people who are on an accrual basis, my suggestion

is that by statute they be entitled to set up a reserve, say up to 25 or 33 1/3 per cent of their accounts receivable at the end of the fiscal year. That would cover the question as to whether it is an account receivable or not; and, secondly, the difficulties of professional people being in touch with their clients to determine whether they are solvent or able to pay. They could say, "We are all right. We are on an accrual basis, but we are not like the merchant who bills or the manufacturer who bills." Professional people who are being forced on an accrual basis should be entitled to set up a statutory percentage reserve of their accounts receivable at the end of the year. That would be my suggestion.

Senator Cook: If 25 per cent did not cover it, they could be overcharged, anyhow.

The Chairman: Is there any other point you wish to develop?

Mr. Lalonde: There are some points, which are self-explanatory.

Mr. Rounthwaite: For the record, we would like to say that the suggestion which has just been made, Mr. Chairman, is very welcome.

Mr. Lalonde: As you have said, Mr. Chairman, we had a batting average of 66, and it seems that this is mostly due to your collaboration and your knowledge of the situation, and we are now looking forward to an increase in it to 75 per cent.

The Chairman: Thank you very much. That is fine. We will give the best thought we can to that.

Hon. Mr. Phillips: Mr. Chairman, before these gentlemen leave, a question was raised in the brief on non-taxation of fellowships and the like. This is one which was taken up when we considered the White Paper. I think our chairman was against that, and supported the principle that there should be taxation on fellowships, bursaries, special prizes and so forth. Some of us took the contrary position—with the greatest respect, of course, to our chairman—that professional people, in the academic sphere and in the sphere of science and research and scholarship generally, should be exempt.

I have a situation on my desk where there is a particular major financial institution that gives $50,000 annually to an outstanding Canadian, because of the great service rendered in particular fields. Cardinal Leger was one recipient; Dr. Penfield, the great neurologist, was another.

Senator Flynn: A kind of Nobel prize.

Hon. Mr. Phillips: Yes. These were non-taxable under the old law. They are to be taxable under the new law. I am merely suggesting to the chairman that this brief which has been submitted to us should give us the opportunity of reconsidering what was said in the White Paper. I did not bring a copy down, but I think we did not support the exemption.

The Chairman: I am not accepting that as being the way we went at it. I am looking it up to see.

Hon. Mr. Phillips: I thought you pinned my ears back on that.

The Chairman: Oh, never; I would never use a pin!

Mr. Lalonde: Mr. Chairman, may I look back at our position there, on these fellowships, scholarships and bursaries—including that $50,000 that was granted this year to an architect, a fact of which we are very proud.

Hon. Mr. Phillips: That is correct.

Mr. Lalonde: We think the $50,000 might be something else and I would put that aside. Normally, however; in the case of a fellowship or scholarship, if it becomes taxable it will have to be increased, otherwise it will not do the same job that it is intended to do.

Senator Flynn: It is like a scholarship; it is intended for learning and is usually deductible from income.

Hon. Mr. Phillips: With the brief, Mr. Chairman and honourable senators, we have a chance to deal with it again.

Senator Cook: Have we considered a limitation, in other words, extending it to a certain amount?

Hon. Mr. Phillips: Let me see.

The Chairman: One of the areas the Government looks at is that, if there is no limit, they are missing out on some tax revenue that they should get.

Senator Connolly: Would it help my friend here if I referred to page 70 of the Summary of 1971 Tax Reform Legislation, where it says that fellowships, scholarships and bursaries under the old law are "not taxable unless related to employment", and under the new bill are "taxable with an annual exemption of $500." Also the Commons report recommends the same as the bill proposes, the Senate report recommended that these fellowships, scholarships and bursaries should not be taxable, and the White Paper suggested that they should be taxable, with no exemptions.

The Chairman: I would not accept the attribution that the hon. Mr. Phillips made.

Mr. Sandford: There is one additional point, Mr. Chairman. Some of these fellowships are travelling fellowships where expenses are incurred. At least, it would appear that if the recipient has to travel to Paris, or to some other place, to enjoy the benefit of the fellowship, the expenses incurred should be deductible.

The Chairman: We will look at that, too.

Senator Flynn: There should be a proportion of a scholarship that should not be taxable—possibly the amount which is paid for living expenses and for travelling and learning.

Senator Connolly: The exemption in the act is $500, but that may not be enough. Perhaps the exemption cannot be related to a specific sum, but may have to be related to some such items of adjustment referred to, namely to exempt the cost of the expense incurred in enjoying the fellowship.

The Chairman: All right. Thank you very much.

The Chairman: We have one more submission to hear this morning. Representing The Teachers' Insurance and Annuity Association of America is Mr. John T. DesBrisay, Q.C., Councel, and Mr. Wilfred Wilson, vice-president. We will now hear from Mr. DesBrisay.

Mr. John T. DesBrisay, Q.C., Council, The Teachers' Insurance and Annuity Association of America: Mr. Chairman, we are grateful for the opportunity of appearing before you, particularly in that our brief was submitted to you at the eleventh hour and we have been afforded the opportunity of this hearing on such very short notice. I am not sure whether honourable senators will have had an opportunity to read the brief, in view of the fact that it was only filed on Monday of this week.

The Chairman: Some of us have read it, Mr. DesBrisay. We have also talked with others about it.

Mr. DesBrisay: Thank you, Mr. Chairman. Perhaps I could just summarize it. The brief deals with certificates of exemption from non-resident withholding tax on interest paid from Canadian sources to the tax-exempt non-resident. Section 106, subsection 9 of the Income Tax Act, as it is now worded, provides that if a non-resident who is tax-exempt in his own jurisdiction satisfies the Minister of National Revenue as to that exemption in his own jurisdiction, he can qualify for a certificate that will exempt him from paying non-resident withholding tax on the Canadian debt obligations that the non-resident buys.

Senator Connolly: Right there, I think it would be very helpful to the committee if you could give us a specific example of the Canadian and American company involved.

Mr. DesBrisay: The American company which I represent, and of which Mr. Wilson is Vice-President, is The Teachers' Insurance and Annuity Association of America. It carries on on a non-profit basis the business of funding retirement programs for educational institutions. Its activities are restricted to the retirement programs of universities, colleges and research organizations.

Senator Connolly: You mean, people who work in those colleges and organizations?

Mr. DesBrisay: Yes.

Senator Connolly: All right.

Mr. DesBrisay: The staff of those organizations.

The Chairman: This organization, as I understand it, is tax-exempt in its home territory.

Mr. DesBrisay: Yes.

The Chairman: Perhaps the senators would like to know the wording of the section in the act. Section 106 (9) says this:

> The Minister may, upon application, issue a certificate of exemption to any non-resident person who establishes to the satisfaction of the Minister that
>
> (*a*) an income tax is imposed under the laws of the country of which he is a resident; and
>
> (*b*) he is exempted under the laws referred to in paragraph (*a*) from the payment of income tax to the government of the country of which he is resident.

Senator Connolly: Apparently this company qualifies.

The Chairman: Yes, it qualifies. Now, I have gone to the trouble of excerpting from the Commons *Hansard* and the Budget Speech in 1963 what the minister said in supporting this amendment. You will find it very interesting.

Senator Flynn: That was Mr. Gordon in 1963.

The Chairman: Yes. Even some of the Opposition commended him.

Senator Flynn: Oh, yes. Nobody suggests that there has been any improvement since then!

The Chairman: Well, that might be questionable. Perhaps I should read this to the committee now. This was clause 13 in the bill for the year 1963. When I went back and read what we said about the whole bill in the Senate, I discovered that I was the one who gave the explanation of the bill. I was prompted a few times to say to myself, "Did I say that?". However, here is what Mr. Gordon said:

> This paragraph of the resolution proposes that interest paid to certain non-residents be exempt from withholding tax. The Income Tax Act imposes a tax of 15 per cent on interest paid by residents of Canada to non-residents. This tax is withheld at the source by the Canadian payer. This paragraph of the resolution proposes that non-resident persons such as pension trustees or charitable foundations that are exempt in their country of residence be granted an exemption from this withholding tax. The objective of this paragraph is to broaden the market for Canadian securities in other countries and in this way to help in the policy of keeping interest rates in Canada at as low a level as possible.

And then all the other members joined in.

So you have the net situation that an exemption was offered to attract a non-resident investor to enter the Canadian market in these fields. Now he is here. Perhaps he has dug himself in and it is difficult to get out, and he is faced with a tax situation.

Senator Everett: Not only that, but it would appear that it is retroactive.

Senator Connolly: Not only has he dug himself in, but he has dug himself in very deeply, as the brief would seem to indicate.

The Chairman: Mr. DesBrisay, we are taking over from you. Perhaps you had better go ahead.

Mr. DesBrisay: You are saying it for me, Mr. Chairman, which is obviously better than my saying it for myself.

The Chairman: The situation, as I understand it, is that you have $135 million invested in Canadian bonds and securities, and now the bill says that the income on those—that is, the interest—is subject to a 15 per cent withholding tax on and after 1974. In other words, the certificate which

you now hold becomes invalid in 1974. As I understand the nature of the investments that you have, the primary purpose was not looking to marketability but was looking to security of investment. Therefore, there would be great problems involved in trying to prepare those for the market, to develop marketability, to clear with the Securities Commission and to deal with $135 million all in a period of three years. So on and after 1974 they are subject to the 15 per cent, and since they have no off-setting taxes in the United States it is a tax they pay here.

Senator Connolly: If I may, Mr. Chairman, I would like to probe this matter a little more. I do not question the decision of the department to exempt this organization, but perhaps a further probing might give us the reason why this was imposed. As I understand it, what your organization does to a certain extent, is subsidize the retiring allowances of people in universities and other institutions engaged primarily in education and research on a non-profit basis. You make no profit yourselves, and your only expenses are the expenses of operating the business of your company. The ultimate beneficiary is not a charitable organization; the ultimate beneficiary is a person, a taxpayer and a learner. Is there something in the background to the thought behind the proposal in the bill that they should not take a benefit from an organization like this and have the organization escape the tax? I know it will be taxable in their hands when they get their retiring allowance, but the rate will be lower. So what about your tax-exempt companies that pay this retiring allowance? It is not like an educational institution, as such, where the benefits are to be distributed to a broad group like a group of students. The benefits are going to be had by former professors, researchers, teachers and people like that. So perhaps I should ask you first of all if it is relevant.

Mr. Wilfred Wilson, Vice-President, the Teachers' Insurance and Annuity Association of America: I think it is particularly relevant.

The Chairman: Why is it relevant? We are dealing with the question whether certain income in Canada going to a non-resident should not be subject to withholding tax.

Mr. Wilson: I think in the proposed statute the relevance is this, that the pension trust, the United Mine Workers or some organization like that, would be exempt. I think we are stuck, in a sense—I was going to say, "because of an accident of birth"—because when Carnegie shifted from the free pension system to T.I.A.A. the organization was set up in a certain way to provide supervision, and it seems to fall into a sort of a trap because of its form.

The Chairman: But your organization is not a pension trust.

Mr. Wilson: No, it is not, but it is organized as a legal reserve life insurer and is considered tax-exempt, unlike other insurers in the United States. I think Senator Connolly's point is particularly well taken, because every other similar type of organization—again, other than in the legal form—is considered exempt even under the proposed tax structure.

The Chairman: You mean in Canada?

Mr. Wilson: Yes. So, I think it is a technical error.

The Chairman: So there are two points, and the first point is that you should be tax exempt here. Have you applied?

Mr. Wilson: No.

Mr. DesBrisay: In 1963 we were told by the Department of National Revenue that they did not consider we were tax-exempt. Up until 1963 we had been exempt from withholding tax under article 10 of the tax treaty which provides that there will not be any tax on a charitable organization in the United States if that organization would also qualify as a charitable organization in Canada. So, until 1963 we had paid no tax either on dividends, if we had any—and I am not sure whether we did or not—or on interest. Then in 1963 the Department of National Revenue said, "We have reviewed your charitable status in Canada and we think that really you are benefiting the individuals rather than the educational institution."

Senator Connolly: That is the point I was making. It puzzled me, and that is the reason I raised the question.

Mr. DesBrisay: The United States has said that T.I.A.A. is benefiting the educational institutions by subsidizing their retirement programs. Canada has said, "You are benefiting the individuals." So it is really a difference in attitude.

Senator Connolly: It is a matter of what pocket you should take it out of.

Mr. DesBrisay: Yes. So in 1963 we were told that they would remove our article 10 exemption, but they would then issue us a certificate of exemption as a tax-exempt non-resident, so that as long as our investments were restricted to the purchase of debt obligations we would continue to be tax exempt. We went ahead and purchased $113 million worth of debt obligations.

It is my information that there are no equity kickers attached to any of these investments and there are no participation features. They are straight fixed interest rate investments. It has been T.I.A.A.'s feelings that this is exactly the kind of money that Canada wanted coming in. In 1963 section 106(9) was enacted encouraging us to buy securities. We have done this, and now we are told that in 1974 we will have to pay a 15 per cent tax.

Senator Everett: Mr. DesBrisay, you say this is all debt money. Would you have any idea at what average rate of interest that $113 million was loaned?

Mr. DesBrisay: I think it was around 6 per cent, because our return is about $6 million a year.

Senator Everett: And that is without any equity kickers at all?

Mr. DesBrisay: That is correct.

Senator Connolly: This is not directly related to the point, but are any of the benefits that are paid to persons retiring from universities, research centres, and so on, paid in Canada, or are they all paid in the United States?

Mr. DesBrisay: There are benefits which are paid in Canada.

Senator Connolly: Paid to Canadians?

Mr. DesBrisay: Yes, to Canadians.

Senator Connolly: Paid to Canadians who are retiring from Canadian institutions?

Mr. Wilson: Yes, there are around 10 institutions that still participate.

Senator Connolly: In other words, your company is not simply a non-resident owned investment company—and I am using that in very broad terms—but you are actually conferring benefits to Canadians from these funds as well?

Mr. DesBrisay: In 1963 we had funded a number of Canadian organizations' pension plans.

Senator Connolly: Would you care to identify a couple of them?

Mr. DesBrisay: St. Francis Xavier University.

Mr. Wilson: Mount Allison, British Columbia Research Centre, Lethbridge University.

Mr. DesBrisay: St. Thomas University—and prior to that we had the University of British Columbia, the Universities of Toronto and McGill. Then article 10—Exemption—was lost. This meant that we would ordinarily start to pay income tax in Canada. In 1963 we arranged with the department that if we were to fund no more plans, if we did not issue new policies in Canada and gradually phased the existing policies out, they would unofficially exempt us from tax on the contracts we had already written up.

Senator Connolly: I do not think that we understand this aspect of it. This is not simply a gratuity which you offer to supplement the normal pension plan of an individual in a university situation. But you actually sell a policy and the beneficiary pays a premium to you. Is that correct?

Mr. Wilson: Perhaps I can answer that with a little history. Mr. Carnegie, when he set up the free pension system in Canada, the United States and Newfoundland, as it then was, in the early part of this century, intended to provide out of his own resources the pension benefits for faculty members at approximately 450 institutions in North America. He provided also the Carnegie Free Libraries, and so on.

It became clear to him at just about the time of the First World War that even he did not have sufficient money to do this. A committee of businessmen, educators and others was therefore appointed to examine the situation. They arrived at the idea of setting up the equivalent of a co-operative, which in a sence teachers' insurance is, to provide fully transferable annuity contracts for people of higher education in both countries. Contributions for the annuity contracts would be paid on the one hand by employers and on the other hand by the employees, or faculty members at the institutions. The secret of the success of the plan is that it is very inexpensive to operate.

The other thought, which is becoming more popular in both Canada and the United States today, is that these were fully vested and transferable contracts which give the faculty member an opportunity to move.

The Chairman: That is portability.

Mr. Wilson: Yes. Another great attraction, of course, is our tax exemption. In a sense, therefore, although it is a corporation it is run essentially as a foundation.

Senator Everett: Could you give us some idea as to how substantial Teachers' Insurance is?

Mr. Wilson: Teachers' has assets of approximately $2 billion.

The Chairman: Let us consider Mount Allison as an illustration. You used the expression that there you fund their pension plan.

Mr. Wilson: Yes, the board and faculty there both contribute to the contracts. It is 5 per cent of salary.

The Chairman: Is that the entire contribution?

Mr. Wilson: No, I think the administration contributes another 10 per cent.

Senator Connolly: Does Carnegie provide anything?

Mr. Wilson: Yes; many of our old contracts and some of our overheads are still covered by original Carnegie grants.

Senator Connolly: Which you hold?

Mr. Wilson: That is correct. However, primarily the cost of running the system now comes out of current income.

The Chairman: To follow this up, we discussed Mount Allison. You funded the plan and receive contributions from the faculty and the administrative body itself. What do you do then?

Mr. Wilson: We issue a contract. The other outstanding feature of this contract, which is very popular, with regard to mobility, is that rather than have a vast "carrot and stick" pension contract, the faculty member at Mount Allison has one which is his own. Should he choose to move, all those years are not lost to him.

The Chairman: He has contributed from year to year.

Mr. Wilson: That is right.

The Chairman: The type of contract allows for that and builds up a pension.

Mr. Wilson: That is right.

The Chairman: He personally receives a policy or a contract.

Mr. Wilson: Yes, with the exception of a few institutions, such as Princeton which likes to holds its contracts, the man usually has it in his own safety-deposit box. He also has a piece of paper which I think is generally looked upon by all of us as being something symbolic.

The Chairman: May I add a few sentences from what the Minister of Finance said in 1963?

> The purpose of this resolution is, of course, to make it easier or make it more desirable for pension funds in other countries to invest in Canadian bonds. As we all

know, we are primarily interested in thinking about the inflow of capital. Certainly, in totals and magnitudes, we are primarily interested in the sale of Canadian bonds abroad rather than Canadian equities.

That is the sum total of the effect of what he said. How it can lose that character now puzzles me.

Senator Isnor: Who made that statement?

The Chairman: The then Minister of Finance, Mr. Walter Gordon, in July, 1963, when introducing this amendment that is now being taken away.

Senator Everett: As I understand it, Teachers' was insuring professors and researchers in universities like UBC and Toronto, and by an action of the Department of Revenue they were asked not to.

Mr. DesBrisay: I do not think that is right. I believe that what happened was that, prior to this, interest rates in Canada were substantially higher than those in the United States, and the pension plans which Teachers' was funding for major Canadian universities were then being calculated actuarially on the United States interest rate rather than on a Canadian rate, so that for a period we really ceased to be competitive.

Mr. Wilson: I would like to avoid use of the word "competitive", but that is about right. It really started in the Second World War with foreign exchange problems.

Mr. DesBrisay: There was a gradual decline in the plans that we were funding, and in 1963 an agreement was struck whereby, in effect, we undertook not to expand the business there and gradually to phase it out.

Mr. Wilson: This is again up for discussion between some of the educational associations in Ottawa and ourselves. They would like to work out some kind of mechanism, associated directly with us, or perhaps by forming their own organization which might be patterned after ours, and we could consider whether we would transfer our Canadian liabilities and certain or our Canadian assets to cover them. There is an interesting facet of the phenomenon in that of $113 million of Canadian investments, $35 million represent liabilities that we have to Canadians, so in a sense that would be taxed.

The Chairman: What about the cnaracter of the investments? The incentive in acquiring these investments? The incentive in acquiring these investments is not necessarily that they must be highly marketable.

Mr. Wilson: One of the things that worries me about the current proposal is the basic proposition that they are not highly marketable. It seems to me also that we would be very vulnerable to any buyer. Obviously, if we have to go out of the market we would not be in a very good position.

Mr. DesBrisay: We have a number of Governement and municipal bonds.

Mr. Wilson: Yes, about $40 million.

Mr. DesBrisay: And I believe they are not taxed.

Senator Connolly: They are what?

Mr. DesBrisay: I believe they are tax exempt, in any event. When this concept of certificate of exemption was introduced in 1963, it was also provided that federal, municipal and provincial bonds would be tax exempt on their own. Even if we lose our certificate of exemption, we will not pay tax on those investments; but with respect to all of the others we would be exposed to withholding tax.

The Chairman: Have you a suggestion for relief?

Mr. DesBrisay: Mr. Chairman, I think there are really two parts to our submission. One is one behalf of the holders of all certificates of exemption. It seems wrong that the Canadian Government could withdraw, in effect retroactively, and exemption so that holders of such certificates will have to pay tax on the interest from investments which they purchased in good faith, assuming that they would continue to be tax exempt. That applies to $113 million invested by Teachers' and also to the investments on the part of other non-residents who will likewise lose their exemption. Perhaps the best example is that of the United States Regulated Real Estate Trust. These trust have had a certificate of exemption, and they will now lose it. There are a number of those trust which have made significant investments in Canada.

Our first submission, Mr. Chairman, would be that there should be a provision in the bill which allows the interest from the investment which the non-resident now holds to continue to be tax exempt as long as the non-resident itself remains exempt in its own jurisdiction. We have attached to our brief a specific suggestion as to the actual amendment which might be made to the bill in this regard.

Secondly, Mr. Chairman, specifically on behalf of ourselves, we would ask this committee to consider that it is really a technical oversight that organizations such as ours will hereafter be unable to continue to purchase this type of Canadian debt. The urgency in this regard is that we now have an $8 1/2 million commitment to finance the new Holiday Inn building in the Toronto Civic Square. That money is to be advanced towards the end of 1972, and we suddenly find that in 1975 we will lose the exemption which was really basic to our entering into that commitment. We have to review, whether or not we have some "out" clause with respect to that investment. This is going to reduce our yield by 15 per cent. We also have current negotiations for financing other Canadian projects, and we do not know what to do about those.

We are asking this committee to consider recommending an amendment which would allow us to qualify for a certificate of exemption in the same way as the pension trusts and certain other foreign tax-exempt organizations will continue to qualify in Canada.

Senator Connolly: That is given under the new bill.

Mr. DesBrisay: Under the bill this type of organization will continue to have a certificate of exemption.

Senator Connolly: That is right.

Mr. DesBrisay: I believe I have enumerated these organizations in our brief.

The proposed amendment now says that in order to qualify for a certificate of exemption, the non-resident

must show, as before, that he is exempt in his own jurisdiction.

Senator Connolly: Yes.

Mr. DesBrisay: And he must also show that if resident in Canada he would be exempt here.

Senator Everett: You are referring to section 212(14), I take it?

Mr. DesBrisay: Yes.

Senator Connolly: Section 212(14) of the bill?

The Chairman: Yes.

Mr. DesBrisay: Those exemptions are all listed in section 149. In other words, if you qualify under section 149 of the bill for exemption from tax in Canada, then you would qualify for this certificate of exemption. Those organizations that would qualify under section 149 include labour organizations, fraternal benefit societies, any type of non-profit organization. A mutual insurance company that receives its premiums wholly from the insurance of churches, schools or other charitable organizations would qualify for exemption. An insurer engaged during the period in question in the business of insuring farm properties and properties used in fishing, or residences of farmers or fishermen, as long as 50 per cent of their income comes from that source, will qualify. Unless we want to keep out Teachers' money, what is the point of allowing these other organizations to continue to invest in Canada and, in effect, prohibit Teachers'? We cannot imagine that it is deliberate, and we therefore assume it is a technical oversight in the bill.

The Chairman: You do not think you would come within the language of trusts or corporations?

Mr. DesBrisay: We do not think so.

Senator Connolly: In other words, what you are saying is that the broadening of the section, giving them tax exemption status, is not broad enough to catch you, and you are the sore thumb that sticks out and needs some kind of medication, the medication here being to put you in somehow in general language, so that other organizations who do the kind of work you do should be on the same basis as labour unions and these other groups you have referred to.

Mr. DesBrisay: Yes.

The Chairman: What you say is that what you do, in substance, can be equated to the pension trust.

Mr. DesBrisay: We are a pension trust with a number of different employer members. We receive the contributions of employer and employee. Then, instead of using the accumulated benefits of those members to buy an annuity for them from some outside source, we actually fund our own annuities and issue our own policies.

The Chairman: Are there any questions?

Senator Everett: Mr. DesBrisay, would you mind dealing with just one more point, and that is paragraph 14 on page 6?

Mr. DesBrisay: We have been advised by the Department of Finance that, because of pressures on the Canadian dollar, their present policy is to try to reduce foreign investments of all sorts, whether it be debt or equity. In paragraph 14 of the brief we submit that the denying of exemption for Teachers', when foreign pension trusts, the Ford Foundation, and so on, will continue to have their exemption, is not really relevant to any problems we may have with the strength of the Canadian dollar relative to the United States dollar.

Senator Everett: In other words, you would be discriminated against as one of a vast number of people in the same business.

Mr. DesBrisay: Yes. Keeping us out is not relevant.

The Chairman: Are there any other questions, or is there anything more you would like to say?

Mr. DesBrisay: If I might make one very quick point on our suggested revision; on page 9 of the brief we have suggested the addition of a subparagraph to grant exemption to:

> an association, society or corporation established or incorporated for the purpose of providing retirement annuities in connection with retirement programs of educational or research organizations, no part of the income of which association

is of benefit to anyone.

Perhaps we should suggest that there be added the word "religious" in connection with retirement programs of "religious," educational or research organizations. I am advised that there are certain pension trusts of various church organizations which operate in a similar way.

The Chairman: We shall note it. Are there any other questions? We thank you very much.

Honourable senators, this concludes our hearings on the reference. Your staff and your chairman are starting to prepare the second instalment of our report. We will try to have it ready within a week or ten days.

Senator Cook: The committee members will praise it. That is all we can do.

The committee adjourned.

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THIRD SESSION—TWENTY-EIGHTH PARLIAMENT

1970-71

THE SENATE OF CANADA

STANDING SENATE COMMITTEE ON

Banking, Trade and Commerce

The Honourable SALTER A. HAYDEN, *Chairman*

No. 50

WEDNESDAY, NOVEMBER 24, 1971

Preliminary Report *No. 2*

on

The Summary of 1971 Tax Reform Legislation

24315—1

MEMBERSHIP OF THE COMMITTEE

THE STANDING SENATE COMMITTEE ON BANKING, TRADE AND COMMERCE

The Honourable Salter A. Hayden, *Chairman,* and

The Honourable Senators:

Aird	Grosart
Beaubien	Haig
Benidickson	Hays
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Burchill	Lang
Carter	Macnaughton
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Cook	Smith
Croll	Sullivan
Desruisseaux	Walker
Everett	Welch
*Flynn	White
Gélinas	Willis
Giguère	

**Ex officio members*

(Quorum 7)

Order of Reference

Extract from the Minutes of the Proceedings of the Senate, September 14, 1971:

"With leave of the Senate,

The Honourable Senator Hayden moved, seconded by the Honourable Senator Denis, P.C.:

That the Standing Senate Committee on Banking, Trade and Commerce be authorized to examine and consider the Summary of 1971 Tax Reform Legislation, tabled this day, and any bills based on the Budget Resolutions in advance of the said bills coming before the Senate, and any other matters relating thereto; and

That the Committee have power to engage the services of such counsel, staff and technical advisers as may be necessary for the purpose of the said examination.

After debate, and—

The question being put on the motion, it was—

Resolved in the affirmative."

Robert Fortier,

Clerk of the Senate.

24315—1½

Wednesday, November 24, 1971.

INTRODUCTION

On September 14th, 1971, there was tabled in the House a document entitled "SUMMARY OF 1971 TAX REFORM LEGISLATION" and, by resolution of the Senate on the same date, consideration of same was referred to the Standing Senate Committee on Banking, Trade and Commerce.

For the purposes of brevity and identification, the "SUMMARY OF 1971 TAX REFORM LEGISLATION" will be referred to in this report as the "proposed legislation" and the Standing Senate Committee on Banking, Trade and Commerce will be referred to as "your Committee" or "the Committee".

On Thursday, November 4th, 1971, The Honourable Salter A. Hayden, Chairman of your Committee, submitted a preliminary report on the proposed legislation and, in such report, a number of recommendations were submitted with respect thereto.

In the report of November 4th, 1971, hereinbefore referred to, the following statement was made:

> "Having regard to the urgency of the matter and the problem of time, your Committee is submitting for your approval at this time a limited number of recommendations but it is hoped that the Committee will still be in the position to make further recommendations before the proposed legislation reaches this House. Alternatively, the Committee will submit these further recommendations when the said proposed legislation reaches this House after having passed the other House."

Since the submission of the preliminary report, your Committee has heard a further number of representations and has received further written submissions on the proposed legislation. Having studied these further submissions and representations which were received in the period following the 27th day of October, 1971, to the 10th day of November, 1971, when the last hearing took place, your Committee has concluded that it is desirable to submit to the Minister of Finance, as expeditiously as possible, a number of further recommendations in respect to the proposed legislation which is presently being considered by Committee of the Whole of the other House. It is the hope that, upon receipt by the Minister of Finance of these further recommendations, the same will be accepted by him as again being pertinent and relevant, and to the extent so regarded, that appropriate amendments will be submitted by him to the other House while the said proposed legislation is still being considered in the Committee stage.

In your Committee's report of November 4th, 1971, and in the section captioned "EPILOGUE", your Committee recorded its intention to present a second report after the termination of its hearings covering submissions made subsequent to October 27th, 1971. Your Committee referred in such captioned "EPILOGUE" to some of the topics which it intended to cover in its second report. Having regard to the exigencies of time, your Committee has been able to deal with only some of the topics referred to in the "EPILOGUE". The proposed recommendations with respect to these topics are hereinafter submitted.

PULP AND PAPER INDUSTRY

1. General considerations

The pulp and paper industry plays a vital role in the economy of this country. It is because of this predominant role that your Committee has given special attention to the representations made by the Canadian Pulp and Paper Association.

Corporations in the natural resource industries are characterized by the following common factors:

(a) development and processing of natural resources,

(b) investment of large amounts of capital,

(c) creation of substantial employment, and

(d) sales on a world-wide basis.

Corporations in the natural resource industry are also characterized by a large degree of risk. Part of such risk is represented by the huge capital investment in machinery and equipment required in the pulp and paper industry.

From the information provided to your Committee, the following resume is submitted:

> For the year 1970 the industry exported 12.54% of the total Canadian domestic exports and ranks as one of the largest exporters in Canada. In 1970 the industry employed 156,400 persons including permanent and seasonal woodland operators. In addition, a substantial number of persons are employed in related fields. The statistics submitted by the representatives of the industry indicate that the five major suppliers of wood pulp and newsprint in the world are Canada, United States, Scandinavia, Japan and Russia. United States and Scandinavia are Canada's main competitors in this industry.
>
> The following table illustrates the change and the continuous deterioration in Canada's position in this field in relation to its major competitors over the last 20 years.

	Relative Percentage Share of Production			
	Wood Pulp		Newsprint	
	1950	1970	1950	1970
Canada	28	23	72	58
United States	49	53	14	22
Scandinavia	23	24	14	20
	100%	100%	100%	100%

> Representatives from this industry have expressed the view that this decline is caused by, among other factors, tax disadvantages suffered by Canadian corporations in relation to their major foreign competitors. These representatives prepared an analysis of comparative income tax payable by United States corporations and Canadian corporations for the 5 years ended

in 1969. This analysis indicates that these United States corporations incurred average taxes of 34% of income (taking into account both capital and income) whereas Canadian corporations incurred comparable average taxes of 49%.

As to Sweden's tax treatment, the current annual rate of corporate income tax payable is approximately 40% as compared with 51% to 54% in Canada. To this tax advantage Swedish corporations obtain more generous capital cost allowance (depreciation and depletion) and also investment reserves. In Finland, the currency devaluation of 31% which occurred in 1967, coupled with that country's fiscal policy has further placed its pulp and paper industry in a relatively advantageous competitive position as a world supplier.

It is therefore apparent that the Canadian pulp and paper industry is at a great disadvantage vis-a-vis its international competitors. It is therefore essential that special consideration be given to assist the industry to maintain and improve its international position.

This industry's reliance on world markets also has an important direct effect on employment in Canada.

It is generally acknowledged that Canadian corporations which sell their products in international markets are in a difficult competitive position if their tax burden is much greater than that applicable to their competitors. It is apparent that the incidence of tax on the pulp and paper industry in Canada deserves to be examined carefully and that some attempt should be made, if at all possible, to place this industry in a reasonably fair position vis-a-vis its foreign competitors if Canada wishes to promote its export trade and employment in this industry.

At the risk of repeating itself, your Committee would again quote part of a statement made by the Government in the White Paper Proposals for Tax Reform.

"6.9—. Going international is frequently necessary to enable Canadian companies to achieve the economies of scale which are otherwise denied them by the relatively small size of the Canadian domestic market. Such companies would find it hard to compete on the international scene if they were subject to more onerous taxes than those which apply to their competitors.—."

Your Committee concurs with this statement but deplores the fact that no recognition has been given to this very problem in respect of the pulp and paper industry under the proposed legislation.

The pulp and paper industry is subject to high capital requirements. As a consequence, carrying charges and amortization costs have a very great effect on the cost of production. For this reason, your Committee is of the opinion that any alleviating measures should be related to this factor, and that a concept of "earned depreciation" should therefore be given consideration in the proposed tax legislation.

The concept of "earned depreciation" could be formulated in the following manner: a corporation would earn the right to claim a special deduction based upon amounts incurred in respect of any qualified expenditures made after the commencement of the new system.

Earned depreciation would be in addition to the normal capital cost allowances. It would not reduce undepreciated capital cost and would not be subject to recapture of capital cost allowance. The corporation would have the right to claim all, or part, of this earned depreciation in the year in which its capital expenditures are made or to defer all, or any part, until some subsequent year. Appropriate safeguards could be introduced to prevent abuses.

In order not to discriminate against corporations which embarked upon a modernization or expansion program prior to the commencement of the new system, it would be necessary to establish a deemed earned depreciation. The amount of this deemed earned depreciation could be calculated as a certain percentage of the undepreciated capital cost of qualified expenditures on hand at the commencement of the system. If necessary, a limit could be placed on the maximum amount deductible in any year.

2. Pollution abatement and control

Apart from the tax disadvantages mentioned above, a new factor has recently been added to the industry's operating costs. This is the requirement to install and improve equipment and measures for the abatement and control of pollution.

Pollution abatement and control is not merely a local problem: it is primarily a national problem. The need for anti-pollution measures cannot be overemphasized, however. At the same time as Canada is endeavouring to improve the general environment for all Canadians, it would be short-sighted to overload the costs of some of our exporting industries which are competing in world markets.

Without debating the relative effectiveness or fairness of the use of tax incentives for the purpose of abatement or control of pollution generally, the nature of the pulp and paper industry is such that it must be located near large bodies of water for both production purposes and for direct, inexpensive transportation. Apart from the requirement of adequate hydro-electric power, such locations are usually somewhat remote from centres of population except where the concentration of people and ancillary businesses have developed in that particular area. The importance of the contribution to the national wealth produced by this industry clearly appears to warrant some spreading of the cost to include more than local communities and the pulp and paper industry.

With a view to correlating the national and local objectives of pollution abatement and control and to obtain a fair sharing of the cost burden, it appears advisable to supplement existing grant programs and tax incentive programs by developing a special loan program for the pulp and paper industry. This could consist of long-term federal loans without interest or federally guaranteed loans to pulp and paper corporations.

Alternatively, if interest be charged, part or all of such interest might be rebated from year to year. This could be achieved by allowing an annual additional capital cost allowance whereby the original capital cost could be increased by a percentage factor sufficient to accomplish the desired after-tax effect equivalent to a rebate of interest.

Your Committee considers that the foregoing would prevent an undue loading of additional costs on production by distributing some of the burden on a national basis.

While loan programs, forgiveness of loans and rebate of interest cannot be expected to fall directly within the scope of fiscal policy, your Committee is of the opinion that equivalent results could be produced by translating the after-tax effect into special capital cost allowance (depreciation) measures and rates in the proposed legislation.

Such measures are now available under the present legislation. As a matter of fact, in the government's budget tabled on December 3, 1970, additional capital cost allowances were created whereby manufacturing and processing enterprises are permitted to value new investments in machinery, equipment and structures at 115 per cent of their actual cost as a base for calculating capital cost allowances. This is applicable to new capital investments acquired during the period commencing December 4, 1970, and ending March 31, 1972.

Having regard to the foregoing factors and special disabilities affecting this industry *YOUR COMMITTEE RECOMMENDS:*

1. that a concept of "earned depreciation" be introduced in the proposed legislation or, alternatively, that additional capital cost allowances be granted by one of the following methods:

   (a) increasing the present rate of capital cost allowances,

   (b) introducing additional yearly capital cost allowance through permitting the original capital cost or the undepreciated capital cost as at the commencement of the new system to be valued at more than 100 per cent, and

   (c) granting accelerated capital cost allowance.

2. that expenditures by corporations in the pulp and paper industry for the control and abatement of pollution be financed and assisted by one of the following methods:

   (a) government grants or long-term interest-free loans, or

   (b) special capital cost allowances such as those referred to above.

3. *Logging tax credit*

It was submitted to your Committee that there exists an element of double taxation for some corporations because the abatement for the provincial logging tax is not 100 per cent. This is caused by the fact that the credit for federal abatement is not calculated on the same basis as that calculated for the logging tax itself. This present anomaly, far from being cured by the proposed legislation, has been compounded by a further limitation in calculating the logging tax credit, namely the required inclusion of taxable capital gains in the tax base, which gains are to be excluded from the taxable income available for the logging tax credit (although such gains could be included in the calculation of the logging tax itself). This double taxation becomes very severe in a loss year or when the non-logging operations suffer a loss.

Furthermore, there are provinces which do not levy a logging tax as such, but instead levy other taxes corresponding to the logging taxes of other provinces. It is suggested that the government should examine the various taxes levied on the pulp and paper industry in provinces which do not have a formal logging tax, and determine if some provinces or municipalities are levying taxes which are in substance similar to logging taxes but which are nevertheless not deductible from income tax payable.

YOUR COMMITTEE RECOMMENDS:

1. that the amount of provincial logging tax paid be credited against federal income tax payable within specified limits and with the following additions:

   (a) that the base upon which the logging tax credit is calculated for federal purposes should be the same as that upon which the provincial logging tax was imposed, and

   (b) that any creditable logging tax not deductible in a taxation year be carried forward and be deductible against future federal income tax payable.

2. that the government consider the possibility of granting similar relief to those corporations that are paying provincial or municipal taxes on their logging operations not levied as logging taxes but which are in substance similar to a logging tax (and are not subject to the federal abatement).

TAX-EXEMPT NON-RESIDENT INVESTORS

Under the present Income Tax Act the Minister of National Revenue is authorized to issue a "certificate of exemption" to any non-resident person who establishes that he resides in a country which imposes an income tax and that he is exempt from such tax under the laws of that country. The effect of obtaining a certificate of this kind is that the non-resident person is exempt from Canadian non-resident withholding tax in respect of interest payable on any bond, debenture or other similar debt obligation that was issued to him after June 13, 1963.

The obvious purpose of this provision (as hereinafter noted) was to encourage the sale of Canadian debt obligations to tax exempt non-residents by removing the tax disadvantage which such persons otherwise would suffer if they reinvest in Canada rather than in their country of residence. Unlike the non-resident person who is subject to tax in his country of residence and who is generally able to recover part, if not all, of the Canadian income tax payable on Canadian source income by way of credit against the income tax otherwise payable by him, the tax-exempt non-resident is unable to recover any part of the Canadian income tax which he may be required to pay. Therefore, but for the "certificate of exemption" provisions, a tax-exempt non-resident would suffer a tax disadvantage by investing in Canadian debt obligations rather than in securities issued by persons resident in his country of residence (the income from which would be exempt from tax).

In order to qualify for a certificate of exemption under the proposed legislation, a non-resident must not only be exempt from income tax in the country in which he resides but must also be

1. a person who would be exempt from Canadian income tax under the relevant exempting provisions of the proposed legislation if he were resident in Canada, or

2. a trust or corporation established solely in connection with an employee's superannuation or pension fund or plan.

Any non-resident person failing to qualify under these new requirements who holds a certificate of exemption which was issued under the provisions of the present Income Tax Act and which is still in force on December 31, 1971, will continue to be exempt from Canadian non-resident withholding tax in respect of interest payable to him on or before December 31, 1974—provided that he continues to be exempt from tax in his country of residence. Interest received by him thereafter will be subject to the normal withholding tax provisions unless he is able to meet the new requirements of the proposed legislation.

In considering the effect of these new provisions, your Committee heard evidence presented on behalf of a major non-resident investor who now holds a certificate of exemption but who will fail to qualify for a similar certificate under the proposed legislation. This organization has invested substantial amounts in long-term Canadian debt obligations and has entered into commitments to purchase additional Canadian bonds, in each case on the assumption that its exemption from Canadian non-resident withholding tax would remain in force as long as it continued to qualify as a tax-exempt person in its country of residence. Having regard to the amount invested in Canada and having regard also to the fact that many of the debt obligations were purchased privately (consisting of securities in respect of which no prospectus has been filed), this particular organization appears to have valid reasons to believe that it will encounter considerable difficulty in selling its Canadian securities and thereby avoid the tax disadvantage which it would suffer if it continued to own such investments after December 31, 1974.

This particular situation is presumably by no means unique and your Committee considers it inequitable that the exemption should be withdrawn with respect to investments or commitments which have already been made—and on such short notice. In fact, your Committee believes that the sale of Canadian debt obligations (as distinct from Canadian equities) to non-residents should be encouraged by extending the present exemption from withholding tax provisions instead of restricting it.

When the exemption presently accorded to tax-exempt non-residents was first introduced, the Honourable Mr. W. Gordon, the then Minister of Finance, stated as follows:

> "The purpose of this resolution is, of course, to make it easier or make it more desirable for pension funds in other countries to invest in Canadian bonds. As we all know, we are primarily interested in and thinking about the inflow of capital: Certainly, in totals and magnitudes, we are primarily interested in the sale of Canadian bonds abroad rather than Canadian equities."

In the opinion of your Committee the circumstances above described have not changed and indeed are perhaps more necessary than ever.

YOUR COMMITTEE RECOMMENDS that the exemption accorded to tax-exempt non-resident persons under the present Income Tax Act should be continued in the proposed legislation.

MINING AND PETROLEUM (NON-OPERATORS)

Your Committee stated in its preliminary report of November 4, 1971, that the 3 31/3% automatic depletion which is allowed under present law to an operator of a resource property will be abolished under the proposed legislation at the end of a five year transitional period (i.e. after 1976) and will thereafter be replaced by an earned depletion allowance equal to $1 for every $3 of eligible expenditures incurred on exploration and development after November 7, 1969. The Committee recommended in this connection that the transitional period be extended to the end of 1980 or, alternatively, that taxpayers be allowed to "bank" for earned depletion purposes an amount equal to all eligible expenditures incurred, whether incurred before or after November 7, 1969, but that all depletion previously allowed be deducted in determining the balance of the "bank" available for earned depletion allowance.

As a result of its continuing study of the tax reform measures, your Committee has noted that the proposed legislation would also remove, as of the end of 1976, the 25% automatic depletion that is now allowed to non-operators in respect of income such as royalties which they may derive from resource properties. Royalty income received after 1976 is to be treated in the same manner as productions profits and therefore, will be eligible for the proposed 3 31/3% earned depletion.

Your Committee is of the view that it is equally important that the five year transitional period relating to the withdrawal of the automatic depletion allowance should also be extended to non-operators, at least in respect of income derived from a royalty or other similar interest in a resource property which the taxpayer acquired prior to June 18, 1971, or which he was obligated at that date to acquire. The alternative recommendation which the Committee put forward in its preliminary report with respect to the basis of computing earned depletion for operators of a resource is unlikely to afford much relief to non-operators in respect of interests acquired prior to June 18, 1971, as these taxpayers will not have incurred as extensive exploration and development expenditures as operators. They will therefore not be entitled to a comparable amount of earned depletion if the Committee's alternative recommendation is implemented.

YOUR COMMITTEE RECOMMENDS that the 25% automatic depletion now allowed to non-operators in respect of income derived from a royalty or other similar interest in a resource property be continued for royalties received prior to 1981 in respect of interests which the taxpayer owned at June 18, 1971, or which he was obligated at that date to acquire.

TRANSITIONAL AVERAGING PROVISIONS CONCERNING LUMP SUM PAYMENTS OUT OF PENSION PLANS AND DEFERRED PROFIT SHARING PLANS

Single payments out of a pension plan or deferred profit sharing plan which are received in a taxation year ending after 1973 will be eligible for relatively generous averaging provisions presently afforded by section 36 of the Income Tax Act to the extent of amounts vested up to January 1, 1972. The proposed legislation would restrict the right to

such averaging by providing that once a taxpayer has elected to utilize section 36 averaging in respect of amounts vested up to January 1, 1972, he is precluded from invoking the general and forward averaging provisions of the proposed legislation in the same year in respect of amounts vested after 1971. The amount available for section 36 averaging is thus limited to that portion of the lump sum payment which accrued up to January 1, 1972.

It is apparent that as the benefits under pension and deferred profit sharing plans which vest after 1971 increase in relation to those which vested prior to 1972, the benefit afforded by section 36 averaging will decline in respect of lump sum payments received after 1973, until the point is reached when section 36 averaging will become unattractive.

YOUR COMMITTEE RECOMMENDS that

(a) section 36 averaging should be available in respect of the portion of a lump sum payment received in a taxation year ending after 1973 out of a pension plan or deferred profit sharing plan which the taxpayer would have received pursuant to such a plan if he had withdrawn therefrom on January 1, 1972, and also

(b) the general and forward averaging provisions of the proposed legislation should be available in respect of the portion of such payments which have vested after 1971.

Single payments received out of a pension plan or a deferred profit sharing plan made in a taxation year ending after 1971 and before 1974 are to be entitled to section 36 averaging in their entirety. Your Committee considers such treatment to be equitable.

NON-RESIDENT-OWNED I NVESTMENT CORPORATIONS (N.R.O.'s)

The effect of the provisions of Section 70 of the present Income Tax Act (which relates to non-resident-owned investment corporations) is, in general, to treat non-resident who hold Canadian investments indirectly through the medium of a Canadian holding company in substantially the same manner as they would have been taxed if they had owned such investments directly—provided, of course, that the Canadian holding company qualifies as a non-resident-owned investment corporation (referred to hereinafter as an N.R.O.).

Certain exceptions to this general rule do exist in the present Income Tax Act. For example:

1. A non-resident who owns shares of a corporation which has a degree of Canadian ownership (as defined in Section 139A of the Act) is subject to a 10 per cent Canadian non-resident withholding tax on dividends received from that corporation whereas all dividend income flowing through an N.R.O. attracts a 15 per cent tax under Section 70.
2. Interest payable to non-residents on certain types of Canadian debt obligations (e.g. certain federal and provincial bonds) is now exempt from Canadian non-resident withholding tax but is subject to the 15 per cent N.R.O. tax if paid to an N.R.O.
3. Any investment income which an N.R.O. may derive from non-Canadian sources is subject to Canadian tax under the N.R.O. provisions whereas such income would not be subject to Canadian income tax if paid to the non-resident directly.

However, these and the various other exceptions which exist under the present Income Tax Act have generally been considered relatively insignificant and have not discouraged non-residents from investing in Canada through the medium of an N.R.O.

It is implied on page 58 of the "Summary of 1971 Tax Reform Legislation" that this neutrality in the taxation of non-resident investors, whether they invest directly in Canada or indirectly through an N.R.O., would be continued under the new system; and, in particular, that non-resident shareholders of an N.R.O. would not be subject to Canadian income tax in respect of any capital gains which would not be taxable in Canada if realized personally by a non-resident investor. However, contrary to the statements contained in the Summary, the tax position of a non-resident shareholder of an N.R.O. is not equated with the treatment accorded to non-residents who invest directly. For example:

1. Capital gains realized by an N.R.O. on the disposition of capital property other than "Canadian property" will be subject to Canadian non-resident withholding tax when ultimately distributed by way of dividend to the N.R.O.'s non-resident shareholders. This treatment is clearly anomalous and the proposed legislation should be amended to provide that any net gains realized on the disposition of non-Canadian property should form part of an N.R.O.'s "capital gains dividend account" which may ultimately be distributed to shareholders free from Canadian non-resident withholding tax.
2. Any capital gain realized by a non-resident on the disposition of shares of an N.R.O. (including a gain arising on death) will be subject to Canadian income tax under the proposed legislation. This treatment is inequitable as it could result in double taxation or in the taxation of amounts which should not attract Canadian income tax. For example, part or all of the gain realized by non-resident shareholders could be attributable to gains realized by the N.R.O. on the disposition of taxable Canadian property which had not been distributed to shareholders at the date on which the particular shareholder disposed of his shares of the N.R.O. These gains would have been taxed in the N.R.O.'s hands and would accordingly be available for distribution as a tax-exempt dividend out of the N.R.O.'s "capital gains dividend account". Therefore, the non-resident shareholder should not be subject to Canadian income tax on any portion of the gain realized on the disposition of his shares of the N.R.O. that is attributable to gains previously realized by the N.R.O. on the disposition of taxable Canadian property.

   Similar problems exist where the gain ralized by the non-resident shareholder is attributable to:

   (a) undistributed capital gains which the N.R.O. previously realized on the disposition of any other type of capital property,

   (b) any unrealized appreciation in the value of the N.R.O.'s capital property, and

(c) any accumulated income already taxed in the N.R.O.'s hands.

It follows that, unless appropriate amendments are made to the proposed legislation so as to ensure that N.R.O.'s and their shareholders are treated in a manner consistent with the treatment accorded to non-resident persons who invest directly in Canada, non-resident investors will no longer look upon N.R.O.'s as a suitable investment vehicle and many of these corporations will be wound up. In the result, a considerable amount of the capital now invested in Canada through the medium of N.R.O.'s may be lost. Such a consequence would be most unfortunate having regard to the importance of the role played by N.R.O.'s as a source of capital in Canada and to the contribution which such corporations otherwise make to the Canadian economy.

YOUR COMMITTEE RECOMMENDS that further consideration be given to the provisions of the proposed legislation relating to non-resident-owned investment corporations and appropriate amendments be made to ensure that there is neutrality (similarity) of tax treatment as between non-residents who invest directly in Canada and those who choose to invest through the medium of a non-resident-owned investment corporation, particularly with respect to the treatment of capital gains.

INSURANCE CORPORATIONS

A. Life insurance corporations

There was referred to your Committee a matter which does not arise directly out of the proposed legislation but, rather, represents a problem which exists under the present Income Tax Act and which will continue to exist under the proposed legislation. In view of the fact that this matter will continue to represent a problem under the new legislation, the Committee considers it appropriate and proper to raise this issue at this time.

The problem which has been raised relates to the income tax treatment of dividends received by life insurance corporations in respect of investments in shares of other taxable Canadian corporations and which are acquired out of non-segregated funds. These funds (which, for the sake of simplicity, are hereinafter referred to as the "General Funds" of a life insurance corporation) are invested and held for the benefit of the following groups of persons:

1. tax exempt policyholders, e.g., any person who owns a policy which is registered with the Department of National Revenue as a registered retirement savings plan or which is issued pursuant to a registered pension plan;
2. other polycyholders (excluding those persons owning policies, the reserves for which are invested in "segregated funds"), and
3. the corporation itself or, in the case of corporations other than mutual life insurance corporations, the corporation's shareholders.

In order to determine the amount of the corporation's liability for income tax, it is necessary to allocate the corporation's total investment income amongst these groups in accordance with a formula set out in the Income Tax Act and the Income Tax Regulations.

In examining this matter, your Committee was advised that the total amount of investment income allocable to each group under the provisions of the present law is reasonable in the circumstances and that no objection is taken to the use of a statutory formula for this purpose. The problem lies in the fact that each group is deemed under the allocation formula to share proportionately in each type of investment income earned by the General Funds (including dividends received from taxable Canadian corporations even if such corporations are subsidiaries of the life insurance corporation in question). As a result, part of such dividends are allocated to tax exempt policyholders, thereby reducing the amount of the deduction allowable in computing the corporation's taxable income in respect of dividends received from other taxable Canadian corporations. This also holds true under the proposed legislation.

As is often the case, the assumptions made in devising statutory formulas such as this can be in error. In the case of life insurance corporations, the polycyholders' funds must be invested in such a manner as to ensure that policy guarantees can be made and that such obligations can be met when the policies mature. Therefore, policyholders' funds are generally invested in fixed-interest type securities rather than in shares of other corporations. Most, if not all, of the investments in corporate shares are acquired out of the corporation's (or shareholders') funds and it follows that any allocation of dividend income contrary to this fact will result in the life insurer being effectively denied all of the dividend deductions to which it should properly be entitled. Most certainly, such a problem does not exist with respect to other corporations such as banks, trust companies and other similar financial institutions.

YOUR COMMITTEE RECOMMENDS that corporate dividend income received and arising from investments made by a life insurance corporation out of its non-segregated funds in shares of capital stock of corporations be excluded from the allocation of investment income formula set forth in the proposed legislation.

PRIVATE GENERAL INSURANCE CORPORATIONS

Under the proposed legislation there exists in at least two respects, a distinction between a private and public corporation. That is to say, depending on whether a corporate taxpayer is public or private, the income tax treatment of transactions may differ. These two differences may be summarized as follows:

1. A public corporation may receive dividends from other corporations without payment of tax, while a private corporation receiving a dividend from a non-controlled corporation, is subject to a tax of 33 1/3 per cent. This tax however is refundable to the corporation upon the payment of a further dividend to its shareholders.
2. A public corporation will not be entitled to any preferential tax treatment in respect of its taxable business income, however, a small private business corporation will be entitled to preferential tax treatment on its first $50,000 of taxable business income. This preferential treatment is subject to a number of restrictions. One of

these restrictions is that the after-tax profits of such a corporation must not be applied towards defined "ineligible investments" otherwise the corporation will be subject to a tax for so doing.

At the outset, your Committee wishes to commend the Government for retaining the concept of a preferential tax treatment for the small business corporation. However, as will be noted, your Committee believes that, first, the requirements are unusually restrictive and may defeat the purpose of the relieving provision; and secondly, little account appears to have been taken of other statutory provisions, both Federal as well as Provincial, relating to the business conduct of corporations, which provisions may be in conflict with the restrictions as set forth in the relieving provisions. Private general insurance corporations are but one example of this latter category.

Moreover, the private general insurance corporation may not only be at odds with the proposed legislation in respect of "ineligible investments", because of other legislation that is imposed upon it, but such a corporation may also be unable to comply with the proposed "33 1/3 refundable tax" rule, for the same reason. Both of these matters are hereinafter dealt with.

Your Committee would turn first to the question of the "33 1/3 per cent refund tax" rule and its application to a private corporation. In the case of private general insurance corporations, your Committee has ascertained that the *Canadian and British Insurance Companies Act* (R.S.C., 1970, Chap. 1-15) will severely limit such a corporation from applying this rule in its favour. There are two reasons:

1. Pursuant to Section 105 of this Act, a federal Canadian insurance company is prohibited from declaring and paying dividends in excess of 75 per cent of its average profits for the three preceding years.
2. Further, pursuant to Section 103 of this Act, a federal Canadian insurance company must maintain at all times, assets of 115 per cent in relation to 100 per cent of its liabilities as a solvency test, this test conditioning as well, the payment of dividends. Unfortunately, "refundable tax" would not be treated as an admitted asset for the purpose of rhe solvency test under this Act.

The only comment which your Committee can make with regard to this question is that it represents an almost classic example of income tax theory being contrary to the required practice of the everyday business world.

Similarly,and as already noted, there is danger that an analogous result may also occur in respect of the private general insurance corporation and the tax to be levied where a corporation has made an "ineligible investment". Pursuant to Section 63 of the *Canadian and British Insurance Companies Act* (R.S.C., 1970, Chap. I-15) an insurance company is obliged to invest in securities that would otherwise be considered as "ineligible" for the purpose of the proposed legislation. In this respect the proposed legislation is therefore possibly in conflict with and inconsistent with, another federal statute known as the *Canadian and British Insurance Companies Act* (R.S.C., 1970, Chap. I-15). A similar result will also prevail in respect of the various Provincial acts.

YOUR COMMITTEE RECOMMENDS that special provisions be introduced to alleviate the position of those private corporations which cannot take advantage of "refundable tax" by reason of any conflicting or inconsistent statutory law governing their conduct.

Similarly, that special provisions be introduced to provide that in the case of a private general insurance corporation, compliance with the investment requirements of governing federal or provincial legislation shall not constitute "ineligible investments".

Respectfully submitted,

Salter A. Hayden,

Chairman.

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THIRD SESSION—TWENTY-EIGHTH PARLIAMENT

1970-71

THE SENATE OF CANADA

PROCEEDINGS
OF THE
STANDING SENATE COMMITTEE ON

BANKING, TRADE AND COMMERCE

The Honourable SALTER A. HAYDEN, *Chairman*

No. 51

MONDAY, DECEMBER 13, 1971

Thirteenth Proceedings on:

"Summary of 1971 Tax Reform Legislation"

FINAL REPORT OF THE COMMITTEE

(Witnesses—See Minutes of Proceedings)

THE STANDING SENATE COMMITTEE ON BANKING, TRADE AND COMMERCE

The Honourable Salter A. Hayden, *Chairman*

The Honourable Senators,

Aird	Grosart
Beaubien	Haig
Benidickson	Hayden
Blois	Hays
Burchill	Isnor
Carter	Lang
Choquette	Macnaughton
Connolly (*Ottawa West*)	Molson
Cook	Smith
Croll	Sullivan
Desruisseaux	Walker
Everett	Welch
Gélinas	White
Giguère	Willis—(28)

Ex officio members: Flynn and Martin

(Quorum 7)

Order of Reference

Extract from the Minutes of the Proceedings of the Senate, September 14, 1971:

"With leave of the Senate,

The Honourable Senator Hayden moved, seconded by the Honourable Senator Denis, P.C.:

That the Standing Senate Committee on Banking, Trade and Commerce be authorized to examine and consider the Summary of 1971 Tax Reform Legislation, tabled this day, and any bills based on the Budget Resolutions in advance of the said bills coming before the Senate, and any other matters relating thereto; and

That the Committee have power to engage the services of such counsel, staff and technical advisers as may be necessary for the purpose of the said examination.

After debate, and—

The question being put on the motion, it was—

Resolved in the affirmative."

Robert Fortier,
Clerk of the Senate.

24317—1½

Minutes of Proceedings

Monday, December 13, 1971
(67)

Pursuant to adjournment and notice the Standing Senate Committee on Banking, Trade and Commerce met this day at 2.30 p.m. to further examine and consider:

"Summary of 1971 Tax Reform Legislation".

Present: The Honourable Senators Hayden (*Chairman*), Beaubien, Burchill, Carter, Choquette, Connolly (*Ottawa West*), Cook, Croll, Desruisseaux, Flynn, Gelinas, Giguère, Grosart, Haig, Isnor, Lang, Macnaughton, Martin, Molson, Smith and Welch. (21)

Present, but not of the Committee: The Honourable Senators Argue, Basha, Boucher, Bourget, Duggan, Fergusson, Forsey, Fournier (*de Lanaudière*), Inman, Kinnear, Lafond, Langlois, McGrand, McNamara, O'Leary, Paterson, Phillips, Quart and Rattenbury. (19)

WITNESSES:

Department of Finance:

The Honourable Edgar J. Benson, P.C.,
Minister.

Mr. M. A. Cohen,
Assistant Deputy Minister.

At 4.05 p.m. the witnesses departed and the Committee then proceeded *in camera.*

The Chairman read to the Committee a draft of the Final Report on the above Summary and after discussion and certain revisions being made thereto, it was *Resolved* that the said Report be tabled this night.

At 4.25 p.m. the Committee adjourned to the call of the Chairman.

ATTEST.

Frank A. Jackson,
Clerk of the Committee.

FINAL REPORT OF THE COMMITTEE

The Standing Senate Committee on Banking, Trade and Commerce having completed its examination and consideration of the Summary of 1971 Tax Reform Legislation and bills based on the Budget Resolutions in accordance with its terms of reference of September 14, 1971, now makes its final Report, as follows:

Two earlier reports called Preliminary Report and Preliminary Report No. 2 were tabled in the Senate on November 4, 1971, and November 30, 1971, respectively.

Attached to this Report is a statement prepared by our advisers setting out a list of technical changes required in Bill C-259 to clarify or correct the language of many provisions of the said bill.

Also attached is a list of the persons who made submissions to and appeared before your Committee to present their case for changes in the said Bill to avoid hardship in their operations. There is also set out a list of those who made submissions but did not personally appear.

Earlier today your Committee held its final meeting in connection with the reference made to it by the Senate. At this meeting the Minister of Finance appeared in response to an invitation extended by your Committee. Prior thereto the Chairman, with the approval of the Committee had several interviews with the Minister of Finance to discuss the recommendations made by the Committee in its several reports to the Senate and to obtain, if possible, some indication of the attitude of the Minister in relation thereto.

With the approval of the Committee, a list of top priority items among the recommendations in our two Reports was submitted to the Minister, together with amendments which in the view of our expert advisers and our Committee would incorporate the substance of the top priority recommendations contained in your Committee's Reports. This list is also attached hereto. In speaking by way of explanation to the Senate the Chairman of the Committee will discuss these items indicating how many have already been dealt with and the reaction of the Minister to other of these items expressed in the House of Commons on December 10, 1971, and to your Standing Committee earlier this day.

The Minister of Finance stated in the House of Commons and before our Committee that an amending Bill would be put forward in the next session. In the House of Commons he said:

> "There are a number of areas that the Government is actively studying at this time and I want to give the House some indication of our present thinking—there will undoubtedly be a number of important amendments introduced next year and I think it is only fair that people should be aware of the direction of our planning."

In the Committee the Minister repeated what he said in the House of Commons and dealt in a particular way with the subject matter of the recommendations in your Committee's several Reports. These will be referred to in the course of the explanations given by the Chairman and will appear in the printed report of proceedings this day of the Committee.

Your Committee would direct your attention to the printed reports of its proceedings, particularly numbers 35 and 39. There you will find clear explanations of the principal subjects dealt with in Bill C-259, namely:

(1) Changes in personal Tax	Report P. 35-5 to P. 35-16
(2) Capital gains (with Summary at P. 35-16)	Report P. 35-16 to P. 35-42
(3) Valuation and Tax Free Zone	Report P. 35-39 to 40
(4) Partnerships and Professional Income	Report P. 35-43 to 51
(5) Corporations and Distributions to Shareholders	Report P. 35-51 to 61
(6) Dividend Tax Credit	Report P. 35-52
(7) Small Business	Report P. 35-54
(8) Inter Corporate Dividends	Report P. 35-54
(9) Designated Surplus	Report P. 35-54 to 55
(10) Investment Income of Private Companies	Report P. 35-55
(11) Complexity	Report P. 35-56 and 57
(12) International	Report P. 35-17 to 25
(13) Taxation with Summary	Report P. 39-17
(14) Estates and Death Duties (Summary at P. 39-5) and Trusts	Report P. 39-5 to 16

The above references are to a series of lectures or explanations on the various provisions of Bill C-259 with section references. Your Committee wishes to express its great appreciation to Mr. Arthur R.A. Scace and Mr. Stephen Smith and for their assistance. It should be noted that their services were given without remuneration—expressly so stipulated.

In many of its aspects this Bill C-259 is very beneficial to taxpayers in Canada. The elimination from the tax rolls was estimated in 1970 at approximately 750,000 persons* now subject to tax and the increase in personal exemptions of all the taxpayers, the improved deductions for wage and salary earners, the incentives to small business, the deductibility of interest on money borrowed by one company to buy shares in another company, the ability of a corporation to distribute its 1971 undistributed income on hand on payment of a special 15% tax and thereupon to distribute without further tax its 1971 capital surplus on hand, the elimination of gift taxes and estate taxes, the continuance of dividend tax credit although different in form but beneficial—all these are some of the beneficial features of Bill C-259.

*Source: Senate Report on White Paper Proposals for Tax Reform.

In addition to the above sources of information available to Senators, Senate Hansard of November 24 and December 1, 1971, contain statements in narrative form of the meaning and scope and effect of the various provisions in Bill C-259 referred to in the several reports of your Committee.

Further however, there is the Report of your Committee to the Senate on the White Paper Proposals for Tax Reform, dated September 1970. Therein you will find all the subject matter of the White Paper Proposals dealt with. Many of the headings are carried through to the Summary of 1971 Tax Reform Legislation and Bill C-259.

Your Committee wishes to acknowledge in a particular way the contribution of the Honourable Lazarus Phillips to our study of this Tax Reform Legislation and Bill C-259 as Chief Counsel to the Committee. You will recall he was Vice-Chairman of the Committee in its study of the White Paper Proposals. In the drafting of the Report of the Senate thereon and in the preparation of the several reports of the Committee on its examination and consideration of Bill C-259, his advice and direction were invaluable.

Mr. Alan Irving and Mr. Douglas Ewens were part of our team of legal advisers. We were very fortunate in securing Mr. Irving's services at this time as he had worked with your Committee throughout the study of White Paper Proposals. Mr. Ewen's services were valuable to your Committee in the analysis of the submissions received and as an adviser to the Chairman. Both these men worked on the preparation of our several Reports and in the drafting of amendments. We wish to acknowledge the skill and judgment they brought to bear on the consideration of these matters.

Your Committee retained the services of Mr. Albert Poissant and Mr. Charles B. Mitchell, senior partners in the accounting firm of Thorne, Gunn, Helliwell and Christenson. Their services were invaluable in every phase of the work of your Committee.

As a result of all this work and the information thereby available to Senators, the consideration of this bill should be greatly facilitated. The introduction of an amending bill next year, which the Minister's statement would indicate, will afford the opportunity to the Senate to propose further amendments at that time, the nature and extent of which may be governed by such further and amending provisions as are incorporated in the amending Bill.

Respectfully submitted,

Salter A. Hayden,
Chairman.

APPENDIX "A"

THE STANDING SENATE COMMITTEE ON BANKING, TRADE AND COMMERCE

SUBJECT: Summary of 1971 Tax Reform Legislation

BRIEFS SUBMITTED AND HEARD BY THE COMMITTEE

Date	Proceeding Number	
October 6, 1971	36	The Canadian Chamber of Commerce.
October 13, 1971	40 (A.M.)	Canadian Federation of Agriculture.
October 13, 1971	40 (P.M.)	Canadian Construction Association.
October 14, 1971	41	National Association of Canadian Credit Unions; Co-Operative Union of Canada; Allstate Insurance Company of Canada.
October 20, 1971	42 (A.M.)	Massey-Ferguson; Canadian Jewish Congress.
October 20, 1971	42 (P.M.)	Aluminium Company of Canada Limited.
October 21, 1971	43 (A.M.)	Canadian Bar Association.
October 21, 1971	43 (P.M.)	Simpsons Sears Ltd. and Simpsons Limited; Independent Petroleum Association of Canada.
October 27, 1971	44 (A.M.)	Noranda Mines Limited; Bethlehem Copper Corporation Ltd.; The Canadian Gas Association.
October 27, 1971	44 (P.M.)	ad hoc Committee of Voluntary Agencies.
October 28, 1971	45 (A.M.)	Canadian Petroleum Association; Mining Association of Canada; The Canadian Mutual Funds Association.
October 28, 1971	45 (P.M.)	The Canadian Pulp and Paper Association.
November 3, 1971	46 (A.M.)	Hollinger Mines Limited; The Canadian Life Insurance Association; Dominion Foundries and Steel Limited.
November 3, 1971	46 (P.M.)	The Canadian Institute of Chartered Accountants.
November 3, 1971	8:00 (P.M.)	*In camera Meeting.*
November 10, 1971	49	Institute of Profit Sharing; Insurance Bureau of Canada; The Royal Architectural Institute of Canada; Teachers Insurance and Annuity Association of America; Mining Association of British Columbia; Texaco Canada Limited.

BRIEFS SUBMITTED BUT NOT HEARD BY THE COMMITTEE

Investment Dealers Association of Canada;
Canadian International Power Company Limited;
Trans Canada PipeLine Limited;
Trust Companies Association of Canada;
Vancouver Board of Trade;
John Labatt Limited.

September 29, 1971 and September 30, 1971	Education Sessions on Bill C-259 with Messrs. Scace and Smith.

APPENDIX "B"

Top Priority Recommendations by the STANDING COMMITTEE ON BANKING TRADE AND COMMERCE OF THE SENATE in its consideration of the Summary of 1971 Tax Reform Legislation.

1. Gifts, Bequests and Devises to Charities (1st Senate Report P. 47-10)
2. Employees Profit Sharing Plans (1st Senate Report P. 47-8)
3. Deferred Profit Sharing Plans (1st Senate Report P. 47-8)
4. Passive Income (1st Senate Report P. 47-5)
5. De Minimis Rule (1st Senate Report P. 47-7)
6. Tax-Exempt Non-resident Investors (2nd Senate Report P. 50-7)
7. Non-Resident owned Investment Corporations (2nd Senate Report P. 50-9)
8. Private General Insurance Corporations (2nd Senate Report P. 50-10)
9. Deemed Realization on Ceasing to be a Resident of Canada (1st. Senate Report P. 47-9)

Secondly—An Assurance that further consideration will be given to items recommended in the Senate Reports but not set out in the list of Top Priority Recommendations, more particularly in relation to rollovers (1st Senate Report P. 47-4) Consolidated Returns (1st Senate Report P. 47-15) Mining and Petroleum (1st Senate Report P. 47-10) (2nd Senate Report P. 50-8).

APPENDIX "C"

TAXATION OF INDIVIDUALS

1. Section 6(1)(e) and 15(5)—standby charge for automobile

Section 15(6) provides that the formula set out in Section 6(2) for determining the amount that would be a reasonable standby charge for an automobile that was made available to an employee by his employer shall also apply where a company car has been made available to a shareholder. These subsections fail to consider the situation where one car is made available for several shareholders and/or employees and appropriate amendments should be made.

2. Section 62(3)—Moving expenses (C.I.C.A.)

Subsection (3) of Section 62 provides that the cost of cancelling a lease on one's residence is an allowable moving expense for purposes of determining the amount deductible under Section 62(1) in respect of expenses incurred in moving to a new work location. There is no similar provision for bona fide costs incurred in connection with the assignment of such a lease. As all landlords may not be prepared to cancel a taxpayer's lease and the taxpayer may therefore be forced to sublet (incurring costs in connection therewith), the definition of the term "moving expenses' should be extended by amending paragraph (d) of Section 62(3) to read as follows:

> "(d) the cost to him of cancelling or <u>otherwise disposing</u> of the lease, if any, by virtue of which he was the lessee of his old residence".

3. Section 63—Child care expenses (C.B.A.)

Where a taxpayer is employed by his spouse, the taxpayer's remuneration from such employment is to be included in the spouse's income for tax purposes under the provisions of Section 74(3) of Bill C-259 and excluded from the taxpayer's income for tax purposes. Because of this and because one of the limitations on the amount allowable as a deduction under Section 63 in respect of child care expenses is that the deduction cannot exceed two-thirds of the taxpayer's earned income for the year, a married woman who is employed by her husband may be unable to take advantage of the child care expense deduction. Further, no deduction will be allowed to the husband in these circumstances as he will not comply with the conditions contained in paragraph (b) of Section 63(1) because his wife was not incapacitated or confirmed to prison. Provision should be made to allow the husband a deduction in these circumstances, at least in those cases where it can be established that his wife was a bona fide full-time employee for the period in respect of which the expenses were incurred.

A similar problem arises as a result of the attribution rules in Section 74(4) where a married woman is employed by a partnership of which her husband is a partner.

In addition, where a husband and wife are partners in a business and the Minister of National Revenue exercises his discretionary power under the provisions of Section 74(5) and thereby attributes all of the firm's income to the husband, one of the effects may be to deny any deduction for child care expenses even though the expenses were incurred to enable the taxpayer's wife to devote her time and energies to the partnership business.

APPENDIX "D"

CAPITAL GAINS

1. Section 2(3)(c)—Tax payable by non-resident persons (C.A.B.)

The first specific clause in Bill C-259 which deals with disposition of properties on which a taxable capital gain may be realized by non-residents is Section 2(3)(c). This provision appears to define persons not resident in Canada who can fit within the categories outlined in Division D of the Bill and implies that any person who at any time in the past disposed of "taxable Canadian property" (as defined in Section 115(1)(b)) is subject to the provisions of Division D—even though he may have no taxable income for purposes of Division D and, hence, not be subject to tax in any event. There seems to be no apparent necessity for drawing the net so wide.

2. Section 13(4)—Insurance proceeds and other compensation in respect of the loss or destruction of property (C.I.C.A.)

Section 13(4) of Bill C-259 has the same technical defect as its predecessor in the present Income Tax Act (viz. Section 20(5a)).

The purpose of this provision is to allow taxpayers an additional period of grace in which to expend insurance proceeds or other compensation received in respect of the loss or destruction of depreciable assets without being subject to tax on recaptured capital cost allowance. Ordinarily, where a class of depreciable assets is in credit balance at the end of a taxation year because the taxpayer disposed of assets for an amount in excess of the undepreciated capital cost of property in that class and did not expend a sufficient portion of the proceeds in that same year to bring the class into debit balance at the end of the year by acquiring additional depreciable assets of that class, the amount of the credit balance is included in income as recaptured capital cost allowance. However, where the credit balance arises because of insurance proceeds or other compensation receivable in respect of the loss or destruction of depreciable assets, then, by virtue of Section 13(4) the amount of the credit balance will not be treated as recaptured capital cost allowance to the extent that it is expended by the taxpayer in the immediately following taxation year on the acquisition of depreciable property of the same class as that lost or destroyed.

Where the asset destroyed is a building, the taxpayer will obtain the benefit of this relieving provision to the extent that any credit balance in the relevant class of buildings at the end of the taxation year in which the insurance proceeds or other compensation becomes payable is expended by him in the immediately following taxation year on the acquisition of a building of any class, whether or not it is of the same class as the building that was destroyed. However, because of an anomaly in the Bill (and in the present Act), where a taxpayer chooses to replace a destroyed building by a building of another class and he does so by acquiring such other building in the taxation year in which the proceeds of insurance or other compensation becomes payable (rather than in the immediately following taxation year) he will, upon a technical interpretation, be subject to tax on recapture.

In order to remove this anomaly, it is recommended that paragraph (c) of Section 13(4) be amended to read as follows:

> "(c) the amount shall, to the extent that it has been expended by the taxpayer
>
> (i) in the taxation year immediately following the initial year on acquiring property of the same class,
>
> (ii) in the initial year or in the taxation year immediately following the initial year on acquiring, if the property so lost, destroyed, taken or sold was a building, a building of a prescribed class, or
>
> (iii) ....."

3. Section 44—Deferral of gain on involuntary dispositions (C.C.C.)

Section 44 provides for a deferral of gain on involuntary dispositions of capital property where the gain arises by virtue of the fact that the taxpayer has received (or is entitled to receive)

> (a) proceeds of insurance or other compensation in respect of the loss or destruction of capital property,
>
> (b) compensation for capital property taken under statutory authority, or
>
> (c) the proceeds of sale of capital property which was sold to a person by whom notice of intention to take under statutory authority was given,

and the taxpayer has expended an amount at least equal to the gain before the end of the immediately following taxation year acquiring a replacement for the former property.

It is recommended that these deferral provisions be extended to apply to a gain realized where capital property is unlawfully taken and the taxpayer becomes entitled to receive compensation therefor. This amendment may be accomplished by changing Section 44 to read as follows:

> "Where in a taxation year a taxpayer has received proceeds of disposition described in subparagraph 54(h)(ii), (iii) or (iv) of any property . . ."

4. Section 53(2)(a)(i)—Adjustments to the cost base of capital property (C.C.C.)

Subparagraph (i) of Section 53(2)(a) provides that any amount received by a taxpayer after 1971 as a dividend (other than a taxable dividend or a capital dividend) on the share of the capital stock of a corporation resident in Canada shall be deducted in computing the adjusted cost base to the taxpayer of such share. Any dividend received from a mutual fund corporation that is deemed under Section 131(1) to be a capital gains

dividend should also be excluded, along with taxable dividends and capital dividends, from the amounts that are to be deducted under Section 53(2)(a)(i) in computing the adjusted cost base of shares to the taxpayer. A capital gains dividend is deemed to be a capital gain in the year in which received and is taxed accordingly. Therefore, it should not reduce the adjusted cost base of shares since such an adjustment would result in double taxation.

5. Section 53(2)(m)—Adjustments to cost base of capital property (C.B.A.).

Section 53(2)(m) provides that, in computing the adjusted cost base to a taxpayer of capital property at any time, there shall be deducted

> "such part of the cost to the taxpayer of the property as was deductible (otherwise then by virtue of this subdivision) in computing the taxpayer's income for any taxation year commencing before that time."

It is to be noted that the deduction to be made under this paragraph is based on the deductibility of the amount specified therein regardless of the amount actually deducted in computing income. It is recommended that the paragraph be amended to read as follows:

> "(m) such part of the cost to the taxpayer of the property,
>
> (i) as was deducted (otherwise than by virtue of this subdivision) in computing the taxpayer's income for any taxation year that ended on or before that time, or
>
> (ii) where the adjusted cost base in being computed as of a date other than the end of a taxation year, as was deductible (otherwise than by virtue of this subdivision) in computing the taxpayer's income for the first taxation year ending after that date."

6. Section 54(g)—Principal residence (C.B.A.)

It is recommended that the definition of the term "principal residence" be amended specifically to include,

> (a) a condominium unit (which may not fall within the present definition), and
>
> (b) a dwelling-place located on property which is held under a long term lease rather than owned by the taxpayer

7. Section 74—Income or gains from property transferred to one's spouse

Subsections (1) and (2) of Section 74 provides that a taxpayer must include in his or her income for tax purposes any income and net taxable capital gains (i.e. taxable capital gains less allowable capital losses) which his or her spouse may derive from property transferred to the spouse by the taxpayer (or from property substituted therefor). The purpose of this provision is to prevent a taxpayer from reducing his income for tax purposes by transferring income-producing properties to his spouse.

It has been suggested that Bill C-259 be amended specifically to provide that these attribution rules will not apply in respect of property transferred to a spouse more than one year prior to the date on which the transferor first became a resident of Canada. This suggestion appears to have merit and it is recommended that the following amendment be made:

Section 74(6)

> "Subsections (1) and (2) of this section do not apply in respect of property transferred to a spouse more than one year prior to the date on which the transferor first became resident in Canada or in respect of property substituted for such transferred property."

A similar amendment should be mare to the attribution rules contained in Section 75 which relates to property transferred

> (a) to a person under eighteen years of age, and
>
> (b) to certain inter vivos trusts.

APPENDIX "E"

Corporations and their shareholders

1. Section 83(2)—Capital dividends (C.B.A.)

Section 83(2) provides

> (a) that a private corporation may elect, subject to specified conditions, to treat a dividend payable by it to its shareholders after 1971 as a capital dividend if the amount does not exceed the corporation's capital dividend account immediately before the date on which the dividend becomes payable,
>
> and
>
> (b) that no part of such a dividend shall form part of the recipient shareholder's income.

Under Section 89(1)(b), a corporation's capital dividend account at any particular time is defined to include only amounts attributed to such account in taxation years ending before that time. Accordingly, if a corporation paid a dividend in kind by distributing part of its capital assets and the fair market value of the property distributed exceeded the adjusted cost base of the assets to the corporation, gain would only accrue on payment of the dividend and the corporation could not elect to treat the dividend in kind as a capital dividend out of the one-half non-taxable portion of that capital gain. It is recommended that provision be made to enable a private corporation to treat the one-half non-taxable portion of any

capital gain arising from the payment of a dividend in kind as part of its capital dividend account at the time the dividend became payable.

2. Section 87(1)—Definition of an amalgamation (C.C.C.)

The definition of the word "amalgamation", as defined in Section 87(1) of Bill C-259, is similar to that contained in Section 851 of the present Act in that, in order to qualify for the treatment set out in Section 87 of the Bill (previously Section 85I), it will still be necessary that all of the assets and liabilities of the amalgamating corporations become assets and liabilities of the amalgamated corporation. This requirement often causes corporate taxpayers an undue amount of trouble and expense arranging to settle amounts owing between amalgamating corporations immediately prior to an amalgamation so as to ensure that the amalgamation will in fact be treated as such for income tax purposes.

It is accordingly recommended that paragraphs (a) and (b) of Section 87 be amended to read as follows:

> "(a) all of the property of the predecessor corporations immediately before the merger (other than amounts receivable from, or investments in shares of the capital stock of, any of the other predecessor corporations) becomes property of the new corporation by virtue of the merger,
> (b) all of the liabilites of the predecessor corporations immediately before the merger (other than amounts owing to one predecessor corporation to another predecessor corporation) becomes liabilities of the new corporation by virtue of the merger, and"

3. Section 87(2)(r)) Amalgamated corporation's 1971 capital surplus

4. Section 87(2)(s)) on hand or paid-up capital deficiency (C.C.C.)

Paragraphs (r) of Section 87(2) provides that, in computing the 1971 capital surplus of an amalgamated corporation, any 1971 capital surplus which the amalgamated corporation may itself have on hand shall be increased by the amount, if any, by which

> (a) the aggregate of each predecessor corporation's 1971 capital surplus on hand, if any, immediately before the amalgamation
> exceeds
> (b) the aggregate of each predecessor corporation's paid-up capital deficiency, if any, immediately before the amalgamation.

There is no provision to the effect that, where the amount described in (b) above exceeds the amount described in (a), the excess must be deducted from the amount otherwise determinable in computing the amalgamated corporation's 1971 capital surplus on hand. Unless such a provision is introduced, it may be possible to eliminate a corporation's paid-up capital deficiency by means of an amalgamation without decreasing the 1971 capital surplus of the amalgamated corporation by a like amount. It is therefore recommended that a new paragraph be added to Section 87(2) to the following effect:

> "(r. 1) where the amount described in subparagraph (r)(ii) exceeds the amount described in subparagraph (r)(i), there shall be deducted from the aggregate of the amounts determined under subparagraphs 89(I)(l)(i) to (iv) for the purpose of computing the 1971 capital surplus on hand of the new corporation at any particular time an amount equal to such excess."

A similar problem exists with respect to subparagraph (s) of Section 87(2), relating to the computation of an amalgamated corporation's paid-up capital deficiency.

5. Section 87(2)(aa)—Amalgamated corporation's refundable dividend tax on hand for purposes of determining its cumulative deduction account (C.C.C.)

Section 87(2)(aa) provides for the flow-through to an amalgamated corporation of any refundable dividend tax which each predecessor corporation may have on hand immediately prior to the amalgamation. It is not clear, however, whether the amalgamated corporation will be deemed to have inherited such amounts as of the end of a taxation year immediately preceding its first taxation year, or whether such amounts will not be included in computing its own refundable dividend tax on hand until the end of its first taxation year (following the amalgamation). If the latter interpretation is correct and the amalgamated corporation is, therefore, not entitled to deduct the predecessor corporation's refundable dividend tax on hand for purposes of computing its cumulative deduction account immediately prior to the amalgamation (see Section 87(2)(y)), an amalgamated corporation which qualifies as a Canadian-controlled private corporation (as defined in Section 125(6)(a)) could be deprived of a small business deduction for its first taxation year even though it should, in equity, be entitled to such a deduction.

To ensure that there is no anomaly in this regard, it is recommended that Section 87(2)(aa) be amended to read as follows:

> "(aa) in the case of a new corporation that is a private corporation for the purpose of computing the refundable dividend tax on hand (within the meaning assigned by subsection 129(3)) of the new corporation at the end of a taxation year immediately preceding its first taxation year or at the end of any subsequent taxation year, where a predecessor corporation had refundable dividend tax on hand immediately before the amalgamation the amount thereof shall be added to the aggregate determined under subsection 129(3) from which the new corporation's dividend refunds are to be subtracted;"

6. Section 129(3)(a)—Refundable dividend tax on hand (C.C.C.)

Section 129 provides that a corporation "Canadian investment income" and "foreign investment income" are to be computed separately but it does not provide that a loss obtained from one or other of these "sources" is to be deducted from income derived from the other "source"

in computing the amount described in paragraph (a) of Section 129(3). As a result, the amount of refundable dividend tax which may be credited to a private corporation's refundable dividend tax account in respect of a particular taxation year could be greater than the amount properly creditable thereto.

It is suggested that this anomaly could be eliminated by making the following amendments:

(a) Paragraph (a) of Section 129(3) would be amended to read as follows:

"(a) 25% of the amount, if any, by which its 'total investment income for the year', as defined in paragraph (4)(c), exceeds the amount deductible under paragraph 111(1)(b) from the corporation's income for the year,"

(b) Subsection (h) of Section 129 would be amended by the addition of the following paragraph:

"(c) 'total investment income' of a corporation for a taxation year means the amount, if any, by which the aggregate of

(i) the aggregate of the amounts described in subparagraphs (a)(i) to (iii) in respect of the corporation for the year, and

(ii) the amount that would be determined under subparagraphs (a)(i) to (iii) in respect of the corporation for the year if the references in subparagraphs (a)(i) to (iii) to 'in Canada' were read as references to 'outside Canada',

exceeds the aggregate of

(iii) the aggregate of amounts each of which is a loss of the corporation for the year from a source that is a property or business other than an active business, and

(iv) the aggregate of all amounts deductible under section 113 from the corporations income for the year."

7. Section 129(3)(b)—Refundable dividend tax on hand (C.C.C.)

Any inactive business income from foreign sources will form part of "foreign investment income" for purposes of the refundable dividend tax provisions but any foreign tax credit relating to such income (being a credit allowed under Section 126(2) will not be taken into account in determining whether the limitation contained in Section 129(3)(b) is applicable. Thus, even though no Canadian income tax is payable on inactive business income from foreign sources after deducting the provincial tax abatement and the foreign tax credit, an amount equal to 25% thereof could be credited to the refundable dividend tax account.

8. Section 189(4)(b)—Ineligible investments (C.C.C.)

Further statutory clarification is required to minimize the number of problems which could be encountered in determining the cost of ineligible investments on hand at any time. For example:

1. Where there is a change in the use made of a capital asset, will the use to which it was originally put govern its classification for the purpose of Section 189(4)(b) for all subsequent years?

2. If a capital asset, such as a building, is used in part for active business purposes and in part for rental purposes, will the entire cost be treated as not falling within the ineligible category?

3. If, for example, a Canadian-controlled private corporation owned a minority interest in another company at December 31, 1971, and it acquired a further 100 shares of that company but disposed of the latter before the end of its 1972 year should not be treated as an ineligible investment?

APPENDIX "F"

BUSINESS AND PROPERTY INCOME

1. Section 16—Debt obligations issued at at discount (C.I.C.A.)

Subsections (2) and (3) of Section 16 provide that, where a debt obligation is issued at a discount by a tax-exempt person, a non-resident person not carrying on business in Canada, a government or certain other public bodies, the amount of the discount is, under certain circumstances, to be included in the investor's income for tax purposes. Subsection (2) relates to debt obligations which are issued before June 18, 1971 and subsection (3) deals with debt obligations issued after that date. Neither deals with debt obligations which are issued on June 18, 1971. Subsection (2) should accordingly be amended to apply to debt obligations issued on that date as well as to those issued prior thereto.

2. Section 24—Deduction in respect of eligible capital amounts (goodwill and other "nothings") on ceasing to carry on business (C.C.C.)

The combined effect of subsections (1) and (2) of Section 24 in a situation where an individual ceases to carry on business and the business is thereafter carried on by his spouse or by a corporation controlled by him appears to prevent any deduction under Section 20(1)(b) (relating to the amortization of goodwill and other "nothings") for either the individual, or his spouse or the controlled corporation for the year in which the business is transferred if both the transferor and the transferee have the same fiscal year end or if the fiscal year of the transferor ends at a later date in the year than the transferee's.

In order to remedy this inequity, it is recommended that subsection (2) of Section 24 be amended to read as follows:

Section 24

"(2) Notwithstanding subsection (1), where an individual has ceased to carry on a business and thereafter his spouse, or a corporation controlled directly or indirectly in any manner whatever by him, has carried on the business,

(a) in computing the individual's income for his fiscal period in which he so ceased to carry on the business, the following rules shall apply;

(i) the provisions of subsection (1) shall be read without reference to paragraphs (a) and (b) thereof and as if the reference in paragraph (c) thereof to 'the time he so ceased to carry on the business' were read as a reference to 'the end of the fiscal period in which he so ceased to carry on the business'; and

(ii) the amount allowed as a deduction under paragraph 20 (1)(b) in respect of the business shall not exceed that proportion of the maximum amount otherwise allowable that

(A) the number of days in the period from the commencement of the fiscal period to date on which he ceased to carry on the business,

is of

(B) 365;

(b) in computing the cumulative eligible capital in respect of the business of the spouse or the corporation, as the case may be, at any time after the end of the fiscal period in which the individual so ceased to carry on the business, there shall be included the amount of the individual's cumulative eligible capital in respect thereof at the end of that fiscal period; and

(c) in computing the income of the spouse or the corporation, as the case may be, for the fiscal period in which the spouse or corporation commenced to carry on the business, the amount allowed as a deduction under paragraph 20 (1) (b) in respect of the amount included in the spouse's or corporation's cumulative eligible capital amount under paragraph (b) shall not exceed that proportion of the maximum amount otherwise allowable in respect thereof that

(A) the number of days in the period from the date on which the spouse or corporation commenced to carry on the business to the end of the fiscal period,

if of

(B) 365."

APPENDIX "G"

Certain of the proposals made by the Canadian Bar Association

Subdivision K—Trusts and their Beneficiaries

Sec. 104. Reference to trust or estate.

(1) In this Act, a reference to a trust or estate (in this subdivision referred to as a "trust") shall be read as a reference to the trustee or the executor, administrator, heir or other legal representative having ownership or control of the trust property.

Sec. 104 (2)

(2) Taxed as individual. A trust shall, for the purposes of this Act, and without affecting the liability of the trustee or legal representative for his own income tax, be deemed to be in respect of the trust property an individual; but where there is more than one trust and

(a) substantially all of the property of the various trusts has been received from one person, and

(b) the various trusts are conditioned so that the income thereof accrues or will ultimately accrue to the same beneficiary, or group or class of beneficiaries,

such of the trustees as the Minister may designate shall, for the purposes of this Act, be deemed to be in respect of all the trusts an individual whose property is the property of all the trusts and whose income is the income of all the trusts.

(See also S. 128 (1); S. 248 (1); Regs. Part 11.)

Sec. 104 (3)

(3) Deductions not permitted. No deduction may be made under section 109 or paragraph 110 (1) (d) from the income of a trust.

(See also S. 109 (1); S. 110 (1) (d).)

Sec. 104 (4)

(4) Deemed disposition of property by a trust. Every trust shall, on each of the following days, be deemed to have disposed of each capital property of the trust, other than depreciable property, for proceeds equal to its fair market value on that day, and to have reacquired such property immediately thereafter for an amount equal to

that fair market value; and for the purposes of this Act those days are:

(a) where the trust is a trust created by a taxpayer, whether during his lifetime or by his will, under which

(i) his spouse is entitled to receive all of the income of the trust that arises before the spouse's death, and

(ii) no person except the spouse may, before the spouse's death, receive or otherwise obtain the use of any of the income or capital of the trust, the day on which the spouse dies;

(aa) Where the trust is a classified trust the day prescribed by regulation.

Comment: This amendment is designed to permit the Minister to prescribe alternative rules for trusts such as protective trusts which are worthy of special treatment.

(b) that day that is 21 years after the latest of

(i) January 1, 1972,

(ii) the day on which the trust was created, and

(iii) where applicable, the day referred to in paragraph (a); and

(c) the day that is 21 years after any day that is, by virtue of this subsection, a day on which the trust is deemed to have disposed of each such property.

Sec. 104(5)

(5) Idem. Every trust shall, on each day described in subsection (4), be deemed to have disposed of all depreciable property of a prescribed class of the trust for proceeds equal to,

(a) where the fair market value of that property on that day exceeds the undepreciated capital cost thereof to the trust on that day, the amount of that undepreciated capital cost plus ½ of the amount of the excess, and

(b) in any other case, the fair market value of that property on that day plus ½ of the amount, if any, by which the undepreciated capital cost thereof to the trust on that day exceeds that fair market value,

and to have reacquired each such depreciable property of that class immediately thereafter at a capital cost (in this subsection referred to as the "deemed capital cost") equal to that proportion of the proceeds determined under paragraph (2) or (b), as the case may be, that the amount that was the fair market value of that property on that day is of the aggregate of the amounts that were the fair market values of all properties of that class on that day, except that

(c) where the amount that was the capital cost to the trust of any particular property of that class exceeds the deemed capital cost to the trust of the property, for the purposes of sections 13 and 20 and any regulations made under paragraph 20(1) (a) as they apply in respect of the property at any subsequent time,

(i) the capital cost of the trust of the property shall be deemed to be the amount that was the capital cost to the trust of the property, and

(ii) the excess shall be deemed to have been allowed to the trust in respect of the property under paragraph 20(1)(a) in computing income for taxation years before the reacquisition by the trust of the property, and any other amount allowed to the trust in respect of the property under that paragraph in computing income for those years shall be deemed to be nil, and

(d) subsection 13(2) is not applicable in respect of any such reacquisition.

Sec 104(6)

(6) Deduction in computing income of trust. For the purpose of this Part, there may be deducted in computing the income of a trust for a taxation year such part of the amount that would, but for this subsection (12) and subsection 105(2), be its income for the year as was payable in the year to a beneficiary.

Sec. 104 (7)

(7) Non-resident beneficiary. No deduction may be made under subsection (6) in computing the income for a taxation year of a trust in respect of such part of an amount that would otherwise be its income for the year as was payable in the year to a person who, at the time such part of that amount became so payable, was not resident in Canada, unless at that time, the trust was resident in Canada.

(See also C. 104(6).)

Sec. 104(8)

(8) Limitation on deduction. No deduction may be made under subsection (6) in computing the income for a taxation year of an inter vivos trust that had income for the year from a business carried on by it in Canada, in respect of such part of an amount that would, but for subsections (6) and (12), be its income for the year as was payable in the year to a person who, at the time the amount became so payable, was

(a) a non-resident person;

(b) a non-resident-owned investment corporation; or

(c) a trust resident in Canada other than

(i) a testamentary trust, or

(ii) a trust that throughout the period commencing on April 26, 1965 and ending at the time the amount became so payable, was a beneficiary under the trust by whom the amount became so payable, which latter-mentioned trust was throughout such period carrying on a business in Canada.

(See also S. 2(1); S. 104(6).)

Sec. 104(9)

(9) Idem. No deduction may be made under subsection (6) in computing the income for a taxation year of a trust other than a mutual fund trust, in respect of any amount that is deemed by subsection (21) to be a taxable capital gain for the year of a non-resident person or of a non-resident-owned investment corporation from the desposition of capital property.

Sec. 104(10)

(10) Where property owned for non-residents. Where all the property of a trust is owned by the trustee for the benefit of non-resident persons or their unborn issue, in addition to the amount that may be deducted under subsection (6), there may be deducted in computing the income of the trust for a taxation year for the purposes of this Part, such part of the dividends and interest received by the trust in a year from a non-resident-owned investment corporation as are not deductible under subsection (6) in computing the income of the trust for the year.

(See also S. 106(1)(b).)

(Sec. 104(11)

(11) Dividend received from non-resident-owned investment corporation. Where any part of the dividends received in a taxation year by a trust described in subsection (10) from a non-resident-owned investment corporation are deductible under subsection (10) in computing the income of the trust for the year, for the purposes of Part XIII the trust shall be deemed to have paid to a non-resident person on the last day of the year an amount equal to that part, as income of the non-resident person from the trust.

Sec. 104(12)

(12) Deduction of part of accumulating income included in preferred beneficiary's income. For the purposes of this Part, there may be deducted in computing the income of a trust for a taxation year such part of its accumulating income for the year as was required by subsection (14) to be included in computing the income of a preferred beneficiary.

Sec. 104(13)

(13) Such part of the amount that would be the income of a trust for a taxation year if no deduction were made under subsection (6) or under regulations made under paragraph 20 (1)(a) as was payable in the year to a beneficiary shall be included in computing the income of the person to whom it so became payable whether or not it was paid to him in that year and shall not be included in computing his income for a subsequent year in which it was paid.

Comment: The purpose of this subsection is to make an amount deductible by reason of its allocation to a beneficiary, taxable in the hands of the beneficiary. The words "or (12)" deleted in the version above, are unnecessary in that subsection (14) provides for the inclusion of the amount deducted under (12) in the income of the preferred beneficiary concerned.

Sec. 104(14)

(14) Where a trust and a preferred beneficiary thereunder jointly so elect in respect of a taxation year in prescribed manner and within prescribed time, such part of the accumulating income of the trust for the year as is designated in the election, not exceeding the preferred beneficiary's share therein, shall be included in computing the income of the preferred beneficiary for the year, and shall not be included in computing the income of any tax payer in a subsequent year in which it was paid.

Comment: "The income of any tax payer" is substituted for the words "his income" as the accumulating income may in a subsequent year be paid to someone other than the person so electing.

Sec. 104(15)

(15) Preferred beneficiary's share. The share of a particular preferred beneficiary under a trust in the accumulating income of the trust for a taxation year is,

(a) where the trust is a trust described in paragraph (4)(a) and the taxpayer's spouse referred to therein is alive at the end of the year, an amount equal to,

(i) if the particular preferred beneficiary is the taxpayer's spouse, the trust's accumulating income for the year, and

(ii) in any other case, nil;

(b) in any case not referred to in paragraph (a), where the shares in which the accumulating income of the trust would be payable to the beneficiaries thereunder do not depend upon the exercise by any person of, or the failure by any person to exercise, any discretionary power,

(i) if at the end of the year a particular beneficiary was a member of a class of beneficiaries under the trust each of whom was prospectively entitled, as a member of that class, to share equally in any accumulating income of the trust the portion of the trust's accumulating income in the year that may reasonably be regarded as having been earned for the benefit of beneficiaries of that class divided by the number of beneficiaries (other than registered Canadian charitable organizations) of that class in existence at the end of the year.

Comment: This subsection provides a code to establish the amount in respect of which a particular preferred beneficiary can elect for the purposes of 104(14). The whole context, therefore, is one of income which is not, in fact, being paid but which is prospectively allocable to a particular preferred beneficiary. Consequently, in sub-paragraph (b) and particularly in clause (i) thereof, words suggesting that anyone is "entitled" to share in income should be changed. In addition, the right to elect only arises in connection with accumulating income so

that any reference to income should be modified by the adjective "accumulating".

(ii) in any other case, the portion of the trust's accumulating income for the year that may reasonably be regarded as having been earned for the benefit of the particular preferred beneficiary;

(c) in any case not referred to in paragraph (a) or (b), where each beneficiary under the trust whose share of the accumulating income of the trust depends under the exercise by any person of, or the failure by any person to exercise, any discretionary power, is a preferred beneficiary or a registered Canadian charitable organization, the portion of the trust's accumulating income for the year that may reasonably be regarded as having been earned for the benefit of the particular beneficiary, not exceeding the amount determined in prescribed manner to be his or its discretionary share of the trust's accumulating income for the year; and

(ca) in the case of a classified trust the amount prescribed.

(d) in any case not referred to in paragraph (a), (b), (c) or (ca), nil.

Comment: These amendments are designed to permit the Minister to prescribe alternative rules for trusts such as protective trusts which are worthy of special treatment.

Sec. 104(16)

(16) Capital cost allowance deduction. A beneficiary under a trust may deduct from the amount that would otherwise be his income from the trust by virtue of subsection (13) or (14), as the case may be, such part of the amount that would otherwise be deductible from the income of the trust for the year under regulations made under paragraph 20(1)(a) as the trust may determine; and any amount deductible under this subsection for a taxation year shall be deducted from the amount that the trust would otherwise be able to deduct under those regulations but shall, for the purposes of section 13, be deemed to have been allowed to the trust under those regulations in computing its income for the year.

(See also S. 20(1)(a).)

Sec. 104(17)

(17) Depletion allowance. Where an amount is payable in a taxation year by a trust to a beneficiary under the trust, no part of that amount shall be deemed, for the purpose of subsections (6) and (13), to be payable out of an amount deductible in computing the income of the trust for the year under regulations made under subsection 65(1) except such part thereof as the trust designates as being so payable.

Sec. 104(18)

(18) Trust for infant. Where the income of a trust for a taxation year or any part thereof was not payable in the year but was held in trust for an infant or minor whose right thereto had vested and the only reason that it was not payable in the year was that the beneficiary was an infant or minor, it shall, for the purpose of subsections (6) and (13), be considered to have been payable.

(See also S. 65(1).)

Sec. 104(19)

(19) Portion of taxable dividends deemed to be dividends received by beneficiary. Such portion of

(a) the aggregate of taxable dividends received by a trust in a taxation year on shares of the capital stock of taxable Canadian corporations,

as

(b) may reasonably be considered (having regard to all the circumstances including the terms and conditions of the trust arrangement) to be part of the amount that, by virtue of subsection (13) or (14) or section 105, as the case may be, was included in computing the income for the year of a particular beneficiary under the trust, and

(c) was not designated by the trust in respect of any other beneficiary thereunder,

shall, if so designated by the trust in respect of the particular beneficiary in the return of its income for the year under this Part, be deemed, for the purposes of section 82 and this subsection, to be a taxable dividend received by the particular beneficiary in the year from a taxable Canadian corporation, and not to be a taxable dividend received by the trust in the year from a taxable Canadian corporation.

Sec. 104(20)

(20) Portion of non-taxable dividends not to be included in beneficiary's income. Where an amount has, in a taxation year, become payable by a trust to a particular beneficiary thereunder, such portion thereof as

(a) may reasonably be considered (having regard to all the circumstances including the terms and conditions of the trust arrangement) to have derived from an amount received by the trust in the year as, on account or in lieu of payment of, or in satisfaction of, a dividend on a share of the capital stock of a corporation resident in Canada other than a taxable dividend, and

(b) was not designated by the trust in respect of any other beneficiary thereunder,

shall, if so designated by the trust in respect of the particular beneficiary in its return of income for the year under this Part, not be included in computing the income of the particular beneficiary for the year.

Sec. 104 (21)

(21) Portion of taxable capital gains deemed gain of beneficiary. Such portion of

(a) the amount, if any, by which the aggregate of the taxable capital gains of a trust for a taxation year exceeds the aggregate of

(i) its allowable capital losses for the year, and

(ii) the amount, if any, deductible under paragraph III (1) (b) from its income for the year

as

(b) may reasonably be considered (having regard to all the circumstances including the terms and conditions of the trust arrangement) to be part of the amount that, by virtue of subsection (13) or (14) or section 105, as the case may be, was included in computing the income for the taxation year of a particular beneficiary under the trust, and

(c) was not designated by the trust in respect of any other beneficiary thereunder,

shall, if so designated by the trust in respect of the particular beneficiary in the return of its income for the year under this Part, be deemed, for the purposes of sections 3 and 111, to be a taxable capital gain for the year of the particular beneficiary from the disposition of capital property.

Sec. 104 (22)

(22) Deduction for foreign taxes. For the purpose of section 126, the following rules apply:

(a) such portion of the income of a trust for a taxation year (before making any deduction under subsection (6) or (12)) from sources in a foreign country as

(i) may reasonably be considered (having regard to all the circumstances including the terms and conditions of the trust arrangement) to be part of the income that, by virtue of subsection (13) or (14), as the case may be, was included in computing the income for a taxation year of a particular beneficiary under the trust, and

(ii) was not designated by the trust in respect of any other beneficiary thereunder,

shall, if so designated by the trust in respect of the particular beneficiary in its return of income for the year under this Part, be deemed to be income of the particular beneficiary for the taxation year from sources in that country;

(b) a beneficiary under a trust shall be deemed to have paid as income tax for a taxation year, on the income that he is deemed by paragraph (a) to have for the year from sources in a foreign country, to the government of that country an amount equal to that proportion of the income or profits tax paid by the trust for the year to the government of that country or to the government of a state, province or other political subdivision of that country (except such portion of that tax as was deductible under subsection 20(11) or (12) in computing its income for the year) that

(i) such portion of the amount included in computing his income for the year by virtue of subsection (13) or (14), as the case may be as is deemed by paragraph (a) to be income for the year from sources in that country,

is of

(ii) the income of the trust for the year from sources in that country (before making any deduction under subsection (6) or (12));

(c) the income of a trust from sources in a foreign country for a taxation year shall be deemed to be its actual income therefrom for the year minus the aggregate of the amounts deemed by paragraph (a) to be the income therefrom for the year of all beneficiaries under the trust; and

(d) a trust shall be deemed to have paid as income tax to the government of a foreign country for a taxation year an amount equal to the income or profits tax actually paid by it for the year to the government of that country, or to the government of a state, province or other political subdivision of that country (except such portion of that tax as was deductible under subsection 20 (11) or (12) in computing its income for the year), minus the aggregate of the amounts deemed by paragraph (b) to have been paid to the government of that country for the year by all beneficiaries under the trust.

Sec. 104 (23)

(23) Testamentary trusts. In the case of a testamentary trust, notwithstanding any other provision of this Act the following rules apply:

(a) the taxation year of the trust is the period for which the accounts of the trust have been ordinarily made up and accepted for purposes of assessment under this Act and, in the absence of an established practice, the period adopted by the trust for that purpose (but no such period may exceed 12 months and a change in a usual and accepted period may not be made for the purpose of this Act without the concurrence of the Minister);

(b) when a taxation year is referred to by reference to a calendar year, the reference is to the taxation year or years coinciding with, or ending in, that year;

(c) the income of a person for a taxation year from the trust shall be deemed to be his benefits from or under the trust for the taxation year or years of the trust that ended in the year determined as provided by this section and section 105;

(d) where an individual having income from the trust died after the end of a taxation year of the trust but before end of the calendar year in which that taxation year ended, a separate return of his income from the trust after the end of the trust's taxation year to the time of death shall be filed and tax under this Part shall be paid thereon as if that income were the income of another person; and

(e) in lieu of making the payments required by section 156, the trust shall pay to the Receiver General of Canada within 90 days from the end of each taxation year, the tax for the year as estimated under section 151.

(See also S. 70(2); S. 105(1); S. 150(4); S. 151; S. 156; S. 249(1).)

Sec. 104(24)

(24) "Amount payable". For the purposes of subsections (6), (7), (8), (13) and (20), an amount shall not be considered to be payable in a taxation year unless it was paid in the year to the person to whom it was payable or he was entitled in that year to enforce payment thereof.

(See also S. 104(6); S. (7), (8), (13).)

Sec. 104(25)

(25) An election under subsection (14) hereof on behalf of a preferred beneficiary under a disability can be made by the person designated in the trust to make such election and if none by a parent or guardian of such preferred beneficiary and if none by the trustee.

Comment: Doubt has been expressed as to the ability of persons to elect when otherwise entitled to do so as preferred beneficiaries in respect of accumulating income. It is understood that the Department of Justice has given the opinion to the Department of Finance that no problem arises under the provincial law with these elections. It is further understood that the Department of National Revenue has informed the Department of Finance that no problem arises in connection with the rights to elect which presently exist insofar as persons under a disability are concerned. The Bar Association does not dispute the advice tendered by either Department but in the particular context under discussion here, it does not consider that either advice meets the problem. It is perfectly true that the legal institutions exist in all of the provinces under which a person could become competent to elect on behalf of an infant but the institutions often involve tedious procedures and considerable expense as they are necessarily designed to cope with the awkward problems which arise in connection with the property of a person under a disability. The most common disability with which we will be concerned in connection with the right of election by a preferred beneficiary will be the disability of infancy. Other disabilities such as mental incapacity or absenteeism are uncommon or even exotic and the likelihood of resort to a proper procedure which would result in the appointment of a legal personal representative is great. Very few parents however, bother to become guardians of their own children. It is considered that the Statute should give the right to a parent to make the election. This would not interfere with the provincial right to determine the matter of guardianship but would simply say that a federal election can be made by a particular category of person.

SEC. 105. Benefits under trust, contract, etc.

(1) The value of all benefits (other than a distribution or payment of capital) to a taxpayer during a taxation year from or under a trust, contract, arrangement or power of appointment, irrespective of when made or created shall, subject to subsection (2), be included in computing his income for the year.

(See also S.56(2); S.76(1).)

Sec. 105(2)

(2) Upkeep, etc. Such part of an amount paid by a trust out of income of the trust for the upkeep, maintenance or taxes of or in respect, of property that, under the terms of the trust arrangement, is required to be maintained for the use of a tenant for life or a beneficiary as is reasonable in the circumstances shall be included in computing the income of the tenant for life or other beneficiary from the trust for the taxation year for which it was paid.

(See also S. 12(1)(m); S. 104(6), (13); S. 248(1).)

SEC. 106 Income interest in trust.

(1) Where an amount in respect of a taxpayer's income interest in a trust has been included in computing his income for a taxation year by virtue of subsection 104(13) or subsection (2) of this section, there may be deducted in computing his income for the year the lesser of

(a) the amount so included in computing his income for the year, and

(b) the amount, if any, by which the cost to the taxpayer of the income interest exceeds the aggregate of all amounts in respect of the interest that were deductible by virtue of this subsection in computing his income for previous taxation years.

Sec. 106(2)

(2) Disposition by taxpayer of income interest. Where in a taxation year a taxpayer disposes of an income interest in a trust,

(a) except where subsection (3) is applicable, there shall be included in computing his income for the year the proceeds of the disposition;

(b) any taxable capital gain or allowable capital loss of the taxpayer from the disposition shall be deemed to be nil; and

(c) for greater certainty, the cost to the taxpayer of each property received by him as consideration for the disposition is the fair market value of the property at the time of the disposition.

Sec. 106(3)

(3) Proceeds of disposition of income interest. For greater certainty, where at any time any property of a trust has been distributed by the trust to a taxpayer who was a beneficiary under the trust in satisfaction of all or any part of his income interest in the trust, the trust shall be deemed to have disposed of the property for proceeds of disposition equal to the fair market value of the property at that time.

SEC. 107 Disposition by taxpayer of capital interest.

(1) Where a taxpayer has disposed of a capital interest in a trust,

(a) for the purposes of computing his taxable capital gain, if any, from the disposition of the interest, the adjusted cost base to him thereof immediately before the disposition shall be deemed to be an amount

equal to the greater of the adjusted cost base to him thereof otherwise determined immediately before that time and the cost amount to him of the interest immediately before that time, and

(b) for greater certainty, for the purposes of computing his allowable capital loss, if any, from the disposition of the interest, the adjusted cost base to him thereof immediately before the disposition is the adjusted cost base to him of the interest immediately before that time as determined under this Act without reference to paragraph (a),

except that where the interest was an interest in an inter vivos trust not resident in Canada that was purchased by the taxpayer, paragraph (a) does not apply in respect of the disposition thereof except where subsection (2) is applicable in respect of any distribution of property by the trust to him in satisfaction of all or any part of the interest.

Sec. 107(1)

(1) Where a taxpayer has disposed of a capital interest in a trust,

(a) for the purposes of computing his taxable capital gain, if any, from the disposition of the interest, the adjusted cost base to him thereof immediately before the disposition shall be deemed to be an amount equal to the greater of the adjusted cost base to him thereof otherwise determined immediately before that time and the cost amount to him of the interest immediately before that time, and

(b) for greater certainty, for the purposes of computing his allowable capital loss, if any, from the disposition of the interest, the adjusted cost base to him thereof immediately before the disposition is the adjusted cost base to him of the interest immediately before that time as determined under this Act without reference to paragraph (2),

except that where the interest was an interest in an inter vivos trust not resident in Canada that was purchased by the taxpayer, paragraph (a) does not apply in respect of the disposition thereof except where subsection (2) is applicable in respect of any distribution of property by the trust to him as or on account of all or any part of the interest.

Sec. 107(2)

(2) Where at any time any property of the trust has been distributed by the trust to a taxpayer who was a beneficiary under the trust as or on account of all or any part of his capital interest in the trust.

Comment: Some doubt has been expressed as to whether a capital encroachment for a beneficiary represents the distribution of property by a trust to a beneficiary "in satisfaction of all or any part of his capital interest". The problem seems to be with the word "satisfaction". The doubt has been expressed in print by writers such as David Ward and has been felt privately by those in the Bar Association concerned with the preparation of this brief. It seems to us that the problem can simply be solved by changing the phrase where it appears in both subsections from "in satisfaction of" to "as or on account of".

Sec. 107(3)

(3) Determination of cost of property other than non-depreciable capital property. Where the property referred to in subsection (2) that was distributed by a trust to a taxpayer was property, other than capital property that was not depreciable property, for the purpose of determining the cost to the taxpayer of the property under paragraph (2)(b) (except for the purposes of paragraph (2)(b) as it applies to determine the taxpayer's proceeds of disposition of his capital interest under paragraph (2)(c), the reference in paragraph (2)(b) to "that proportion" shall be read as a reference to "$\frac{1}{2}$ of that proportion".

Sec. 107(4)

(4) Where trust in favour of spouse. Where the trust referred to in subsection (2) was a trust described in paragraph 104(4)(a) and

(a) the property so distributed by the trust was capital property other than depreciable property,

(b) the taxpayer to whom the property was so distributed was a person other than the spouse, and

(c) the spouse was alive at the time the property was so distributed,

notwithstanding paragraphs (2)(a) to (d), the following rules apply:

(d) the trust shall be deemed to have disposed of the property for proceeds equal to its fair market value at that time;

(e) the taxpayer shall be deemed to have acquired the property at a cost equal to that fair market value, and

(f) the taxpayer shall be deemed to have disposed of all or part, as the case may be, of his interest in the trust, for proceeds of disposition equal to that fair market value.

Sec. 107(5)

(5) Distribution to non-resident beneficiary. Where subsection (2) is applicable in respect of the distribution by a trust of any property of the trust to a non-resident taxpayer who was a beneficiary under the trust and the property was not taxable Canadian property or property that would be taxable Canadian property if at no time in the taxation year of the trust in which it was so distributed the trust had been resident in Canada, notwithstanding paragraphs (2)(a) to (c) the provisions of paragraphs (4)(d) to (f) are applicable in respect of the property as if the reference in paragraph (4)(f) to "that fair market value" were read as a reference to "the adjusted cost base to him of the interest or part thereof, as the case may be immediately before the property was so distributed".

SEC. 108. Definitions.

(1) In this subdivision,

Sec. 108(1)(a)

(a) "Accumulating income".—"accumulating income" of a trust for a taxation year means the amount that, but for subsections 104(6) and 104(12) would be its income for the year;

Comment: The words "104(6)" would appear to have been omitted by oversight.

Sec. 108(1)(b)

(b) "Beneficiary".—"beneficiary" under a trust includes a person beneficially interested therein;

Sec. 108(1)(c)

(c) "Capital interest".—"Capital interest" of a tax- or future and whether absolute or contingent) of the taxpayer as a beneficiary under the trust to, or to receive, all or any part of the capital of the trust;

Sec. 108(1)(d)

(d) "Cost amount" of capital interest.—"cost amount" of any capital interest of a taxpayer in any trust at any time means,

(i) in any case where any money or property of the trust has been distributed by the trust to the taxpayer in full satisfaction of the whole of his capital interest (whether on the winding-up of the trust or otherwise), the aggregate of the money so distributed and all amounts each of which is the cost amount to the trust, immediately before the distribution, of each such property so distributed to the taxpayer, and

(ii) in any other case, that proportion of the amount, if any, by which the aggregate of all money of the trust on hand immediately before that time and all amounts each of which is the cost amount to the trust, immediately before that time, of each property of the trust exceeds the aggregate of all amounts each of which is the amount of any debt owing by the trust, or of any other obligation of the trust to pay any amount, that was outstanding immediately before that time, that

(A) the fair market value at that time of the capital interest in the trust, is of

(B) the fair market value at that time of all capital interests in the trust;

Sec. 108(1)(e)

(e) "Income interest".—"income interest" of a taxpayer in a trust means a right (whether immediate or future and whether absolute or contingent) of the taxpayer as a beneficiary under the trust to, or to receive, all or any part of the income of the trust;

Sec. 108(1)(f)

(f) "Inter vivos trust".—"inter vivos trust" means a trust other than a testamentary trust;

Sec. 108(1)(g)

(g) "Preferred beneficiary".—"preferred beneficiary" under any trust means an individual resident in Canada who is a beneficiary under the trust and is

(i) the settlor of the trust,

(ii) the spouse or former spouse of the settlor of the trust, or

(iii) a child, grandchild or great grandchild of the settlor of the trust, or the spouse of any such person;

Sec. 108(1)(h)

(h) "Settlor".—"settlor",

(i) in relation to a testamentary trust, means the individual referred to in paragraph (1), and

(ii) in relation to an inter vivos trust,

(A) if the trust was created by the transfer, assignment or other disposition of property thereto (in this paragraph referred to as property "contributed") by not more than one individual and the fair market value of such of the property of the trust as was contributed by him at the time of the creation of the trust or at any subsequent time exceeds the fair market value of such of the property of the trust as was contributed by any other person or persons at any subsequent time (such fair market values being determined at the time of the making of any such contribution), means that individual, and

(B) if the trust was created by the contribution of property thereto jointly by an individual and his spouse and by no other person and the fair market value of such of the property of the trust as was contributed by them at the time of the creation of the trust or at any subsequent time exceeds the fair market value of such of the property of the trust as was contributed by any other person or persons at any subsequent time (such fair market values being determined at the time of the making of any such contribution), means that individual and his spouse;

Sec. 108(1)(i)

(i) "Testamentary trust".—"testamentary trust" means a trust or estate that arose upon the death of an individual and in consequence of his death, but for greater certainty does not include any such trust that was created by any person other than that individual; and

Sec. 108(1)(j)

(j) "Trust".—"trust" includes an inter vivos trust and a testamentary trust but, in subsections 104(4),

(5), (12), (14) and (15) and sections 105 to 107 does not include

(i) a unit trust, or

(ii) a trust governed by a registered pension fund or plan, an employees profit sharing plan, a registered supplementary unemployment benefit plan, a registered retirement savings plan or a deferred profit sharing plan.

Sec. 108(1)(k)

(k) "Classified trust".—"classified trust" means a trust which has been accepted by the Minister for inclusion in a class prescribed by regulation.

Comment: This amendment is designed to permit the Minister to prescribe alternative rules for trusts such as protective trusts which are worthy of special treatment.

Sec. 108(2)

(2) Meaning of expression "unit trust". For the purposes of this Act, a trust is a unit trust at any particular time if, at that time, it was an inter vivos trust the interest of each beneficiary under which was described by reference to units of the trust, and

(a) the issued units of the trust included

(i) units having conditions attached thereto that included conditions requiring the trust to accept, at the demand of the holder thereof and at prices determined and payable in accordance with the conditions the surrender of the units, or fractions or parts thereof, that are fully paid, or

(ii) units qualified in accordance with prescribed conditions relating to the redemption of the units by the trust,

and the fair market value of such of the units as had conditions attached thereto that included such conditions or as were so qualified, as the case may be, was not less than 95% of the fair market value of all of the issued units of the trust (such fair market values being determined without regard to any voting rights attaching to units of the trust), or

(b) throughout the taxation year in which the particular time occurred it complied with the following conditions:

(i) it was resident in Canada,

(ii) its only under taking was the investing of funds of the trust,

(iii) at least 80% of its property throughout the year consisted of shares, bonds, mortgages, marketable securities, or cash, or of rights to or interests in any rental or royalty computed by reference to the amount or value of production from an oil or gas well, or from a mineral resource, situated in Canada,

(iv) not less than 95% of its income for the year was derived from, or from dispositions of, investments described in subparagraph (iii),

(v) at no time in the year did more than 10% of its property consist of shares, bonds or securities of any one corporation or debtor other than Her Majesty in right of Canada or a province or a Canadian municipality, and

(vi) all holdings of and transactions, if any, in its units accorded with prescribed conditions relating to the number of its unit holders, dispersal of ownership of its units and public trading of its units.

Sec. 108(3)

(3) For the purposes of paragraph 70(6)(b), paragraphs 73(1)(a) and (b), paragraph 104(4)(a) (herein called the "rollover provisions:) and of paragraph 108(1)(e)

(a) the income of a trust is its income computed without reference to the provisions of this Act.

(b) where the trust directs the application of the income of the trust for the benefit of the spouse, the spouse, shall for the purposes of this Act, be deemed to be entitled to receive the income so directed to be applied.

(c) the fact that debts of the taxpayer or taxes exigible by reason of his death or administration expenses of the trust are payable out of the property of the trust shall not for that reason only prevent the application of the rollover provisions.

Comment: The Bar Association feels concern on two points in connection with the exclusive trust for a spouse. In the first place if money is spent for the benefit of a spouse rather than being paid to a spouse it ought to be treated in the same way. There is some concern that it would not be so treated and that the possibility of spending income for the benefit of a spouse would disqualify the trust. Similarly there is concern that if the trust must bear taxes payable to a province or to a municipality or debts of the deceased, that the trust would be disqualified. A section such as section 7(4) of the Estate Tax Act together with its interpretation is required and the Association is satisfied with the language which is proposed for this purpose.

Additional Sections to be amended

110(2)(a) Where an individual was, during the taxation year a member of a religious order and had, as such, taken a vow of perpetual poverty, he may, in lieu of the deduction permitted by paragraph 1(a), deduct from his income for the year an amount equal to his earned income for the year as defined by section 63 if, of his income, that amount has been paid to the order.

(b) Where a taxpayer has died in a taxation year in applying paragraph (1)(a) for the purpose of computing his taxable income for that year that paragraph shall be read without reference to the words "not exceeding 20%".

Comment: The Bill now limits charitable deductions to an amount equal to 20% of the taxable income in the terminal period. It is, in fact, not uncommon for a taxpayer to give all of his property, or all of his property subject to a life interest in favour of his spouse (and perhaps other dependants) to charity. The effect of the present provisions of the Bill would be to make some part of the charitable gift an amount in excess of the 20% limit and hence taxable. It is, therefore, suggested that in the year of death a 100% deduction should be available for charity. It is to be noted that this is not a novel suggestion. A 100% deduction is now available under the Estate Tax Act when a gift is being made to that well-known charity, the Crown. The Bar Association requests that the 100% deduction be generally applicable to all charitable gifts in the year of death.

54(e) "listed personal property" of a taxpayer means his personal-use property that is all or any portion of, or any interest in or right to, any

(i) print, etching, drawing, painting, sculpture, or other similar work of art,

(ii) jewellery,

(iii) rare folio, rare manuscript, or rare book,

(iv) stamp,

(v) coin,

(vi) antique furniture,

(vii) gold, silver, antique flatware or plate,

(viii) antique or rare china.

Comment: In the Minister's explanation of the Bill, the categories of listed personal property were explained as being examples of items which did not normally depreciate through use and would hence normally attract a gain on disposition. However, the technique in the Statute understandably has been to define a specific list for the purposes of listed personal property and the list contains omissions. Ordinary furniture depreciates through use but genuine antiques do not. The difficulty of establishing what is an antique can be resolved and is resolved for the purposes of the customs regulations. The present list includes coins, jewellery and works of art. These categories do not embrace gold or sterling silver tableware. Such articles do not depreciate through use and as they acquire patina of age they also acquire value. Similar articles made of more base metals such as pewter or copper or brass while normally belonging to the category of things which depreciate through use, may, if they are very old, move into the category of antiques and like the antique furniture, begin to appreciate by the passage of time whether or not used. Finally, antique or rare china describes two classes of pottery which do not depreciate through use. Every member of the Senate must be acquainted with particular items which, whether or not used, are more valuable now than when they were purchased. The characteristic of antiquity is here the more important qualification. Rare china which is not also old china will not commonly arise. However, certain of the most artistic makers of fine china are in the habit of issuing special limited editions which immediately commence growing in value.

40(2)(k) For the purposes of paragraph 69(1)(b) and subsections 70(5) and 104(4) there may be deducted from the proceeds of disposition otherwise determined of property (other than depreciable property) an amount equal to the reasonable expenses which would have been incurred by the taxpayer in the disposition of the property deemed to be disposed of by him had he actually disposed of that property.

Comment: Commission on the sale of property and other similar expenses are deductible in computing the capital gain to be paid by the taxpayer. It seems only fair that allowance be made for this type of expense which the property is deemed to be realized rather than actually realized.

122(2) Subsecion (1) is not applicable for a taxation year of an inter vivos trust other than a mutual fund trust or a classified trust if the trust

(a) was established before June 18, 1971

(b) was resident in Canada on June 18, 1971 and without interruption thereafter until the end of the year,

(c) did not carry on any active business in the year,

(d) has not received any property by way of gift after Royal Assent has been given to this Act,

(e) has not after Royal Assent has been given to this Act insured

(i) any debt

(ii) any other obligation to pay an amount to, or guaranteed by, any person with whom any beneficiary of the trust was not dealing at arms length.

Comment: Many trusts have been unintentionally put into the minimum 50% taxation category by additional gifts or borrowings since June 18, 1971. The authors of the Bill have their sights set upon sophisticated taxpayers indulging in constant tax planning. For such persons the rule of June 18 is undoubtedly fair. Those people all heard about this particular provision over the weekend of June 19 and 20. However, small trusts, often for children, are legion, not attended by formality and not always or even most largely, created by sophisticated people. The mother who banks her family allowance cheques in the name of the children, the grandfather who buys a $50 Canada Savings Bond each year for his grandchildren, are examples. Those trusts should be saved by the creation of a new category of infants' trusts but pending such salvation, it would be more equitable to give a greater amount of time to taxpayers to become acquainted with the rule. At the time of the last amendment Section 13(4) of the Estate Tax Amendment Act, 1968-1969 allowed taxpayers to engage in post mortem variations of wills in order to qualify within the definition of the spouse-exempt trust created by section 7(1)(b) of the Estate Tax Act. Such variation was permitted until August 1, 1969 and the purpose was to allow a sufficient period of time to elapse to catch the cases where persons would not have had a reasonable opportunity to alter wills. The same principle is applicable here.

Comment for Classified Trust. At present the Bill recognizes the following categories of trusts:

Unit Trusts

Testamentary Trusts

(a) exclusive spouse trust

(b) other trust

Inter Vivos Trusts

(a) exclusive spouse trust

(b) other trust created before June 18, 1971 and not contaminated by gifts or borrowing since that time

(c) other inter vivos trusts

The effect of the Bill is to treat generously spouse trusts, testamentary trusts and pre-June 18 trusts but all living trusts created after June 18 are treated punitively as if there never were any reason for employing them except tax avoidance. The Bar Association finds it tiresome to have to reiterate over and over again in argument with tax policy officials at the federal level that there are other uses and reasons for trusts than tax avoidance and that these uses are of everyday application. In the 1968-1969 amendments it was recognized that an infant's trust was a legitimate device. There was also recognition in the estate tax context of a trust for an incapable person. It is suggested that the revenue has nothing to fear from the creation of further types of trusts to be treated on a less punitive basis both as to the time when the trust is deemed to dispose of its capital assets and as to the applicable rate of tax on accumulating income. The Bar Association would suggest that the two categories most urgently required are the category of a protective trust and the category of infant's trust. In each case conditions could be established to protect the revenue while at the same time leaving criteria which could be met in ordinary cases. The Bar Association considers that flexibility could be obtained in this connection by building in the possibility of prescribing categories of trusts by regulation and in this way making provision in the future not only for the two types mentioned, but also for other types. The required amendment is extremely simple.

The Standing Senate Committee on Banking, Trade and Commerce

Evidence

Ottawa, Monday, December 13, 1971

The Standing Senate Committee on Banking, Trade and Commerce met this day at 2.30 p.m. to give further consideration to the Summary of 1971 Tax Reform Legislation, and any bills based on the Budget Resolutions in advance of the said bills coming before the Senate, and any other matters relating thereto.

Senator Salter A. Hayden (*Chairman*) in the Chair.

The Chairman: Honourable senators, I call the meeting to order. We have the Minister of Finance here today. The main purpose is to deal with any questions which we may wish to ask him, but I think he has a short statement to make first.

I wish to inform you that the copies of this bulky volume which you have are all that are available to us at this time. If honourable senators wish to keep them for reference during the next few days they should take them with them to their offices, because they cannot be replaced.

Honourable Edgar John Benson, Minister of Finance: Gentlemen, firstly, in appearing here today at the request of Senator Hayden it is not my intention to make a general or lengthy statement. I will appear again before the Senate when the bill is officially in your hands next week, if you so desire. At that time, if you so wish, I will make a longer statement.

Now I would like to indicate the appreciation of the Government and, indeed, of myself for the work done from the beginning by this Senate committee on the tax legislation. Relating the reports produced by the committee with respect to the White Paper on Taxation to the budget of June 18, if I recall correctly, some 44 recommendations of the Senate committee which were adopted in Bill C-259. Since debate on the bill commenced in the House of Commons this fall, the Senate has been considering the subject matter and has so far made two reports. We have studied these very carefully, and have made certain amendments in the House of Commons. I think of such amendments as those with respect to credit unions and co-operatives, as well as a great many other technical amendments, as being in conformity with the suggestions of this committee. I would like to repeat that your recommendations have been very helpful and will be the subject of our continuing study. An amending bill will be introduced next spring as, indeed, there always is an amending bill to a taxation statute. There has been one every year since 1918, when income tax was first imposed in Canada.

However, there are specific areas in this bill which are troublesome to ourselves, to you and to the business community, and they are areas which cannot be ignored. Rather, we have undertaken to continue studying them and, indeed, we will move forward and produce some amendments in the spring.

I indicated some of these amendments in the House of Commons last week, but they will not be in your records. I will inform you briefly of the areas we are considering. First of all, there is the matter of gifts in kind to charities, to which a gains tax would apply. A great deal of difficulty was experienced in this regard in the United States, as you know, because of loopholes which developed through this being allowed. Very lengthy legislation was passed there in 1969 in an attempt to close those loopholes. We hope, through further study, to be able to introduce provisions which will allow gifts in kind without involving a similar mass of legislation to that which exists in the United States. There is also an amendment with regard to profit-sharing plans.

Senator Connolly: Before you leave that subject, I read your comment about two ways in which this could be done. It mentioned the tax-paid aspect of it. In other words, if the gift were made in cash, presumably any capital gain which might have been realized would have been accounted for in the donor's tax return. The specific problem we had here, as you are well aware, was raised by the Jewish Congress, regarding gifts in kind, particularly real estate, given to camps, where capital gains were deemed to have been made at the time of the gift and therefore the tax was payable by the donor in addition to giving the property.

Hon. Mr. Benson: This is true. If he sold property and gave cash, he would have to pay tax on it. If one is making a gift in kind, the gains tax that might have accrued would have to be paid by the donor. In the result, the charity might receive a lesser amount by way of gift.

The Chairman: The real difficulty there is that the gift is valued at the date that it is made in kind. If the man lived for another 10 years and died and there was a disposition, it would then go back and the gain determined would be the difference between the value at the time he gave it and the disposition. This would be particularly harmful in the case of wills. The man who may thing that he is leaving an estate in liquid form might find out that he has made a gift in kind to a registered charitable organization, and some 10 years later, when there has been a gain realized, this comes back to his estate, and he is not there to manipulate the affairs of this estate at that time.

Hon. Mr. Benson: And when he is dead he does not get the charitable donation deduction. That is the problem that we are studying at the present time. It is not an easy problem. If one could say, "Well, distinguish charities, pick out legitimate charities and say all these are legitimate and all those are not legitimate"—and here one could think of

personal charitable trusts—it would be relatively easy to do. The United States, in trying to do this in 1969, got into a great volume of legislation, and we are trying to find an easier way of doing it.

It is not a problem that may come up next year, but somebody may want to do something in his will next year and we feel that we should treat it as a matter of urgency, because it would stop these gifts in kind on death for a period of time. As a matter of fact, we are in favour of charities receiving gifts in this way and are determined that we will find a method of solving the problem.

In the case of employees' profit-sharing plans, which was another point raised here, as distinguished from deferred profit-sharing plans, there is an amendment which we think should be made in order to recognize that the funds which go into such a plan are tax paid and therefore the recipient of a distribution in print should be faced with a deemed realization of the accrued capital gain. We think this can be done. Here again, my advisers tell me that one can get into all kinds of problems, but we are looking into this.

With regard to the deferred profit-sharing plan area, in the legislation we mentioned two things that we can do. I indicated that we would give section 36 treatment to all amounts credited to a person up to the end of this year. This will in no way affect his right to average in the future the amount which may be put into the plan in the future. He will have both of these benefits. That was our intention, but the legislation is not worded that way. I made a promise to do this a while ago, but the first time I realized that I had not fulfilled my promise was when I read the Senate committee report, and the day after when I saw people representing a deferred profit-sharing plan.

There are a great many areas which I have mentioned. There is the matter of passive income and the treatment of foreign income of corporations. As a Government, we are in favour of multinational Canadian corporations, and we believe they should have fair tax treatment. The aim of some of the foreign income sections has been to prevent the avoidance of Canadian income tax through schemes whereby funds are funneled into tax havens. Unfortunately, in stopping this we find that it may affect a great many foreign corporations and Canadian corporations operating abroad. We are looking at the passive income section. It has been misinterpreted to some degree by the public, in that the definition is fairly broad and it allows such things as interest on receivables and normal amounts that a corporation would receive in their business operations as being non-passive income.

Senator Connolly: Income from active business.

The Chairman: The one thing that bothers me about that, Mr. Minister, is that there is a good deal of jurisprudence which has been developed over the years as to what is income from a business and what is income from property; and, unfortunately, we have many cases which say that rental income is income from property.

If we are going to have conflicts, we feel there should be some clarification so as to be sure that active business should not exclude income from property. As to the ramifications of that, I cannot tell you at the moment.

Hon. Mr. Benson: This is what we have been looking at, but our view was that we should make the definition as broad as possible so that the normal business operations would not be subject to the passive income rules.

When we started looking at this we felt that if we further confined it it would make the jurisprudence more confining than we want it to be. We are trying to determine how we can best do this.

The Chairman: If I may just give you an illustration, Mr. Minister. Routine maintenance and care of rental properties has been held not to constitute the carrying on of an active business. Rental income from apartment buildings and shopping centres, where services are provided by the owners, including heat, and so forth, has also been held not to be income from an active business. A private company operating an apartment building is held to be a personal corporation because it was not carrying on an active business. This is what you have to face in trying to interpret income from an active business operation.

I feel there has to be some broadening or clarification, but I agree too that if you push in a balloon in one spot it has to come out somewhere else. The point is you have to put all those things together.

Hon. Mr. Benson: That is true. It was not our concept of what we are trying to do in the act. The definition of passive income relates only to income earned abroad. We conceived that normal business income of firms operating outside the country, whether from rentals or various sources, would not be classified as passive income, and we are, as I have indicated, having a look at this section to try to find something that will make clear out intention.

The Chairman: In any event, you know the problem and the scope of our amendment, and you are looking at it.

Hon. Mr. Benson: That is right. This also applies to the *de minimus* rule with regard to passive income.

We have been looking at other areas as well, and I am just indicating the kind of things we have to think about in the interim, between now and when we introduce an amending bill.

There is also the matter of people coming to Canada to work for a few years who upon departure might be deemed to have realized capital gains, even though they never intended to become residents of Canada. We find this arising in some of our multinational corporations. For example, you could have a resident of the United States working in Britain, who is asked to come to Canada to manage the operation here for four or five years, until he retires, and who, at the end of that time, returns to the United States. That person could get stuck with capital gains in Canada. We are having a look at this to see if something can be done about it.

Senator Isnor: Why should he not be taxed in the same way as a Canadian?

Hon. Mr. Benson: I can tell you that such situations do arise. For example, supposing a resident of the United States living in Britain had bought shares of stock at $20 and that stock went up to $40. If his company wanted him to come and work in Canada, he would say: "Well, the

stock market is such now that the stock which was up to $40 is now down to $20, and if I go to Canada for a period of four years and then leave the country, I will have to pay tax on the amount of money involved in my stock going back up to where it was before, so I will not go; it is not worth my while going". We feel we should be in a position to encourage people in our multinational corporations to move from one country to another without an undue penalty.

The real purpose of the realization on leaving a country is to stop people who have been living in Canada for quite a long time accumulating wealth and then leaving the country in order to avoid a gains tax. That is what we are trying to stop, and we want to stop that without putting undue penalties on somebody who might come to work in Canada as compared to the situation if he went to work in the United States.

Senator Lang: Why have any penalty, Mr. Minister?

Hon. Mr. Benson: He might have some tax to pay. We will try and have a look at it.

Senator Molson: The principle might be that he should have to pay tax only once somewhere.

Hon. Mr. Benson: That is right. Of course, if we worked out our tax treaties this would presumably be the case.

I think that indicates some of the problems. We have gone over, in detail, a great many of the problems you have raised in your reports to date, including the one with respect to the pulp and paper industry. Indeed, we met with the pulp and paper industry last week as a Cabinet, and are taking a look at the taxation position vis-à-vis other countries. We fully recognize that they have serious problems—all of which do not arise out of taxation, incidentally.

Senator Connolly: What do you think of the concept of earned depreciation for the pulp and paper industry?

Hon. Mr. Benson: I would not commit myself to this. If I were going to do it for the pulp and paper industry, I think one could bring forward arguments that we should extend this to other manufacturing industries. We have done it for mines and oil. It might be great to do it, but one has to consider how much it would cost. If you move in the case of the pulp and paper industry it might not involve a move in other cases, but this has to be looked at very carefully.

Senator Connolly: Perhaps our staff and our chairman came up with a lable for the concept, because it is a resource industry in a large measure, and in a sense a wasting resource, although it is replaceable. What we were trying to provide there was something that would help them over the long run, hopefully that would not make too much of an impact on the loss of revenue.

Hon. Mr. Benson: We are looking at this and are working with the pulp and paper industry. Incidentally, a couple of provinces are also involved in looking at the tax position of the pulp and paper industry in Canada vis-à-vis other countries. We have been in consultation with the provinces and the industry in trying to work out what the taxes are in the various jurisdictions. You can pick out situations where in the United States the tax might appear to be very much higher than it is in Canada, but then you have to start looking at the implications and what other things are involved.

Senator Connolly: That applies even between provinces with the logging tax. We had a long discussion on that here with some industry people, and some of our own people who were very knowledgeable because they had pulp and paper industries in their own areas.

The Chairman: I think the minister has noticed that. We thought that the logging tax credit should not be limited only to the provinces and people subject to what is specifically called the logging tax. We thought that if the tax, no matter what its name, applies the same as a logging tax, then for tax credit purposes it should be included, and this was one of the recommendations we made.

Hon. Mr. Benson: We have looked at your recommendations, and I assure you they will be given full consideration as we continue studying this problem.

The Chairman: On the good side, I can tell you that I had a letter from the Pulp and Paper Association after their visit and interview with a number of ministers. They were very appreciative of the work we had done, and also of the reception they had from you and other ministers.

There is another item, if I might mention items, Mr. Minister, that we included. It is mentioned in our two reports. We included it in the list we established as being a top priority list. It is the so-called tax exempt non-resident investors. Perhaps I can identify it more closely by saying that we relate it to the Teachers' Insurance and Annuity Association. They had a problem of having a benefit taken away from them, which the Minister of Finance in 1963 granted them, that is, exemption from withholding tax.

Hon. Mr. Benson: Yes. They made representations to us also. We can fix them up on a temporary basis, and we think that this may be the kind of thing that perhaps should be not subject to a tax. This is our general opinion on that point. What we have considered doing is giving them a two-year exemption and in this period looking at hardship cases, where there may be others as well as this, and developing some rules with respect to hardship cases, that do not go contrary to the basic law, but where we recognize special circumstances in these special cases.

The Chairman: Except that the basic law, as we thought of it, was to cover non-resident investment in debt securities, rather than equity. This seems to be quite a topic of national interest nowadays and it certainly was so in 1963 when Mr. Gordon brought this change in. This company, the Teachers', were investing only in debt securities in Canada, and they were tax-exempt organization in the United States. Obviously, on any withholding tax they paid in Canada, they would have no place to write it off; they would have to eat it. They have entered into transactions in Canada since 1963. I know one of them was the financing of the fuel pipe installations at Malton. They made it on the basis of their exemption from withholding tax.

Hon. Mr. Benson: We think, on our problem vis-à-vis the United States, we would be able to take care of that

without too much difficulty, if they are in the United States. But there are some investments in Canada, in some other areas, where we are not sure of the legitimacy of the tax exempt organization, or whether the money is really being funnelled through a tax exempt organization in order to be invested in Canada and avoid the 15 per cent withholding tax. We are looking at these and, as I said, it is our aim to have the law applied fairly. Here we have a sympathy certainly for the one you particularly raised and, as a matter of fact, we are building in an exemption in order that we may build a general rule to take care of the situation, and yet not allow the kind of flow through to individuals from pseudo charitable or non-taxable organizations in other countries.

Senator Connolly: Are you telling us that the tax deal with other countries may have to be revised on this point?

Hon. Mr. Benson: No. I think we may be able to do it within the law, but we just do not know of all the cases. We have asked people to come to us, and over a period of time they will come to us, then we will know what the situation is. I think that we can revise our own law on this point; we need not necessarily depend on our treaties.

Senator Lang: In a case where an occasional pseudo charitable organization might apply, could you not just withhold the certificate?

Hon. Mr. Benson: But you cannot find them. Under the provision in the law, if they are exempt from tax in the country of origin, they are tax exempt here. That is all right with the United States, where the basis of determination on what is charitable and exempt is very similar to what we have here in Canada. But if you go to other countries, you might find that something which is taxable in Canada would be tax exempt there and yet they could claim a certificate exempting them.

Senator Beaubien: It seems to me that about 99 per cent of the cases would be in the United States. It does not seem to make much sense to penalize those in the United States because there might be a few outsiders.

Hon. Mr. Benson: There are very few exempt in the United States that are not exempt in Canada and the law is only changing for those that are exempt in the United States and not exempt in Canada.

Senator Beaubien: What about Teachers'?

Hon. Mr. Benson: They would not be exempt in Canada.

Senator Beaubien: They would be?

Hon. Mr. Benson: No, they would not be. That is their problem. They are one of the few that would be exempt in the United States but would not be exempt in Canada, and there are not many of those.

The Chairman: Well, Senator Beaubien, I did not understand the minister to say that he was not proposing to grant any relief in this case. All I understood him to say was that this would be a deserving case. Certainly that is my view. It fits in with the political philosophy and everything else, that is, of getting non-residents to invest in debt securities in Canada instead of in equities. I do not want to be taken by that statement to be subscribing to all that has been said recently about the acquisition of equities by non-residents. All the minister is saying is that they have to have a good look at it in all its ramifications, but I did not understand him to say that this was not a deserving case.

Hon. Mr. Benson: Oh, no, this is a hardship case.

Senator Beaubien: What is the difference?

Hon. Mr. Benson: The difference is that the tax law in the United States would make Teachers' exempt, whereas, if they were residents in Canada they would not be exempt. It is the difference in the tax law. Therefore, under the new provision they are not exempt from the withholding tax. We think it may be a hardship case. What you might do is to change your Canadian law and make them tax exempt here, but that would have a lot of other ramifications, because we would be getting into the whole insurance business and the taxation of insurance companies. So we have to take a look at the hardship cases. There are not that many of them, and we have to try to find a way to solve that problem. As an interim measure we have solved it for Teachers' for a two-year period until we get to the permanent solution.

Senator Lang: Could the issue of this certificate not be made discretionary in your hands, Mr. Minister? Would that not be the answer to the problem?

Hon. Mr. Benson: Perhaps it is the answer in the long run, but besides all the other things I have been asked to do in this tax bill I have been asked not to have my discretion extended.

Senator Lang: We would be quite pleased to extend it in this matter.

The Chairman: Would you like our approval of that, Mr. Minister?

Hon. Mr. Benson: Well, you can so recommend, if you like.

Senator Connolly: We have taken a dim view of too many discretions in the past. I think the policy has been to avoid them as much as possible.

Senator Molson: Mr. Chairman, may I ask the minister about the question of consolidated returns?

Hon. Mr. Benson: We have not got that far at this point.

Senator Molson: May I ask if you are working at it?

Hon. Mr. Benson: We are working at it. It took a lot of time to develop this tax legislation to where it was, and we did not know until the very end where we were going to end up in a great many matters. Integration was one of them. Finally, we accepted your recommendation from the Senate committee and did not have integration, but amended the dividend tax credit.

Now, when you get to this stage, then you can start taking a look at what would happen if you had consolidated returns with various kinds of companies in it and so on. We are presently looking at this. I cannot promise we are going to have it solved in a few months or anything, but we are looking at the problem.

The Chairman: Well, you would have to study the effect on tax revenues.

Hon. Mr. Benson: That is right.

Senator Connolly: I take it that your advisers will review the evidence we had before us here by various multinational, Canadian-based corporations, where they do make a very good case for hardship; you know, where they have various corporate units in different places and where the losses in one are not offset against the gains in others.

The Chairman: Mr. Minister, one of the recommendations we made had to do with non-resident-owned investment corporations, and we felt that what you said in the summary was exactly what we thought should happen; that is, because you are in corporate form instead of individual form your position should be equative. But the legislation does not do that.

Hon. Mr. Benson: I will let Mr. Cohen answer that.

Mr. M. A. Cohen (Assistant Deputy Minister, Department of Finance): Mr. Chairman, if you take into account the amendments that were tabled by the Government you get a situation where, by and large—I cannot say 100 per cent, but by and large—the treatment of a foreigner investing in Canada, whether directly or indirectly through an NRO, is to a large extent the same. Where you have significant differences is where you have an individual from one country investing in a third country using Canada as an intermediary and using an NRO for that purpose. There there are differences. But for an individual investing into Canada, by and large the treatment is the same, given the amendments that were put in to permit the flow-through of the capital gains. I think that was the main criticism made to us by people who were involved in NROs and the Government responded to that criticism.

The Chairman: Well, if you read the submissions that we received, these people who were affected were substantial people carrying on substantial operations and representing very substantial investment of non-resident funds in Canada, and they were getting unequal treatment as against what an individual would get. And they referred to the capital gains situation.

Hon. Mr. Benson: That is taken care of in one of our amendments. It was taken care of in the house recently. Their main complaint in dealing with us was about the gains situation and we have taken care of that.

Senator Connolly: Perhaps we can have that section later.

The Chairman: Mr. Minister, the next one deals with the private and general insurance corporations who appeared before us, and the main burden of their complaint was that a great many of these would qualify under the small business concept. Their main difficulty was that on investments they are governed by the Canadian and British Insurance Companies Act, but when they come to try to qualify under the small business corporation provisions there is a definition of what is called "ineligible investments". An investment that might be approved under the Canadian and British Insurance Companies Act might be in the category of an ineligible investment for the purposes of qualifying for the lower rate of tax on a small business. This would appear to be something that was not intended and should be corrected.

Hon. Mr. Benson: In the first case there are really two problems. Because of federal and provincial regulations they may be precluded from making full use of the small business deductions and also may be unduly suffering from the topping-up tax. In regard to the first complaint, this is another example of a taxpayer arguing for a more precise definition, in this case the term "ineligible investment". But once more, a more precise definition may turn out to be a more narrow definition. In our opinion the bill as drafted poses no problem to the private general insurance corporation.

With regard to the second complaint, these corporations want to be classified as public corporations in order to avoid the topping-up tax, but to do so would open the door to many other types of corporations making the same argument, and we should look further at this. That is our general position. We think they are all right in the first part, but in the second part we have to worry about other things.

The Chairman: Well, when you say that they are all right, does that mean that if administratively the problem subsequently arises the administrators will take cognizance of the views that have been expressed here today?

Hon. Mr. Benson: I would think they would, but when we get into the law and if we find something does not work out in law according to our intention in presenting it, then we have to consider what we think is missing in the procedure and then amend the law.

The Chairman: Another item was in connection with deemed realization on ceasing to be a resident of Canada. I think you have some comment on that.

Hon. Mr. Benson: Yes, I mentioned earlier we were looking at this particularly with regard to people coming in and working temporarily because it might inhibit our getting good people for good jobs and I think we have to watch that very carefully.

The Chairman: There was a point raised before us by the agricultural associations, and we did include a recommendation in our report on the question of what is called the "family farm". We recommended that so long as the title to the farm passed down the family line to a son or daughter, but remained in the family and was still utilized for farming purposes, there should be a roll-over as far as any capital gain is concerned. I believe you did make some changes in that area, and you provided for an amortization of the capital gain which might result over a period of six years. We have had a lot of submissions asking, "Why is it only six years? Why is it not a longer period of time?"

Hon. Mr. Benson: This was under debate in the House of Commons. We also had submissions before us. The roll-over concept within a family is a very difficult thing to follow through as you might well know. We decided on the six-year period.

The Chairman: From our saying that it should be 20 years.

Hon. Mr. Benson: The question is how long is a reasonable time, and if you go the 20-year period and charge current interest rates it is not a very great advantage.

The Chairman: That is true.

Hon. Mr. Benson: I should point out that the amendment to make it six years is not in the bill. This will be in the amended bill. It was missed, but it is my intention to put it in the amended bill in the spring. I will undertake to do this.

The Chairman: We will have another chance to raise the issue as to whether it should be a longer period of time than six years at that time.

Senator Lang: Before we pass from this subject, would you comment on the basic herd concept?

Hon. Mr. Benson: Basically, the problem of the basic herd concept is that the cattle farmers want to pay capital gains tax rather than income tax on money realized out of ranching. They have the advantage of building up their herd. They are not on a cash basis. They can invest in their herd and it can grow and grow. But under the law as it is proposed we say that this is a business and when you come to dispose of everything it should be treated as income subject to all the other averaging provisions, and so on. If you go on an accrual basis perhaps you would not have anything piled up at the end. But with the capital gains concept the basic herd concept no longer becomes a great advantage except if one takes the position that profits on cattle ranching should be taxed as capital gains rather than income. The position I have taken is that this is income the same as with any other farmer such as a wheat farmer. If he piles up a lot of inventory and realizes a gain he has to pay tax on it. I maintain they should have equal treatment. This is the same as the businessman who builds an inventory and is not on an accrual basis. However, businessmen are on an accrual basis and they have to pay as they go along. Perhaps my position is wrong. But that is the position the Government is taking.

The Chairman: Mr. Benson, we have asked for further consideration on the question of roll-overs. I believe you made some statement in the House of Commons concerning that.

Hon. Mr. Benson: Roll-overs on re-organization is one place it comes up.

The Chairman: Yes, that is correct.

Hon. Mr. Benson: I said in *Hansard* that, "Finally I want to refer to the many representations I received in connection with the relation of the rules relating to roll-overs and corporate re-organizations. This is a very complex area and I have instructed my department to carefully review the proposals under Bill C-259 to see if they could be extended without undue prejudice to the system. . . . I am hopeful that early next year we will have some positive steps to be recommended to the house in this area after we have had a general study of the matter and have seen the present rules in operation."

The Chairman: Another item we requested be given further consideration was in relation to the mining and petroleum industry and those organizations which we term non-operative. Of course, under the present law they enjoy a 25 per cen automatic depletion, which is to go out the window.

Senator Flynn: Did you say "law" or "regulations"?

The Chairman: Under the regulations. I used the word "law" in a very broad sense, Senator Flynn. They lose the 25 per cent automatic depletion, and I believe that when the cut-off date occurs they may have positions which developed prior to that, in which they have incurred liabilities which carry on. They do not have a free royalty income position to the extent of taking care of the liabilities in their position. Have you some comment on that?

Hon. Mr. Benson: I can only say that this is under consideration. I would like to defer comment until we decide where our studies are in this regard.

The Chairman: By the time the amending bill is introduced next year this will be good fodder to throw out again.

Hon. Mr. Benson: There are a few areas in which people arrived in that position a long time ago and then have moved forward to a position where they would have become taxable some years ago, but they still had a depletion allowance and now, when the system runs out which, admittedly, will not be for several years, 1976 or 1977, they find they lose the 25 per cent or 33 per cent and have nothing from that point onwards.

Several cases have been drawn to our attention in which it is pointed out that there would have been no objection to the law being changed had it been known in advance so that a different type of contract would have been drown initially. Many are trapped by this aspect, but we wish to make sure that they are not treated unfairly. Several mining companies have brought such cases to our attention. That is why I do not wish to comment definitively at this time.

The Chairman: One submission of the construction industry was in connection with joint ventures. We were told that it is a practice in that industry that if a job is too much for any one construction company, two or more will combine on a joint venture basis. In their opinion, since there is no clear-cut definition of a partnership, the joint venture concept in the construction industry should at their option be excluded or exempted from the partnership provisions.

Hon. Mr. Benson: I am told by my advisors that if they can avoid classification as a partnership they will have no problem.

The Chairman: The problem is as to what is a partnership. If two construction companies contribute funds and share the profits, I am sure the sharing of the profits might contain an element of partnership.

Senator Connolly: The law says it is a partnership.

The Chairman: That is correct.

Hon. Mr. Benson: I am told that we will consider this further and that it might in fact be a partnership in such a case. There are methods to avoid being classified as a

partnership, by arrangements. If they end up as a partnership, my people tell me that if we say there is no partnership, we cannot avoid saying that many other kinds of manufacturing partnerships and other businesses are not partnerships. It is a matter of attempting to exempt a certain class of taxpayers. One thing I have learned about tax laws is that whenever we attempt to draw a line we are in trouble. That is the difficulty in our saying that one is automatically not a partnership.

The Chairman: Some people put a declaration in their agreement to the effect that it is not a partnership, but that is meaningless. I do not think that they would be held to be a partnership if the case ever went to court in relation to joint ventures.

Hon. Mr. Benson: There are a lot of people who work together and do things.

Senator Rattenbury: I have come out of a joint venture now and have some knowledge of them.

Hon. Mr. Benson: If one could make sure that one is not going to lose money one could organize it as a limited company.

Senator Connolly: That is not always the most convenient way.

Senator Rattenbury: You do not treat it in that way.

Hon. Mr. Benson: I recall a case where the people concerned suffered a huge loss, and they chose to become a limited company. Many people entering into a joint venture could lose money. They want to be a partnership instead of a limited company. Now they are saying, "If we want to be a partnership, we should be treated as a non-partnership for tax purposes if we take a profit. If we make a loss, we are happy to be a partnership."

The Chairman: You have excluded joint ventures in the mining areas.

Hon. Mr. Benson: No, only on earned depletion, not on ordinary income. They are only exempt on their earned depletion.

Mr. Cohen: In all other respects national resource partnerships are treated like any other partnerships. Exemptions are only for depletions and fast write-offs.

Senator Molson: The minister has said on many occasions that it would be very awkward if the bill were not passed by the end of the year. I think I am right in saying that. He considers it highly desirable that it should be passed. In view of this list of problems that we see in the legislation as it is now, is there any way the minister can assure us that we will have an opportunity of seeing some amending legislation in the immediate future, either at the beginning of the next session or after the adjournment?

Hon. Mr. Benson: I have said, in regard to most of the problems, that they are not immediate. Most of them do not have to be solved next month, although some of them do. I have indicated some of the changes that will be made.

Senator Molson: That is a little different. They are immediate problems to us, perhaps.

Hon. Mr. Benson: Perhaps they are, but they do not affect one's taxation liability immediately. I am thinking of problems connected with international income. There are other things that will have to be changed as of January 1. For instance, there will be one change with regard to deferred profit-sharing plans, as well as others.

Senator Connolly: The proposed changes would not be made in this bill?

Hon. Mr. Benson: They will be made in the next amending bill. I cannot promise to have it for February, but the normal budget comes along in March or April and has to be through by June. It was in June last year, but normally in preparing for the next budget we would conduct our studies and come up with a solution to these problems.

Senator Molson: I am not well informed on these things, Mr. Minister, but every now and then I hear rumours of an election, and perhaps that might change some of the normal processes from one year to the other.

The Chairman: Well, you cannot expect the minister to give an undertaking.

Senator Molson: I do not expect him to give an undertaking, Mr. Chairman. I am simply saying that if the date is in the indeterminate future I am not quite sure whether I am as relaxed about the present as I would be if the minister could assure us that some action is going to be taken with regard to the matters which he has discussed and which he and his staff know about which the Senate over a period of three months has come up with as being problems in this legislation.

Hon. Mr. Benson: Well, I can assure you that we will proceed with action forthwith. As a matter of fact, in some cases we have already done things, and we will proceed forthwith towards the preparation of legislation. I cannot assure you when there is going to be an election, but I can assure you—

Senator Flynn: Nor of the result.

Hon. Mr. Benson: Well, I can assure you of the result, but I cannot assure you—

Senator Flynn: If we can count on that in the same way as we can with respect to the amendments, it is not very reassuring.

Hon. Mr. Benson: We would normally produce a budget so that the budget could be completed by June, and these changes would be outlined in the budget statement. Under our new arrangements in the House of Commons, this is the way we operate.

Senator Beaubien: Mr. Minister, this bill contains a great many things with which the Senate disagrees. The Senate would not think of passing such a bill under normal conditions unless these amendments are made. I am not being unduly critical; you have admitted this yourself. It seems terribly difficult to get an amendment passed in the other place in a reasonable amount of time, and if the Senate was willing to pass a bill because of those difficulties, a bill which has been studied very carefully and which the Senate feels needs amendment, I would think that the

Senate would want to have at least an expression from the minister that "not in the due course of events", but just as soon as he could he would introduce a bill—and we are not asking you to tell us what you are going to put in the bill—which would take these things into consideration. If you expect the Senate to pass this bill—and I am speaking for myself, not for the Senate—we would have to be assured that there would be a special bill to deal with the amendments.

Hon. Mr. Benson: I am not saying there will be a special bill, but there will be a budget—

Senator Beaubien: There will be another Christmas too, Mr. Minister, but what I am asking is: Can we expect a special bill for the purpose of these amendments?

Hon. Mr. Benson: There will be a bill to amend the Income Tax Act and it will take into consideration the propositions brought forward by the Standing Senate Committee on Banking, Trade and Commerce and, indeed, by a great many other people as well, and also other matter that we want to build into it, but I am certainly in no position to give an undertaking that we would have this bill introduced in February or at the end of January, or whenever. We intend to proceed with all due despatch to study the propositions brought forward by the Senate, as well as those brought forward by various associations. The propositions brought forward by the Senate are not simple ones when you look at the whole bill. I think some of the senators will admit that.

Senator Beaubien: We have studied it enough to realize that.

Hon. Mr. Benson: It will take some time to work it through, but the intention is, of course, to correct it. As I indicated in my speech on Friday, many of the matters will be amended just as soon as it is conveniently possible.

Senator Gélinas: Mr. Minister, I think what my colleagues are worried about is this period of uncertainty we have been going through for the last two years.

Hon. Mr. Benson: Well, the uncertainty has been eliminated to a major degree by this legislation. The points which the Senate has brought forward are in specialized areas concerning which it is difficult to come up with the right solution; and I do not want to come up with the wrong solution. There are holding provisions with respect to foreign businesses, for example, so that there will not be big loopholes created. We are studying the matter and have been working on it since before the Senate report—and, I might add, we have been helped by the Senate report—and we hope to come up with solutions in the near future. We are getting representations from a great many people. We have to listen to them, and then we will produce a bill. It will be this spring. We will have to produce a budget and we intend to include an amending bill to amend this act.

Senator Cook: This will be the end of round one. In other words, the door will be opened for amendments.

Hon. Mr. Benson: This is the end of all the rounds except the knockout round, I hope. I certainly hope we do not have to have too many more, anyway. We are down to the point now of dealing with very specialized areas. I would like to deal with these in an amending bill in a way which will stand up over a period of years.

Senator Beaubien: If we had a little time the Senate would insist on putting in certain amendments. I think the Senate should not pass this bill unless the minister agrees. He has agreed. We are not really fighting too much on what we want in the amending bill; we all seem to be agreed. It seems to me that the Senate is entitled to have the minister say, "I know you have not had the time to insist on these things, and I do not argue with the fact that they should be done." If the minister will say, "We will put in a special bill; we are not going to have when the time comes, another budget and have it in there," we would not insist on certain amendments now, if we had time.

The Chairman: You do not want to tie the amending bill to budget time.

Senator Beaubien: No.

Senator Molson: No, and we do not think it should be necessary to wait so long.

Hon. Mr. Benson: If you want a better definition I will bring in an amending bill, but I cannot promise I will have the amending bill by the end of January or the end of February.

Senator Molson: Bring it in at the earliest possible date.

Senator Beaubien: That is all we ask you, Mr. Minister.

Senator Molson: Will you take into consideration the recommendations of the Senate, Mr. Minister?

Hon. Mr. Benson: Yes, but I do not say that I will agree with them.

Senator Molson: I did not ask you that. I asked whether you would take them into consideration in producing the amending bill?

Hon. Mr. Benson: Yes.

Senator Beaubien: We realize that the Senate cannot say to the Minister of Finance, "You have got to do so-and-so!"

Senator Molson: You may not agree to it.

Hon. Mr. Benson: Some may be impossible.

Senator Molson: We know this.

The Chairman: All we really need here is the assurance that there will be an amending bill, because with that assurance we can make our own amendments if we do not like what is in the bill.

Senator Molson: Mr. Chairman, that is what your committee said to you in its meetings.

The Chairman: That is right.

Senator Molson: That we should be able to say, "All right, the bill right now does not suit us, but rather than hold it up and cause unnecessary complications, we are willing to pass this, provided we get an assurance that there will be a chance to bring in the amendments we feel keenly about." I do not think it is unreasonable.

The Chairman: I understood the minister had said that now.

Senator Molson: I think he has now. I think we have just reached that point now.

Senator Beaubien: We want him to repeat it.

Hon. Mr. Benson: I have said that there will be an amending bill.

Senator Molson: But then you said the budget.

Hon. Mr. Benson: But an amending bill will form part of the budget; it has to.

Senator Molson: Maybe, but why could it not be before the budget?

Hon. Mr. Benson: It is another budget then.

Senator Molson: All right.

Hon. Mr. Benson: It is a change in ways and means.

Senator Molson: All right.

Hon. Mr. Benson: It has to be a budget.

Senator Flynn: Since Senators Beaubien and Molson have put this question to the minister, I should like to intervene, if the committee would permit me, for about 15 minutes, because I think it is about time we clarified the scope and meaning of the appearance of the minister this afternoon.

This committee has dealt with the White Paper and has produced a report. That is one thing. It has now considered the bill in a very technical way, which is something else. However, I think the Government would be under a wrong impression if it thought that we are concerned only with the recommendations of the last two reports we have made. This is something of a technical nature. It has been clearly understood that we would be dealing only with technical aspects of the bill, that we were not dealing with the principle of the bill in studying the bill since last fall. We restricted ourselves to the legislation as drafted. We forgot about some of the recommendations we had made in our report on the White Paper, because we said that it was a policy matter. However, because it was a policy matter it does not mean it is without the competence of the Senate when the bill reaches us to deal with it, or that we have completely forgotten about these other problems. I think it would be very wrong to give the impression that the Senate is willing to pass the bill if the minister gives us the assurance that we are going to have an amending bill along the lines of our reports. The problem is not restricted to that at all, to my mind.

I want to ask the minister about the consequences of our attitude in these reports. If my understanding is correct, the minister comes here to deal with the recommendations or the suggestions we have made in our last two reports.

The Chairman: That is right.

Senator Flynn: Is that correct?

Hon. Mr. Benson: That is correct?

Senator Flynn: That is the point. Now, is my understanding correct, that the minister is telling us, as far as these technical recommendations—and I call them "technical" intentionally—as far as these technical recommendations are concerned, "I suggest to you, do not worry, we will come with an amending bill eventually"?

Senator Beaubien: We do not want "eventually".

Hon. Mr. Benson: We will consider it—not "eventually"—

Senator Flynn: Well, let us say "eventually" at this point.

Hon. Mr. Benson: We will consider them "in the near future", and we will consider the Senate's recommendations in producing an amending bill, but I do not say we will adopt them all.

If you go back to the previous Senate recommendations, and if you look at my June budget, or the booklet I issued with it, you will see we show on page 66 how we dealt with all of the Senate recommendations and the House of Commons committee recommendations over the whole area, and that was our decision at that time.

Senator Flynn: I know.

Hon. Mr. Benson: Of course, we did not agree with all of them.

Senator Flynn: I know, and that is why I do not want to draw the minister outside the field of our two reports. If the minister comes back to us, when the bill reaches us—and I understand that the deadline has been indicated in the other place to be 4 o'clock on Friday afternoon—then of course we can deal with all of the other problems that we dealt with in the White Paper or that we did not deal with in the White Paper. But at this time we are concerned only with the two reports, which are of a technical nature. But the debate is not limited to that, when the bill reaches us in the Senate.

I just wanted to ask the minister: Is he suggesting at this time, as far as these specific recommendations are concerned in our two last reports, "Forget about them for the time being; adopt the bill as it is now; otherwise . . ."—I am not speaking of the other provisions but in connection with these special provisions—" . . . adopt the bill now, and we will correct it later"?

Hon. Mr. Benson: What I am saying really is that the bill is being presented to the Senate. It will be through the House of Commons on Friday, as you indicated. In the consideration of the bill, I simply want to assure the Senate that I have considered some of its recommendations, as well as recommendations from other people, and that I am willing now to undertake that certain of them will be changed, in an amending bill, and that in producing an amending bill we will consider submissions not only from the Senate committee but indeed from many other people outside who are making submissions to us presently.

Senator Flynn: Then you suggest that if we were to make some amendments along the lines of our two reports, that you would not be prepared at this time to accept them or to recommend them to the other place, if we return the bill with these amendments?

Hon. Mr. Benson: Well, you know it is not within my jurisdiction to control what the Senate does, and I am not saying to the Senate what they should do in any way.

Senator Flynn: You are not suggesting that you would refuse amendments?

Hon. Mr. Benson: I am not suggesting anything. I am not here to tell the Senate what to do. I am simply here to answer questions.

Senator Flynn: There was some misunderstanding—

Hon. Mr. Benson: You are master in your own house.

Senator Flynn: There was clearly in the minds of Senator Beaubien and Senator Molson that if we passed the bill as it is without the amendments we are suggesting, we would be satisfied with your undertaking to amend it later, or to consider amending it, or to consider very seriously amending it later.

The Chairman: Senator, you have jumped from one position to the other.

Senator Flynn: I thought you would jump, too, at this point.

The Chairman: There is nothing being done here that inhibits any senator, or all the senators, dealing with the bill in any way they wish.

Senator Flynn: I know. That is what I want to clarify.

The Chairman: Yes.

Senator Flynn: Because there is some understanding, from the questions that have been put, that our recommendations would be considered and that we only have to forget about them for the time being, because the minister will bring in an amending bill eventually in the New Year.

The Chairman: Only in relation to those items.

Senator Flynn: That is right, and that is what I want to clarify.

The Chairman: It is clear to me.

Senator Flynn: Yes, I know it is clear to you. It is clear to me, too, I can assure you of that, but I do not know if it is as clear to the public, and I want the public to know where we stand, and I want to know where we stand too.

The Chairman: That is right.

Senator Flynn: And that is why I say this.

Now, there is another point I want to raise. It has been suggested that we should get this bill through by December 31. Of course, the easiest way to do that would be to adopt an attitude towards the bill, whether in connection with the recommendations in our last two reports or the objections that we have had to the White Paper or the other objections that we have had in other ways, such that we would pass the bill by December 31 with the intention that we would correct it all sometime in the year 1972, 1973, or else. But does the minister feel that it is necessary for the Senate to go through this huge bill at this time? I may restrict my question to the amendments which are covered by our two reports, because again I do not want to be illogical and I know that the minister is only here for that. But let us say we postpone the consideration of the bill to January 11, for instance. Suppose we come back then and in the meantime the minister and his officials have had time to consider our recommendations further and some amendments are brought in and finally the bill receives Royal Assent by the end of January. Supposing all of that, what practical difference would it make to the people of Canada generally?

I will add just one comment before I give the minister the opportunity to reply, and this is in connection with something said by Senator Gelinas, that there is uncertainty and that we should pass his bill to dissipate the uncertainty. Why? What is the difference between the uncertainty of passing this bill and being faced with an amending bill, or delaying the passage of this bill in order to adopt it in its final form or in a better form at the end of January?

Hon. Mr. Benson: First of all, senator, I think I explained the answer to this very carefully in the house on Friday.

Senator Flynn: I saw that. I even saw what you said about the Tories.

Hon. Mr. Benson: I was not referring to you, senator. I was referring to some people—Well, I don't want to get into a political argument here.

The Chairman: No.

Hon. Mr. Benson: It is advantageous, as I outlined in the house, to have the bill through by the end of this year in order that we may have certainty.

It is not for me to comment on the procedures in the Senate, but I believe that at least this committee of the Senate has given this bill very careful study. In fact, I was congratulating you earlier on the amount of study you had done ever since the bill was introduced in June. I can in no way indicate to the Senate what their procedures must be or how they must operate. That is not up to me to do.

Senator Flynn: That was not my question.

Hon. Mr. Benson: If the Senate operates in certain ways, then the Government is in a position where it has to decide on its own position. But I do not think it would be useful for me to read into the record here the long explanation which I gave in the House of Commons on Friday as to why we believe the bill should be got through. One can say, "Sure, there are going to be uncertainties in the legislation." There are always going to be uncertainties in the tax law. There were always uncertainties in the old law, even after it had been operating from 1918 to 1971.

The Chairman: Mr. Minister, do not forget that we had a new tax bill in 1949. We have had amendments practically every year since.

Hon. Mr. Benson: Sure, and you are going to have more. There is always going to be uncertainty. Take the dividend stripping cases. Look at the number of years of uncertainty there were there and the results ultimately. But we will do our best to clear up this uncertainty as soon as possible in the limited number of areas in which it is left, and in so doing we will consider the recommendations of the Senate committee.

Senator Flynn: This is my last question. Should I draw the conclusion that we should only spend a few hours on the

bill and send it back to you because you are eventually going to consider what has been said, and so it is absolutely useless for us to spend more than a few days on this bill?

Hon. Mr. Benson: I do not say anything of the kind.

Senator Flynn: You have not said it, but then we draw that conclusion.

Hon. Mr. Benson: You cannot draw that conclusion from anything I have said.

Senator Flynn: Well, read the record tomorrow.

Hon. Mr. Benson: I have indicated the problems that will arise if the bill is not passed, and it is up to the Senate to decide how it will proceed. We will not in any way try to tell the Senate what to do.

Senator Phillips: I am sorry, Mr. Chairman, but I arrived rather late and missed certain points covered earlier dealing with the basic right of a farmer to pass property on to his son, and so on. I am very much confused here in that I understood that there would be certain agreements and that if these things were passed and agreed upon now, there would be a review. But now I find that there is no limit as to when the review should take place. Now, while I am willing to submit these objections to a review, I would like very much, Mr. Chairman, to have a time limit placed on it. I am rather surprised that we have gone from a review to a budget, and it disturbs me very much, Mr. Chairman. Therefore my willingness to accept or adopt these measures diminishes as I see them going from budget to budget.

Hon. Mr. Benson: I do not think I indicated that. I indicated that, having had the submissions of the Senate which were considered, I had certain comments to make and I agreed to come here this afternoon to make those comments. We will review, if you want to use that word, the recommendations from the Senate,—and I believe there is another report on the way from you—and also submissions from other people, and then we will present amendments to the Income Tax Act. If that deals with ways and means, it is probably a budget we are producing. As you know, if there are major changes in revenues and expenditures, you present them in the form of a budget.

Senator Connolly: You have to have a resolution.

Hon. Mr. Benson: You have to have a resolution, and there is another way of getting a resolution in, but if they are comprehensive amendments, the only logical way to present them is in the form of a budget.

Senator Phillips: But there is nothing, Mr. Minister, that says you or the Government are bound by any time limitation; you can present a budget this year or five years from now.

Hon. Mr. Benson: That is not true, We will bring in a budget. I have undertaken to bring in a budget. We will have to do it in the spring, or as soon as we can, and then we will present amendments to the Income Tax Act which will take care of these things. I cannot tie myself down and say I am going to do this in February or in January or by the 15th of March. I have tried doing that before, and I have gone through this whole tax bill, and every time you do it you get yourself into a mess. But I have said that we will move forward with all due dispatch, and I already have my people working on it. We are seeing people now and are reviewing the submissions brought forward by the Senate and by other people, and in due course or with all due dispatch we will consider amendments to the bill.

The Chairman: Are there any other questions?

Senator Welch: I would like to say to the Minister of Finance that we began our meetings here around the 1st of September; some days we sat in the morning as well as in the afternoon. I cannot understand why all these amendments and recommendations have not been brought to our attention before this. Why wait until the deadline and then say that we have to have this bill passed, you might say, in a matter of 24 hours? You cannot impose closure on the Senate, so why does the Senate not hold this bill up until we have a chance to obtain these amendments?

The Chairman: Our first report was tabled on November 4 and the second on November 24.

Hon. Mr. Benson: Yes, and they came to me a day or so later, so I have not had them for very long.

Senator Welch: If we are going to be held up with these amendments for this long, what is there to assure us that we are not going to be held up for just as long a period when the new bill comes in the spring? Will we wait until vacation time and then either pass it or sometime after the vacation? That is the old story.

Hon. Mr. Benson: One of the problems, senator, is that the Government can introduce legislation in the house but it cannot determine how long the house is going to take to deal with the legislation unless there is a time limit put on the debate. The House of Commons have had almost 50 days on the bill already. That is not under my control. I might introduce an amendment in February—

Senator Flynn: It was to some extent.

Hon. Mr. Benson: —and they might go on for three months. I cannot stop them.

Senator Welch: This probably has very little to do with the situation, but, on the other hand, if you had brought in closure a week before you did, you would have had that much more time to solve some of these problems.

Hon. Mr. Benson: Usually time allocation is a step you take reluctantly.

Senator O'Leary: Mr. Chairman, am I right in saying that what the minister has said to us today, and that all he has said to us, is that at some unspecified date in the coming year he will bring in an amending bill under the budget, and he may or he may not incorporate in that amending bill some of the amendments which your committee has suggested? Is that correct?

Hon. Mr. Benson: I think it has gone further than that. I indicated in the House of Commons on Friday, and again here today, that I will incorporate some amendments.

Senator O'Leary: Not necessarily our amendments.

Hon. Mr. Benson: Some of the amendments recommended by the Senate. I have also indicated that we will move forward with all due dispatch to examine the more complicated suggestions which the Senate, as well as others, have made, and produce new legislation in the form of an amending bill. Now, I cannot say whether that is going to be introduced in January or February; but we will move forward just as fast as we can in order to produce legislation. The only reason this got tied up with the budget is that if you make substantial changes in the House of Commons, under our procedure, I normally introduce it in the form of a budget.

Senator Paterson: Is the minister aware of the hours our Chairman has put in on this tax bill? I feel that probably he is the best tax adviser in Canada.

Senator Flynn: Let that show on the record.

Senator Paterson: Is he aware of all the amendments which you propose and is he in favour of them?

Hon. Mr. Benson: Senator, first of all, I indicated earlier that the Government appreciates very much what the Standing Senate Committee on Banking, Trade and Commerce has done. We have recognized the work which the Chairman has done, along with the committee, by adopting, I believe it was, 44 of the amendments suggested by the Senate in our June budget. The present amendments are under consideration by the Government. I have indicated some that will be adopted, and in the case of others we are considering the difficulties and will decide whether we can adopt them and produce legislation.

Senator Paterson: If this tax bill is passed in the other place to take effect on January 1, 1972 it will remain in effect after we conclude our debating it on the February 1? Is it true that it can date back?

The Chairman: That is a legal question, Senator Paterson.

Senator Paterson: Well, do not answer it if it will be embarrassing.

Senator Croll: The Chairman has already answered the question.

The Chairman: I expressed an opinion in the Senate.

Senator Desruisseaux: There have been strong objections by five of the ten provincial premiers with respect to accepting the bill at the end of the year. I believe one said he would go along with the old method this year. Another said he may well do that. Would you comment on the confusion this will cause in the minds of taxpayers?

Hon. Mr. Benson: First of all, all provinces that are involved, which excludes the Province of Quebec, in the tax collection agreement have indicated that they will adopt basically the same legislation. We have sent bills to them to be effective January 1. Quebec, I believe, have indicated that in principle they will follow this legislation in their own, which is quite independent; they collect their own taxes. Ontario have indicated that in some corporate areas they will not be able to make the changes immediately. Therefore, only the corporate taxpayers in Ontario, and maybe the corporate and personal taxpayers in Quebec, can be affected. I am not sure, however, how they will proceed. All other provinces with which we have collection agreements have indicated that they wish to continue. This means they will adopt the tax law in this bill. Some have indicated that they do not like everything in it, but I do not believe we can produce law which ten premiers would approve in toto. Nevertheless, they will proceed with the tax collection procedures and introduce the legislation.

Senator Desruisseaux: This can lead to confusion.

Hon. Mr. Benson: I would like to see Ontario move as fast as possible with regard to its corporate tax legislation.

Senator Croll: When we last considered the amendments to the White Paper, Mr. Chairman, we made certain recommendations.

The Chairman: Yes.

Senator Croll: How many did we make? Have you any idea?

The Chairman: Offhand, I cannot tell you how many. I know how many were accepted.

Senator Flynn: Do you know the percentage?

Hon. Mr. Benson: I do not have the numbers here, senator. We adopted them in some cases and partially adopted others. In certain areas we went one better, for example with regard to exemptions.

Senator Croll: I understood you to say, if you recall, that you adopted 44 of our amendments.

Hon. Mr. Benson: That is right.

Senator Croll: How many more could we have? I cannot remember the number, but it seems like a very good proportion.

Senator Flynn: It all depends; we might have recommended 200.

The Chairman: It is a problem in arithmetic to total them. I have not taken the time. It would mean not going through our report on the White Paper, which could be done, but it would take a little time.

Senator Macnaughton: Mr. Chairman, at the beginning of this meeting, if I understood you correctly, you said that you had a personal statement to make. It seems to me that it might be very helpful to our committee at this time if you were to make that statement now.

The Chairman: When the meeting concludes I would like the members of the committee to remain, because we have prepared in draft form a final report which we would like to table tonight, if the committee approves.

There is one question that I should like to ask of the minister, for the purposes of our record. In the case of credit unions and caisses populaires, we made certain recommendations to enable them to be in a better position to qualify as small businesses. I believe that the amendments which you subsequently introduced accepted those recommendations 100 per cent.

Hon. Mr. Benson: That is right.

The Chairman: An additional amendment was inserted in the case of co-operatives, where you had 5 per cent of working capital as an income tax base.

Hon. Mr. Benson: Yes. We moved away from the percentage-of-capital concept. Under the new legislation co-operatives are better off than they were under the previous legislation.

Senator Isnor: Why do you not put them on exactly the same footing as small businessmen?

The Chairman: They are now, if this amendment becomes law.

Senator Burchill: Have we nothing to say with regard to the pulp and paper industry?

Hon. Mr. Benson: We had their representatives in to see the Prime Minister and a large number of the cabinet last week. One of the problems raised was that of taxation. They have agreed with us that we take a look at their taxation vis-à-vis that of other countries. We are proceeding to do this. I mentioned that two provinces are doing the same thing, and we are co-operating with them in looking at the problem.

Senator Burchill: Are they satisfied?

Hon. Mr. Benson: They are quite satisfied that we should proceed in this manner.

The Chairman: I mentioned to the minister earlier that I had received a letter from the Pulp and Paper Association indicating how pleased they were with what we did and with the reception they received from the minister and the cabinet ministers. They feel that the problem is being looked into. Nobody can formulate what can be done until the matter is studied completely.

Senator Lang: Based on the minister's remarks in the House of Commons last Friday, and from the way his presentation has evolved today—I would like to be corrected if I am wrong in this assumption—I take it that he agrees in principle with our recommendations regarding gifts to charities, profit-sharing plans, deferred profit-sharing plans, foreign affiliate passive income, and ceasing to be a resident.

Hon. Mr. Benson: We cannot go quite that far. We have indicated that we believe changes need to be made in these areas, but in some areas changes cannot be made exactly as recommended by the Senate.

Senator Lang: But you agree in principle?

Hon. Mr. Benson: In principle we agree that something has to be done.

Senator Flynn: There are problems.

Hon. Mr. Benson: There are problems in doing it. With regard to deferred profit-sharing plans, the two things that I mentioned can and will be done in that form. In the case of ordinary profit-sharing plans we have to find out how to do it, and we are working on that. In the case of the passive income rules, we are looking at this matter and are trying to find out how we can avoid the pitfalls that may exist. With regard to foreign operations of Canadian corporations, the same thing applies. I have indicated that we will act on these as soon as we can do so. The other problems are being looked at. There are many complicated matters that have to be dealt with.

Senator Lang: Mr. Chairman, I was just wondering if the minister would care to comment on three items which are contained in our report and which have not heretofore been mentioned. They are: firstly, with respect to contracts in the construction industry; secondly, the designated surplus concept; and, thirdly, the problems which arise in connection with life insurance corporations.

Hon. Mr. Benson: First of all, with regard to the construction industry, senator, nothing in this legislation changes the basis of computation of tax. If the Department of National Revenue proceeds as they have been proceeding I do not think the people will worry about it. They would like to have something put into our regulations to add additional clarity to this, and we are taking a look at it.

Senator Lang: The second point was with respect to designated surplus.

Hon. Mr. Benson: We think it is necessary at the present time, but we are looking at it. If we had gross-up and credit, which the Senate recommended against, it would not be necessary, but because we do not have gross-up in credit and we do have a partial dividend tax credit and a half rate gains tax it can still be a method of avoiding tax.

Senator Lang: The final one was the recommendation with respect to life insurance corporations, and in this regard we made the following recommendation:

> —that corporate dividend income received and arising from investments made by a life insurance corporation out of its non-segregated funds in shares of capital stock of corporations be excluded from the allocation of investment income formula set forth in the proposed legislation.

Hon. Mr. Benson: We are presently talking to the industry about this. It is a technical amendment which would be of some advantage to them. That law has been running for two or three years now and this legislation has just shaken it down so that they now know where they stand. As I say, we are presently discussing this matter with them.

Senator Lang: Just one final comment, Mr. Chairman. On my way up here today I met a legal colleague of mine, and he said, "I hope you will pass this legislation and have it in force on January 1st". I replied, "I am rather surprised that you would make that comment." He said, "Well, in our firm alone we have already found 141 loopholes and we want to get them into operation."

The Chairman: Why did they stop at 141?

Senator Flynn: We should put on the record what an expert said when we began the study of this bill. The expert had been discussing the complexities of the legislation with officials of the department, and the officials said to this expert who was a lawyer, "You should be grateful to us because we are putting all of you on the same level as Stikeman. No one is an expert any more."

The Chairman: Are there any other questions?

Hon. Mr. Benson: They will have to develop new experts.

Senator Phillips: Mr. Chairman, perhaps I would be in disagreement with members of the committee if I said I do not consider this bill a tax reform bill but rather a tax imposition bill. In other words, more taxes are being imposed than was the case under the old system.

How much extra revenue is expected to be collected as a result of this bill, Mr. Minister, and what will be the cost of collecting that revenue? There are certain sections in the bill, as I see them, where it is going to be very costly to collect the additional taxation revenue.

Hon. Mr. Benson: Well, senator, I can answer your question quite simply. So far as the federal Government is concerned there is no additional tax revenue as a result of this bill over a five-year period. As a matter of fact, we have built into the legislation tax reductions to make sure that this does not occur. We would get the same amount of money under the old system as we will get under this new system, as best we can forecast it.

Senator Phillips: Under parliamentary rules, Mr. Minister, I must accept your statement. However, may I add that I do it with certain reservations?

The Chairman: That is your privilege.

Senator Carter: I would like the minister to clarify his last statement.

You are not going to get an increase in revenue over the next five years?

Hon. Mr. Benson: There will be an increase in revenue inasmuch as there will be an increase in our Gross National Product, but it is exactly the way it would be under the old system. In order to ensure that this is the case we have built into this legislation both personal and corporate tax reductions to make sure the level would be exactly the same as under the old system.

Senator Grosart: Mr. Chairman, I think what is worrying some of the senators here is the rather extraordinary situation we find ourselves in, that we have amendments to a summary bill approved by the Senate when it approved the committee reports, and we are now in the position of having amended the bill or of having approved amendments to the bill. The Senate has accepted the amendments.

The Chairman: No, the Senate has not. There has been no vote.

Senator Grosart: The Senate adopted the report.

The Chairman: No.

Senator Grosart: I am sorry. Then we are in a position of having suggested amendments.

The Chairman: Yes.

Senator Grosart: And they are now going to the minister, or to the Government.

The Chairman: We call them recommendations.

Senator Grosart: Recommendations.

Senator Flynn: They were very prudent.

Senator Grosart: They are suggested amendments. We are now placing these in the hands of the Government. We are not sending them back to the other place, as we would normally.

The Chairman: That is right.

Senator Grosart: We are dealing with the recommendations and a bill in what we would call the normal way, time permitting. I presume the Senate still has the opportunity to move these amendments when the amending bill comes forward.

The Chairman: Certainly, on second reading.

Senator Grosart: I am for the time being assuming that we do not make amendments when the bill comes before us, between now and January 1. We still have the opportunity to put our amendments in a form in which they will go back for re-consideration by the other place when the amending bill that the minister has, I think I can say, promised comes before us.

The Chairman: It is my view, as a matter of law, that when an amending bill comes before the Senate amending this Bill C-259, we can deal with that bill in the same way as we would deal with any other bill, except that we cannot levy taxes or raise taxes. We can put in the amendments we are talking about today; we can put them in if they are not already in the bill; or we can put in other amendments if we decide to hear more evidence.

Senator Flynn: But they have to be relevant to the amending provisions of the bill. We cannot add to a tax bill.

The Chairman: This is what I said. You cannot add anything that will increase rates or levy taxes.

Senator Flynn: Even if it does not touch ways and means, you cannot include provisions that are without the general ambit of the amending bill.

The Chairman: That is where you and I disagree on a matter of law.

Senator Flynn: I am not too sure that you entirely disagree with me, maybe because we have not got time to discuss our opinions.

The Chairman: Nothing can become law at any time in relation to any matter unless the Senate passes the bill.

Senator Flynn: That is right.

The Chairman: Is that not enough authority?

Senator Flynn: I think you did not get my point.

The Chairman: Yes, I did.

Senator Flynn: I say that if the minister brings in an amending bill dealing with the gift problem, we could not add to the bill a provision concerning the profit sharing plans, because it would not be relevant to the amending bill.

The Chairman: We have done it in the past.

Senator Flynn: Well, I doubt that we can do it.

The Chairman: We disagree on that point.

Senator Grosart: Just to make my point perhaps a little clearer: Would you say as a matter of opinion, as the chairman of this committee, that in due course, when the amending bill comes before us, if we do not make amendments now, we will be in a position generally to make any of the amendments we have suggested?

The Chairman: In my opinion, yes.

Senator Grosart: That is the answer I wanted.

Senator Flynn: In my opinion, no.

The Chairman: So we are both batting 500 per cent.

Senator Grosart: It is yes and no.

The Chairman: Are there any other questions?

Senator Beaubien: Mr. Chairman, I would like the minister to be a little more specific about that amending bill, when he brings it in.

Senator Flynn: You have done your best up to now.

Hon. Mr. Benson: I can undertake no more than I have now. There will be a bill coming in in due course, with all due dispatch, amending this legislation. I cannot go any further than that. If I did and said January 15, or February 15, or March 15, and I did not meet that deadline, people would tell me I had broken my word with the Senate, and I have no intention of doing that.

The Chairman: You might be talked out of an opportunity to do it.

Senator O'Leary: The amending bill may or may not incorporate the proposed amendments.

Hon. Mr. Benson: The decision has to be made. We will look at the amendments. I have indicated some that would be incorporated.

Senator O'Leary: As long as that is quite clear.

Hon. Mr. Benson: That is absolutely clear.

The Chairman: If there are no other questions, we will conclude this meeting. Thank you very much, Mr. Minister.

The committee adjourned.

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THIRD SESSION—TWENTY-EIGHTH PARLIAMENT

1970-71

THE SENATE OF CANADA

PROCEEDINGS

OF THE

STANDING SENATE COMMITTEE ON

BANKING, TRADE AND COMMERCE

The Honourable JOHN J. CONNOLLY, P.C., *Acting Chairman*

No. 52

MONDAY, DECEMBER 20, 1971

Complete Proceedings on Bill C-259

intituled:

"An Act to amend the Income Tax Act and to make certain provisions and alterations in the statute law related to or consequential upon the amendments to that Act"

REPORT OF THE COMMITTEE

(Witnesses—See Minutes of Proceedings)

THE STANDING SENATE COMMITTEE ON

BANKING, TRADE AND COMMERCE

The Honourable Salter A. Hayden, *Chairman*

The Honourable Senators:

Aird	Grosart
Beaubien	Hayden
Belisle	Hays
Benidickson	Isnor
Bourget	Lafond
Buckwold	Lang
Burchill	Langlois
Choquette	*Martin
Connolly (*Ottawa West*)	McElman
Cook	Molson
Desruisseaux	O'Leary
Everett	Phillips
*Flynn	Quart
Gélinas	Sullivan
Giguère	Walker
Goldenberg	Willis

*Ex officio members

(Quorum 7)

Order of Reference

Extract from the Minutes of the Proceedings of the Senate, December 20, 1971:

"The Honourable Senator Martin, P.C., moved, seconded by the Honourable Senator Langlois, that the Bill be referred to the Standing Senate Committee on Banking, Trade and Commerce.

After debate, and—

In amendment, the Honourable Senator Grosart moved, seconded by the Honourable Senator O'Leary, that the following words be added to the motion:

"and that the Committee be instructed to bring back to the Senate a report incorporating the amendment to Bill C-259, intituled: "An Act to amend the Income Tax Act and to make certain provisions and alterations in the statute law related to or consequential upon the amendments to that Act", which have been drafted by the Committee and other amendments recommended to the Senate as "top priority" changes in the bill necessary to correct existing defects in the bill as reported by the Standing Senate Committee on Banking, Trade and Commerce."

RULING BY THE HONOURABLE THE SPEAKER

Honourable Senators:

I have now had time to examine the authorities on similar amendments where instructions were to be given to a committee. In fact, although I cannot recall the exact circumstances, we did have a similar case one or two years ago. At any rate, I should now like to read from *Bourinot's Parliamentary Procedure*, Fourth Edition, page 513. It reads as follows:

"Considerable misapprehension appears to exist as to the meaning of an instruction. An instruction is given to a committee to confer on it that power which, without such instruction, it would not have. If the subject-matter of an instruction is relevant to the subject-matter and within the scope and title of a bill, then such instruction is irregular since the committee had the power to make the required amendment."

Therefore, Honourable Senators, since the Standing Committee on Banking, Trade and Commerce has all of the powers to do what is the purpose of this motion in amendment, I must rule it out of order.

Debate was resumed on the motion of the Honourable Senator Martin, P.C., seconded by the Honourable Senator Langlois, that the Bill C-259, intituled: "An Act to amend the Income Tax Act and to make certain provisions and alterations in the statute law related to or consequential upon the amendments to that Act", be referred to the Standing Senate Committee on Banking, Trade and Commerce,

After debate, and—

The question being put on the motion, it was—

Resolved in the affirmative."

Robert Fortier,
Clerk of the Senate.

24349—1½

Minutes of Proceedings

Monday, December 20, 1971.
(68)

Pursuant to adjournment and notice the Standing Senate Committee on Banking, Trade and Commerce met this day at 10:00 a.m. to examine and consider Bill C-259, intituled:

"An act to amend the Income Tax Act and to make certain provisions and alterations in the statute law related to or consequential upon the amendments to that Act"

Present: The Honourable Senators Aird, Beaubien, Benidickson, Bourget, Buckwold, Choquette, Connolly (*Ottawa West*), Cook, Everett, Gélinas, Goldenberg, Grosart, Hays, Isnor, Lafond, Langlois, Martin, McElman, O'Leary, Phillips and Quart—(21).

Present, but not of the Committee: The Honourable Senators Bonnell, Duggan, Fergusson, Forsey, Laird, Lawson, McNamara, Michaud, Nichol and van Roggen—(10).

In attendance: The Honourable Lazarus Phillips, Chief Counsel and E. Russell Hopkins, Law Clerk and Parliamentary Counsel.

In the absence of the Chairman and upon motion duly put it was *Resolved* that the Honourable Senator Connolly (*Ottawa West*) be elected Acting Chairman.

WITNESSES:
Department of Finance:

The Honourable Edgar J. Benson, P.C. Minister;

Mr. M. A. Cohen, Assistant Deputy Minister.

Department of Justice:

Mr. D. S. Thorson, Associate Deputy Minister.

The Committee then proceeded to the consideration and examination of the said Bill and heard the Minister in explanation thereof, assisted by Messrs. Cohen and Thorson.

At 12 Noon the Minister departed.

At 12:10 p.m. the Committee adjourned until the Rise of the Senate this afternoon.

2:15 p.m.
(69)

At 2:15 p.m. the Committee *resumed.*

Present: The Honourable Senators Connolly (*Ottawa West*) (*Acting Chairman*), Aird, Beaubien, Belisle, Benidickson, Bourget, Buckwold, Cook, Everett, Gelinas, Goldenberg, Grosart, Hays, Isnor, Lafond, Langlois, Martin, McElman, O'Leary, Phillips and Quart—(21).

Present, but not of the Committee: The Honourable Senators Bonnell, Duggan, Fergusson, Fournier (*Restigouche-Gloucester*), Laird, Lawson, McGrand, McNamara, Michaud, Nichol, Paterson, Petten, Rowe and van Roggen—(14).

In attendance: The Honourable Lazarus Phillips, Chief Counsel and E. Russell Hopkins, Law Clerk and Parliamentary Counsel.

WITNESSES:
Department of Finance:

Mr. M. A. Cohen, Assistant Deputy Minister.

Department of Justice:

Mr. D. S. Thorson, Associate Deputy Minister.

After discussion the Honourable Senator O'Leary moved the following motion:

That Section 147(10) of Bill C-259 should be amended to read as follows:

"147(10) There shall be included in computing the income of a beneficiary under a deferred profit sharing plan for a taxation year each amount received by him in the year from a trustee under the plan, minus

(a) any amounts deductible under subsections (11) and (12) in computing the income of the beneficiary for the year,

(b) amounts paid by a trustee under the plan pursuant to the plan to a person describedd in subparagraph (2)(k)(vi) to purchase an annuity described in that subparagraph,

(c) the amount by which the aggregate of

(i) each amount allocated to the employee or other beneficiary by a trustee under the plan in respect of a capital gain made by the trust, and

(ii) each amount allocated to the employee or other beneficiary by a trustee under the plan in respect of the increase in the value of property of the trust over its cost amount to the trust

exceeds the aggregate of

(iii) each amount allocated to the employee or other beneficiary by a trustee under the plan in respect of a capital loss of the trust, and

(iv) each amount allocated to the employee or other beneficiary by a trustee under the plan in respect of the decrease in the value of property of the trust from its cost amount to the trust,

(d) the fair market value of property (other than money) transferred in kind to the employee or other beneficiary by a trustee under the plan."

That Section 147(10.1) should be added to Bill C-259 in the following terms:

"147(10.1) Where any property (other than money) has after 1971, been transferred in kind to an employee or other beneficiary by a trustee under a deferred profit sharing plan, the employee or other beneficiary shall be deemed to have acquired the property at a cost to him equal to its cost amount to the trust at the time of its transfer."

After lengthy discussion and the question being put, the Committee divided as follows:

YEAS—5 NAYS—10

The motion was declared *lost.*

The Honourable Senator Hays made the following motion:

"That all the recommendations contained in the first, second and third Reports of the Standing Senate Committee on Banking, Trade and Commerce respecting the Summary of 1971 Tax Reform Legislation, as tabled in the Senate, be submitted to the Minister of Finance for further consideration, and that appropriate action be incorporated in the legislation to be introduced at a later date in accordance with the undertakings of the Minister as given this day".

The question being put, the Committee divided as follows:

YEAS—17 NAYS—1

The motion was declared *carried.*

The Honourable Senator Grosart moved the following:

That Clause 52(5)(b) be amended to read as follows:

"52(5)(b) The beneficiary shall be deemed to have acquired the property at a cost equal to its cost amount to the trust at the time of the transfer".

The question being put, the Committee divided as follows:

YEAS—4 NAYS—10

The motion was declared *lost.*

Following further discussion the Honourable Senator Phillips moved that Clause 29 of the Bill be deleted.

The question being put, the Committee divided as follows:

YEAS—4 NAYS—10

The motion was declared *lost.*

The Honourable Senator Grosart moved that Clauses 69, 70, 91, 91(2), 91(1)(b), 127(1) and 212(14) be amended as contained in a document described as "Draft amendments, November 30, 1971" all relating to Bill C-259.

The question being put, the Committee divided as follows:

YEAS—4 NAYS—10

The motion was declared *lost.*

It was moved by the Honourable Senator Cook that the Bill be reported without amendment.

The motion was declared *carried.*

It was moved by the Honourable Senator Everett that the following Recommendation be included in the Report of the Committee:

"(1) That a method be found to deal with the subject-matter of the distribution of corporate undistributed income accrued subsequent to December 31, 1971, in a manner similar to the method proposed in Bill C-259 for dealing with corporate undistributed income accrued prior to January 1, 1972; and

(2) That the Minister of National Revenue give binding advance rulings on a written set of facts as to:

(a) the exercise of ministerial discretion under the Income Tax Act.

(b) As to whether a receipt would be an income receipt or a capital receipt under the Income Tax Act."

The question being put, the Committee divided as follows:

YEAS—13 NAYS—1

The motion was declared *carried.*

At 5:10 p.m. it was agreed that the Committee adjourn for approximately half an hour in order that the Acting Chairman and the Chief Counsel be given sufficient time to prepare a Draft Report for the consideration of the Committee.

At 5:40 p.m. the Committee resumed.

The Chairman read to the Committee a proposed draft report and after discussion and certain revisions having been made thereto, it was Resolved that the Report be tabled in the Senate by the Acting Chairman.

At 6:10 p.m. the Committee adjourned to the call of the Chairman.

ATTEST:

Frank A. Jackson,
Clerk of the Committee

Report of the Committee

Monday, December 20, 1971.

The Standing Senate Committee on Banking, Trade and Commerce, to which was referred the Bill C-259, intituled: "An Act to amend the Income Tax Act and to make certain provisions and alterations in the statute law related to or consequential upon the amendments to that Act, has in obedience to the order of reference of December 18, 1971, examined the said Bill and now reports the same without amendment.

Your Committee, however, considers it urgent that the following observations be made.

As a result of a reference to your Committee by the Senate on September 14, 1971, your Committee considered the Summary of 1971 Tax Reform Legislation and the Bill based thereon, being Bill C-259, which Bill received first reading in the House of Commons in June. The present Bill C-259, although amended in part, is in substance the same Bill which received first reading in June in the House of Commons.

As this Committee's first preliminary report states: "your Committee has heard a number of representations and has received a number of written submissions on the proposed legislation." As a result of its deliberations and studies your Committee submitted to the Senate its First Preliminary Report on November 4, 1971, its Second Preliminary Report on November 30, 1971, and its Third and Final Report on December 13, 1971.

These Reports include a series of recommendations for suggested amendments to Bill C-259. In approving this Bill today this Committee reiterates with the greatest possible emphasis that the recommendations for changes in the Bill as contained in these Reports, are of continuing importance and relevance.

Your Committee further recommends to the Minister of Finance and the Minister of National Revenue the following:

(1) That a method be found to deal with the subject-matter of the distribution of corporate undistributed income accrued subsequent to December 31, 1971, in a manner similar to the method proposed in Bill C-259 for dealing with corporate undistributed income accrued prior to January 1, 1972; and

(2) That the Minister of National Revenue give binding advance rulings on a written set of facts as to:

(a) The exercise of ministerial discretion under the Income Tax Act.

(b) As to whether a receipt would be an income receipt or a capital receipt under the Income Tax Act.

Your Committee, nonetheless, is of the view that the content and context of the Bill urgently calls for a series of amendments which will clarify and simplify certain sections thereof and excise others.

In view of the statements made by the Minister of Finance before your Committee on December 13 and this day, your Committee confidently expects that the Government will give meaningful consideration to the recommendations of your Committee in respect of Bill C-259 in amending legislation to be presented to the House of Commons as soon as possible in 1972.

It is therefore expected that the Government will give intensive and meaningful attention to the views expressed herein having regard to the important role that the Senate of Canada has played and is playing in the government of this country as one of its two constituent parliamentary Chambers.

Respectfully submitted.

John J. Connolly,
Acting Chairman.

Report of the Committee

Frank A. Jackson,
Clerk of the Committee

The Standing Senate Committee on Banking, Trade and Commerce

Evidence

Ottawa, Monday, December 20, 1971

The Standing Senate Committee on Banking, Trade and Commerce, to which was referred Bill C-259, an act to amend the Income Tax Act and to make certain provisions and alterations in the statute law related to or consequential upon the amendments to that act, met this day at at 10 a.m. to give consideration to the bill.

Senator John J. Connolly (*Acting Chairman*) in the Chair.

The Acting Chairman: Honourable senators, I am most grateful for your continued confidence. I note that the Christmas spirit has already taken hold of the Leader of the Government, and I hope that some of it will spill over on to everyone present.

We have before us Bill C-259, which has already been the subject of debate in the Senate. We are expecting to have the Minister of Finance with us this morning. He was to have been here at 10 o'clock, but he may have been delayed by the poor weather conditions. Meanwhile, we have with us Mr. Donald S. Thorson, Associate Deputy Minister of Justice.

Is it your wish to discuss the bill with Mr. Thorson prior to the arrival of the minister?

Senator Choquette: Mr. Chairman, I would like to make our position clear. We, the official Opposition, are a group of five or six here, and we do not intend to use delaying tactics. However, we should have a definite plan at the outset. For instance, I would like to know how we are going to proceed. Are we going to go over this bill clause by clause? Is there a deadline; and, if so, what is that deadline, or have we all the time we need?

The Acting Chairman: Of course, the chairman is always in the hands of the committee, but I think, speaking personally, that we should first of all hear from the minister, unless he is delayed; and if he is unduly delayed, that we should proceed in some other fashion. Thereafter, I think we should follow the usual practice of this committee; that is, that we should deal with any item or any part of the bill about which any senator would like to have some information.

In answer to Senator Choquette's other point, certainly there is no deadline. The committee will sit, as it always sits, until it finishes its work. I think we would like to do that with the usual expedition this committee has shown through the years.

Here is the minister.

Senator Choquette: Mr. Chairman, I am happy to see the minister here, but I think that if we start with the minister's evidence we are starting from the bottom and working upwards. I thought this was work for a committee. Since the minister is here, I expect we will have a definite commitment from him, but it may be that that is just wishful thinking for the moment. I am sure we will have a promise that some of our amendments, that were so well prepared under the chairmanship of Senator Hayden, will come in the form of a special bill as soon as possible. I am not putting words in the mouth of the minister, but that is my hope. So I am wondering if we should start with the minister.

The Acting Chairman: This committee has always taken the view that when we have a minister here, we hear him at his convenience. I would be inclined to deal with the minister's evidence at this time, if that is the wish of the committee.

Hon. Senators: Agreed.

Senator Beaubien: Mr. Chairman, just speaking for myself, I think what this committee would like to have is three very simple commitments. If the minister could convince us that for the good of the country this bill should pass before the end of the year, that would be a great thing for the Senate and would be a good thing for the country. After he has done that, if the minister would tell us that as soon as he found it practicable he would bring in a special bill, and that when he does prepare the special bill he will give full consideration to the recommendations of the Senate, especially with respect to our three reports, then, speaking for myself, I think that would help us tremendously in making up our minds on this bill.

Senator Benidickson: Senator Beaubien, I think you have made a very important point and it impresses me very much.

Senator O'Leary: I propose that we hear the minister first and then, when he has finished, we can cross-examine him, if he will permit.

Honourable Edgar John Benson, Minister of Finance: First of all, as you know, I was here last week and I reviewed generally the recommendations made by the Senate committee. I indicated that we had your reports and were looking very carefully at them. I indicated several areas where we felt that amendments were necessary, both along the lines that the Senate committee had indicated and in other areas. I indicated that we would continue

looking at them and that, indeed, we would bring forward an amending bill. We will bring in an amending bill. Some people object to my using the term "budget," but an amending bill of the Income Tax Act which will affect the balance of the Ways and Means is a budget, in effect. There are other ways of bringing it in. We can bring it in through a resolution and carry it along, but, in any event, we will bring in an amending bill to this legislation as soon as we possibly can. But this does not mean that we can promise that we can do it in January or early in February. There are very complicated matters involved in some of these amendments. For example, in the field of foreign income, I do not want to bring in amending legislation which again will have to be amended and will not solve the problems that we see. The problem of passive income, for example, which you dealt with in your report, is a very complicated matter which affects different companies operating abroad in very different ways. They are making representations to us, we are looking at these, and we intend to bring forward amending legislation. I have made that quite clear.

Why should the bill pass by the end of the year? First of all, I gave a good many reasons in the Commons, which I would be glad to repeat here, but, basically, if we do not pass this bill at the end of the year we are going to be in a period where people do not know what the law is. We have reached the stage now—indeed, a month ago we had reached the stage—where there is no question of splitting this bill. It is just not that easy to split the bill. People say that you can take out sections and do these things, but it just does not work that way. The legislation going through will provide tax relief for a great many Canadians. It will provide for the imposition of a gains tax for the first time in Canada. It will provide such things as higher exemptions, child care allowances, allowances for working people up to $150 a year, additional allowances for older people—a tremendous number of changes. It brings into income things that have not been included in income before, such as capital gains. It also brings in unemployment insurance benefits and a great many minor things that have not been treated as income before.

Also, if we do not have the legislation a hiatus period is created. In the Commons I pointed out that by the end of January, 1972, there will be about 15,000 corporations which will have completed their 1971-72 fiscal year, the one ending in 1972. By the end of February this will be close to 30,000 corporations. These companies would not know whether they should be reporting their income under the old or the new system.

Similarly, there are thousands of partnerships with year-ends that would fall into this particular period, and they would face the same kind of problem.

Difficult problems of administration would arise. For example, would it be open to taxpayers to assert that they had no liability in respect of a transaction or an event because the bill had not been put into effect? This could have arisen previously, of course, on a small scale when budgets were announced and the legislation was enacted some months later. However, here the problem is one of magnitude because the whole Income Tax Act has been changed.

The Acting Chairman: Can you give an example of that, Mr. Minister?

Hon. Mr. Benson: Well, a good example would be, supposing people wanted to distribute part of their accumulated surpluses. One of the alleviating provisions in the new act is that all surpluses can be cleared up to the end of December 31 by a payment of a flat 15 per cent tax and distributed tax-free to the shareholders. Now, supposing somebody had to do this because they needed the cash out, or they just wanted to go ahead and do this; the question is, which law applies—the old law, where half of it was taxable income and the other half was distributed tax-free, or the new law, where the whole thing is tax-free?

These are the kinds of decisions people have to make and their advisers have to make all the time, and this is just one example that comes very quickly to mind.

Another problem that would arise is what would happen in the case of interest paid by a corporation to purchase shares of another corporation. Would this be allowable or not? There are many business transactions of that kind. In the new act we are allowing the deduction of this kind of interest. So people will not know whether they should go ahead with the transaction or not. These are the kinds of difficulties that arise.

I mentioned the surplus account with respect to distribution. With regard to taxpayers making payments to non-residents, for example, which withholding tax rules apply? Under Bill C-259 there are a number of transactions, particularly in the corporate sector, which require that forms or the elections be filed with the Department of National Revenue. There would not be any election forms existing, if the bill was not proclaimed.

Those are just some of the reasons why I think it essential that people know what the law is and that the law go into effect on January 1.

I do not say it is going to be the end of the world if the bill is not passed by January 1, but I think it should be passed, if you can possibly do it with due dispatch. And in saying that, I am in no way indicating what the Senate should do or urging the Senate to do anything. What you do is entirely up to yourselves. I am simply here to try to answer questions.

Senator O'Leary: Mr. Minister, you used the words "tax relief." How is that going to be affected? It will not be affected, will it, if this bill is not passed?

Hon. Mr. Benson: There is another bill that I have to get through after this one, as you know. I have some tax reductions, outside of this bill, which started in June last. It is a very small bill; it is a relieving bill. That bill cannot be passed until after this bill is passed, because it amends this bill. That means that the tax relief I have given from last June until the present time for individuals and corporations is not really legal. It has been done before; but, goodness, it seems to me that before the end of this year or, at least, before the end of the session this has to be cleaned up in order that one legalizes the tax relief one has been giving to people.

You know, there is precedent for giving people tax reductions and carrying them on, but the question arises

as to how long you do this. If you are moving from January on and there is a completely new tax system, is it correct to change the amount of deductions from people? Indeed, some people will be paying additional tax, although the amounts are not very high—I think it comes to a maximum of $100, or something like that. The question arises: Is it proper to deduct the tax from these people? You can do it. Legally I think you can do it, but it is much better to have the law to support you, I think, than to just move forward in that way.

Senator Grosart: How soon after the passage of this bill, Mr. Minister, would you see that relieving act being passed—or being introduced, I should say?

Hon. Mr. Benson: This is very difficult. I did not want to tie myself down to this last week, and that was quite intentional. We are now working on the various problems that have been raised, some of them by the Senate committee and some by people outside. We have our people in the Department consulting with businesses involved, to see what can be done and what the various situations are. We will start writing legislation, but it is not a fast process. I have been through this once before, as you know, to develop this bill, and I know it is difficult. Many of the things, or at least some of the things, if the bill went through in February, March, April or May, would be effective as of January 1—for example, the decisions with respect to deferred profit-sharing plans which I indicated I was going to make. They would have to be effective as of January 1. But we will work ahead as fast as possible, senator, in order to produce a bill.

The Acting Chairman: Senator Grosart, you are talking not about the bill to reduce the taxes, to which Senator O'Leary was referring, but about the general amending bill?

Senator Grosart: Oh, no, I am not. I was asking how long after the passage of this bill, C-259, would the minister expect—and that is the word I used—to introduce the bill he referred to in reply to Senator O'Leary.

Hon. Mr. Benson: I will introduce it right away. It will not take any time to pass. You will have it this week, if you get this one through.

Senator Grosart: It is written?

Hon. Mr. Benson: Yes, it is written, and it is a very simple bill. It is simply reducing people's taxes, and there will not be many complaints about that; that is, unless they say that we are not reducing them enough.

Senator Grosart: And the amending bill, if I may call it that, is the bill that you said would come subsequently, perhaps in the spring. You have said, I believe, Mr. Minister, that that could very easily be retroactive in its effect to January 1. Would that not apply to Bill C-259?

Hon. Mr. Benson: Well, if you are making small or relatively small changes to the Income Tax Act, I think it is fine to make them retroactive, but when you are introducing an entirely new piece of legislation, building from the bottom up, then you really have no tax law if you do not have this. All you are left with of the old law is the title. Therefore, I think there is a difference in magnitude in trying to make this retroactive.

Senator Grosart: But the old act is not repealed.

Hon. Mr. Benson: No, the title is left; the only thing that is left is the title, and that is for technical reasons.

Senator Grosart: So what you are saying is that it is better to have a bad bill than no bill at all, and that it is better to have confusion and uncertainty with the bill than to have confusion and uncertainty without the bill.

Hon. Mr. Benson: Well, first of all, I will not admit it is a bad bill; it is probably the best piece of tax legislation in the western world. Certainly, I think it is useful to have certainty. There will certainly be amendments to this bill, and I think we will consider all the Senate committee recommendations. These are amendments which affect a very small segment of the Canadian population. These are specialized cases and specialized problems that arise, and I congratulate the Senate on looking into them and finding these particular problems, mainly in the corporate area, which affect a relatively small number of the Canadian population.

Senator Grosart: I cannot agree with you on that, Mr. Minister, because, certainly, in thinking of some of them which relate to our capability in export markets, I would say that it affects every Canadian perhaps even more significantly than the very helpful benefits there are in this bill. I do not think you really mean to say that the amendments, for example, which the Senate committee in Appendix "B" of its third report referred to as "top priority", are ones whose effects are confined to a small segment of the Canadian population. These top priority amendments affect the whole Canadian population. I do not like the suggestion that the Senate amendments are zeroed in on corporate benefits.

Hon. Mr. Benson: Well, I should mention, Senator Grosart, that I indicated when I was last before the Senate, a week ago, that I would be making changes which are rather broad in nature. Deferred profit-sharing plans and profit-sharing plans is one example that comes to mind. These have a broader application, but those amendments will be made, and they will be made presumably effective January 1. But if one gets into the area of foreign corporate operations, we asked for representations in this regard and we have less than a handful of representations from these corporations. So the number of corporations anxious about this is not really that great. We are trying to get them to come forward so that we can look at the various problems, and these problems do differ as between different types of corporations, how they operate, and so on.

Senator Grosart: I would suggest, Mr. Minister, that it is possibly a non sequitur to say that because you had representations from only five or six corporations this means that only a small number of corporations is interested. Of course, that is not so. It is normal in such cases for corporations to let one or two take the lead because they have the experts, the information and the available data to carry the ball.

The Acting Chairman: In that connection, Senator Grosart, I think we can say at this stage to the Minister that in our consideration of this legislation all fall we did not have too many representations from individual corporations, but we have had them from associations representing various industries like the pulp and paper industry, the construction industry and the petroleum industry, and there are ten or fifteen such organizations.

We have also had representations which apparently came from the corporate level but which do affect many individuals. For example, on the profit-sharing plans, and the deferred profit-sharing plans, those representations usually were made not by the beneficiaries under the plan but by the companies that operate the plan. The ramifications of the representations were wide, although perhaps it was put to us here from the corporate side rather than from the individual side.

Senator Grosart: Well, Mr. Chairman, you have still objecting to the bill the Retail Merchants' Association. At least they are objecting to some aspects of the bill and certainly to its quick passage. They could hardly be said to represent the big corporations; they represent everybody down to my barber and taxi-driver.

The Acting Chairman: We have had representations too, in the course of the fall, from the people who were very interested in the problems of small businesses and particularly businesses who want to qualify under the definition of the act as a small business with the $400,000 ceiling that the act proposes. We have heard a great deal about that.

Senator Grosart: Mr. Minister, we, as the Senate, are in a somewhat embarrassing situation in that we have a recommendation to the Senate from this committee that there are at least nine items—and I am sure you are aware of them—which are described as top priority recommendations. I think the assumption is that these are changes that the committee felt should be made before the bill is passed. I am sure you know the list to which I refer, and you gave us interesting answers. You are trying to work one out; you are looking favourably at another; and you are examining a third. The chairman reported that this does not mean that you will make a change. The chairman also reported to us, summarizing your reply in connection with one, and that is that all they are saying is that they are going to look around. Now, I do not want to be unfair. The chairman generally reported that you gave sympathetic consideration and some indication that at least some of them would appear or would be made effective in the amending bill. I want to say that I was very much impressed that you were able to go as far as you did when you were last before this committee, and I am in no way critical of the replies which you have given. I feel they were generous and that you were certainly trying to assist us in what I have referred to as our dilemma, and I believe it is a dilemma.

It has been said in the Senate and in press editorials that you have made no commitment.

Senator Beaubien: Just a moment, I think the minister made a commitment this morning.

Senator Grosart: Let me finish, please. It has been said that, firstly, you have made no commitment, and, secondly, that you were casual in your remarks regarding the fact that there is always an amending bill to a tax act. I am not saying this critically. Would you say that you have gone a little beyond that today by making a commitment to this committee that there will be a specific bill which will take into consideration recommendations contained in our report? I realize you cannot make a commitment on behalf of the Cabinet; at least, I do not think you can.

The reason I ask this question is that all honourable senators have actual draft recommendations made by this committee. You can help us in our proceedings by going further than you have. I feel we will have to look at this bill clause by clause, and I do not mean we should take every single clause and spend a lot of time on it, but we will have to look at each clause and determine how sensible this committee was in drafting these amendments—Do we abandon these amendments now? Perhaps you can help us on that. I do not mean abandon them forever. We have drafted amendments before us called "top priorities." What do we do with them?

Hon. Mr. Benson: First of all, I have indicated there will be an amending bill. I will not say that the amending bill will only cover your committee's recommendations.

Senator Grosart: No, we are not asking for that.

Hon. Mr. Benson: There will be an amending bill, as I have said before. Perhaps I have caused you some difficulty because I indicated it would be a budget; but an amending bill which affects the balance of Ways and Means, to my mind, is a budget. There will be an amending bill to the Income Tax Act.

Senator Grosart: Would you use the word "specific" in respect to recommendations which are already before you?

Hon. Mr. Benson: Yes, and also recommendations I may receive. We are seeking recommendations from industry and business in an attempt to solve some problems that have arisen, including the problems which you have mentioned. There will be a specific bill amending the Income Tax Act as it is amended by Bill C-259. I cannot be any more specific than that. With regard to timing, I feel I have gone as far as I can go. We have to work these items out and properly determine and insert these amendments.

Senator Buckwold: Will it be some time during the next year?

Hon. Mr. Benson: Oh yes.

The Acting Chairman: I am sure counsel for the committee, or perhaps members of the committee will correct me if I am wrong. What our Senate committee has given to the Government is a series of recommendations, and we have endeavoured to make concrete suggestions regarding the form of the amendments. We have listed some as being more important than others. I do not think the word "priority" goes any further than that. Senator Hayden's appreciation of this particular situation is important here. I do not want to engage in a debate regarding what amendments a Senate committee can make to a tax bill. However, Senator Hayden indicated that rather than have confrontation between the two houses on specific

amendments to a tax bill, what our committee should do is to make recommendations, and if the Government can accede to some of the suggestions made by the committee—perhaps they cannot accept all of them, and I think that is understandable—the amendments should not be made through the Senate but through the House of Commons. I think that is a practical way of looking at the procedure in connection with our treatment of a tax bill.

Having said that, perhaps what the committee meant by priority items emerges a little more clearly. Perhaps some honourable members of the committee assumed a different connotation of the word "priority". I put it to the committee that this is what we had in mind.

The Honourable Lazarus Phillips, Chief Counsel to the Committee: I think you are right, Mr. Chairman. I was working with Senator Hayden on the concept of priorities which related itself to the subject matter included in the recommendations rather than to the timing itself in terms of this bill.

Senator Grosart: Mr. Chairman, I do not know in what capacity you make that statement.

Senator Beaubien: I have two questions to ask of the minister,—

Senator Grosart: I am not sure in what capacity you have made that explanation. Certainly, it was not made to the Senate, nor was it part of the report of the committee. The words "top priority" are understandable English words. I feel it is quite proper to assume that "top" means "most important", and that "priority" means "items that go ahead of any others". I am not suggesting for a moment that you are not accurate in explaining the committee's interpretation of the word. However, this is not what the committee has reported to the Senate. I was not aware that the drafted amendments had been sent to the minister. I do not know by what procedure the committee sent these draft amendments to the minister, especially before they were reported to the Senate. However, that is another matter.

The Acting Chairman: Senator Hayden has ways and means of accomplishing certain things.

Senator Grosart: Yes, I am aware of that. However, there are rules which govern our behaviour.

The Acting Chairman: The very fact that the draft recommendations were put on the Senate record would necessarily ensure that they be given to the minister.

Senator Beaubien: And they were approved by our committee.

Senator Grosart: Yes, but there is no reference to the drafted amendments, and I want to point that out. There is a general description of top priority items. But several honourable senators had no way of knowing that these drafted amendments were communicated to the Government. That is not the issue before us. But I think it is important that we look very carefully at this bill with respect to the suggested amendments.

Hon. Mr. Benson: Regarding the nine or ten areas considered by the Senate to be of top priority—

Senator Benidickson: In the third report?

Hon. Mr. Benson: Yes, in the third report—we indicated that we had sympathy for some, accepted changes in other areas and that we would implement them. In other areas we indicated that we were considering them. Mr. Cohen and Mr. Thorson are here and will go through this specific area in detail, if you wish. They will be glad to point out some of the difficulties we encounter in making a quick decision with respect to them. I outlined this particular problem in a general way last week. One aspect is the matter of gifts in kind to charitable organizations, with reference to which we said we have great sympathy and think something should be done. However, we do not wish to get into a similar mess to that in the United States when they had to introduce massive legislation in 1969 to plug loopholes which were created. So we would do something about it, but must find a means of attempting to avoid such a situation. I am just picking this one out.

Senator Grosart: Well, Mr. Minister, I have no quarrel whatsoever with that. I was quite convinced myself that you need time. You made out an excellent case for it. There is no question that you need time perhaps to hear other representations and to integrate in the bill such parts of these amendments as you may find viable. I have no doubt about that; you do not have to prove it to me.

Of course, it does raise the question, if that is so, of why this bill must be passed by January 1. It is not for me to go back at this time to quarrel with the manner in which it was brought here, except to say that it raises an obligation for us in the Senate, in that it does not come to us as a vote from a free Parliament—I will put it another way, a free vote in Parliament.

Senator Isnor: What do you mean by that?

Senator Benidickson: What does that mean?

Senator Grosart: I did not wish to go into it, but I will. I am merely saying that with closure—

Some hon. Senators: Oh, oh.

Senator Isnor: What do you mean? That is a statement of your own view.

Senator Hays: I would like to hear your answer to the three questions raised by Senator Beaubien.

Hon. Mr. Benson: I think I did answer them.

Senator Hays: I thought you might go into them in more detail.

Hon. Mr. Benson: I went quite thoroughly into the reasons why the bill should be passed before the end of the year. Senator Beaubien asked only two questions. The second was as to how soon a bill to amend the Income Tax Act will be introduced.

Senator Beaubien: You covered that.

Hon. Mr. Benson: I think I covered that, honourable senators, as well and as reasonably as I can.

Senator Phillips: Mr. Chairman, I have two questions. The first relates to the priorities. The minister has indicated that some of the so-called priorities will be adjusted. There

are changes not included in the priorities which I would like to see included in the bill. Could you give some indication of the priorities which the Government will not accept?

Hon. Mr. Benson: I went over this in some detail last week when I was here. The nine that I had seen in the Senate report were: Gifts, Bequests and Devises to Charities, Employees Profit Sharing Plans, Deferred Profit Sharing Plans, *De Minimis* Rule, which is somewhat related to the Passive Income, Tax-Exempt Non-resident Investors, Non-Resident Owned Investment Corporations, Private General Insurance Corporations, and Deemed Realization on Ceasing to be a Resident of Canada. Those were the areas contained in the Final Report.

Incidentally, I think that this committee does not receive enough credit for the amount of study that it has devoted to the contents of this bill. I have been concerned recently by such statements as "Well, the Senate is only looking at the bill for four days." In my opinion, that is downgrading this committee, which has been considering the bill since September.

Hon. Senators: Hear, hear.

Senator Benidickson: This committee has been considering this bill for three months, not four days.

Hon. Mr. Benson: In my opinion, this committee has carried out a much more through study of the bill than some of those who have commented on it. It has produced three very useful reports and, indeed, for several months has been studying the contents of the legislation in great detail.

Senator Benidickson: Thank you very much.

Senator Phillips: My second question, Mr. Chairman, relates to the minister's statement that so many firms would be completing their taxation year in January, and in February it will increase to approximately 30,000. I am concerned by section 221(2), at page 545 of the bill. This may be strictly a legal and technical regulation which is provided for in the bill, but it causes me some concern in its wording:

> No regulation made under this Act has effect until it has been published in the *Canada Gazette* . . .

etcetera.

The point that bothers me is that it states:

> . . . a regulation shall, if it so provides, be effective with reference to a period before it was published.

There is no limitation on that period. It could be retroactive for five weeks or five years. My point is that I do not see how anyone can prepare a tax return without an infraction of such a section.

The Acting Chairman: The minister will read the clause.

Hon. Mr. Benson: Clause 221(2) provides:

> No regulation made under this Act has effect until it has been published in the *Canada Gazette* but, when so published, a regulation shall, if it so provides, be effective with reference to a period before it was published.

This has been in the Income Tax Act since the act was first enacted. As far as we are concerned, under the act the regulations will become effective as of the effective date of the act, January 1, except for certain regulations of a relieving nature which may have to be made in the early period. It is simply the method which has always been used. Sometimes on budget night the Minister of Finance states that the rate of depreciation on certain assets will be increased. The regulations are not published that night, but as of that night they will be effective. This may happen two or three months before the regulations are published, but they become effective as of budget night. That is the type of regulation covered by this clause.

Senator Phillips: The fact that I had marked it in the old copy merely illustrates that we did consider it.

Senator Buckwold: Mr. Chairman, what I have to say is probably a consideration of the role of this committee, rather than a question and I may be corrected by the minister if necessary.

First, we have been assured that the reasons are cogent that it is important for this act to become effective on the first of the new year; that the difficulties would be tremendous if it went on for some weeks after that time. The calendar year is important.

The second point is that we have been given an assurance that full consideration will be given to the amendments which have been proposed. It would seem to me that point No. 3 would be the continuing study of this bill, if necessary clause by clause, by this committee.

The idea that suddenly this committee is dealing with this whole bill in a few days is really not the case. It is a continuing study, one that will continue, I hope, by careful consideration on the part of this committee, and as further amendments are proposed they will be submitted, as have others, for full consideration in a continuing process of amending this particular act. Would that basically be the position in which we find ourselves?

The Acting Chairman: Perhaps that is hardly a question for the minister to answer. It might be appropriate if, on behalf of the committee, I say that we have had on-going studies on tax reform legislation, because we sat for an enormous amount of time on the White Paper. We then had, as the minister indicated, a very fruitful discussion during the fall on Bill C-259. Concerning amendments that will come to us in due course by a further amending bill, I am sure the Senate and the regular chairman of the committee will take whatever steps are necessary to ensure that this committee is seized of the subject matter of that new legislation.

Senator Buckwold: Are you suggesting that the committee would deal only with further amendments? I presume we would have a continuing study of the act.

The Acting Chairman: That is really a matter for the committee to decide. Usually it takes the lead from the permanent chairman of the committee.

Senator Cook: May I say to my colleague that the Income Tax Act is something like a subscription, in that there is always some new interpretation of it; it never stops.

The Acting Chairman: And there may be some new archaeological diggings that raise problems.

Senator Buckwold: I do not find the so-called pressure on the Senate to get the bill finalized intolerable. I am not suggesting that there is any pressure, but, in my opinion, the deadline does not mean that this is a finalized act so far as the Senate is concerned. We will continue to play our role in amending the legislation.

Senator O'Leary: This is not a question. This is a speech that the honourable senator is making. We heard all of this in the Senate the other night. I said some of it myself. We will never get through our work if alleged questions are turned into observations, which observations constitute a speech.

The Acting Chairman: I would ask honourable senators to observe the injunction of Senator O'Leary. In this committee we like to plot our way as we go along.

Senator Beaubien: I have prepared an imaginary portfolio. I have put down that a man has 100 shares of Bell Telephone, for which he paid $65; he has 400 Molson, for which he paid $7; and 400 IAC, for which he paid $9. At the moment, if the value date was today, on the Bell Telephone he would have a loss of $1,900; on the Molson he would have a profit of $4,400; on the IAC he would have a profit of $4,000. Supposing the man decided, after the bill came into effect, that he had to raise some money, and he decided that he wanted to sell the Bell Telephone. I would like to ask the minister, if the man wanted to sell the Bell Telephone—bearing in mind the fact that it is $46 today and he paid $65 for it—has he got to go back and take costs for all the stocks he holds, or is he free in every security to take either cost or valuation day value?

Hon. Mr. Benson: I will let Mr. Cohen answer that question.

Mr. M. A. Cohen, Assistant Deputy Minister, Department of Finance: Senator, on the figures that you have given us, if he sold all those securities . . .

Senator Beaubien: I said he was going to sell only one.

Mr. Cohen: You have asked the question whether or not he can take either market or cost. The bill is not drafted in quite that way. The bill says that taxpayers have a tax-free zone. They are protected on the gain side by the higher of market or cost, and on the down side we do not recognize a loss except to the extent it is below the lower of cost or market; in other words, if the Bell stock kept falling below the lower of cost or market. That is the way the scheme is developed for most taxpayers. It produces what we call the tax-free zone.

In some situations, taxpayers holding old securities, which they have had for a long period of time, or other assets, might not be able to establish cost on all of their securities or assets, and so we have an exception to the general rule. That exception says that if you choose, you can elect fair market value on V-day for all of your assets. I underline the word "all". You cannot choose fair market value on one asset and cost on another asset.

Senator Beaubien: That is in the regulation?

Mr. Cohen: No, that is in the bill. That is in the transitional rules, in Part III of the bill. It is not a choice between market and cost. You can elect fair market value on all of your assets or you can take the general rule, which is the higher of cost or market on the up-side and the lower of cost or market on the down-side. There has been a great deal of confusion over this question as to whether or not one had a choice. I suppose the reason why we do not have that choice in there is that it produces a random adverse selection for taxpayers. The tax-free zone should protect most taxpayers in most circumstances, and the fair market value rule is an exception that one can elect.

Senator Beaubien: Supposing he sells the Bell and has a loss of $1,900, and for some reason he is forced, after that, to sell the IAC, he would then have a gain of $4,000. How could he work out the grey zone?

Mr. Cohen: If he sells the securities at the prices you have indicated on Valuation date, in all three of those transactions he has no tax consequences whatsoever. He has no gain on the Molson stock or on the IAC stock, and he has no loss on the Bell Canada stock. Any transaction in the Bell Canada case between $65 and $46 is within the free zone.

Perhaps I could extend this for you. If he sold the Bell at $40, he would have a $6 loss, because he is down below the free zone. Similarly with the Molson stock, if he sold it at $20, he would have a gain of $2, being the gain that accrued after the $18 figure of fair market value. Any transaction between the cost and fair market value on Valuation day falls within the tax-free zone, is completely irrelevant, and has no tax consequences whatsoever.

Senator Everett: You have used the term "taxpayers". Do you mean it in that sense, or do you mean an individual?

Mr. Cohen: The election on fair market value, senator, is restricted to individuals.

Senator Everett: So in the answers that you have given you would preface the word "taxpayer" with "'individual' taxpayer"?

Mr. Cohen: Yes. We assume that corporations will be able to ascertain costs on all of their records.

Senator Everett: So they are into the tax-free zone automatically.

Mr. Cohen: They cannot get out of the tax-free zone rules.

Senator Everett: Does that also apply to personal corporations?

Mr. Cohen: There are no more personal corporations under the new system.

Senator Everett: I appreciate that, but there are under the old system.

Hon. Mr. Benson: It would include corporations where the majority of shares are held on behalf of an individual owner. The tax-free zone is fair, I think. The only reason for putting in the other option with respect to the market value of all one's assets is that some people may have assets that they just could not find a cost for.

Senator Beaubien: In grossing-up, Mr. Minister, you add a third of your Canadian dividends and then you deduct a third. Now, subsection 121 says that it is four-fifths. I realize that is in there because of the provinces, but how is someone living in Prince Edward Island, for example, where there is no such tax, going to be affected?

Hon. Mr. Benson: It is automatic under the draft act of the provinces.

Senator Beaubien: Are the provinces going to accept the act?

Hon. Mr. Benson: All of the provinces where we have tax collection agreements have agreed to take the personal income tax *per se*, so that you will get the full credit. The Province of Quebec will put their own act in, but I imagine it will be the very same.

We had to put it in that way in order to show the federal figures in the bill, but it will take care of the provinces as well.

Senator Grosart: May I ask a supplementary, Mr. Chairman?

The Acting Chairman: Yes.

Senator Grosart: Mr. Cohen, when you say "all assets," do you mean just that? You are not suggesting it would just apply to securities?

Mr. Cohen: Yes, sir, all assets, You make the election to go on fair market value for all assets.

Senator Grosart: So if you have real property—a painting or something—you must apply the same criteria all the way through?

Mr. Cohen: Yes, sir.

Senator Everett: Mr. Minister, one of the serious problems in the old act which is solved in the new act, is the right to elect to pay a flat rate of 15 per cent on undistributed income, thereby distributing corporate surpluses. That is valid up until December 31, 1971.

In the White Paper you recommended a means through integration which, perhaps, would make it possible in the future to solve the problem of corporate surpluses. I do not find anything in this present act that solves that problem. Have you given consideration to that? I am wondering if you will not find yourself in a position, say, ten years from now, where you will be confronted with all of the problems of the 1948 act in reference to surplus stripping and all of the manipulation that went on, and which you tried to solve by the flat rate of 15 per cent.

Hon. Mr. Benson: The problem, first of all, is basically one of private corporations. It has never really been a problem with public corporations because they never pay out their surpluses if they are widely spread.

The provisions in the act, I believe, are really quite generous in taking care of surpluses accumulated up to January 1, 1972. If we had full integration, then, indeed, the problem in the future would have been solved as well. You are quite correct in saying that there may be a problem in the future, but one of the things offsetting this problem in the future, I feel, is the limit of $400,000 at the low rate. In other words, in order to continue this on and get the low rate in the future, I believe—and this is just speculation—that people will pay out dividends in order to continue the low rate of tax. If they get to the $400,000 figure, I believe there will be an encouragement for distribution of surplus even though it may be loaned back to the company.

Senator Everett: Is that not based on whatever the difference between the corporate rate and the personal rate is?

Hon. Mr. Benson: And the low rate, yes. It may not solve all of the problems, but—

Senator Everett: If that difference is too wide, then is it not a fact that taxpayers will then elect to leave the money in? I am not saying that the taxpayer would be right or wrong in doing so. I am simply saying that the effect of the legislation will be that the taxpayer will leave the surplus in and when it builds up to a large enough amount you will again be confronted with the problem of how to strip off surplus and all of the difficulties that led to ministerial discretion. The problem of designated surplus will return to haunt us again, will it not?

Hon. Mr. Phillips: Senator Everett, you should remember the refundable tax of 33 1/3 per cent which is now applicable to private corporations. This will exert terrific pressure for distributing surplus.

Senator Everett: Not necessarily.

Hon. Mr. Phillips: Well, a refnudable asset against the Crown is not quite the same type of asset as a marketable bond.

Senator Everett: That is a very interesting argument, but it does not hold.

Hon. Mr. Phillips: No, but I am simply pointing out that it is an argument for distribution.

Senator Everett: But what you are pointing out, sir, is something that does not in fact hold, because it depends on the difference between the corporate rate and the end rate, which is probably the top marginal rate to the taxpayer. If that is great enough, it seems to me the taxpayer will elect to leave his surplus in.

Hon. Mr. Benson: the rates get very close, because after the $400,000 level, if one chooses not do do anything, ther is a 10 per cent differential, roughly, or 11 per cent differential between the corporate rate and the personal rate; it is 61.3 as compared to 50 per cent. In Ontario, it is 52 per cent.

Senator Everett: In the long run the corporate rate will be 46 per cent, will it not?

Hon. Mr. Benson: Yes.

Senator Everett: It seems to me it will be 46 per cent as compared to a top marginal personal rate of 61 per cent, and that is a difference of 15 per cent. Now, based on 15 per cnet, it is actually a difference of 30 per cent , is it not? In fact, you would ohave to take 15 per cent of 46 per cent which amounts to about a 30 per cent surcharge.

Hon. Mr. Benson: Full integration would solve the problem, but we have not got full integration. I might add that the Senate recommended against full integration. We have a continuing problem, but the problem, I believe, is not as great as it is at the present time, although a problem could develop.

Mr. Cohen: I wonder if I could add one other feature. In addition to the 61 per cent top rate and the point which Mr. Phillips makes with respect to the investment income being available for refundable tax, there is a third factor here which should take some of the pressure off, although I agree with you that in the end it may build up again. Under the old system you had to take your earned surplus out before you could get out your capital gains or any other non-earned surplus. We have now turned the act on its ear, in a sense, and we now permit corporations to distribute these capital gains and anything else that is not earned surplus first, without any pressure to take out the earned surplus in the initial instance. A great part of the problem—not all of it, I quite agree, but a great part—was the possibility of a large capital gain getting trapped in behind a significant amount of earned surplus, and in order to get at the large capital gain you had to clear your earned surplus. That built up the pressures. I submit to you that in turning this thing backwards, in permitting capital gains and paid-up stock to be redeemed free of tax at least some of the pressure to distribute surplus will be relieved.

Senator Everett: On the other hand, Mr. Cohen, it may work the other way around. One of the pressures to get the earned surplus out is the fact that there was a large capital surplus sitting there, and the taxpayer might very well pay the penalty on the earned surplus to get out the capital surplus. Under the new act he does not have that incentive. Admittedly, there is a limited integration, but the danger is that the provincial governments, in adding tax points to the personal rates, can make that integration largely ineffective.

The Senate report, indeed, did come out against integration, but it also recommended some means of solving the on-going corporate surplus problem. If I have any disappointment with this legislation it is that the very problem that probably more than anything else caused the act to be reviewed in the first place is still with us.

Hon. Mr. Benson: The first investigation of how to do this, as I can recall, started with the Rowell-Sirois Royal Commission back in 1941.

Senator Everett: That is before my time.

Hon. Mr. Benson: And we still have—and I do not like this fact—ministerial discretion in the act with regard to distribution. The reason we had to leave it in was because of the problem you are raising.

Senator Everett: That is correct.

Hon. Mr. Benson: I just do not think there is any easy solution to this problem except integration. There is no other way I can think of that you can get through the corporate surplus problem and have an ultimate solution to it, except through integration, and we just do not have integration.

The Acting Chairman: Which we rejected.

Hon. Mr. Benson: It is just that many people were not in favour of integration. We listened to them and came up with a different dividend tax credit.

The Acting Chairman: This is a highly technical area, of course, as Senator Everett recognizes. I was just speaking to our counsel, and I know we discussed this at great length during the fall study, and while we made no specific recommendations on it, perhaps we did it for the reasons that have been emerging here.

Hon. Mr. Phillips: We made the first move by the suggestion that we dispose of designated surpluses, so it would at least simplify the structure with respect to surpluses by its elimination, which would be a very important step in the right direction. That is one of our major recommendations. That is not so much an ad hoc recommendation in respect of any particular category of taxpayers, but rather going to the, shall we say, basic philosophy of the bill, such as consolidations, extension of roll-overs, and elimination of designated surpluses, all of which this committee thought, if approved, would clarify the statute considerably.

Senator Benidickson: That was one of your main points.

Hon. Mr. Phillips: That is right; it was.

Hon. Mr. Benson: Designated surplus is still a problem which I have indicated we have to study. Unfortunately, when we had full rate gains tax it was easy to get rid of designated surplus. Once you move to a half rate gains tax you have great problems in getting rid of designated surplus.

Hon. Mr. Phillips: For whatever it is worth, now that I have the forum, I think if we have relief in the amending statute on consolidation, elimination of designated surplus, extension of roll-overs, and provision on capital gains, we will have a statute that we will not recognize. The baby will be consideraly improved in terms of beauty.

The Acting Chairman: It will have a nice complexion. Senator Everett, had you finished?

Senator Everett: Well, I think that is very interesting, but I believe the Honourable Mr. Phillips has indulged in a diversion. I still come back to reiterate that point, Mr. Minister. You have the problem of undistributed income, and that problem will build up again, because it really is not going to bother the taxpayer; he will allow his surplus to build up, and he will save the tax. He will wait for the day when some method of distribution, such as an Ives Commission or the flat 15 per cent tax on undistributed income offered by C-259, is made available to him. All I say is that it is unfortunate that you have not, at this stage, nor apparently has this committee, been able to solve that very difficult problem, which has led to all sorts of problems, such as ministerial discretion. It is not the entire reason for ministerial discretion, but it is to a large extent.

I am a member of this committee but, unfortunately, I was tied up with another report and was not able to attend the meetings on the subject. However, I do not glean anything from the report of this committee to indicate that

this matter was really that seriously considered, so I raise it now as something that I think the minister, in his wisdom, would be wise to give very serious consideration to.

Hon. Mr. Benson: I am willing to have any representations made or any ideas you may have in this regard. We just have not found a solution to it, and neither has anyone else—provided you do not have full gross up in credit. That is the only solution that has been found to it since 1941. It was decided not to proceed along that line. We have the problem, and I would like to know a solution. Indeed, I am sure that a great deal of time and effort will be put forward in the future towards finding a solution to the problem, but there just is not one at the present time that I know of.

The Acting Chairman: Have you finished, Senator Everett?

Senator Everett: Yes, thank you.

Senator Hays: Mr. Minister, the first recommendation this committee made in its first report dealt with capital gains on farm land. I would just like to make an observation before I ask you a question. In Canada we as agriculturists, due to our geography, have to be much more efficient than people who are permitted to ship food into Canada without tariff, or with very little tariff. In Canada we have at the very best 150 frost-free days. In the areas where we produce most of our grain we are down to 100 frost-free days. Of the ten developed nations, I think Canadians enjoy probably the cheapest food. We get very little subsidy. We compete on an open market with most of our exports. We buy on quite a protective market. I think of the beef situation, where we have been an importing country for most of the last 18 months, whereas we should possibly be an exporting country.

If we have a capital gains on these farms when they are turned over to a son, it seems to me that the Canadian people will have to pay more for their food. We buck quotas; we buck complete prohibition. For instance, we are not allowed to ship a pound of wool to the United States. We are allowed to ship only a million pounds of cheese to the United States, and you were there when we negotiated that. We used to ship over 50 million pounds. We are locked in at 30 million pounds to Britain. This is the situation in which the farmer finds himself. You are the Minister of Finance, and you know that those who pay income tax are a very small group. We have suggested that there should be no capital gains on farm land, and if there is there should be a roll-over for bona fide farmers.

My first question is: Are you going to give consideration to this or not?

Hon. Mr. Benson: What we have done in the bill is to eliminate death duties and gift taxes as far as the federal Government is concerned. The provinces may impose some, but if they just go to the levels they were at before, our calculation was that roughly the elimination of our death duties would offset any gains tax that had to be paid. Gains tax will start from this point forward, and it will be quite a long time before it accumulates to a lot of money.

What we have also done, after some discussion in the other place, where this matter was discussed fairly thoroughly, I think, is to provide in the bill, or should I say intended to provide in the bill, a period for payment of the gains tax on death. There is the exemption, as you know, of $1,000 a year, plus the cost of the residence, or the alternative of having the residence and a portion of land free, so that is taken out.

Senator Hays: May I just ask one question on that point. What good is the house 50 miles from the city if you do not have any farm land?

Hon. Mr. Benson: I agree. You have got the exemption; it is built in for the principal residence. If there is a house on the farm you can add $1,000 a year to the value of the property. Our present feeling with respect to it is that we could not provide an exemption from the gains tax, but we could provide a period of payment of six years. That did not get into the act ultimately as an amendment, because of procedural difficulties. We intend to put that into an amending act, along with some of the Senate recommendations.

Senator Hays: How did you arrive at six years? Why not 25 years?

Hon. Mr. Benson: It was the same period as allowed under the Estate Tax Act.

Senator Hays: Would the Government give consideration, if they do not see that they can live with eliminating the capital gains tax, to making this amortization over 20 or 25 years?

Hon. Mr. Benson: It might do so. This is subject to amendment, Senator Hays, in the future. The problem is that if you get into too long a period of time and apply interest rates to it, it becomes much more costly to the person. Generally speaking, people do not want to spread the period over that long, because of the increase in cost.

I believe this is an area, the area of farm land, in which there will be many representations in the future. The difficulty is that if we exempt one asset from a gains tax or something else, it makes it terribly advantageous to get into that particular type of asset. Then people who are not necessarily interested in farming, but who are not interested in gains tax, will get into that particular type of asset. We have it in homes now, where there is exemption provided in the act for a principal residence. For people who do not want to pay gains tax, there is a great advantage in getting into that kind of investment and increasing the value of it so that there is a gain accumulated.

I was talking with one former Secretary of the Treasury in the United States and he said he started out with a modest home and now he has reached a $150,000 apartment in New York City and he cannot afford to get rid of it.

Senator Hays: What happens to him when he dies?

An hon. Senator: He will not worry about that!

Hon. Mr. Benson: This is what a gains tax does when these things are gains free. It encourages people to buy expensives homes.

Senator Hays: What is the difference between a home in the city and a farm in the country? This is the farmer's whole livelihood. The first exemption was homes, before the bill got to the House of Commons. It was not going to be included. It seems to me that the family farm we talk so much about is the home; the home is no good without the land.

Hon. Mr. Benson: You are really taking two things. You are taking the home as a personal asset where you live, and the farm land as a business asset. One can argue that if it is a business asset it is to produce income and it should be as much subject to gains tax as a garage or a grocery store making income for an individual person, which would be subject to tax.

Senator Phillips: Mr. Chairman, I should like to raise a point of order. I understand we started out in a very indefinite way as to the manner in which we intend to proceed. I think we should decide now on this. I am very interested in the question Senator Hays is asking, but if we keep waffling from corporations to farms we will not get a very thorough examination of the bill.

The Acting Chairman: It seemed to me that the sense of the committee was that while we have the minister here we should have as many, even wide-ranging questions as the members of the committee would like to put. Then, if further clarifications are required on this or on any other point, most of them could be dealt with by the officials, who will remain when the minister has to leave us.

Senator Phillips: We will still have an opportunity to go through the bill clause by clause?

The Acting Chairman: Yes, indeed.

Senator Phillips: I am satisfied with that.

Hon. Mr. Benson: Both of the officials who are here—Mr. Thorson and Mr. Cohen—will stay and deal with individual clauses. They cannot deal with policy matters, of course, as they are matters for Government decision, and that is basically why I am here.

The Acting Chairman: The committee makes that distinction all the time.

Senator Lawson: I have a brief point I wish to raise while the minister is here. I raised it the other day, and I might have caused minor confusion. The question relates to trade unions. Subsequent to my raising it, Senator Martin was kind enough to arrange a short meeting for me with Mr. Cohen, so that I could explain it to him. He said it had not been raised before.

Mr. Minister, the point is that under the present act, under the present regulations, there is no reference whatever to trade unions. By that I mean trade union representatives as a classification. When we deal with it from a tax point of view, the only category they can fit us in, they tell us, is that of salesmen. It bears no relation to that activity. One could probably make as good a case for having them classed as professionals, other than giving up their amateur status, as you could for making them salesmen.

When we are talking about expense allowances, *per diems* and so on, that are related to the particular occupation or job or profession of trade union representatives, they may be allowed at the discretion of the tax department in one province, but will be just as quickly disallowed in another province. If we can make a case that there should be separate classifications, either in the regulations or by a specific future amendment, it would satisfy my desire in this regard. Is there anything to prevent such a specification or classification? It would serve two purposes. It would avoid the confusion we are now faced with by different decisions in each province; and, secondly, it would avoid any abuse that may arise as a result of the confusion.

Hon. Mr. Benson: As a matter of fact, this is the first time that this matter has come to my attention. I see no reason why we should not look at it and see if there is any way that we can define it within the law. If you call it a profession, you might lose your amateur status. We will be quite willing to look at this and see what can be done about it.

Senator Lawson: I am satisfied with that. I did not want any confusion. I think some people thought that I was speaking about members. I think you have covered the question of trade union members, but not that of trade union representatives.

Hon. Mr. Benson: We will be glad to look at it.

Senator Grosart: Mr. Chairman, I have two questions for the minister and I think they are policy questions. One arises out of the recommendation of this committee and its report on the White Paper. It is pretty well carried through the discussions. The recommendation is that co-ordination with the provinces be improved. We seem to have evidence that five provinces have asked for a delay in the implementation of the bill. It seems to create serious problems for them. I have no doubt there are pros and cons, but would you be good enough to indicate the two sides of that problem?

Hon. Mr. Benson: As far as co-ordination and consultation with the provinces are concerned, the income tax changes are probably the best example of consultation that has existed since I have been around here. On no other particular subject can I recall so many consultations and discussions with the provinces.

Of course, we ultimately get down to the point where we have to proceed with law. It has been a long process and we have been talking about it for a long time. At that time, when we have to proceed with the law, people often say that it would be easier to put it off, and, of course, it always is easier if we put things off. However, the provinces have come to the stage where they have all agreed to proceed with the same income tax legislation and they are going to enter into tax collection agreements—that is, all except Quebec—and, basically, they will enact the same income tax legislation as we have.

In the case of corporate tax legislation the provinces, other than Quebec and Ontario, have accepted it. Quebec and Ontario have their own taxation laws, which presently differ in minor degrees from the federal law. As a matter of fact, it used to differ a lot more in Quebec, but ultimately they have to get together, it has to end up in the same

way. They are proceeding with their corporation law, and the basic principle is the same as federal corporation law.

In the case of Ontario, they are going to consider continuing with the present law at the present time, but they will be able to enact new law very soon, closer to the federal law, because it would facilitate the operation of corporations in Ontario.

I think there have been co-ordination and co-operation as much as physically possible in this particular instance. Of course, you never get legislation, particularly tax legislation, with which everyone will agree. Indeed, I can think of things that I would disagree with if I took a look at the tax law as it is presently worked out. But I do think that a good deal has been done in producing this legislation to try to go along with the provinces in areas where we could. Integration was one obvious area where we went along, because it was an area the Senate disagreed with us on. The provinces had some qualms about integration. We talked about it, and the Government decided to move out of the area. Similarly, there are a great number of other changes that took place because of consultations with the provinces.

Senator Grosart: I think the committee, in using the word "co-ordination rather than "co-operation" in our consultations, was thinking of integration in a different sense than we have been using it. We were thinking of integration of the eleven sets of laws.

Hon. Mr. Benson: Canada has the most co-ordinated personal and corporate income tax law of any federation in the world—much more so than the United States. The personal income tax law across the whole country, with a few exceptions in Quebec, is the same. In the corporate field up until the present time, before adjustments have taken place, virtually the same corporate law applies across the whole country. So there is great co-ordination, I think—more than in any other country.

One of the things in tax reform that we are trying to maintain is co-ordination so that there will not be varying laws on personal income tax and corporate income tax in the various provinces.

Senator Grosart: Do you see a problem arising in the estate tax field?

Hon. Mr. Benson: We have not had the same success in co-ordination there as in the other fields, because we have had the federal estate tax, which applied to most of the provinces, and then there were three provinces, Ontario, Quebec and British Columbia, which had quite different succession duty acts. Then we had one province, and later two, that decided to get out of the succession duty field entirely. So we were developing into a kind of tax system in Canada which I did not think should be run by a federal government.

Senator Grosart: A tax incentive system.

Hon. Mr. Benson: And I encouraged them to get together and have a similar law. If they had had a similar law, or if I had seen any possibility for this in the long run, we might have continued with a single death-duty system across the country. But the federal Government cannot be involved in tax laws where the provinces decide to go their own way and where you have very different treatments in areas in which the federal Government collects the taxes, and in areas in which the provinces collect the same taxes. If four or five of the provinces get together and want a common succession duty act, as I am sure they will, we will help them administer it and will help them to get going on it. But I think we are out of that field to stay.

Senator Grosart: My second question refers to the problem of tax treaties. It has been said that it seems unfair to certain taxpayers to be penalized in circumstances where the federal Government has been unable—I will not say "unwilling"—to conclude a tax treaty. Do you see any way out of that by which, where a tax treaty has not been concluded between Canada and another country, some relief could be given to those who would seem to be affected in a very unfair way by a tax measure that is completely beyond their control to influence or even live with?

Hon. Mr. Benson: First of all, the effects of a differentiation in withholding tax treatment, for example, will not take place until 1976. This was intentional because we want tax treaties with the major countries of the world. Indeed, I think by that time we will have tax treaties with the countries where Canadians do business.

One of the reasons for putting the differential in was to urge people in other countries to have tax treaties with Canada. We find, generally, that our Canadian corporations, for example, and individuals are treated better in countries where we have tax treaties than in countries where we do not have tax treaties. So we are trying to put pressure on people to have tax treaties with us.

If there are particular problems, the Government will have to deal with them as they occur. Indeed, a few have been brought to my attention already, and we are trying to deal with them. Because the people involved have to plan beyond the 1976 period, we are trying to see what we can do in order to facilitate assistance to them.

It is not in any way intended to penalize Canadian taxpayers. The provisions are put in there in order to encourage other people to have tax treaties with us so that our taxpayers can be fairly treated. That is the angle.

Senator Grosart: But if they are not, do you see any method of resolving the problem in the interests of those who might be adversely affected?

Hon. Mr. Benson: Certainly. Of course, the Government can resolve the problem, if it wants to, at any time. You could put a fairly simple change in the act, if you wanted to, by putting in exceptions or that kind of thing; or you could do it in the regulations.

Senator Grosart: Would you say, in your view, that the Government would, or will, do so?

Hon. Mr. Benson: That would be a very dangerous thing for me to say, because I want to put pressure on these fellows to give us tax treaties.

Senator Everett: Mr. Minister, with respect to these amendments which you propose in the new budget, do you intend that some of them will be retroactive?

Hon. Mr. Benson: Yes.

Senator Everett: This question probably has been asked before, but for my own clarification, if a taxpayer moves under the present act and if, subsequent to that, you bring in this legislation which is retroactive, presumably in law he will be affected by the retroactive legislation. Yet, on the other hand, he will have moved on the basis of legislation as it has been passed and exists at that time. Have you any policy or provision to take care of that situation?

Hon. Mr. Benson: The amendments that we are presently thinking of, including those recommended in the Senate committee reports, are just about all relieving provisions. Any retroactivity would be a relieving retroactivity rather than the imposition of an additional burden on taxpayers. Anything that is tightening will not be retroactive.

Senator Everett: Will "not" be retroactive?

Hon. Mr. Benson: That is right. Anything that is tightening will not be retroactive. Relieving provisions might be retroactive until January 1, if it would be advantageous; if it should be done.

Senator Everett: So, then one could say that retroactivity will not affect any taxpayer adversely who takes advantage of the present act.

Hon. Mr. Benson: In the areas involved.

Senator Everett: Oh, yes, of course. Well, are there any other areas?

Hon. Mr. Benson: Well, you know, I cannot think of every situation, Senator Everett.

Senator Everett: No, but I am talking about a general question.

Hon. Mr. Benson: Well, as a general principle, you do not put in retroactive legislation that increases the tax burden. That would not be our intention.

Senator Everett: Thank you.

The Acting Chairman: Mr. Minister and honourable senators, I should like to ask a question for myself, if I may, as a member of the committee.

A few days ago, Mr. Minister, a number of senators received a delegation from an organization called the Montreal Property Owners' Association. I undertook to raise this matter in the committee and I spoke to Mr. Cohen about it. Their problem is in connection with depreciation on personally-owned property as against corporately-owned property. The corporate owner apparently is entitled to take depreciation on real estate while the individual with personnally-owned property does not have that advantage. I undertook on behalf of the senators to raise these points with you in the hope you might have something to say about them.

Hon. Mr. Benson: I have not gone into that and, in fact, have just read a note from Mr. Cohen about it. So, since you discussed the matter with him, perhaps I could let him answer it.

The Acting Chairman: Perhaps I should say that the senators directed that, if possible, one of the officials from the department should come, and he did and he reported that to Mr. Cohen as well, so now perhaps we could go on from there on this specific point.

Mr. Cohen: As I understand it, what the property owners asked was, firstly, that rental losses created by capital cost allowance should be deductible against any other income of the individual; and, secondly, that individuals should have the same privilege as real estate corporations to deduct rental losses against other income.

Here I have to move into policy discussion and say that the Government has taken the view that capital cost allowances should not be permitted to produce losses which can be offset against other income. That, I suppose, is the basic policy position and its purpose was to curb the so-called abuse of the system whereby many, many people were sheltering all kinds of income under the umbrella of excessive capital cost allowances.

That is the Government's policy, and it has struck to it, with one particular exception, and that is in the case of the integrated real estate corporation. There we have a provision to the effect that if you are what we would loosely call an integrated real estate corporation, then you can take those capital cost allowance losses and offset them against other business income.

That does not extend to an individual for three reasons. First, most integrated real estate developers are incorporated. Secondly, I think what the urban league was talking about was the ability to set these losses off against other investment income. Thirdly, on a practical level, it is rather difficult for the Department of National Revenue to administer a system which would involve ascertaining what the principal business of an individual is. It is much easier to contain and define and administer that kind of concept in the case of a corporation, and anybody who has more than one principal business will be able to isolate his principal business of real estate by setting up a corporation. That becomes very tricky when you get involved with individuals, because there you are talking of branch operations as opposed to separate corporate entities. So I do not think the Government could assist the league in regard to their requests without upsetting the basic policy question, and I will leave it to my minister to speak to the basic policy.

Senator Bourget: And in that policy there is no change, I think, from the old bill?

Hon. Mr. Benson: There is quite a change. One of the things we decided to do was to stop people who had a high personal income buying an apartment building and not paying any tax. It was possible for somebody with a $50,000-a-year income to take depreciation on an apartment building in which he had made an investment and to write off his entire income and pay no tax. We thought these two should not be combined, and the law is designed to prevent that. I gather the urban league disagrees with this, and I disagree with the urban league.

Senator Hays: On the question of the distribution of capital gains tax—and I do not know if the Government has dealt with this—will it be Government policy to distribute a certain amount of the capital gains tax, just as they have done with the estate tax?

Hon. Mr. Benson: To the provinces?

Senator Hays: Yes.

Hon. Mr. Benson: Yes, it will be shared in the same way as other income. The capital gains tax will be distributed in the same way as the personal income tax, because it forms part of personal income, and this works out at 77 per cent to 23 per cent for the provinces basically.

Senator Hays: The provinces will get 23 per cent of the gains and the federal Government will get 77 per cent?

Hon. Mr. Benson: But the provinces can still keep their own succession tax and estate duties, if they want to, and get the same amount of money, and the overall tax burden would roughly not be any greater on the taxpayer.

Senator Hays: I think you had a rough figure as to what the amount of capital gains tax would be by 1974.

Hon. Mr. Benson: We have never given this.

Senator Nichol: I am not a member of the committee, as you know, but I have some questions I want to ask anyway. How many people are coming off the tax rolls as a result of this bill?

Hon. Mr. Benson: Here we pre-judged what was going to happen through some of our actions last June and December, and the figure is that there would be one million people off the tax rolls and something like 4.7 million people paying less tax under the new system. No married person with salary income would have additional tax—that is, married people deriving their income from salaries, no matter what their level—and those filing as single people with salary income would not have any additional tax up to $8,000, and the calculation was, before some amendments in the bill, that the maximum would be about $78. I cannot say exactly what it would be at the present time.

Senator Nichol: Then, assuming that one million people were dropped from the tax rolls, that figure is a balance sheet figure which means that at a certain point in time it will be reduced in absolute terms because of inflation, since you are dealing with real dollars and they are dealing with flexible or rubber dollars. Therefore, the figure will be reduced in relative terms by population growth, so that that figure, as I say, is a balance sheet figure at the time you put it in.

Presumably you can correct this by changing your exemption rate over a period of time. Do you have projections on this? How long will that figure of one million last? And, secondly, how do you measure what is a desirable level in this field as to who gets exempted and who does not?

Hon. Mr. Benson: First of all it is very difficult to pick a desirable level. We have tried to go as far as we could, through the increase in exemptions and additional allowances, to get the people at the lower end of the roll off, and this is how the million is calculated after these things to into effect.

Certainly, as the private income of individuals goes up, if it goes up through inflation, they will have a higher dollar income, and unless the exemptions and rates are changed, more people will come on the tax rolls. There is a provision in the act to reduce the tax over the next five years, that is, the federal tax at any rate, which would tend to relieve the burden on individuals. We have not worked out the exact balance as yet. Indeed, I do not think there is an exact balance. There is a decrease in personal rates at the bottom of the scale which is built into the legislation over the next five years.

Senator Nichol: I am concerned that the benefits remain benefits, and that they do not become dissolved through inflation and population growth, et cetera.

Senator McElman: Mr. Minister, is that figure of 4.7 million inclusive of the one million who will come off the rolls?

Hon. Mr. Benson: No, it is a total of 5.7 million. These are ball park figures.

Senator O'Leary: Mr. Chairman, God forbid that I try to filibuster the work of this committee. I wonder if I could work as a reporter for a moment and, through you, ask the minister a question before he leaves. I hope he will remain for a while longer. May I ask what, in the name of God, happened in Washington last week? As I read the press the surcharge is being lifted, is that correct?

Hon. Mr. Benson: Yes.

Senator O'Leary: Do you mean today, tomorrow, or next week?

Hon. Mr. Benson: He said it would be lifted this week. Apparently, it takes a day or so for presidential action. But the decision was made on Saturday at the Group of Ten meeting, where currency re-alignment was decided, and the communiqué indicates that at the same time the surcharge and discriminatory features of the job development tax credit will be lifted.

Senator Cook: Are congratulations in order?

Hon. Senators: Hear, hear!

The Acting Chairman: I think we should inform the minister that during the course of our discussions last fall we spent some time talking about the effects of the American economic policy. Our committee is very interested in the subject which Senator O'Leary has raised. And if it is the desire of the committee, would you be willing to report, to use Senator O'Leary's words, on some of the highlights of the Washington meeting? Is that the desire of the committee?

Hon. Senators: Hear, hear.

Hon. Mr. Benson: It has been a long process since the surcharge was put on in August of last year. Shortly after that, we had the first Group of Ten meeting in London. At that time I was chairman. Secretary John Connally, through the process of rotation, became chairman in Washington, and then we moved on to Rome, and then back to Washington on Saturday. During this period, members have been putting forward their cases, both privately and publicly, regarding the type of adjustments which they felt should be made. Our position throughout

the entire period was that we should maintain a floating exchange rate for the present. Some members had other ideas, but this was the nub of the discussion as we moved along.

There were several problems discussed at our meetings on Friday and Saturday. I do not want to point out individual countries with regard to the settlement of their exchange rate. There have been sizable adjustments since last March. For example, the Japanese rate of exchange has gone up 16.9 per cent, and the German rate has increased over 13 per cent. We maintained that we had taken a good deal of the burden through the action which started in May of 1970, and we had seen a gradual increase in the Canadian dollar vis-à-vis the United States dollar, and the market was basically determining the value of our dollar on the free market. We maintained that we should not be required to make further adjustments on a fixed basis, but that our currency should be allowed to float.

After some discussion, and at times it became very heated, the Group of Ten finally agreed to the position that we should continue on a floating exchange rate and that other currencies would be pegged at a much appreciated rate vis-à-vis the United States dollar.

Senator O'Leary: Is Secretary Connally going along with this?

Hon. Mr. Benson: This is the decision of the Group of Ten, and he is the chairman. This is contained in the communiqué of the Group of Ten. I feel this is fair to Canada.

I want to point out that there are no commitments involved in this action. I was rather annoyed last evening when someone referred to a matter being put under the table. We have no commitments other than the commitment which we have had from the beginning, which is to continue discussions with the United States regarding irritant points which arise between the two countries with respect to trade. We intend to continue these discussions. I feel we should develop as good a relationship as we can with the United States, and that we should get these irritant points settled. However, we have no commitments.

Senator O'Leary: Will there be an announcement from Washington when that surcharge is lifted?

Hon. Mr. Benson: Yes. As a matter of fact, it was stated in the communiqué that in consideration of the agreed immediate re-alignment of exchange rates the United States agreed that it will immediately suppress the recently imposed 10 per cent import surcharge and related provisions of the job development credit.

Senator Isnor: I think that was announced this morning on the eight o'clock news.

Senator O'Leary: I do not listen to the eight o'clock news.

Senator van Roggen: You have mentioned irritants, and I vividly recall that when the auto pact was brought in in 1964 or 1965 we were attempting to obtain an equilibrium between the two countries with regard to auto parts. Some people are now saying that we are giving things away to the United States. It seems to me that we are not giving anything away, if it is out of balance in our favour.

Hon. Mr. Benson: There is a great misunderstanding with regard to this. I am not dealing with the trade end of the matter—basically, that is the job of Mr. Pepin—but there has been a long discussion regarding the automotive pact, and this is one of the irritants.

The automotive pact was signed with the United States. There were transitional provisions made in it, and they guaranteed the level of production for 1964. The United States maintains that, since our production is higher by $1 billion, the 1964 level should no longer apply. If one takes a practical look at the situation, it is not much of a safeguard. We are at a figure of $1 billion above that level at present. However, this is not my area of concern and I do not wish to get into a discussion on this matter. Mr. Pepin is negotiating with the United States, and we have not agreed to any proposals on the trade end. There are to be continuing discussions, and that is Mr. Pepin's responsibility. I got rid of the surcharge and he can look after this matter, which we have always maintained was not attached to the surcharge *per se.*

The point I am trying to make is that in our negotiations with the United States we are not giving something away.

Senator Martin: I think Mr. Benson will agree that the very successful negotiations, in which he played an audible part, and the auto pact are two unrelated matters and they were not the subject matter of the Washington discussions.

Hon. Mr. Benson: No, not at all.

Senator Martin: If you had continued, I would have followed you with a very urgent question.

Senator Everett: I would like to congratulate the minister on what must have been an extremely difficult job in maintaining the floating rate for Canada during these negotiations. Secretary Connally has indicated that the Canadian dollar will float freely, without interference except for smoothing operations. He has also indicated that in his judgment the rate will go up. If, indeed, the rate does go up, what is our policy at the present time in relation to the float and what is our likely stance should the rate go appreciably beyond par with the American dollar?

Hon. Mr. Benson: Our undertaking is outlined exactly in the communiqué, as follows:

> The Canadian minister informed the group that Canada intends to permit fundamental market forces to establish the exchange rate without intervention except as required to maintain orderly conditions.

We could intervene in the case of speculation in the Canadian dollar and such circumstances. However, the basic market forces should determine the value of our dollar. Our policy has been determined by basic market forces, as of last Thursday, vis-à-vis the United States. The fact that the United States has devalued its currency, or increased the price of gold, should not in itself change that relationship between the United States dollar and the Canadian dollar.

There may be underlying market forces that will change it. I am not forecasting that there will not be any change in the value of the Canadian dollar, because this cannot be

determined. One of the reasons it has moved up is that we in Canada have operated, in 1970 at least, on a current account surplus and have imported capital. If both of these conditions exist there will naturally be pressure on the Canadian dollar. This has been offset to some degree by an export of Canadian short-term capital, because we have kept interest rates low. However, so long as we in Canada have a current account surplus and continue importing large amounts of capital, there will be pressure on the Canadian dollar, unless we export capital. I have been urging provinces, municipalities and corporations to use the Canadian market to the maximum amount possible, because, in theory, if we have a current account balance we can finance our own capital requirements in Canada.

Senator Everett: What is the life of the undertaking to, presumably, the Group of Ten, not to intervene in the level of the rate? As long as it is floating?

Hon. Mr. Benson: Our basic policy since floating the Canadian dollar in 1970 has been to allow the market forces to determine the value of the currency. We do intervene to make sure this is a smooth float, without a big upward movement through which money would be made, followed by a drop the next day. We accumulate some reserves by doing this. However, if there is speculation in the Canadian dollar, as there has been in the past, or if there is in the future, we will intervene on a more massive scale to prevent its disturbing normal movements of the Canadian dollar. I do not think I made any commitment not to do that.

Hon. Mr. Grosart: Mr. Minister, I have not read the communiqué, but I heard a precis, at least, on the radio this morning. My impression was that it referred specifically only to the surtax and the job maintenance measures arising out of the August 15 situation. Does this leave any other measures to which we object in that group which arose on August 15?

Hon. Mr. Benson: This leaves the DISC proposal, which has now been approved by the Senate and Congress in the United States and, indeed, signed by the President as part of the tax bill. It is in a very much amended form from that presented by the administration, comprising about one-half of the effectiveness of their proposal. We are studying it to see what its effect will be in Canada. The effect will not be immediate, but we are considering the long-range effect and any action we as a Government should take.

This was never included in the discussion at the Group of Ten with respect to the negotiations.

The Acting Chairman: It is really a matter of domestic policy.

Senator Grosart: So are they all, the surtax and everything else.

Hon. Mr. Benson: This has never been part of the discussions, although we have had bilateral discussions and indicated that we are upset by the DISC proposals. Indeed, now that they are law, we are studying appropriate action for the future.

Senator Grosart: Is DISC the only one of that group of measures with which we have to live now?

Hon. Mr. Benson: Yes.

Senator Lawson: Were negotiations satisfactorily concluded with respect to the question of duty-free purchases by Canadians in the United States?

Hon. Mr. Benson: No, we have not concluded negotiations with respect to anything on the trade side. It is being negotiated. This is not something new; there has been a great difference over a long period of years. They allow something like $100 per month, whereas we allow $25 every four months and $100 once a year. However, the dollar figures are not the only consideration in this regard. Canadians, as individuals, buy much more in the United States and bring it back than Americans do in Canada.

Senator Lawson: I suggest it would be less if the level were raised on a par basis.

Hon. Mr. Benson: Do not quote me, but they will probably report more.

Senator Hays: Mr. Minister, under the old Income Tax Act it was considered good to have a basic herd, which was considered to be capital. Why should it not be so under the new legislation?

Hon. Mr. Benson: The basic herd concept will be discontinued at the end of this year. Basic herds may be established until that time. We will then move into a new era, in which profits realized in a ranching business through cattle will be treated similarly to profits in the wheat business, in which when the profit is ultimately realized it is subject to income tax.

Senator Hays: You are comparing wheat with cattle.

Hon. Mr. Benson: No, any farming business. I am not referring only to wheat.

Senator Hays: Is the basic herd not considered as capital in the ranching business? A basic herd of 50, 100 or 500 cows is necessary. Previously this has been considered under the basic herd plan as capital. As inflation or increased costs occur and the animals are disposed of, this type of capital asset item is encountered. However, a combine is still considered to be capital, although wheat cannot be produced without it.

Hon. Mr. Benson: Under the new system, the depreciation on the combine will be recoverable. It will not be treated as a capital asset in the sense that you make a capital gain on it in the future, which you could in the past. Similarly, in the case of a basic herd, if you are in the cattle business you can accrue as you go along and pay tax on it. There are the averaging provisions, both cash and the other, in the event of disposal. It can also be operated on a cash basis.

Senator Hays: I appreciate that. That could also be done under the old system.

Hon. Mr. Benson: It will still be possible.

Senator Hays: Would it be possible, in view of the fact that there will not be a basic herd concept in future, to change from this to the cash basis?

Hon. Mr. Benson: Do you mean from cash to accrual?

Senator Hays: Yes?

Hon. Mr. Benson: Yes.

Senator Hays: This is permissible under the provisions of the new act?

Hon. Mr. Benson: Yes.

Senator Hays: What are the mechanics?

Hon. Mr. Benson: It is reported on another basis. There is a question of an adjustment period.

Senator Grosart: And it might cost you money.

Hon. Mr. Benson: No, it might be to your advantage to move to an accrual basis with your original basic herd in 1972. When adding in the future, you would move to the accrual basis and the tax would be averaged over a period of years.

Senator Hays: If you were on an accrual basis, you would not be able to change.

Hon. Mr. Benson: No, you would not.

Senator Hays: But if you are on a cash basis, you could.

Hon. Mr. Benson: If you are on a cash basis, you can change.

The Acting Chairman: The minister has been with us now for about two hours. If the committee is satisfied with the time that we have had with him and there are no further questions, we might well allow him to go about his other duties. We thank him very much indeed for his help this morning.

The officials of the department are here, and we shall now proceed to deal with any questions which the committee have with regard to details of the bill.

We have with us Mr. Cohen, the Assistant Deputy Minister of Finance, and also Mr. Thorson, the Associate Deputy Minister of Justice who had a large part to play in the drafting of the legislation. Both gentlemen are open to questions.

Senator Buckwold: I have received an item on which I am not an expert. It was handed to me by our own chartered accountants. It concerns the penalty tax on excessive elections. There is a provision in the bill that if you pay out a tax on what you consider capital gains, which is later deemed by departmental decision to be income, you would be liable to 100 per cent of that payment. Has any consideration been given to an amendment to what I and many chartered accountants feel is an excessive penalty for what could be an innocent mistake?

Mr. Cohen: I think I can suggest two answers to that question. First, we did put in an amendment. The bill, in its original form, was much tougher on someone who had made a mistake, because that particular tax would apply to the whole of the amount distributed, if he chose to distribute out of what we might call the wrong pot. We have now amended the bill to provide that only the excess is subject to this tax. In other words, if you distribute $100 and you had only $85 in the proper pot, the tax would apply only to that excess $15.

Secondly, with regard to the 100 per cent tax, I appreciate that it looks very onerous, but that is a tax which is paid by the corporation. If you do the mathematics, I think you will find that that is the appropriate amount of tax in dollar terms, not in rates. In other words, it results in the same net after tax yield to an individual shareholder receiving an ordinary taxable dividend in a 60 per cent marginal tax bracket. Although it looks like a 100 per cent tax, mathematically it works out to be the appropriate level. You might argue that one should have taken a 50 or 40 per cent marginal rate, but it is our feeling that this would probably occur with taxpayers in high brackets. So we chose the 60 per cent marginal rate at the personal level, and mathematically that turns out to be a fraction away from 100 per cent when paid by the corporation. I do not want to take you through the whole mathematics, because I would lose you, and probable lose myself, but that is the underlying genesis of that.

Senator M. Grattan O'Leary (*Acting Chairman*) in the Chair.

Senator Grosart: I should like to move that we now adjourn, because the acting chairman is no longer in the Chair.

The Acting Chairman (Senator O'Leary): He will be back in a moment.

Senator Grosart: I feel that we should go through the bill clause by clause. I do not mean that we should consider each one individually, but I think we have a duty as a committee. This is the first time that the bill has been before us. We have had the summary. I am not suggesting that it has not been thoroughly discussed; it has been.

To revert to the comment I made earlier, there are amendments that the committee has drafted, and I should like time to make up my own mind on the proper way for the committee to proceed.

We have had the minister's statement, which has gone beyond what he undertook when he was last before us. I would like a little time to consider that before deciding what I would suggest to the committee is the way it should proceed. For that reason, it might be well to adjourn until 2 o'clock.

The Acting Chairman: Would it be possible for Mr. Cohen and Mr. Thorson to be with us this afternoon? I know that the Honourable Lazarus Phillips will be here. Perhaps we should adjourn for lunch.

Senator Beaubien: May I remind the committee that the Senate is sitting at 2 o'clock?

Senator Martin: May I say, Senator O'Leary, that you grace the chair with an unusual distinction.

Hon. Senators: Hear, hear.

Senator Martin: If I thought that it would refine your opposition, I would suggest that you sit there more often. We have to consider the fact that the house will be meeting at 2 o'clock. We shall not meet for very long, because the purpose of that is to enable us to proceed with the committee stage. But whatever adjournment time we take into account, we must bear that in mind.

The Acting Chairman: Would someone make a motion to adjourn?

Senator Cook: I move that we adjourn until 2.30 p.m.

The Acting Chairman: A motion has been put that we adjourn until 2.30.

Senator Connolly: It will depend on the business of the Senate, which is to meet at 2 p.m. We might agree, if the Senate gives us permission, that immediately on assembly the Senate adjourn until perhaps later this day. The Committee can then resume.

Senator Langlois: That is what I suggested on Friday.

Senator Grosart: Perhaps the motion should be amended to say that we will meet on the adjournment of the Senate.

Senator Connolly: " . . . when the Senate rises" this afternoon—those are the formal words.

The Acting Chairman: The motion, as I understand it, is that we adjourn until the Senate rises this afternoon.

Hon Senators: Agreed.

The committee adjourned.

Upon resuming at 2.15 p.m.

Senator John J. Connolly (*Acting Chairman*) in the Chair.

Senator O'Leary: I am going to propose moving an amendment dealing with deferred profit sharing plans. Before doing so, I should like to read from the Preliminary Report on the Summary of 1971 Tax Reform Legislation.

The Acting Chairman: That is the report of November 4, 1971.

Senator O'Leary: That is right. On page 8 it says:

> The tax treatment of deferred profit sharing plans differs from the treatment accorded employees profit sharing plans. The provisions of the present law relating to deferred plans are, in summary, as follows:
>
> 1. the employee is not taxed currently on any amounts which his employer may contribute to the plan on his behalf nor on the income earned in the year by the plan; and
>
> 2. instead, the employee is subject to tax on the full amount received on his withdrawal from the plan minus any portion representing a refund of contributions paid by the employee into the plan; the exclusion of the employee's contributions follows from the fact that the employee is not allowed a deduction for contributions but is obliged to make these payments out of tax-paid dollars.

It is significant to note that the amount taxable as income in the employee's hands represents not only his share of (*a*) the employer's contributions, and (*b*) the income earned by the plan, but also (*c*) his share of any net capital gains of the trust. This treatment has been acceptable to member employees partly because of the tax deferral feature inherent in these plans but also in large measure because the employee has the right to avail himself of the special tax averaging provisions of Section 36 of the present Income Tax in respect of a lump sum payment received on his withdrawal from the plan.

Under the proposed legislation, the lump sum distribution from the plan will continue to be treated as ordinary income whether the distribution is made from employer contributions, income accumulated by the trust, capital gains, realized by the trust or unrealized gains in respect of property distributed in specie to the employee.

However, the tax averaging provisions of Section 36 of the present Act are not carried forward into the proposed legislation in respect of amounts accumulated by the trust after 1971. Instead, these provisions are to be replaced by averaging provisions which, for purposes of members of deferred profit sharing plans, appear to be quite inadequate. In this regard transitional provisions are to be introduced to permit employees to take advantage of an averaging provision equivalent to Section 36 of the present Act in respect of amounts accumulated in the trust up to December 31, 1971. However, if such an election be made by an employee, he cannot avail himself either of the proposed averaging provisions (general or forward) in respect of that portion of the amount accumulated in the trust after December 31, 1971. Also, in future years, the transitional rule will be of diminishing benefit.

The general and forward averaging provisions available under the proposed legislation are not only much less generous than the elective provision under section 36 of the present Act, but the requirement to purchase an income averaging annuity in order to obtain forward averaging in effect removes the basic purpose of a deferred profit sharing plan, i.e. the accumulation of a lump sum on retirement.

In the opinion of your Committee, the effect of the proposed legislation will be to legislate these plans out of existence. Relief should be granted; the most appropriate means of achieving this relief is by the application of capital gain rules to the property of the trust.

YOUR COMMITTEE RECOMMENDS the following.

1. that any amount distributed by the trustee of a deferred profit sharing trust out of capital gains realized by the trust should qualify for capital gains treatment in the employee's hands;

2. that where property is distributed in specie to an employee by the trustee, the trustee should be deemed to have disposed of the property for proceeds equal to its "cost amount" (as defined) to the trust;

3. that the employee should be deemed to have acquired the property at the "cost amount" to the trust; and

4. that the employee should not be taxed until he ultimately disposes of the property, at which time any gain should be accorded capital gain treatment.

Based upon that, I beg to be permitted to move the following amendment to section 147(10) of Bill C-259:

1. Section 147(10) of Bill C-259 should be amended to read as follows:

"147(10) There shall be included in computing the income of a beneficiary under a deferred profit sharing plan for a taxation year each amount received by him in the year from a trustee under the plan, minus

(a) any amounts deductible under subsections (11) and (12) in computing the income of the beneficiary for the year,

(b) amounts paid by a trustee under the plan pursuant to the plan to a person described in subparagraph (2)(k)(vi) to purchase an annuity described in that subparagraph,

(c) The amount by which the aggregate of

(i) each amount allocated to the employee or other beneficiary by a trustee under the plan in respect of a capital gain made by the trust, and

(ii) each amount allocated to the employee or other beneficiary by a trustee under the plan in respect of the increase in the value of property of the trust over its cost amount to the trust

exceeds the aggregate of

(iii) each amount allocated to the employee or other beneficiary by a trustee under the plan in respect of a capital loss of the trust, and

(iv) each amount allocated to the employee or other beneficiary by a trustee under the plan in respect of the decrease in the value of property of the trust from its cost amount to the trust,

and

(d) the fair market value of property (other than money) transferred in kind to the employee or other beneficiary by a trustee under the plan."

2. Section 147(10.1) should be added to Bill C-259 in the following terms:

"147(10.1) Where any property (other than money) has after 1971, been transferred in kind to an employee or other beneficiary by a trustee under a deferred profit sharing plan, the employee or other beneficiary shall be deemed to have acquired the property at a cost to him equal to its cost amount to the trust at the time of its transfer."

This suggested amendment, just moved by me, is, I assure you, not for the purposes of obstruction; it is frankly, sincerely and honestly for the purposes of construction.

We had the minister here this morning, and I thought he was very fair, very frank and very able. He practically committed himself—some senators might not interpret what he said as a commitment, but I do—to bring in an amending bill to include some of the amendments already made by this committee of the Senate.

I must say that in moving this amendment we in our small group in this committee are actually trying to strengthen the minister's hand. He cannot do these things on his own; he has to go to cabinet colleagues and put these things before them. We think that by moving an amendment such as this—some others may follow—we are giving the minister the assistance he needs in getting these proposals into his amending bill. Therefore, I commit it to the committee, and I trust and hope it will be given the fair and sincere consideration which I think it deserves.

The acting Chairman: Thank you, Senator O'Leary.

Senator Isnor: Mr. Chairman, might I put a question to Senator O'Leary? I wish to have a clear understanding of the motion. Does he propose to move an amendment to be submitted to the minister for consideration, to be brought in later in the bill?

Senator O'Leary: I am proposing this amendment in the hope that his amending bill will include it. This morning this is what he committed himself to do.

Senator Isnor: The amending bill?

Senator O'Leary: This is an amendment to the bill.

Senator Cook: I understand what the senator is proposing in an amendment to the bill.

The minister has not turned down one single, solitary amendment proposed by the Banking, Trade and Commerce Committee. He has undertaken to give consideration to them all.

We have had the assurance of the minister that there will be an amending bill next year. Therefore, in my opinion, no good purpose would be served in pressing our amendments at this time. I would, in order, amend the motion, if I may—that it be not put. I do not want to vote against it, but I think the motion should not be put at this time. In other words, I think we should not press our amendments at this time.

The Acting Chairman: Do I understand that your amendment to the motion is to the effect that the motion should not carry at this time for the reasons you have given, Senator Cook?

Senator Cook: Yes, that it should not carry.

Senator Phillips: Mr. Chairman, on a point of order, I should like to know if that is a legal amendment to the motion. I would like a ruling on that. I am not so sure the amendment is in order.

Senator O'Leary: You mean the amendment to the amendment?

Senator Phillips: Yes. I would like a ruling on that, and, if my interpretation is correct, I am quite willing to accept the amendment because, if it be not put now, the bill cannot be reported. Nothing would make me happier than that, according to my interpretation of the Rules. But I would like a ruling on that from the Law Clerk.

Senator Cook: That is an unwarranted extension of my motion.

Senator Phillips: I can only hope for the best.

Senator Grosart: If I may speak to the point of order, Mr. Chairman, there appears to be some confusion, because I believe when you phrased the amendment you said that it was that the amendment do not now carry. I would suggest to you that that is obviously out of order because, if an amendment is made, it is voted on. You simply cannot amend to negative an amendment or a motion. I think that is fairly clearly understood in parliamentary procedure. I do not think it is a matter of great moment.

However, the motion is before us, as put by Senator O'Leary, which I take to be a motion before this committee to amend Bill C-259. With respect, I would suggest that that motion is before you, and that perhaps you would wish to put it to the committee for discussion.

The Acting Chairman: I think the consideration that was probably in Senator Cook's mind is that the committee has already proposed suggestions for amendments and these suggestions, in the view of the committee, are valid suggestions with which the minister has been impressed and with which he proposes to deal. I should think that the committee would not want to put itself in the position of negativing what it has already proposed in a positive way.

If the rejection of the amendment at this time does not negative the work that the committee did all fall, then I think Senator Cook's point would be met.

Senator Cook: That is right.

The Acting Chairman: But how to achieve this, I do not know. Perhaps the committee could vote on the amendment with the idea in mind that it is still a valid proposal for consideration. If that is the case, them I have no objection whatever to putting the main motion, which is Senator O'Leary's motion.

Senator Grosart: If I might speak for a moment on a point of order, Mr. Chairman.

The Acting Chairman: Senator Isnor?

Senator Isnor: I want to know whether this is an amendment to the bill now before us, or if it is a recommendation to the Minister?

The Acting Chairman: I see your point, senator, and I think this is clearly, as Senator O'Leary has said, a proposed amendment to Bill C-259.

Senator O'Leary That is right.

The Acting Chairman: What he wants to do by this motion is to amend section 147.(10) and 147.(10.1) now. That amendment, if carried, would have to be reported to the Senate, and if the Senate passed it it would then have to have the approval of the House of Commons before the bill was amended in that form.

Senator Isnor: That means that if the motion is carried the bill will go back to the House of Commons.

The Acting Chairman: If the Senate agrees with the amendment.

Senator O'Leary: Of course, that is as clear as crystal.

Senator Isnor: It is not so clear. It is delaying the bill. That is all.

Senator O'Leary: Is that a catastrophe?

Senator Grosart: On the point of order, Mr. Chairman, perhaps to clarify it, it should be pointed out that the committee has made recommendations to the Senate and those recommendations to the Senate and those recommendations have not been adopted by the Senate. The Chairman has made it quite clear that he was not asking for adoption, but merely for consideration, which I think was a very wise course in the circumstances. So this amendment is in no way out of order on the grounds that the committee has already dealt with it.

The Acting Chairman: There is no question of that.

Senator Phillips: Speaking further on the point of order, Mr. Chairman, and perhaps I misunderstood both the Chairman and the Minister this morning, but I thought we would have the right to move amendments in committee, and if it were left in the position where any amendment is going to interfere with recommendations—the Banking, Trade and Commerce Committee admittedly has studied this and set certain priorities, but they have never been in the form of amendments, and now it seems we are being deprived of the right to make amendments.

The Acting Chairman: There is no suggestion that that would happen.

Senator Cook: My only point, Mr. Chairman—and I made this point on the floor of the Senate and I make it again—is that assuming we really desire to have the bill amended, I think we have a much better chance of getting it amended by having it passed now and having it in definitive form. Then, when we receive the amending bill, to bring forward our amendments once again, because our recommendations have not been rejected by the minister. He has not rejected any of our amendments yet; in fact, he has agreed to give them consideration.

In my view, the most sensible practical and reasonable course to follow would be to allow the bill to become law now, instead of throwing it back again to the House of Commons; and then to persuade the minister again in the new year to accwpt our recommendations.

Let me make it clear that I am not against the principle of the amendment, but I am definitely against the amendment being pressed now. It may be that my only recourse will be to vote against Senator O'Leary's motion, which I will; but I wanted to give the reason why I would vote against it.

The Acting Chairman: Is the committee of the opinion that should this amendment be defeated the proposal which the amendment sets up should still continue to be a valid proposal from this committee?

Senator O'Leary: If it is defeated, I do not know what the effect will be, but this will be on record, and I hope the minister will see it and endeavour to carry out some of the terms which he indicated to us this morning. I feel he was more definite this morning than he was on the last occasion he met with this committee. I was present and I heard

him. All I am endeavouring to do is to get these amendments through. What the procedure is I am not sure, but what is wrong with passing this amendment?

Senator Isnor: There is nothing wrong with passing the amendment, only in the direction in which you are sending it. I would suggest you send it to the minister, and then he can put it in his amending bill.

Senator Martin: Mr. Chairman, I was not aware that we were going to be dealing with this matter at this stage of our proceedings. It seems to me there is important evidence which we should hear, particularly on the consequences of not meeting our target date.

Senator Grosart: We heard that information from the minister this morning.

Senator Martin: No, I am sure he gave us an indication of the consequences. But I, for one, am very anxious to hear what Mr. Thorson has to say concerning the consequences with regard to what are called transaction taxes and the serious legal dilemma in which the country will be put if we do not hold to the effective target date. I am sure this is one of the issues which Senator Cook had in mind. The effect of passing this amendment in this form is to send it back to the other place, with an ensuing long debate which would seriously affect the kind of evidence I have just mentioned. What Senator Cook has indicated, it would seem to me, has great value regarding the fact that we continue to support the recommendations of which this amendment is, in form, one. Our hope is that the recommendation would be embodied in the amending bill which the Minister of Finance said would be brought forward some time in the course of the next few months.

We are not withdrawing our support of the recommendation, but we are endeavouring to have the recommendation accepted in the most effective form. Senator Cook has argued that the most effective way of getting that recommendation accepted is to reaffirm our confidence in the recommendation, with the hope that it will be one of the amendments brought forward in the amending bill, and not as Senator O'Leary has proposed. I feel this logic is fairly clear.

Senator Cook: I would like to make one more comment, Mr. Chairman. It seems to me that the minister has not rejected our proposed amendments. He has indicated that he needs further time to consider them. In effect, we are saying, "We will not give you further time to consider them." He is not rejecting our amendments; he is asking for further time to consider them. By this amendment we are saying, "We will not give you further time. We want to put them through now." I do not think this is reasonable.

Senator Hays: It seems to me, and I will be blunt, that if I was a member of the Opposition I would take the same stand as Senator O'Leary has taken. It embarrasses this committee to no end, and I feel we should vote on the matter now. If it is defeated we should recommend that it be sent to the minister for his consideration.

The Acting Chairman: You are free to make such a motion, if you so desire, after we have considered the specific motion which is before us.

The Acting Chairman: It will be open to you to make such a motion, if you so desire, after we have considered the specific motion now before us.

Senator Grosart: I would like to comment on Senator Martin's remarks, which I find most extraordinary. He suggested that if this amendment were carried we would necessarily be delaying the bill. I suggest to him that it may have been forgotten by some that the essential responsibility of the Senate, or a Senate committee, is to report to the House of Commons, not to the minister. The bill comes to us from the House of Commons. We have an obligation to report to the House of Commons, whether we approve this bill without amendment, or with amendment. I therefore suggest that that particular argument is a complete *non sequitur* in the present circumstances.

As to the effect of a vote, negative or positive, on this amendment, others will decide. It is not for us to decide what will happen if an amendment is carried. Presumably it will go to the Senate, which might or might not accept the report of the committee. The bill might or might not go on to the House of Commons, to whom, I suggest, our major responsibility is in considering legislation. It might or might not be passed there before December 31. That is not the consideration.

Senator O'Leary is presenting an amendment, in which I support him. We think this committee should pass it, because it is its own amendment. The amendment read by Senator O'Leary was drafted by the advisers of the committee. We are faced with that position. The committee considered that it is one suggestion which would help solve the problems it sees in this bill. In my opinion, Senator O'Leary is simply asking the committee if they wish to deal with their own draft amendment now.

The Acting Chairman: That is the point; the pertinent part of your comment is the word "now".

Senator Grosart: That is right.

Senator Buckwold: I listened with interest to the minister this morning. As I recall, he made some mention of proposed amendments to the section on deferred pension plans. I again have to plead ignorance of the detail. Were suggestions along those lines indicated; and, if so, did they involve reference to the questions raised in the motion in amendment of Senator O'Leary?

Senator Grosart: Yes, they did.

Mr. Cohen: The minister's statement related to deferred profit-sharing plans and some changes he was considering in that regard. In fairness, however, they do not relate to the whole of the point raised by Senator O'Leary. They are concerned with the treatment of averaging, but not, to use the short term, the roll-out of capital gains. The minister made a statement in the other place; unfortunately I do not have the exact text. When he was before you previously, he spoke about changing the context in which you can make use of the old from of averaging from amounts vested on January 1, 1972 to amounts standing to your credit, which is a much bigger number in almost every situation. Secondly, he indicated that he was looking carefully at the provision which would permit an individual to take advantage of both the old form of averaging of

amounts standing, to his credit prior to 1972 and the new forms of averaging for current contrbutions.

As Bill C-259 reads, if you choose the old form of averaging on those old accounts, you are precluded from using some of the new forms of averaging. The minister indicated that he was considering taking away that inhibition so that you could use old averaging on old amounts and new averaging on new amounts.

Senator Buckwold: The whole question of profit-sharing plans and deferred profit-sharing plans is still very much in front of the minister?

Mr. Cohen: Oh, yes. He said that he would be looking at those, and he became specific on the two points I have mentioned.

Senator Grosart: On that particular point, would you agree that in general the minister said there are three main objections; that he is looking favourably on two, and has not committed himself to the third—or am I being too general? I think it is important that we know just where we stand on this. Perhaps I may read one paragraph from the report of the chairman of this committee on this very point. In reporting to the Senate on December 13 he said:

> With regard to employee and deferred profit-sharing plans, three recommendations were made and the minister indicated that two of them would be implemented. They have been approved. The third, it will be recalled, concerned capital gains. We stated that in a trust fund which is related to the profit-sharing plan or a deferred profit-sharing plan there may be a capital gains on the buying and selling of securities in the year, and that there was no reason why those capital gains should be taxed as income in the fund. It is the same type of a capital gain which any other person might make, and which would only attract half of the tax rather than the full marginal rate of income tax. The minister stated that they were looking favourably to doing it in that way. Frankly, I do not see how they can do anything else because it is so deserving.

Perhaps we could have a comment on that. I may be in the policy area—

Mr. Cohen: The Senator is partially in the policy area, but he is also asking me to interpret what the minister was saying. I have not the text of what he said to this committee. I have what he said in the other place, in which he dealt specifically with two of the three points made and made no comment on the third, other than to say that he was looking at the general area.

Senator Grosart: I have been concerned with this matter as it affects the Senate. I was personally very happy with the minister's statement this morning. I think he did, in effect, commit himself, and went a little further than he did the other day. He used the words "a specific bill," which satisfied some of my doubts about what this committee should do at this particular time.

This is perhaps an interesting case, where we can say the committee has a degree of assurance on two-thirds of its doubts. It seemed to make sense, and I am sure that is what was in Senator O'Leary's mind, to bring the whole of the amendment before the committee to see what its disposition might be at this particular time.

Senator Everett: May we have the operative words of the amendment?

The Acting Chairman: That the bill be amended in respect of section 147 and the subsections shown in the amendment.

Senator O'Leary: Mr. Chairman,—

The Acting Chairman: Senator O'Leary, would you mind? Senators Belisle, Bonnell and Phillips have indicated that they wish to ask questions. Senator Bonnell.

Senator Bonnell: Mr. Chairman, I am not a member of the committee. This committee has done a good job in their study, and it has made certain recommendations to the Minister of Finance, with certain priorities in relation to those recommendations. I think the Senate as a whole looks upon those recommendations favourably, as, I think, does the Minister of Finance. He feels they are worth consideration and amendment.

Perhaps I look at this thing in a different way from members of the committee or other honourable Senators, but what we have to think about, in my view, is whether or not we want the 4.7 million people who are below the poverty line to get their benefits immediately. If that is our desire, then we should pass this bill without amendment. If we start amending this bill in the Senate and, consequently, drag this thing out for another three months, a great many people below the poverty line will be faced with having deductions from their salaries for the first few weeks of the new year, and they will not get that money back for a year-and-a-half. These people need the money now.

Why do we not pass the bill now, without amendment, and make our recommendations to the Minister of Finance in the spring, when he brings down his amending bill?

I also feel that if we vote in favour of Senator O'Leary's motion today we will void the recommendations of the Senate Committee. If the motion does not carry, it will make them think that the Senate committee does not support its own amendments. The Senate committee, as I understand it, does, in fact, support the amendment, but what they might not support is putting it through now. As I say, if we vote against the motion we will give the impression that we are against the recommendations of our committee which, apparently, are all good recommendations.

Senator Grosart: That is up to the committee.

Senator Bonnell: In my opinion, the way to solve this is to have Senator O'Leary withdraw his motion and then put a motion to the effect that we will not accept any other motions at this hearing.

Senator Grosart: Oh, dear!

Some Hon. Senators: Oh!

The Acting Chairman: Senator Belisle?

Senator Belisle: Mr. Chairman, if you are an impartial chairman, and I believe you to be one, why do you not permit the motion to stand so that we can vote on it? After all, we are only six and you are over 20 in number.

The Acting Chairman: Senator Belisle, let me just say this: Whether I am an impartial chairman or otherwise depends upon the committee, but I do not determine the course of the committee. All I am here to do is to keep order.

Senator Belisle: The committee is here this afternoon, is it not, to consider Bill C-259, and only Bill C-259. It is not here to consider what the minister may or may not do at some time in the future. What is in front of us is the bill; it is not the minister's intentions. If that is not the case, then we are wasting our time and the taxpayers' money.

My honourable colleague who just spoke before me said that we should not propose any amendments. If you are not going to permit us to vote on any amendment, then we are wasting our time.

The Acting Chairman: Certainly, the chairman would never take that position under any circumstances.

Senator Phillips, you are next on my list.

Senator Phillips: Mr. Chairman, throughout the Government Leader's remarks—and I more or less gave him the assurance that I would not go after him personally today—

Senator Martin: I am always afraid of those attacks!

Senator Phillips: Throughout his remarks he kept telling us that there was no target date. He told us we could have as long as we wanted to consider this bill. I am now intrigued by the fact that his objection to the motion in amendment is that we would interfere with the target date of the legislation. What happened over the weekend that we now have a target date, and what is that target date?

Senator Martin: My statement was that there is no restriction on what the Senate does. That is quite clear. I made that clear; the chairman has made that clear. There is nothing to prevent this committee taking any course it wishes.

Senator Cook: We all know that.

Senator Martin: Yes, but Senator Phillips does not feel that is the case.

What I am trying to point out is that unless the due date is kept there will be certain serious legal consequences.

Senator Phillips: And what is the due date?

Senator Martin: That is why I would like an opportunity to ask Mr. Thorson and Mr. Cohen some questions in regard to this very point.

The Acting Chairman: You will have that opportunity in due course.

Senator Cook: Mr. Chairman, you will have to forgive my inexperience. I am trying to put forth a motion which, perhaps, might be in order.

Senator Everett: I wonder if I may interject with respect to a point raised by Senator Martin. It seems to me that the questions he wants to ask of Mr. Thorson and Mr. Cohen, if they relate to what is the underlying effect of this motion, should validly be asked now. In my opinion, the committee needs that information in order to make its decision.

Senator Grosart: I agree.

The Acting Chairman: Is it the desire of the committee to proceed along the lines suggested?

Senator Phillips: Provided anyone else who has a desire to ask a question, in addition to Senator Martin, has that right.

The Acting Chairman: Oh yes.

Hon. Senators: Agreed.

Senator Martin: Mr. Thorson, how many parts are there to Bill C-259?

Mr. D. S. Thorson, Associate Deputy Minister, Department of Justice: Seventeen, sir.

Senator Martin: There are those that impose a tax on the redemption or acquisition by a corporation of capital stock; those that impose a special tax on excessive elections under section 83 of the new act; those that impose a special tax on taxable dividends received by private corporations; those which impose a refundable tax in respect of ineligible investments made by Canadian controlled private corporations. I suppose these might involve what are called transaction taxes. Could you tell us what would be the effect on those taxes and on the persons concerned if there were a delay in acceptance of this bill by Parliament?

Mr. Thorson: I must come back, of course, to the answer that the Minister of Finance gave this committee this morning, namely, that the problem is best expressed in terms of the kind of legal uncertainty that would result if the new law were not to come into force until after the commencement of the new year. The minister has spoken to this point both in the other place and before the committee. In the other place on December 10 he put it this way, that most taxpayers, particularly in the business community, would simply not know how to behave. This is the point he made and elaborated this morning. They would not know whether further amendments were coming which would reach back and affect transactions taking place between January 1 and the date of the tabling of an amendment; they would not know whether to assess their position under the 1948 Income Tax Act, the Act we now have, or under the 1972 reform bill. The minister gave a number of illustrations to indicate that measure of uncertainty.

Perhaps it would be helpful, though, in elaborating on the kind of examples he gave, just to develop the point that Senator Martin has brought to the attention of the committee concerning the other parts of the bill. Could I back up just this much, to say that, as all senators probably know, the main part of the bill, and by far the most important part, is Part I, which imposes a tax on both individuals and corporations measured by reference to their taxable income for a particular taxation year. A precise measure-

ment of taxation income for a particular taxation year can only be made after the end of the year in question. Nevertheless, it is important for a taxpayer, in the conduct of his affairs, to know with reasonable certainty the rules that govern the calculation of his taxable income for the year, in order that he may be guided by those rules in taking decisions that may affect his ultimate tax liability. Furthermore, for the purpose of calculating such things as payroll deductions at source, instalment payments of tax, et cetera, the taxpayer must have an understanding of the rules by which his or his employees' incomes, and therefore taxable incomes for the year, are computed, notwithstanding that the measure of ultimate liability for tax under Part I of the bill is taxable income for the whole year.

As Senator Martin pointed out, in addition to the tax imposed by Part I of the bill, there are other parts of it—and these are listed specifically in the appendix at the end of the printed volume of Bill C-259—that do not use the measure of a taxation year, but instead impose a liability to pay tax based on the happening of certain transactions or events. These are what might be called transaction taxes rather than income taxes in the strict sense. These various transaction taxes are, of course, related to the Part I tax, and are necessary to the total scheme of taxation envisaged by the bill.

I think Senator Martin gave some examples. In addition to the Part I tax there are no fewer than, I think, 13 parts in the bill by which various kinds of special taxes are imposed. I will not trouble you with all of them, but they include Part II, which imposes a tax on the redemption or acquisition by a corporation of its capital stock; Part III, which imposes a special tax on excessive elections under section 83; Part IV, which imposes a special tax on taxable dividends received by private corporations; and Part V, which imposes a refundable tax in respect of ineligible investments made by Canadian-controlled private corporations.

It will be seen that many of these taxes are conditional upon a corporation taking some particular action at a time when the new system is in effect. For virtually all of these new taxes the relevant time is the beginning of the new year. In each of the parts in question the date "after 1971" appears. Since many of these parts are new and have no counterpart in the present law, it will be obvious, I think, that the liability of taxpayers for tax may depend upon whether the new law is in fact in place at the time the corporation pays the dividend, redeems its capital stock, becomes a non-Canadian controlled private corporation, et cetera.

Mr. Chairman, I could perhaps give an illustration of this, if the committee will bear with me for a moment.

Senator Phillips: I presume it is in your prepared text, so you might as well give it.

Hon. Senators: Oh!

The Acting Chairman: That is not a proper remark to make to an official.

Mr. Thorson: I was elaborating by quoting from the outline at the back of the bill and from the minister's own comments.

An example, which I insist is only one single example in terms of the total problem, is the tax imposed by Part XIII of the bill, on payments made by residents of Canada to non-residents. Part XIII is the successor to what is now Part III of the present law. Part XIII requires a withholding tax of 15 per cent, until 1976, to be deducted and withheld by every Canadian resident making a payment of a dividend, interest or rent, et cetera, to a non-resident. The new Part XIII requires that tax be withheld against certain payments going to non-residents that are not now subject to the tax. For example, many pension and annuity payments will now be subject to the withholding tax where the payment is going to a non-resident.

If this part of the act, for example, were not brought into force until some time in the new year, one might ask oneself what would be the position of an employer or an insurance company, or, indeed, any other payer, who was directed by the substantive provisions of the bill to withhold tax from pension or annuity payments made at any time after 1971, which is the relevant date in the bill. If the employer withheld the tax provided for under Part XIII, he would have to do so without the authority of the Income Tax Act, since Part XIII would presumably not yet be in force, and he would be, in the interim, presumably liable to civil action by the recipient of the payment, to enforce payment of the full amount that ought to have been paid.

On the other hand—and I think this describes his dilemma, sir—if he did not deduct withholding tax from the payment and forthwith remit it to the Receiver General, he would be in default under the law as it is now written, at such time as Part XIII came into force, because when it did come into force it would be clear that he should have deducted or withheld the tax from any such payment made after 1971.

Senator Grosart: You mean, Mr. Thorson, that at that point his obligation would be due to retroactive legislation?

Mr. Thorson: Because of the way the bill is written, sir.

Senator Grosart: I am only just asking; I do not care how the bill is written. It would be an obligation that he would not have had at that time, but would be due only to the retroactive nature of the legislation you are speaking of.

Mr. Thorson: Because of the—

Senator Grosart: I do not care what the because is; it is yes or no.

Mr. Thorson: The person making the payment would be in a very uncertain position.

Senator Everett: I am sorry, but unlike Senator Grosart I do care about the "because," and I would like to get that straight in my mind.

Mr. Thorson: "Because" the bill, as written, provides that the liability to deduct, or withhold and remit to the Receiver General of Canada, on payments out to non-residents, exists in relation to any payment made after 1971; that is to say, from January 1, 1972 forward.

Senator Everett: Thank you.

Mr. Thorson: It would appear, therefore, that the payer is in something of a dilemma, Mr. Chairman. He may be in some difficulty if he decides he must be guided by the provisions of the new legislation, and he is certainly in difficulties if he chooses to ignore the new legislation.

I am fully aware that in relation to the above example—as I pointed out earlier, it is only one example—it could be argued that this type of situation is not unprecedented in the history of Canadian tax legislation. Indeed, I would readily concede that on occasions in the past taxpayers have been faced—as Senator Grosart will agree—with the kind of dilemma described.

The point that has to be made, it seems to me, however, relates to the order of magnitude of the difficulties that taxpayers would face under the new income tax act because of the complexity and size of Bill C-259. The examples of difficulties of the kind just mentioned would be legion, should there be any uncertainty as to the commencement of the new law.

Mr. Chairman, I think it is worth repeating that the major confusion—and this is the point which the minister stressed—the major confusion, if the commencement of the new law is left uncertain, will be in the area of corporate business activities. If a corporation cannot be sure about the tax consequences of paying out dividends to its shareholders, proceeding with a re-organization of its business, investing its surplus funds in one kind of asset, as opposed to another kind of asset, et cetera, the corporation will be effectively paralyzed in many important aspects of its business. This is the point that was made by Mr. Benson and that seems to me to be central to the problem of the difficulties that would arise should there be continued uncertainty as to the exact date of the commencement of the new legislation.

Senator Grosart: Mr. Chairman, I hope we will get back to the amendment, because, with all due respect, I would suggest that we are not faced with a position where, if this amendment is passed, the enactment of the bill will necessarily be delayed. This simply is not the case. We are faced with an amendment that this committee is asked to make. As I said before, it will go to the Senate; it may go to the Commons; it may be dalayed in either place, it may not be. But we are faced here with a motion to amend the bill here and now. I do not think the consequences that are anticipated are realistic or likely to happen. Therefore, I suggest that a good deal of this discussion is irrelevant to the question as to whether we should pass or reject this motion.

The second point is that on the very area—and Mr. Thorson has given an adequate and eloquent description of the difficulties that will arise, and I am not denying it—we know already that the minister is going to make amendments. Most of them, as he said himself, are in the area of corporate taxation. So I am not greatly impressed with the uncertainty argument as it affects business. I think it is highly important as it affects the administration. Perhaps the greatest difficulty might be created in respect to the computerization problem, but I would hope the science of the Juggernaut without a driver is not going to be the main consideration here as to whether this bill is delayed or not.

With that, Mr. Chairman, I am prepared—and I am sure Senator O'Leary is, because he has so indicated to me—to see the amendment voted on.

Senator McElman: Mr. Chairman, I know we are all trying to seek a means whereby we can achieve the best bill possible, and in that light I should like to make a suggestion. For the first time, we are now seized of the actual bill. The committee made a series of recommendations, previously to its being seized of the bill. Perhaps the committee would like to confirm its support of those recommendations, which have been called "priority" and otherwise. It seems to me that there is a means of doing that.

This committee of itself cannot amend the bill; it can only report to the Senate, which can amend or not amend, as it may wish to do. It seemed to me that, if it were the wish of the committee to confirm the recommendations that it has made previously, it could so do by proposing them as amendments. Then, if it should be the consensus of this committee when it formulates and approves its report to the Senate, it could state that it understood the complexity of the situation, the dangers involved in the observance or non-observance of the January 1 date, the commitments that were received from the minister, and its wish that this be gotten on with. Up to this point, and up to the point of doing this with the bill now before us, we really have not, in effect, gotten any message to the minister. Once that becomes a paper of our house, accepted by the house, with such a codicil to it, it is not just our paper, it is a paper of Parliament and it is in the hands of the minister as well as of every member of Parliament.

Senator Benidickson: You mean, our report?

Senator McElman: Exactly. The report that we might now make. If the draft amendments were now confirmed by this committee, and our report should so state, that we understand the problem and that we accept the assurances that these, in such form, would reach the places that they should reach, it seems to me that we could achieve the purpose of all honourable senators in this committee, and in the Senate itself; and by consensus we can do anything we want in this committee by way of recommendation, be it amendments or representations to the Senate itself in our report, and then the Senate as well can deal with those things as it sees fit.

Senator Grosart: A very excellent suggestion, that there is nothing in the world to stop the committee rejecting these amendments and then telling the Senate it is sorry it did.

Senator McElman: That is not what I proposed.

Senator Phillips: Mr. Chairman, later on might be a more opportune time to ask this question. It seems to me we are getting into several different fields.

I would like some clarification on the various forms of pensions that are included in that. I defer to your wisdom, sir, on whether that should be decided now or at a later date. Perhaps we are getting sufficient before us now that it would be better to put this off until later.

The Acting Chairman: You can ask Mr. Thorson questions on that now, if you like, or you can raise the point at a later time. Whatever you say.

Senator Phillips: Well, I have it in my mind now, Mr. Chairman.

Mr. Thorson, you have mentioned pensions and annuities. What pensions are included in that?

Mr. Thorson: Specifically, senator, the additional amounts I was referring to are those set out in section 212(1)(h), pension benefits. That is on page 520. The paragraphs in question are 212(1)(h), (i), (j), (k), (l), (m), (n) and (o). These are the new provisions, sir, that I was referring to.

Senator Phillips: Specifically, are veterans' pensions affected in any way? I refer to both disability and war veterans allowances.

Mr. Thorson: Yes, they would be; yes, if remitted to a non-resident.

Senator Phillips: In other words, a non-resident in receipt of a disability pension under this act would now become taxable whereas, I understand, under the previous act he would not be taxable.

Mr. Thorson: That is right, subject to the qualifications set out in the concluding portion of paragraph (h).

Senator O'Leary: Mr. Chairman, if we cannot hear amendments moved, mine or others, what on earth are we doing here?

The Acting Chairman: I have not said that.

Senator O'Leary: I asked that there be a vote on my amendment, and the members of the committee are free to vote against it or for it.

Senator Cook: Mr. Chairman, I have been giving some thought to this matter and, with the co-operation of the committee, I think I have an amendment which meets my views and which might be in order. May I read my amendment to Senator O'Leary's motion?

> That the bill be not so amended at this time, but that the proposed amendment be brought to the attention of the minister with the request that it be made part of the amending act promised for next year.

I move that as an amendment to Senator O'Leary's motion.

Senator Grosart: On a point of order, Mr. Chairman, I suggest that that amendment is completely out of order. The principle is clearly established that an amendment cannot completely negative a motion. The motion is that an amendment be made. This completely negatives that motion, because it starts with the words "That it be not now taken into consideration".

Senator Cook: I said, "at this time".

Senator Grosart: I suggest to you, Mr. Chairman, that if it were possible in any way, with an amendment, to make it impossible for an amendment to be carried, even if there are sub-amendments and you can go back to it, that would be denigrating the whole parliamentary process. Surely, we have the right to vote on an amendment.

The Acting Chairman: Senator Cook, I think that your proposed amendment to the motion does in fact do what Senator Grosart has pointed out, namely, negatives the original motion, and I think we can do that on the vote which is taken on the main motion. I realize that a good many senators here are concerned about the effect of negativing a proposal that has been made in respect of this measure already, and what the consequences would be if this amendment were voted down. I am assured by our counsel that the recommendations which we have made in respect of tax reform legislation still stand and that we can nonetheless deal with specific amendments of this character without affecting our general recommendations in respect of our general views on tax reform.

Senator Cook: With all respect, Mr. Chairman, the amendment is dealing with the report of the Standing Senate Committee on Banking, Trade and Commerce, and they are suggesting that it should be dealt with in such a way—in other words, to amend the act.

My suggestion is that the amendment be approved and be sent to the minister. I do not think it disposes of the original motion at all. The motion was dealing with the suggestion of the Standing Senate Committee on Banking, Trade and Commerce, which we are here, and the suggestion was that it be handled in a certain way. I am suggesting that it be handled in another way, and I do not think it vitiates it at all.

Senator Grosart: Mr. Chairman, in this motion of Senator O'Leary's we are not in any way dealing with any recommendation of this committee. We are dealing with the bill before us in the way that a committee of this kind is expected to deal with it.

Senator Cook: It seems to me that I have heard over and over again that these are recommendations of the Standing Senate Committee on Banking, Trade and Commerce.

Senator Grosart: It does not matter. It could be a recommendation from the race track.

Senator Cook: So long as it is clear that it is not a recommendation of the Standing Senate Committee on Banking, Trade and Commerce, but is a recommendation of Senator O'Leary's.

Senator O'Leary: You can vote against it.

Senator Cook: I intend to.

Senator O'Leary: Well, certainly.

The Acting Chairman: There seems to be some doubt as to whether or not we can vote upon an amendment. I think the committee is now in the frame of mind where it will decide whether or not we should vote on this amendment and what the disposition of it should be.

Those in favour of the amendment, please indicate in the usual way.

Those of the committee who are opposed to the amendment, also please indicate in the usual way.

There are five for and ten opposed.

I declare the amendment lost.

Senator Hays: Mr. Chairman, I would like to make a motion now that all the recommendations of the Standing

Senate Committee on Banking, Trade and Commerce be sent forward to the minister to be considered in the amending bill.

The Acting Chairman: In an amending bill?

Senator Hays: Yes.

Senator Phillips: What is the amending bill, Mr. Chairman?

Senator Grosart: Mr. Chairman, just to speak to that, I would have no objection to Senator Hays' amendment so long as the emphasis is on the word "all," because we have to remember that recommendations were made by this committee in its report on the White Paper, many of which are not incorporated in the bill as it stands. Many recommendations were made in the three subsequent reports known as the preliminary report, the second report and the final report. So this committee has made far more recommendations than those which merely appear as top priorities in the third and final reports. I think it should be clearly understood that we are speaking of all the recommendations of this committee.

Hon. Mr. Phillips: Would it not be in order to word the proposed resolution simply in the context of saying that the minister's attention is again drawn to the reports filed in the three instances?

Senator Grosart: I do not care how it is worded. Our job here is not to send messages to the minister.

Senator O'Leary: Hear, hear! We are dealing with Parliament, not the minister.

Senator Grosart: We are dealing with the bill, and we have to decide what we are going to recommend when we send this bill back to the House of Commons. I have no objections to this at all, so long as we remember that our obligation, our primary obligation, our minimum obligation, as a Senate, in dealing with legislation is to decide whether amendments should be made and, if so, to communicate those to the House of Commons. So long as we remember that, I do not mind this motion at all.

Senator Martin: I suggest, Mr. Chairman, that Senator Grosart may have his own concept of duty, but that does not mean that because he suggests that this is what we should do that it is of necessity what we should do.

Senator Grosart: I said that I "suggested".

Senator Martin: That is a question of technique, but what most of the members of this committee are concerned about is to see that the recommendations of the committee are met, if that is possible.

The minister said this morning that he would bring in an amending bill. He said that he was impressed with some of the recommendations, and that he would give consideration to other recommendations that had been made by the Standing Senate Committee on Banking, Trade and Commerce after its prolonged study, and if they satisfied him—and, of course, he had to add the Cabinet, without whom there could be no action taken by the executive—he would bring forward these as part of the amending bill.

Senator Grosart: We heard him.

Senator Martin: And we have heard you too, and I hope you will allow others to speak as well. That being the case, and since the members of the committee are anxious to see something done about their recommendations, surely we must ask what is the most effective way of getting these recommendations attended to.

Senator O'Leary has proposed one way, but that way, in the judgment of some of us, would clearly have a delaying result. Surely, in the light of what the minister said this morning—and everyone has commended his frankness and the assurance he gave—we are more likely to achieve what we have in mind by the kind of direction that Senator Cook and even Senator McElman mentioned than by the other method.

Senator Benidickson: And achieve a better result than we thought a week ago.

Senator Martin: Exactly, we would achieve a better result than we thought some time ago. But this explanation I think is due, because if we do not offer this kind of explanation it will be charged in one of the Ottawa papers—and I do not say which one—that senators were not anxious to support the bill, and were not anxious to continue to support the recommendations of the Banking, Trade and Commerce Committee, and that the only stalwarts in the country were the three horsemen from the Senate who sat in the front row of the Senate committee on this day prior to the day of St. Nicholas.

Senator Grosart: And one horsewoman.

Senator Martin: So that is the situation and Senator Grosart is a very sincere and active senator, as is Senator O'Leary, but so are other senators.

Senator O'Leary: But, Senator Martin, you are anxious to approve the bill, and I move an amendment with that anxiety in mind and you are against it. What do we do in that situation?

Senator Martin: I did not say we were against it.

Senator O'Leary: Well, if I were to judge by the tenor of the talk, you are. Let us be fair and frank. And if you are for it, then I am going to move that we have a vote.

Senator Martin: We just had it.

Senator O'Leary: I would like the members of the committee to stand.

Senator Martin: We have voted.

Senator O'Leary: Are we precluded from moving other amendments today? Is the same treatment to be given to other amendments that was given to mine?

The Acting Chairman: I do not answer for that; the committee has the answer to that.

Senator Everett: I wonder if we could answer Senator O'Leary's question by proceeding with the motion by Senator Hays, because if that motion is rejected, Senator O'Leary might very well be right.

The Acting Chairman: Could Senator Hays repeat the motion?

Senator Hays: I need some help, but you know what I mean.

The Acting Chairman: Perhaps the committee would help the chairman in this respect. Senator Hays moves that all the recommendations made by this committee in its three reports be submitted for consideration and appropriate action taken in legislation to be introduced at a later time.

Senator Grosart: As indicated by the minister.

The Acting Chairman: All right, as indicated by the minister.

Senator Isnor: Why not leave out the word "three"?

The Acting Chairman: I think the idea in Senator Hays' motion, as I recall it, is that all the recommendations made by this committee in its study of Bill C-259 in the fall of 1971 be placed before the minister for consideration, as was done again this morning and as he commented upon this morning.

Senator Grosart: Perhaps you would include the words "recommendations to the Senate".

The Acting Chairman: Now perhaps they become recommendations to the minister from the Senate.

Senator Grosart: But these were recommendations to the Senate.

The Acting Chairman: Yes, but they become that, perhaps, as a result of the action that might be taken here.

Senator Grosart: I would be a little careful about that because, as I said, we do not have any responsibility here to give advice directly to the minister, we are under the obligation to report to the House of Commons. But I will not argue about it.

Senator Phillips: If I may, Mr. Chairman, I would like to raise a point of order. I am not opposing the motion on principle, but I want to establish to whom we refer this motion. I think it is entirely wrong to refer it to the Minister of Finance; and we either refer it to the House of Commons or to Her Majesty's Privy Council, as someone a little more specific than a minister of finance. The Minister of Finance could change tomorrow.

Senator Hays: The Minister of Finance never changes.

The Acting Chairman: I think Senator Grosart has answered that point. Because if the recommendation is made from this committee it is carried to the Senate, and once it is in the Senate, surely, judicial notice is taken of it.

Senator Benidickson: Mr. Chairman, I have no quarrel whatever with Senator Hays' motion, but it is not a substitute, is it, for a final report?

The Acting Chairman: No. Is the committee ready for the question on Senator Hays' motion?

Senator Phillips: Before we vote on it, Mr. Chairman, I would like to know what I am voting on.

The Acting Chairman: I will try to reconstruct it again, and I will ask again for the assistance of the committee. It is this: That all the recommendations made by the Standing Senate Committee on Banking, Trade and Commerce, as contained in its three reports to the Senate, be submitted to the minister for consideration, and that appropriate action be incorporated in legislation to be introduced at a later date in accordance with the undertakings of the Minister given this morning.

That is not the same language that I used a moment ago, but is this the sense of the committee?

Senator Isnor: Why not leave out the word "three"?

The Acting Chairman: All right, we will leave out the word "three". I think I used the words "in the autumn of 1971".

Hon. Mr. Phillips: Yes, I think you should put that in.

The Acting Chairman: "in the autumn of 1971." Are honourable senators ready for the question?

Senator Grosart: I would suggest that we leave the precise wording to the acting chairman.

The Acting Chairman: Would you leave the wording with our counsel from Montreal, the gentleman sitting to my left, Mr. Phillips, and myself to work out?

Senator Grosart: We are indicating our confidence in you.

The Acting Chairman: I am sure Mr. Phillips and I both appreciate that gesture.

Is the committee ready for the question to be put on the unworded motion? You are showing great confidence.

Those in favour of Senator Hays' motion, please indicate in the usual manner.

There are 17 in favour of the motion.

Those who are opposed to Senator Hays' motion, please indicate by raising your hands.

There is one opposed to the motion.

I declare the motion carried.

Honourable senators, are there any other questions to be asked of the officials?

Senator Grosart: Yes, Mr. Chairman.

Senator Benidickson: Will we adjourn while the report is being drafted?

The Acting Chairman: No, Senator Benidickson. We will continue in committee, since Senator Grosart has questions to ask of the witnesses.

Senator Grosart: Mr. Chairman, I believe the witnesses have before them the draft amendments which were proposed by this committee. If I may, I will refer to them.

The Acting Chairman: Senator Grosart, may I identify this for the *Hansard* staff and make a copy of the draft amendments dated November 30, 1971 available to them?

Senator Grosart: Yes, by all means.

The Acting Chairman: Would you indicate the page number which you are quoting from?

Senator Grosart: There are no page numbers. However, it is the third page.

Senator Martin: From what document are you reading?

Senator Grosart: The document which was just referred to, the draft amendments. I would like to ask the officials a question concerning Clause 52(5)(b). It may have been changed, but it is suggested that this clause be amended to read as follows:

> The beneficiary shall be deemed to have acquired the property at a cost equal to its cost amount to the trust at the time of the transfer.

This has been fully explained in the third report of the committee. I will not go into it except to ask the officials whether they see any reason why this amendment could not be incorporated in the bill at the present time.

Senator Martin: I am not clear with what Senator Grosart is dealing.

Senator Grosart: It is on the third page of the document.

The Acting Chairman: It is entitled, "Employees Profit Sharing Plans," and Senator Grosart is referring to item No. 2, Clause 52(5)(b) of Bill C-259.

Senator Martin: Thank you.

Senator Benidickson: Yes, but where does this document come from? Is it a part of the third report?

The Acting Chairman: I understand it has been taken verbatim from the third report of the Senate committee.

Senator Grosart: No, it is not in the report.

The Acting Chairman: It is not part of the recommendations of this committee?

Senator Grosart: Mr. Chairman, I have read these reports, and unless I have overlooked them, these amendments, as drafted, are not in the report which was presented to the Senate.

Hon. Mr. Phillips: Senator Grosart, the copy which has been submitted to us indicates that it is from Report No. 1.

Senator Grosart: Is it in Report No. 1? That is fine. I indicated it was not in the third and final report.

Senator Benidickson: Can we call it Report No. 3?

The Acting Chairman: No, Report No. 1, I am told.

Senator Benidickson: My recollection is that Report No. 1 related to policy, without any specific suggestions or amendments. Am I wrong in that assumption?

Senator Beaubien: You are looking at the White Paper.

Senator Grosart: Does anyone have a copy of Report No. 1?

Senator Benidickson: I am talking about the document dated November 30.

Hon. Mr. Phillips: Senator Grosart, I do not think it is contained in report No. 1.

Senator Grosart: That is what I said. My understanding was that these amendments were never invorporated in a report.

Senator Benidickson: That is what I want cleared up.

Senator Grosart: It was explained to us by the chairman that the committee had begun drafting amendments but, due to the lack of time, they had not completed them. Therefore, they merely set them forth in this mimeographed form.

Senator Benidickson: I see, they are on the shelf then.

The Acting Chairman: Does the same thing apply to Senator O'Leary's amendment?

Senator Grosart: Yes, exactly.

The Acting Chairman: Have these draft amendments, which have been identified, been the subject matter of a report by our committee?

Senator Grosart: No, they have not.

Senator Benidickson: I do not think so.

The Acting Chairman: Where do they originate?

Senator Benidickson: I discussed this matter with you yesterday; that is why I raised this matter.

The Acting Chairman: It is just as well that you did raise the matter.

Senator Grosart: I assure you that this is not a leak, and I was amazed that no one opposed to the original motion raised this matter regarding the fact that it was not part of the committee recommendations.

The Acting Chairman: I think that what was being proposed could have been made clear to the committee.

Senator Grosart: And it was amended by Senator O'Leary.

The Acting Chairman: Perhaps some of the concerns expressed by members of the committee are now dissipated completely.

Senator Langlois: What was the purpose of putting this handwritten note on the document?

Senator Grosart: I do not know. I did not put it on the document.

Senator Langlois: This is your document; you should know.

Senator Grosart: It is not my document.

Senator Langlois: Whose document is it?

Senator Grosart: I do not know. This document was distributed to all honourable members of the committee.

Senator Benidickson: It has the handwritten note, "Top priority."

Senator Grosart: It is a document which was distributed to senators by the staff of the committee.

The Chairman: It was given to the staff of the committee for distribution, I understand, from Senator Flynn's executive assistant. Coming from a high office such as that of Senator Flynn, it seemed to be appropriate that it should be distributed and dealt with on its face value. I directed that it should be distributed, but now we learn that it is not an official document of this committee. I do not know where it originates.

Senator Beaubien: Where does it come from?

The Acting Chairman: I have no idea, Senator Beaubien, where it comes from. I am as puzzled as anyone else.

Senator Grosart: It is a leak.

Senator Phillips: Was the document not part of the last motion?

Senator McElman: I might say that I was not taken in by it. Senator Grosart thought we all missed it. As this was distributed, I asked the question, "from where does it emanate?" I did not receive a direct answer, so repeated the question and asked very urgently for a reply. I was told that it had come from Senator Flynn's office, and I have not regarded it as an official document of this committee; and I do not now regard it as such.

Senator Benidickson: It is entitled "Top priorities, Report No. 1".

Senator Grosart: Mr. Chairman, I do not think we need to waste very much time on it. We know it came from the committee; it does not matter whether it is official or unofficial.

The Acting Chairman: Let us clear up the one point: Were any members of the committee aware of this document? I certainly was not until it was presented to me a moment ago. I thought the situation was that, for the convenience of the committee this afternoon, specific drafts of amendments as suggested by it originally were re-written. Obviously this is something else.

Senator Grosart: No, this has been around for three weeks.

Hon. Mr. Phillips: Mr. Chairman and honourable senators, the three reports of this committee in 1971 consist only of the following: the first dated November 4, 1971; the second dated November 24, 1971; and the third dated December 13, 1971.

Senator Grosart: Yes, we are all aware of that, except that we were told here, both by the chairman—

Hon. Mr. Phillips: This document of November 30, 1971 is not related to any committee report or activities as such.

Senator Beaubien: Was that not prepared by the Senate committee?

Hon. Mr. Phillips: If it was prepared by any of the staff of the committee, of which I am not aware, it is certainly not incorporated in the report.

Senator Grosart: I think we should be clear on one thing, that the chairman told us it was incorporated.

The Acting Chairman: No, I certainly did not say that.

Senator Grosart: Let us forget it then; I do not think it matters. We know it came from the committee.

The Acting Chairman: Is it a working paper of the committee? I think it is up to Senator Grosart, if he knows, to tell the committee where this came from. Is it a working paper of the committee which came into the hands of one of the members of the committee?

Senator Cook: Sure, Mr. Chairman, it is a working paper; it is a first draft.

Senator Beaubien: Our staff can tell us.

Senator Grosart: The staff can tell us. We know perfectly well that this was prepared by the staff of the Senate committee.

The Acting Chairman: But it has not come before the committee for approval.

Senator Grosart: No.

The Acting Chairman: Or for consideration.

Senator Grosart: No.

Senator Cook: It is only a first draft and has been superseded.

Senator Beaubien: Who made the draft?

Senator Cook: I think the chartered accountant on the staff.

Senator Beaubien: I think we should ask them.

Senator Cook: What is the trouble?

Senator O'Leary: We have disposed of it, anyway. What is the use of worrying about where it came from. I do not know where it came from, and I do not care.

The Acting Chairman: Perhaps we have said enough with respect to the document, because apparently no one will admit pride of parentage in any way. Nonetheless, the document itself contains material which may have a bearing upon the bill. If any honourable senators wish to direct questions on the basis of the document, without in any way contributing to its authenticity, they are perfectly at liberty to raise any point which may come to mind as a result of perusing it or, indeed, any other point that comes to mind.

Senator Hays: Mr. Chairman, do you have a record of the number of meetings that the Standing Senate Committee on Banking, Trade and Commerce held to consider the White Paper and since September 10 in dealing with the proposed legislation?

The Acting Chairman: I am sorry you did not hear my great speech, but I did put this information on the record. My memory is very faulty, usually, with regard to figures of this kind. I think, however, there were approximately 80 sittings in the consideration of the White Paper.

Senator Grosart: I do not remember, but it was a very impressive figure.

The Acting Chairman: Yes, it was a great figure.

Senator Cook: Fifty-five.

The Acting Chairman: That would be it, 55. I believe there were 26 hearings since September, 1971.

Senator Hays: Do you have a record of the number of witnesses who appeared?

The Acting Chairman: I did at one stage.

Senator Grosart: It is contained in the report.

The Acting Chairman: I stated these figures in the chamber. There were, I believe, 140 witnesses before the committee this fall, and a little more than 400 during consideration of the White Paper.

Senator Martin: And, Mr. Chairman, we were the only committee in Parliament that did hear witnesses with respect to the bill.

Senator Benidickson: From outside.

Senator Martin: From outside.

The Acting Chairman: That is true.

Senator Grosart: Which, I suggest, greatly increases our responsibility to the House of Commons, which did not have the opportunity to hear those witnesses.

Senator McElman: But they have the benefit of our reports.

Hon. Mr. Phillips: With the concurrence of the chairman, Appendix "A" to our final report contains the dates of the hearings with respect to the summary of 1971 tax reform legislation. It also sets out the organizations and/or individuals and groups which appeared before it.

The Acting Chairman: But, in addition to that, the committee held many other meetings, of course, at which there were no witnesses.

Senator Hays: Does that include these?

The Acting Chairman: No. I believe 26 is the overall figure for the number of hearings.

Senator Grosart, we have delayed you a long time. You have been very patient and have also contributed to the discussion in the meantime. Would you like now to proceed with your questions?

Senator Grosart: I think the officials have my question; I see them referring to the particular quote, if I may use that word, the unofficial quote I gave them.

Mr. Cohen: Senator, I am not sure how to answer your question, because I am not sure that I fully understand it. An amendment is a two-step transaction. The first part is a policy decision; the second part is a question of drafting.

Senator Grosart: Yes.

Mr. Cohen: I am not certain, sir, whether your question relates to the first or second point. If it is on the second point, although I cannot speak for Mr. Thorson, I have not had sufficient time to examine this language in order to determine whether it is appropriate. I understand its intent in a policy context, but when you ask if it will work, I need more time to determine if the precise wording is appropriate.

Senator Grosart: I realize your problem. It was really, in the last analysis, a policy question, whether you see any reason why it should not be incorporated. In view of the fact that the minister has given us reasons for preferring to delay the decision, it is perhaps unfair to ask you.

The Acting Chairman: In any event, you would not ask these witnesses questions dealing with policy.

Senator Grosart: I would not ask them a difficult question if I could avoid it.

The Acting Chairman: Difficult questions are one thing; policy questions are another.

Senator Grosart: Mr. Chairman, I move that section 52(5)(b) of Bill C-259 be amended to read as follows:

> 52(5)(b)The beneficiary shall be deemed to have acquired the property at a cost equal to its cost amount to the trust at the time of the transfer.

Senator Hays: Is that one of the recommendations, Mr. Chairman?

Senator Grosart: One of the secret recommendations.

Hon. Mr. Phillips: It is not one of the formal recommendations referred to in the three reports.

Senator Grosart: It incorporates, in amendment form, I believe, the sense and intent of one of the recommendations appearing in final Report No. 3.

Hon. Mr. Phillips: I think you will probably agree, Senator Grosart, that the subject matter with which you deal in section 52(5)(b) is dealt with in Report No. 3.

Senator Grosart: This is an amendment which gives substance to the recommendation.

Hon. Mr. Phillips: It would be a matter of interpretation as to whether this wording does give sense to the report.

Senator Martin: We want to be precise. We cannot simply accept Senator Grosart's assurance. Would counsel tell us if the language in this document represents one of the recommendations of the Senate committee?

Hon. Mr. Phillips: No, it deals with the subject matter dealt with, but not with the formal recommendation.

The Acting Chairman: Is there further discussion on Senator Grosart's motion? Is it necessary for me to put the motion again? Senator Grosart has moved that section 52(5)(b) of Bill C-259 be amended to read as follows:

> 52(5)(b) The beneficiary shall be deemed to have acquired the property at a cost equal to its cost amount to the trust at the time of the transfer.

Senator Hays: Mr. Chairman, before you put the motion, this deals with charities, does it not?

The Acting Chairman: I am only putting the motion. Senator Grosart is moving it.

Senator Hays: But this motion may not be in order. If we have already moved that all of the Committee's recommendations be sent to the minister, how can we start amending it after we start making these recommendations?

The Acting Chairman: In the light of what counsel has told us, this amendment does not specifically reflect a recommendation of the committee. Is that so, Mr. Phillips?

Hon. Mr. Phillips: As I understand it, Senator Grosart's motion is by way of an amendment to Bill C-259.

Senator Grosart: That is right.

Senator Martin: It is not incorporated in the recommendations of the committee's report.

Hon. Mr. Phillips: The answer is that it is not incorporated in the committee's report other than in respect of the subject matter, but not in the proposed amendment.

Senator Martin: And in connection with this, we have had no explanation whatsoever as to its implications.

Senator McElman: As I understand it, this subject was considered by the committee, but it did not choose to make this recommendation. Is that correct?

Senator Grosart: That is not so.

Hon. Mr. Phillips: Probably we should state the following: In addition to the recommendations that were submitted to the Senate and approved, there was a certain amount of mental and intellectual exercise in terms of draftsmanship, in the hope that in due course, when we were dealing with the acceptance of our recommendations, we might be of assistance in the submitting of some phraseology.

Senator O'Leary: Would you say, sir, that this expresses the spirit and substance of the recommendations?

Hon. Mr. Phillips: I would say that it deals with the subject matter, but I am not prepared to state that it covers the spirit.

Senator Beaubien: If we are going to comment on this, we should know whether it fits in with the committee's wishes.

Senator Hays: Is it in order?

Hon. Mr. Phillips: As I say, the only recommendations approved by this committee and by the Senate are in the three reports. These so-called draft amendments are merely exercises in draftsmanship from the point of view of what might come before the Senate in due course in dealing with the subject matter of the legislation.

Senator Martin: I am sure that Senator Beaubien's remark is one that we all accept. We have to know more about what this means, its origin, and so on.

Senator Buckwold: Mr. Chairman, would you accept an amendment in the form of a referral motion, in which Senator Grosart's motion is referred to this committee for further study?

Hon. Mr. Phillips: No. This is a motion to amend Bill C-259.

Senator Buckwold: But the committee has not had an opportunity of reviewing it.

The Acting Chairman: I think we should deal with this matter as it stands. I am bound to say that when a member of this committee moves an amendment, as did Senator O'Leary, and as I am sure Senator Grosart is prepared to do, an honourable senator should be prepared to express the reasons why he moves an amendment in a specific form. If the committee is satisfied with his reasoning, it then votes accordingly. It can vote either in favour of the amendment or against it.

Senator Grosart: Mr. Chairman, I will gladly respond to the request that I indicate the purpose, intent, and origin of this amendment. If honourable senators care to refer to Report No. 3, Appendix "B" at page 8, they will find that this committee named nine proposed changes in the bill and described them as "top priority recommendations."

No. 2 is "Employees Profit Sharing Plans," which is the matter dealt with in my amendment. Report No. 3 refers specifically, for information, to pages 47-8 of Report No. 1. If the committee desires, I will be very glad to read almost the full column which fully explains this amendment and makes it very clear that its intent is to give effect to the recommendations made by the committee. I leave it in your hands, Mr. Chairman, whether the committee wishes me to read that. It is on page 47-8 in Report No. 1 under the same heading, "Employees Profit Sharing Plans".

Senator Hays: I suggest that this is out of order. We have had a motion, which we have dealt with unanimously, that all these go to the minister. I do not see how we can have an amendment on one of these recommendations. I do not think the motion is in order.

Senator Cook: Our colleague very properly keeps on giving top priority to the words "top priority". I would point out that this was done at the request of the minister. He asked us to let him know what we considered to be top priority, which we did. In committee he said that he would give them consideration. This top priority business was done at the request of the minister. He said, "You have a great number of items. Which ones do you want to be considered at the top?" We gave them to him, and he said he would give them consideration. I keep on making the point as to why, when the minister says he requires a little more time, we say to him, "No, you must take our amendments now." He said he would give them consideration at the earliest possible opportunity, and we are now saying, "No, do it now." It does not seem to me to make any sense.

The Acting Chairman: Is the committee ready for the question?

Some Hon. Senators: Yes.

The Acting Chairman: Those in favour of Senator Grosart's amendment will please signify in the usual way.

Four in favour.

Those against Senator Grosart's amendment will please signify in the usual way.

Ten against.

I declare the amendment lost.

Senator Hays: Mr. Chairman, I would like to move that this motion that has just been defeated be now referred to the minister for consideration in the amending bill.

The Acting Chairman: The chair is in a difficult position, Senator Hays. It has been almost impossible to determine the origin of this material.

Hon. Mr. Phillips: Mr. Chairman, may I deal with the subject? In Report No. 1 of this committee, Senator Grosart said at page 47-8, in the second column at the top—

Senator Grosart: Mr. Chairman, on a point of order. Is Mr. Phillips dealing with the motion which has just been defeated?

Hon. Mr. Phillips: No, I am not. Senator Hays has suggested a motion, Senator Grosart, to send your motion to the Minister of Finance for consideration. I am now referring to what you referred to where the subject matter of certain transfers acquired by a trust at a given moment is dealt with.

The amendment that the honourable Senator Grosart suggested is at variance with it on a particular technical point with respect to the cost to the trust of a capital asset.

Senator Hays: I will withdraw my motion.

Hon. Mr. Phillips: That which Senator Grosart was dealing with was the insertion of the phrase "at the time of the transfer," which goes to the whole question of the costing of the capital asset. That is why I said to Senator Grosart that that which he dealt with by way of his motion which has just been defeated, in so far as the subject matter is concerned, is dealt with in our report. When Senator O'Leary asked me whether that which Senator Grosart suggested was in accordance with the spirit of what we have reported, I said that I am not prepared to go that far because we were dealing with the crucial question of cost of a capital asset.

I am merely explaining the reason which justifies my saying that the proposed amendment now behind us does conform in spirit. I though I owed it to myself and to honourable senators to explain the reason for my dissent.

Senator Grosart: I am quite prepared to let the record speak for itself.

Senator Phillips: Mr. Chairman, earlier I had asked Mr. Thorson a question concerning the effect of this bill on veterans' pensions and war veterans' allowances. Since that time he has been good enough to send me a couple of notes indicating that neither the disability pensions nor war veterans' allowances are affected in any way by this bill. I am prepared to accept those notes, but I would like the record to show that they state that neither disability pensions nor war veterans' allowances are affected by this bill.

Am I correct, Mr. Thorson?

Mr. Thorson: That is so, senator, in terms of the Part 13 withholding tax on payment to non-residents.

Senator Phillips: And are there any other changes regarding war veterans' allowances or disability pensions in this act?

Mr. Cohen: I do not believe so, senator. The exemptions are contained in section 81(1)(d). They are identical with the old act.

Senator Phillips: I would appreciate you checking that. I am not an expert in tax matters, Mr. Cohen, and, like a good many members of the committee, I share concern in this regard, and I would like to have it clarified.

The Acting Chairman: Perhaps Mr. Cohen and Mr. Thorson can look up that point.

Mr. Thorson: The old provisions and the new provisions are identical with respect to that point.

The Acting Chairman: You are satisfied on that point now, Senator Phillips?

Senator Phillips: Yes, Mr. Chairman.

Mr. Thorson: That is on the exemption as far as a resident Canadian is concerned.

Senator Phillips: I did not mean veterans who are non-residents; I meant Canadian veterans, Mr. Thorson.

The Acting Chairman: They could be Canadian veterans who are non-residents.

Senator Phillips: Yes, but I mean residents in Canada.

The Acting Chairman: I think he has satisfied you on that point, about Canadian veterans who are resident.

Senator Phillips: Well, his last answer left me a little confused. I was satisfied up to that point that they were not being affected.

A Canadian veteran on disability or war veterans' allowance is in no way affected by Bill C-259, is that correct?

Mr. Thorson: That is correct.

Senator Benidickson: Mr. Chairman, I was out of the room for a few moments. Perhaps we are on this point now. I read hurriedly the other day that this bill might involve a change in the net receipt of a Canadian resident who, for retirement or other reasons, decided to go to the United States. Is there anything in this bill respecting the withholding tax for such an individual?

Mr. Cohen: Yes, there is a change in the withholding tax provisions, but there is also a protective clause which says that if the buden of the withholding tax is heavier on a pensioner who has retired out of the country than he would have paid had he stayed in this country, then he could take the latter option. He is no worse off.

Senator Beaubien: Mr. Cohen, if he goes to the United States, is that not covered by a withholding tax treaty?

Mr. Cohen: The withholding tax rate is effected by a treaty and some of the exemptions from withholding tax are covered by treaty, but there is a general provision in our act which would relieve a taxpayer from any heavier burden of Canadian income tax.

Senator Beaubien: If we have a tax treaty with the United States, how can we change it in this bill?

Mr. Cohen: We can reduce our tax.

Senator Beaubien: Does this bill reduce the tax?

Mr. Cohen: We are talking about the imposition of Canadian tax on Canadian source income. We can bring that down, notwithstanding the fact that there is a treaty.

Senator Beaubien: Well, if that is what we are doing, that is not what Senator Benidickson is concerned with, is it?

Senator Benidickson: I was referring to a news item of two or three days ago. We have had so many amendments that I was wondering if one of them provided some relief from the original hardship in this respect?

Mr. Cohen: My recollection, senator, is that that has been in the bill since it was first tabled, but I could be mistaken. It may have been by way of amendment, although I do not believe so.

Senator Benidickson: I am considering the position of a very moderate income earner who in old age decides to go to a better climate, and I thought this bill imposed some hardship upon him.

Mr. Cohen: Well, the answer is the same as before, and that is that there is an exemption in the United States treaty with respect to pensions and annuities.

The Acting Chairman: Are there other questions of the witnesses?

Senator Phillips: Yes, Mr. Chairman, I have several questions.

My first question is with respect to the sale of a property as a result of which there is a capital gains tax. I am thinking of the pattern in the last few years where large numbers of people who built apartment houses, office buildings, and so forth, went abroad for their financing. They probably received a lower rate of interest, but in return the people putting up the financing took an equity position, perhaps, 20 per cent or 30 per cent, we will say for the sake of discussion. I am not going to attempt to give you the section because there are so many of them, but what position are those people in now and how will this affect their source of money in this regard in the future?

Mr. Cohen: Again, I am not certain of the question, senator, but if you are asking how an individual who is not a resident—

Senator Phillips: Yes, a non-resident.

Mr. Cohen: If you are asking how a non-resident investor in Canada would pay his capital gain, it is in the same way as a Canadian resident. The capital gain would be the difference between the original cost of the property and the selling price. He would report that gain just as if he lived in this country. This is part of what we call taxable Canadian property.

Senator Phillips: Is that individual, bank or corporation subject to the 15 per cent withholding tax?

Mr. Cohen: Not on the capital gains portion.

Senator Phillips: But they are still subject to that 15 per cent withholding tax.

Mr. Cohen: On the annual rents or interest, yes, but not on the gain portion.

Senator Phillips: It seems to me that in this clause we are cutting off a very important source of money in a field in which we need it very badly at this time, in the construction industry and so on.

The Acting Chairman: This is policy, I think.

Senator Phillips: I know this is a matter of policy, and I am not going to involve Mr. Cohen or Mr. Thorson in this, but I believe it is a terrific mistake to cut off this source of funds at a time when we need them so badly. I hope that in all the generous entertainment our committee reports are to receive this point will also be included.

Senator Everett: Mr. Cohen, there are three areas of the legislation that bother me greatly, which I do not think this committee has dealt with adequately in all its hearings and examination of this bill: The first is the problem of ministerial discretion, which continues to exist in this amending bill; the second is the matter I raised this morning, that of corporate indistributed income; and the third is the lack of definition between capital receipts and income receipts. It would appear that under this bill it will still be a matter of jurisprudence, and it is quite possible that a whole new set of jurisprudence will be required to determine the difference between the two.

Dealing with the latter point first, I notice there have been recommendations that certain expenditures are not expenses for the purpose of gaining and producing income, and that is just by fiat. The one that I suppose comes readily to mind is yachts, where they just clamp down against yachts, regardless of for what they are used. I am not the owner of a yacht, so I do not have to disclose any particular interest here.

Senator Martin: Perhaps a skidoo.

The Acting Chairman: A prairie schooner.

Senator Everett: It has been possible in the formulation of this bill to have specific definitions of what is a business expense and what is not a business expense. I cannot understand why certain receipts would not have been classified as capital receipts and as income receipts. If, indeed, this did happen it would greatly simplify the operation of the act and would simplify the position of the taxpayer.

Hon. Mr. Phillips: Mr. Chairman, may I be permitted, from my position as counsel for this committee, to answer Senator Everett on one basic point? You were busy, Senator Everett, because you had a very important committee.

The three reports were not intended or claimed to cover the entire gamut of the proposed taxing statute. Because of the limitation of time, they dealt with a number of subject matters that this committee thought most urgent and which required current attention. In dealing with the subject matter, for instance, of deduction from income, or the difference between capital gains and ordinary trading

income and all that sort of thing, there were all sorts of areas that this committee did not cover that, had it been able to do so, it would have covered the entire gamut of the bill and all its ramifications. But it did cover some special aspects of it, and more particularly those that were brought to our attention by very important representative organizations and taxpayers.

Senator Everett: Mr. Chairman, I am sorry that the committee did not see fit to cover probably the three areas that have given more trouble in tax law in Canada than any other three areas.

Hon. Mr. Phillips: This might have been so had your advice and guidance been with us, senator, but you were absent in another committee.

Senator Everett: I am sorry, because perhaps if so we would have dealt with these subjects at that time. However, I am surprised that you did not do so, anyway, without the benefit of my advice.

Hon. Mr. Phillips: However, I thought I would clear up that point.

Senator Everett: You did indeed raise the point that you did not deal with them. It just seems to me that I would like to hear from you, Mr. Cohen, if I could, on this point. The minister says he is considering the problem of undistributed income but, because integration was not acceptable to the taxpaying community, he has left that out, although there might be other means of handling it. Indeed, I would like to hear what you have to say about the problem of definition of receipts and the really serious problem of ministerial discretion.

Mr. Cohen: Taking them in order, senator, and starting with the last one, the definition of capital gains versus income, two points should be made before I answer in general terms. One is that you thought there might be new jurisprudence. There is nothing in this act which would change the direction of the old jurisprudence. It is the same issue as that which existed previously, except that it is, in a sense, if you will, half as important as it used to be, because now it is either half an income or all an income. So we hope that there will be a great deal less pressure on this point in the future.

With regard to the business expense, we specify by fiat, as you suggest, that certain items are to be non-deductible. But they are few and far between. One still has the vast panorama of activities that raise a question on both sides of the fence—that is, the deduction side as well as the receipts side: Is it an expense that was incurred for the purpose of gaining or producing income, that may make it deductible? And on the other side, as to whether an asset is a capital gain receipt or in the nature of an inventory or income receipt.

We did look very extensively and very carefully at a number of tests, which I could describe as arbitrary, that is, holding periods, classifications of assets, and we found, frankly, that no set of arbitrary lines like that seemed to be very satisfactory. They produce too many anomalies, particularly right at the edge. You use a holding period of six months, and six months plus one day has a very different result from six months minus one day.

Similarly, when you try to deal with assets by category, the lines become very harsh and the problem of definition became rather overwhelming. We felt that there was a body of jurisprudence but, again, it being half as important, if I may—which is not to suggest that the problem will not continue. It has continued in the United States, notwithstanding their holding period rules. There is less at stake and hopefully there will be less pressure on this point, but so far, we have not been able to come up with a satisfactory precise and accurate definition that would distinguish and segregate capital receipts from income receipts. So we have continued the present regime.

On the point of ministerial discretion, senator, let me observe, first, that there is no additional ministerial discretion in this statute.

Senator Everett: No, I did not suggest there was.

Mr. Cohen: No, but I am taking the opportunity to speak to others as well, who have suggested that there is an increase in ministerial discretion. In point of fact, there are a number of areas where we have adopted a reasonable test, which is something that the courts can decide. However, I do concede to you that we have retained the ministerial discretion that was present in the previous act—again, I suppose in part because it was needed then and it is needed now and that becomes inter-related, if you will, with the problem of corporate surpluses.

The bulk of the discretion is in that direction. It deals with corporations. Section 138A. (1), using the old section numbers, is a problem of corporate distributions, of surplus stripping and things of that sort. Because we still have the problem of corporate surpluses, we felt we had at least for a number of years to retain ministerial discretion, until we found out whether the new rules worked better than the old ones did. I share with you a hope that some day we will be able to get rid of these.

With regard to the corporate surplus problem, I am not sure I can add a great deal more than was added by the minister this morning. You have an extra level of corporate tax in play, no integration and a capital gains rate that is half of the ordinary income rate. You are always going to get pressure to convert ordinary income streams coming out of a corporation into capital. There is always the pressure to convert dividends into capital gains, as the capital gains for certain taxpayers attract a lesser burden of tax. And given that set of infrastructure we just felt that we had to retain the rules relating to surplus withdrawals.

Senator Everett: I do not think that is really a serious matter from the taxpayers' point of view. The difficulty that obtains there, and I am speaking historically, is that there is a difference between the marginal rate and the corporate rate of any degree and without the provincial increment. I can see a difference when we are speaking in terms of the distribution of surplus of 30 per cent in this act. As long as there is that difference, taxpayers will elect to leave their profits in the form of undistributed income. What happens is that it builds up and up, and eventually the Government comes along and says that for a flat tax of 15 per cent you can get it out. So the net result is that there is a lot of manipulation during that period, during which smart tax layers like Mr. Phillips advise their clients.

The Acting Chairman: Or Senator Everett.

Senator Martin: Or senator Grosart.

Senator Everett: They advise their clients that by doing this or by doing that they can drain their surpluses out. They can use the charitable route, the brokerage route, or they can use another route, but they can get the surplus out. It just seems to me to be unfortunate that we are not addressing ourselves to that problem, because it is just going to be another problem in another ten years, and in another ten years there is going to be this pressure to amend the act.

Hon. Mr. Phillips: Senator Everett, you do not want to take the bread out of the mouth of the tax lawyers, do you? We need the grey areas so that we can advise our clients!

Senator Grosart: There is no danger of that in this bill.

Senator Everett: Well, I thought on the last àgo-round' senator, that you made enough bread to retire for life!

Mr. Cohen: I would like to add one more point to the arguments we suggested to you this morning, senator. I do concede that the build-up will take place but, to put it in proper perspective, in addition to what we indicated this morning on small business deductions and pressure to pay out dividends there and the letting out of capital before surplus, in the same way that there is less pressure on the line between capital gains and ordinary income, now there is less pressure on the problem of surplus distribution because the essence of the surplus distribution under the old act was the fact that we were not taxing capital gains, so you could take it out for free.

Almost every surplus strip, at least that I know of, turns around a sale of the shares. That is going to produce a capital gain. So there is a lot less to be gained in the new system by a surplus strip and hopefully that too will relieve the pressure that does build up on these things. But I can see that over a long period of time surpluses may well reappear, and doubtless the government at that time will take another look at them.

Senator Grosart: Retroactively.

Senator Everett: In fact, it is retroactive, which is what you are now doing with the 15 per cent which is retroactive to the beginning of 1949, really. Two points arise out of that. The first is that there should be a recommendation from this committee that the minister give serious consideration to the on-going problem of corporate surpluses and their distribution, in some sort of conformity with the recommendation for post-January 1, 1972 surpluses. And the second point is that it seems that there should be serious consideration given to rulings by the minister on the subject of capital receipts versus income receipts and on those areas where ministerial discretion is exercised. As I understand the present ruling provisions, the Minister of National Revenue or the Department of National Revenue is not allowed to give a ruling on whether a receipt is a capital gain or income. Am I correct in that?

Mr. Cohen: Well, Mr. Pook is here from the Department of National Revenue, and he may be able to tell you about that.

Senator Everett: I am given to understand that under the present ruling provisions, which were invoked some few months ago, the department is not allowed to rule on whether a receipt is an income or capital receipt.

Mr. Cohen: I am not sure if everyone could hear Mr. Pook's answer, but he said that he is agreeing with the senator that the Department of National Revenue does not give rulings as to whether transactions are capital or ordinary income.

The Acting Chairman: In advance.

Mr. Cohen: In advance. You are talking now of advance rulings, senator?

Senator Everett: Yes, advance rulings—which I think would cut down the amount of difficulty that the taxpayer has and the amount of litigation that goes on between the minister and the taxpayer,—as to whether in specific cases the nature of a receipt is a capital or an income receipt; and the exercise of ministerial discretion. I think there should be a recommendation of that nature.

Senator Martin: I thought Mr. Gray announced, and indeed I said the other day in the house and quoted him, that an endeavour would be made, notwithstanding traditional practice to give opinions in advance of the maturity of a situation, subject, of course, to staff and so on. Is this one of the matters you are asking about senator?

Mr. Cohen: If I could answer that, the Minister of National Revenue did give a speech very recently in which he said that they were expanding the facilities for advance rulings; that he hoped to be able to maintain, at least, the time frame and even accelerate it; and that he was expanding his staff. I do not think that in his remarks he addressed himself specifically to the point that Senator Everett raises.

Senator Everett: Those points are of very great importance because under the present ruling provisions you pay $150 to the Minister of National Revenue, and then you, as a taxpayer, put before him a certain set of facts. The taxpayer also pays a contribution towards the time put in on assessing those facts by the officials of the Department of National Revenue, and is billed for that, in addition to the $150. Then a ruling issues. That ruling can be on the subject of ministerial discretion, although I gather from talking to other taxpayers that it is sometimes very difficult to get the rulings division to rule on the question of ministerial discretion, and they will not rule on the question of whether an income receipt is a capital gain or income.

Mr. Cohen: Forgive me for interrupting you, but by way of clarification, when you are talking about ministerial discretion it has a certain connotation for those of us in the trade; that is, a taxing power by the minister. You are not talking about that when you talk about ministerial discretion. You are talking about the minister exercising his capacity to give an advance ruling, whether it be favourable or unfavourable, as the case may be?

Senator Everett: No, I am talking about the taxing power, for example, as to whether corporations are or are not

associated. I am saying that you ought to be able to have advance rulings and exercise that discretion; and you should also have the discretion as to whether a receipt is income or capital gain based on the written facts which you put before the minister. I feel that recommendation should go to the minister.

The Acting Chairman: This is not the first time this point has been raised. It was considered during the course of our deliberations in September, October and November. Perhaps Hon. Mr. Phillips and other members of the committee can help me. It was taken into consideration but was not included in the specific recmmendations which were made to the minister. We have now drawn it to the attention of the officials. Mr. Cohen has it in his mind, and I am sure that others, including Mr. Pook from the Department of National Revenue, are aware of the intention of the committee.

Senator Everett: I would like to accept that, but I feel very strongly about this matter. I do not necessarily want it was part of the recommendations which have been put forward. I am proposing it as a separate motion. After all, it is a recommendation to the minister, asking him to consider the matter and do something about it.

The Acting Chairman: Senator Everett, when this committee rises some time today, perhaps you would be kind enough to draft a few sentences which could be included in the report which we make to the house.

Senator Everett: As a recommendation to the minister?

The Acting Chairman: As a recommendation to the minister, and the committee will then decide if it will accept the report which contains your suggestion. This will point out more clearly your suggestion than my proposal, which was to have it was part of the record. Will you do that?

Senator Everett: I will. This recommendation is to the Minister of Finance or to the Minister of National Revenue?

The Acting Chairman: Let us make the recommendation to the Government.

Senator Everett: The recommendations we are making are to the Minister of Finance.

Senator Martin: Surely, a question on this matter regarding advanced rulings should be made to the Minister of National Revenue.

Senator Grosart: Why not make the recommendation to the appropriate ministers?

The Acting Chairman: Have you finished, Senator Everett?

Senator Everett: Yes. I am sorry to have taken up so much of the committee's time.

Senator Phillips: Mr. Chairman, I want to be very careful about calling these p pers "official documents." I assume it is an official document, because it has the coat of arms and bears the name of the Honourable Senator Hayden and the Honourable Lazarus Phillips. These are the recommendations contained in the White Paper referring to the accrual system?

The Acting Chairman: Senator Phillips, would you identify this document?

Senator Phillips: It is a condensed report of the committee study on the White Paper.

The Acting Chairman: What is the date of the report?

Hon. Mr. Phillips: "September, 1970" is all that is on the document. The committee was very definite in its rejection of the accrual system for taxpayers in the professions. Yet I find clauses dealing with the matter, and I have not received an explanation as to why it was felt we needed an accrual system for taxpayers in the professions.

The Acting Chairman: This is a policy question.

Hon. Mr. Phillips: I would like to answer Senator Phillips' question for the chair. The subject matter of the treatment of professional income was considered by Senator Hayden and the committee, and the decision was that it not be included as one of the recommendations referred to in the three reports, but that it be put separately in the recommendations of the Senate committee on the White Paper, and it was reflected in the three reports.

It was dealt with, but was not regarded as a point which would be pressed. I may say, en passant, that there were some of us who felt that it should have been considered but, as in all problems of this nature, the consensus was followed and the decision was not to include it in the recommendations. It was not overlooked by this committee in the deliberations from September until we ceased deliberating.

Senator Phillips: May I direct a technical question, which is causing a great deal of concern, relating to my profession? When a patient who is on welfare is treated, the bill is submitted to the Royal College of Dental Surgeons' Welfare Fund. We follow the Ontario Dental College fees schedule, but never know what we will be paid. There seems to be neither rhyme nor reason to it. Apparently, the amount disbursed depends upon the amount of money in the fund at the time. Which are we liable for, when we have no control over collection or the amount paid? Is it the full fee as prescribed by the Royal College of Dental Surgeons or the amount of the payment?

Mr. Cohen: I do not know whether I can answer that specifically. I suppose I would have to get into the details of it. In the final analysis, it is a question of administration by the Department of National Revenue. As a general observation, although we treat professionals on a billed basis, which is a quasi-accrual form of reporting income, there is a provision for bad debts and another for doubtful debts. I presume that if the debts were doubtful or bad they would not be brought into income. I cannot answer specifically on your point, because it is really a matter of interpretation and administration of the act. It is the same type of problem, in a sense, that many, many people have in non-professional, more traditionally business activities, as to when is a receivable a receivable on an accrual basis.

Hon. Mr. Phillips: All bills you send out automatically become income, so a reserve is set up equal to the amount of billing.

Senator Phillips: That was to be my next question.

Senator Hays: Is it not permissible to write off bad debts?

Mr. Cohen: Yes, sir.

Senator Hays: Well, is the situation not the same for all?

Mr. Cohen: Yes, sir.

Senator Hays: If I sell a bull and he does not produce and the man will not pay, I pay it and then receive it back if the bull was no good.

Senator Grosart: Now that Senator Hays has raised the question of paternity, we have had a problem as to the paternity of this document known as "Draft Amendments, November 30, 1971." I thought it might be helpful to the committee if at this stage I state that I have now recalled the paternity. I would not like this valuable document to be given the name usually applied to those whose paternity is in doubt, so I will read to the committee from its final report, dated December 13, 1971. I might say that that date was my birthday and I might not have been so bright as I should have been. The following paragraph appears on page 5:

> With the approval of the Committee, a list of top priority items among the recommendations in our two Reports was submitted to the Minister, together with amendments which in the view of our expert advisers and our Committee would incorporate the substance of the top priority recommendations contained in your Committee's Reports.

I cannot think of any clearer answer to the suggestion that these amendments do not incorporate the substance, which was the word I used, of the top priority recommendations.

Hon. Mr. Phillips: I think it does. The amendments were not incorporated in the report and I, for one, am not aware—

Senator Grosart: It does not say that, Senator Phillips. You were not there. Let me make it clear that it says the committee reported two reports and amendments. I think it is a fair assumption that it can only refer to this document. I say that it is a fair assumption.

Senator Cook: Is that dated November 30? Our report is dated December 13.

Senator Grosart: The date could hardly be prior to November 30, because this refers to—All right, I will leave it.

Senator Martin: I would like to hear what Senator Phillips has to say.

The Acting Chairman: I think it is the second report that you are talking about, Senator Grosart.

Senator Grosart: This is part of the third report, which refers to the first two reports and says that amendments were sent to the minister. I will have to read it again. It says very clearly that:

> With the approval of the Committee, a list of top priority items among the recommendations in our two Reports—

And I interject to say that those top priority items appeared in Report No. 3:

> was submitted to the Minister, together with amendments which in the view of our expert advisers and our Committee would incorporate the substance of the top priority recommendations contained in you Committee's Reports.

I leave it at that, and merely suggest that if that is not good evidence to rescue this document from this—

Hon. Mr. Phillips: Senator Grosart, let me tidy it up this way: there is no question but that some of the experts associated with me were dealing with the subject matter of drafting amendments as an exercise in relationship to the recommendations. Whether these amendments dated November 30, 1971 are the ones referred to in the third report of December, I do not know.

Senator Grosart: I merely say the assumption is that they were, because this document was distributed. It is the only list of draft amendments submitted, and it would seem to me absolutely impossible that the committee would send amendments to the minister without giving copies to the members of the committee.

Senator Beaubien: I was not given a copy of the amendments of the committee. It says here definitely that amendments were sent to the minister, but are these the amendments that were sent to the minister?

Hon. Mr. Phillips: I cannot tell you, Senator Beaubien. I do not know.

The Acting Chairman: I do not remember seeing them before today.

Hon. Mr. Phillips: They were not incorporated in the third and final report, although reference is made to the drafting of amendments. That is as far as we can go.

Senator Grosart: I have no further argument; I will let the record speak.

Senator Phillips: I received one.

The Acting Chairman: Where did you get it?

Senator Phillips: It was on my desk.

Senator O'Leary: I am sure that Senator McElman would now like to withdraw his charge that these documents were Tory propaganda. Those are the words he used. I believe that when a man makes a mistake he should admit it. He made the statement, and he should be prepared to withdraw it right now.

Senator McElman: I was told, Mr. Chairman, that they emanated from Senator Flynn's office.

Senator Grosart: Who told you?

Senator McElman: I was told by the staff when I inquired as to where they emanated from.

I will let the record speak for itself.

The Acting Chairman: Shall we move on, honourable senators? Are there other questions to be put to the witnesses?

Senator Phillips: Mr. Chairman, I place myself in your hands with respect to a point of order.

I would like to move that the section dealing with the basic herd be deleted. However, since we have already adopted the first three reports, I am left in some doubt as to the legality of my motion. As you know, I do not like to make things difficult for a chairman; I always try to be helpful.

Senator Martin: May I ask a question, Senator Phillips?

Did the minister not say that he could not accede to such a request?

Senator Phillips: Yet, that is why I would like to make the motion.

Senator Martin: He did say that.

Senator Grosart: Yes, he did.

Senator Martin: It is not one of the things which we could reasonably expect any action on, then.

Senator Grosart: No, but we have every right to move an amendment to the bill.

Senator Martin: Yes, of course.

The Acting Chairman: Senator Phillips, you may move an amendment to include the proposition for which you speak. I would just ask you to consider that the question of the basic herd has been included in our report and it will be part of the material which the minister will consider.

If you want to move an amendment in any way, you are certainly free to do so.

Senator Hays: Would the amendment be in order?

The Acting Chairman: I do not believe anyone would question it. I believe it is all right to move an amendment.

Hon. Mr. Phillips: Of course it is all right to move an amendment to the bill.

Senator Phillips: Then, honourable senators, I would move that section 29 of the bill, dealing with the basic herd, be deleted.

Senator Grosart: What page is that?

Senator Phillips: It begins at page 85. This will restore farmers to the position that they held under the old system and which has been held by farmers for generations. It is a position that is supported in the report of the committee as submitted to the Senate.

I am in somewhat of a difficult position, being the only member of this committee to vote against the adoption of this recommendation to the minister. However, my purpose in so doing was to have it in the form of a motion rather than a recommendation.

The Acting Chairman: And you so move?

Senator Phillips: I so move.

Senator Hays: It is in order?

Hon. Mr. Phillips: As I understand it, this is a motion to amend Bill C-259.

Senator Martin: Yes.

The Acting Chairman: It does not detract from the recommendation in any way. It simply proposes an amendment to the bill.

Senator Grosart: That is right.

The Acting Chairman: Those in favour of Senator Phillips' amendment will please signify in the usual way.

Those against Senator Phillips' amendment will please signify in the usual way.

The Clerk of the Committee: It is 7 against and 4 in favour.

The Acting Chairman: I declare the amendment lost.

Senator Grosart—

Senator Martin: There is some question with respect to the full vote.

The Acting Chairman: Well, I always ask honourable senators to signify in the usual way , hoping that they will hold their hands high enough and long enough for the clerk to take a count.

Will those against Senator Phillips' amendment please raise their hands and hold them up until the count is finished?

The Clerk: The count is now 10 against, Mr. Chairman.

The Acting Chairman: Senator Grosart?

Senator Grosart: Now that the hidden votes are in, Mr. Chairman, I have an amendment to suggest. I do not want to trespass on the time or patience of the committee, but I have amendments to make to clauses 69, 70, 91, 95, 127, and 212. All of them are contained in the document known as "Draft Amendments, November 30, 1971".

I wonder if you would accept a motion that these amendments, as contained in this document under the heading of the clauses I have just indicated, be passed by the committee? I do that rather than deal with them individually.

The Acting Chairman: In other words, Senator Grosart proposes to lump together proposed amendments to certain clauses. I did not count the number of clauses.

Senator Grosart: Six clauses.

Hon. Mr. Phillips: And you have referred to the actual clauses.

Senator Grosart: Yes.

The Acting Chairman: As contained in a document on which we have had some considerable discussion this afternoon.

Senator Grosart: Might I add that the clause numbers are taken from the draft bill as it was presented to the Committee of the Whole in the other place. They may not, and probably do not, coincide exactly with the numbers now.

Mr. Cohen: May I just comment that the numbering has not changed.

Senator Grosart: In that case, that observation is unnecessary.

Senator Martin: I would like to know what we are going to vote on. Are we voting on amendments that have been discussed here, or that have been discussed in the other place and have not been analyzed here?

The Acting Chairman: May I help, Senator Martin, in this respect. Senator Grosart's proposal is in respect of certain amendments set out in a document described as "Draft Amendments" and dated November 30, 1971. I ask Senator Grosart if he has the patience to give us the clause numbers again.

Senator Grosart: They are clauses 69, 70, 91, 91(2), 95(1)(b), 127(1), and 212(14). I am not breaking them down into whether they are paragraphs or subparagraphs.

Hon. Mr. Phillips: All related to Bill C-259?

Senator Grosart: All related to Bill C-259.

Hon. Mr. Phillips: And we are assured by Mr. Cohen that the numbers are the same as those that came from the other place.

Mr. Cohen: Yes. The numbers in this bill are the same as in the previous versions. There has been no change in numbering.

The Acting Chairman: Does the committee wish me to call the headings of the various clauses?

Hon. Senators: No.

The Acting Chairman: There is a consolidation of all of these amendments.

Shall the motion of Senator Grosart carry?

All those in favour will please signify in the usual way and hold their hands on high.

Those against will please signify in the usual way.

The voting was 4 in favour, 9 against. I declare the motion lost.

Senator Grosart: Horatius had only two with him.

The Acting Chairman: Are there further questions, honourable senators, that it is desired to ask of the witnesses?

Senator Phillips: The punitive clause, as I call it,—I have forgotten which one it is—seems to me a bit harsh. As I interpret it, certain things almost carry a mandatory jail sentence. I never prepare my own income tax, I always have someone do it. He does it on information I give him, and I give it to the best of my knowledge, with records, and so on. I would like to know why it is felt so necessary that the sentence should be so severe.

Senator Grosart: Policy!

The Acting Chairman: As Senator Grosart points out, it is a policy question.

Senator Phillips: I realize that it is a policy question. As the Honourable Mr. Phillips answered a question on policy for me earlier, perhaps he will be able to answer this one.

Senator Grosart: It is very little help to you, when you are behind the bars, to be told it is a policy question.

An Hon. Senator: Behind which bars?

The Acting Chairman: Are there other questions, honourable senators?

Senator Hays: Mr. Chairman, I move that we rise and report the bill.

Senator Phillips: Before we do so, do I not get any more explanation than that it is a matter of policy? Surely someone could answer that question for me?

The Acting Chairman: Senator Phillips, you ask of the witnesses—who cannot discuss policy properly for this committee, and we all recognize that—why the penalty is as harsh as it is in a certain section. Could you rephrase your question to comment on the character—

Senator Phillips: May I add to that, then, that at the next meeting we have an answer to the question? I realize that the witnesses are not in a position to do that, but we could have someone who could have an answer available at the next meeting.

Senator Beaubien: The Minister of Justice? I hope you get it.

The Acting Chairman: The next time that we are in a position to ask policy questions of a witness, at this cimmittee, would be a satisfactory time for you to repeat your question.

Senator Phillips: I would be perfectly happy with that, and at our next meeting perhaps we can have some answer.

Senator Quart: Mr. Chairman, if all the business has been finished, may I end on a "thank you" note to Mr. Cohen and Mr. Thorson and the other gentleman who set me straight on one point?

An Hon. Senator: Were you going off the straight and narrow?

Senator Quart: Do not tease! I am not an economist or a learned person who could comment on this, and I did not dare bring it up this morning. However, I may be good for the economy of the country; I spend money. These gentlemen took a few minutes out this morning. I waylaid them in the corridor to ask about charitable donations and donations to churches, because a group of women asked me yesterday to ask and I really had cold feet this morning and did not ask, until I got these gentlemen alone—

An hon. Senator: Alone?

Senator Quart: There is safety in numbers, gentlemen! There were four of them, and I wish to thank them very much.

The Acting Chairman: Were you satisfied with the answers?

Senator Quart: Very.

Senator Cook: I do not know that the members of the committee want to come back again tonight and if there are no other matters of substance to be dealt with, I would move that we report the bill without amendment.

The Acting Chairman: Before we entertain that motion, Senator Cook, if you do not mind, I think Senator Everett, who spoke to me, has something to contribute.

Senator Everett: It was merely the motion on the recommendation in respect of corporate surpluses and ministerial discretion.

The Acting Chairman: You would like to see it included in the report?

Senator Everett: That is right—if that course is agreeable to the members of the committee.

The Acting Chairman: I would entertain Senator Cook's motion first, to make the proceedings tidy, so that we will know exactly what we are doing.

It is moved by Senator Cook that the bill be reported without amendment.

Senator Martin: Mr. Chairman, may I speak to that, by way of query? Do we not have to have a report?

The Acting Chairman: I will come to that in a moment.

Those in favour of the motion will please signify in the usual way. Please hold your hands up until the clerk has done the counting.

Those against will please signify in the usual way.

I declare the motion carried.

Now, honourable senators, as is our custom here, we prepare a report in writing for approval of the committee. Normally, what has been done is that the chairman asks for approval of the committee to consult with the committee counsel to prepare that document, and then we submit it to the committee. Would it be satisfactory to the committee if we adjourned for half an hour and then brought back to the committee the form of words for a report, for approval by the committee before we submit it to the Senate?

Senator Everett: Before we adjourn, I should like to make my motion.

The Acting Chairman: Certainly. Go ahead.

Senator Everett: My motion is as follows:

The Committee recommends to the Minister of Finance and the Minister of National Revenue as follows:

(1) A method be found to deal with the problem of the distribution of corporate undistributed income accrued subsequent to December 31, 1971 similar to the method proposed in Bill C-259 for dealing with corporate undistributed income accrued prior to January 1, 1972.

(2) That the Minister of National Revenue give binding advance rulings on a written set of facts as to:

(a) the exercise of ministerial discretion under the Income Tax Act;

(b) whether a receipt would be an income receipt or a capital receipt under the Income Tax Act.

The Acting Chairman: What you are moving is that those words be included in the report made by this committee?

Senator Everett: No, as a recommendation to the Minister of Finance and the Minister of National Revenue.

Senator Isnor: Did you say "binding"?

Senator Everett: The minister already gives binding rulings, Senator Isnor. That is an accepted practice.

The Acting Chairman: Senator Everett, am I to understand that what you would like here is the approval of this motion by the committee, but not to have the wording of the motion included in the report made by the committee to the house?

Senator Everett: I would like it in the report, I suppose. I do not see what is wrong with it.

The Acting Chairman: Our counsel tells me that he did not think that was your intention.

Hon. Mr. Phillips: If you desire it as a motion and it be passed, it is an independent item, but it can be included in the report, if you so desire.

The Acting Chairman: Would you like to have it not as a motion but included in the report? If so, would you give us the document that you have and we will include it in the report?

Senator Grosart: Mr. Chairman, on a point of order: Senator Everett has moved a motion. It will then be up to the committee to decide whether or not to include that in its report, just as it would with any other motion.

The Acting Chairman: Even that is satisfactory.

Those in favour of Senator Everett's motion, please signify in the usual way.

Senator Everett: It is not a serious point. I am prepared to withdraw the motion if the committee agrees to let it go forward as part of the recommendations in the report.

Senator Grosart: The committee cannot agree at this time.

The Acting Chairman: Not until it hears the report.

Senator Everett: Very well. If we vote on the motion, we will get an answer, so I will let the motion stand.

Senator Buckwold: Under paragraph (A), in which you are asking for a report on undistributed surplus similar to the legislation of 1971, is not that too rigid in its application?

The Acting Chairman: Why don't you ask the witness?

Senator Buckwold: You are indicating it should be done at 15 per cent.

Senator Everett: No, it could be described as "similar in method". I did not have a rate in mind.

Senator Buckwold: What worries me is the nature of the wording and the fear of an ad hoc decision on these things. I am worried, with all respect, about three items which I am very much in favour of, and that instead of being part of this report they be again referred for further study to this committee so they can be properly worded.

Senator Everett: I have already shown the material to Mr. Thorson, and we have gone over the wording of the recommendation.

Senator Cook: It is only a recommendation anyway.

Senator Everett: It is a recommendation which will be fully understood by the minister and may or may not be acted upon, but it is a serious problem and it is going to be a continuing problem, and I think it should be brought to the attention of the minister. I am prepared to stand or fall on the motion.

The Acting Chairman: Those in favour of Senator Everett's motion will signify in the usual way.

Thirteen.

Those against Senator Everett's motion will please signify in the usual way.

One.

I declare the motion carried.

Hon. Mr. Phillips: Senator Everett, I take it that if the chairman and his counsel come to the conclusion that the substance of this motion be not included in the recommendations we will be framing for a report, you will not take it amiss that it was not included in the report now that you have it on the record?

Senator Grosart: I do not think we should anticipate what the committee will do.

Senator Everett: I think it should be part of the report.

The Acting Chairman: Is it agreed that we should adjourn now and take recess for half an hour to reassemble in this room at 20 minutes to 6?

Hon. Senators: Agreed.

The committee adjourned.

Upon resuming at 5.45 p.m.

The Acting Chairman: Will the committee please come to order.

Senator Grosart: Is this being held in camera, Mr. Chairman?

The Acting Chairman: No.

You have asked Hon. Mr. Phillips and myself to provide a report on the proceedings of the committee, and we are suggesting the following for the consideration of the committee:

The Standing Senate Committee on Banking, Trade and Commerce, to which was referred the Bill C-259, An Act to amend the Income Tax Act and to make certain provisions and alterations in the statute law related to or consequential upon the amendments to that Act, has, in obedience to the Order of Reference of Saturday, December 18th, 1971, examined the said Bill and now reports the same without amendment.

Your Committee, however, considers it urgent that the following observations be made.

As a result of a reference to your Committee by the Senate on September 14, 1971, your Committee considered the Summary of 1971 Tax Reform Legislation and the Bill based thereon, being Bill C-259, which Bill received first reading in the House of Commons in June. The present Bill C-259, although amended in part, is in substance substantially the same Bill which received first reading in June in the House of Commons.

As this Committee's first preliminary report states—"your Committee has heard a number of representations and has received a number of written submissions on the proposed legislation." As a result of its deliberations and studies your Committee submitted to the Senate its First Preliminary Report on November 4th, 1971, its Second Preliminary Report on November 30th, 1971, and its Third and final Report on December 13th, 1971.

These Reports include a series of recommendations for suggested amendments to Bill C-259. In approving this Bill today this Committee reiterates with the greatest possible emphasis that the recommendations for changes in the Bill as contained in these Reports, are of continuing importance and relevance.

Your Committee further recommends to the Minister of Finance and the Minister of National Revenue the following:

(1) That a method be found to deal with the subject-matter of the distribution of corporate undistributed income accrued subsequent to December 31, 1971, in a manner similar to the method proposed in Bill C-259 for dealing with corporate undistributed income accrued prior to January 1, 1972; and

(2) That the Minister of National Revenue give binding advance rulings on a written set of facts as to:

(a) The exercise of ministerial discretion under the Income Tax Act; and

(b) As to whether a receipt would be an income receipt or a capital receipt under the Income Tax Act.

Your Committee is aware that the House of Commons has at times questioned the right of the Senate to amend legislation designed to impose taxes. Without discussing that issue in any way, your Committee nonetheless is of the view that the compendious context of the Bill urgently calls for a series of amendments which will clarify and simplify certain sections thereof and excise others.

In view of the statements made by the Minister of Finance before your committee on December 13 and this day, your committee confidently expects that the Government will give meaningful consideration to the recommendations of your committee in respect of Bill

C-259 in amending legislation to be presented to the House of Commons as soon as possible in 1972.

It is therefore expected that the Government will give intensive and meaningful attention to the views expressed herein having regard to the important role that the Senate of Canada has played and is playing in the Government of this country as one of its two constituent parliamentary chambers.

"Respectfully submitted," blank, "Acting Chairman".

Senator Cook: That is pretty good.

Senator Beaubien: I think it is good.

Senator O'Leary: No, Mr. Chairman, I beg your pardon. It should be stated in this report to the Senate, which will be printed in the press tomorrow morning, that the motion to report the bill without amendment was carried on division. I think it must be made clear that we did not agree to report this bill at this time.

Senator Belisle: And it was in vain that we wasted our time today.

Senator Martin: I understand that is never done.

Senator O'Leary: Never done?

Senator Martin: No.

Senator O'Leary: It is as well to create good precedents as to follow old ones.

The Law Clerk: It is not customary; I have never heard of it.

Senator Grosart: There is a rule, in effect by indirection, against a minority report. It is not quite clear.

The Law Clerk: No, it is ambiguous.

Senator Grosart: The rule says that it shall contain the report of the majority, but I see no reason why it should not be stated in the report that it was not unanimous.

The Law Clerk: May I suggest that the report could be adopted on division?

Senator O'Leary: I would accept that.

Senator Martin: For instance, you refer to the advice given by the Minister of National Revenue as a binding set of rulings. That is quite different from the statement of the Minister of National Revenue, which was that advice would be given in anticipation. It is not necessarily binding, is it, Mr. Phillips?

Senator Grosart: These are two different matters.

The Chairman: I would like to deal, first of all, with the question of whether or not we should reflect in the report the fact that the motion was passed on division. What is the feeling of the committee in that respect?

Senator Martin: What is your view, in your long experience, Mr. Chairman?

The Acting Chairman: It has not been done before, but that does not bother me very much.

Senator Martin: Even on division?

The Acting Chairman: No, we have never actually done it. As a matter of fact, Senator O'Leary, in commenting on the report or at the third reading stage you could always indicate that the motion was passed on division.

We are in the hands of the committee, which is the master of its own decision.

The Law Clerk: That is correct.

Senator O'Leary: Is this debatable when the report is presented?

The Acting Chairman: Yes.

Senator O'Leary: I am satisfied as long as I have the opportunity to state to the country that we did not unanimously in this committee decide to pass this report at this time.

The Acting Chairman: That is your undoubted right.

Senator O'Leary: Leave it to me; I will do it.

Senator Phillips: Mr. Chairman, I do not know why it is necessary to insert a sentence dealing with the historical argument between the Senate and the House of Commons with respect to the Senate's right to deal with a money bill. I do not think that question was raised at any time in these deliberations and I wonder why it is necessary.

The Acting Chairman: We did raise it. The whole tenor of Senator Hayden's dealings has been because of that. I am not too sure that generally it is understood to be one of the facts of life in the Senate. I thought, as did Senator O'Leary who says you have to bring this out, that we can do it effectively in a report such as this. At least, that is what my counsel advises.

Senator Beaubien: Senator Hayden has always maintained that we can amend.

Senator Grosart: I agree with Senator Phillips. I cannot see that it is in any way germane to this report that we should argue that which never came up in committee.

The Acting Chairman: Yes, it came up this morning.

Senator Grosart: I was here and did not hear it. The point is that we have an appropriation bill which comes to us with the consent of the Senate. Why should we worry about that in this report?

Senator Martin: Senator Connolly, you are an experienced man. You must have had good reason. What was in your mind?

The Acting Chairman: I was thinking only of the constitutional position of the Senate and not entering the debate, to say that without discussing that issue at this time your committee is of the view that the bill does call for a series of amendments. We are prepared to see it done, as a result of the minister's statement to us, through the House of Commons rather than through a direct amendment from here. In other words, it is to avoid a clash between the two houses of Parliament. However, if it is not the type of

recommendation that the committee would now like to make to the house, we could say this—

Senator Martin: I think it is a very wise thing for the Senate.

Senator O'Leary: Were we asked to express our opinion on this?

Senator Beaubien: No.

Senator Martin: But do we not want to support the proposition?

Senator Phillips: It is not in our terms of reference.

Senator Beaubien: I think the Senate passed the bill without amendment because it felt that delay would be a bad thing. I think that was the idea of the Senate majority in its willingness to pass the bill. I do not doubt for one moment that had we received the bill at the beginning of the month we would have inserted the amendments we thought we should have in the bill.

The Acting Chairman: The Honourable Mr. Phillips and myself are not married to this form of wording, but we have had to do things pretty fast since we returned to the committee.

Senator Grosart: I am sure that Senator Hayden would not like it. He has said on many occasions that had we received this bill in time we would have sent back amendments.

Senator Goldenberg: Would the Acting Chairman again read that short section?

The Acting Chairman: I will read it first without the words which we are now discussing:

> nonetheless your committee is of the view that the compendious context of the bill urgently calls for a series of amendments which will clarify and simplify certain sections thereof and excise others.

The words which we propose to strke out are:

> Your Committee is aware that the House of Commons has at times questioned the right of the Senate to amend legislation designed to impose taxes. Without discussing that issue in any way.

Is it the committee's desire to remove those words?

Senator Phillips: I would so move.

Hon. Senators: Agreed.

Senator Martin: I can see the great wisdom in that statement.

The Acting Chairman: We can, of course, raise this question in debate on third reading.

Senator Grosart: I should like to raise one small point.

The Acting Chairman: Before you do so, I want to make sure that I have the wording correct. It will read:

> nonetheless your Committee is of the view

et cetera.

Senator Grosart: I think that when you read the word "context", you meant content, compendious content.

Hon. Mr. Phillips: It could be both. I am guilty of the word "context".

Senator Grosart: It is the compendious content that worries us, not the context.

The Acting Chairman: We will therefore eliminate "x" and put in "n".

Senator O'Leary: What is "compendious" in doing that?

Hon. Mr. Phillips: Do we want that out?

Senator O'Leary: I do not see what it is there for.

The Acting Chairman: It is agreed:

> that the compendious content of the Bill urgently calls for a series of amendments.

Senator Grosart: Content and context.

Hon. Mr. Phillips: We would then leave out the word "compendious".

The Acting Chairman: It will read "content and context", and we leave out the word "compendious".

Senator Lafond: It seems to me that earlier the acting chairman used the word "substantially" for the words "in substance".

Senator Grosart: I was going to raise that point.

The Acting Chairman: I noticed that when I was reading. Give me a moment to find it.

Senator Goldenberg: It is right near the beginning.

Senator Martin: Could you read that paragraph, Mr. Chairman?

Senator Grosart: You said it was substantially the same bill. I do not think your friends would like that very much.

Senator Martin: The Senate has been able to facilitate many changes in this bill.

The Acting Chairman: Shall we take out "in substance" or "substantially"?

Senator Goldenberg: Take out "substantially".

Senator Martin: Does that take into account the changes that have been made in the bill?

Senator Grosart: It is not the same bill. Who is kidding who?

The Acting Chairman: I think it puts us clearly on the side of people who feel—

Senator Grosart: The angels.

The Acting Chairman: —people who feel substantial amendments, certainly along the lines recommended by this committee, should be recommended.

Senator Grosart: They have already made quite a number of amendments. I do not recall what the number is.

Senator Martin: Look at the changes they have made in the White Paper. The fact is that there are eight Senate proposals that have been accepted with respect to this bill.

Senator Grosart: The minister stated there were 44 changes made.

Senator Martin: That is on the White Paper. I am talking about the bill.

The Acting Chairman: Senator Martin, with all due respect, I believe, in the deliberations of the committee today, we did not extract from the officials the details of those eight amendments to which you referred. I do not think we should tie ourselves down to those eight amendments.

Senator Grosart: It surprises me, Mr. Chairman, that we should start off a discussion with three possible amendments coming out of Senator Everett's motion—and a good motion it was—without referring to the priority items. I feel there should be a clear reference in this report with respect to the fact that this committee still feels that these nine top priority items should be dealt with and are going to be dealt with.

The way it reads now, we go right into three things which are quite narrow, and it gives the impression that those are all we are worried about.

The Acting Chairman: I would suggest, Senator Grosart, that that is covered in the subsequent paragraph which reads, in part:

> In view of the statements made by the Minister of Finance before your Committee on December 13th and this day, your Committee confidently expects that the Government will give meaningful consideration to the recommendations of your Committee in respect of Bill C-259 in amending legislation to be presented to the House of Commons as soon as possible in 1972.

Senator Grosart: I would like to see us use the phrase, because I think it adds substance to our report, "top priority items". That is in our Report No. 3.

The Acting Chairman: In drafting this clause, Senator Grosart, what I was concerned with was that it would be clear that all of the recommendations proposed by the committee should receive top priority consideration.

Senator Martin: Mr. Chairman, is this not a private meeting at this stage?

The Acting Chairman: No.

Senator Grosart: That has always been the case when we are discussing the report of a committee.

The Acting Chairman: Perhaps it should be a private meeting.

Senator Martin: There are members of the other house present and we also have members of the press here.

I think it should be a private meeting.

The Acting Chairman: Well, I would ask members of the press and other strangers to retire until we complete this report.

I would ask the gentlemen of the press to observe the amenities in this respect, and to consider that they have been sitting in on an *in camera* meeting.

An Hon. Senator: Mr. Chairman, are you suggesting that the two members of Parliament are strangers in this house?

Senator O'Leary: This thing is going to sound like a Toronto *Star* editorial by the time we are finished.

Senator Grosart: I think you had better leave it the way it is, Mr. Chairman. If any harm has been done, it has been done.

Senator Phillips: Mr. Chairman, may I ask why, considering the means we have for photostating, each of us could not have had a copy of this in front of us?

The Acting Chairman: It was just impossible to do it in the time we had, senator.

Senator Isnor: And the staff had already gone home.

The Acting Chairman: Honourable senators, with these changes, is it agreeable?

Hon. Senators: Agreed.

The Acting Chairman: I am afraid that the typing of this document cannot be completed in time for presentation to the Senate this evening, unless we are prepared to sit at a later time.

Senator Cook: It is now past 6 o'clock, so we have to wait until 8 o'clock anyway, I believe. Perhaps Senator Grosart could tell us; he knows all the rules.

The Acting Chairman: The Senate has to reassemble in order to adjourn for the day. Perhaps Senator Martin would give an indication. Is it the intention to reassemble the Senate now, and then adjourn?

Senator Martin: I think we have to meet and adjourn, and then we will assemble at 2 o'clock tomorrow.

The Acting Chairman: Then the report will be prepared in time for the meeting of the Senate tomorrow afternoon. At 2 o'clock tomorrow?

Senator Martin: At 2 o'clock.

The Acting Chairman: Is there a motion for adjournment?

Senator Langlois: I so move.

Senator Martin: I should like to move a vote of thanks to the chairman, to our former colleague the Honourable Mr. Phillips, and to Senator O'Leary.

The committee adjourned.

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THIRD SESSION—TWENTY-EIGHTH PARLIAMENT

1970-71

THE SENATE OF CANADA

PROCEEDINGS

OF THE

STANDING SENATE COMMITTEE ON

BANKING, TRADE AND COMMERCE

The Honourable JOHN J. CONNOLLY, P.C., *Acting Chairman*

No. 53

FRIDAY, DECEMBER 31, 1971

First Proceedings on Bill C-176

intituled:

"An Act to establish the National Farm Products Marketing Council and to authorize the establishment of national marketing agencies for farm products."

(Witnesses—See Minutes of Proceedings)

THE STANDING SENATE COMMITTEE ON
BANKING, TRADE AND COMMERCE

The Honourable Salter A. Hayden, *Chairman*

The Honourable Senators:

Aird	Hayden
Argue	Hays
Beaubien	Isnor
Belisle	Lafond
Benidickson	Lang
Bourget	Langlois
Buckwold	* Martin
Choquette	McElman
Connolly (*Ottawa West*)	Molgat
Cook	Molson
Desruisseaux	O'Leary
Everett	Phillips
* Flynn	Quart
Goldenberg	Sullivan
Grosart	Walker
Hastings	Willis

* *Ex officio members*

(Quorum 7)

Order of Reference

Extract from the Minutes of the Proceedings of the Senate, December 31, 1971:

A Message was brought from the House of Commons by their Clerk with a Bill C-176, intituled: "An Act to establish the National Farm Products Marketing Council and to authorize the establishment of national marketing agencies for farm products", to which they desire the concurrence of the Senate.

The Bill was read the first time.

The Honourable Senator Hays, P.C., moved, seconded by the Honourable Senator Fournier (*de Lanaudière*) that the Bill be read the second time now.

After debate,

The Honourable Senator Sparrow moved, seconded by the Honourable Senator Molgat, that further debate on the motion be adjourned until Tuesday, 11th January, 1972.

The question being put on the motion,

The Senate divided and the names being called they were taken down as follows:—

YEAS

The Honourable Senators

Argue,
Bélisle,
Benidickson,
Fergusson,
Forsey,
Grosart,
McGrand,
Molgat,
Phillips,
Sparrow—10.

NAYS

The Honourable Senators

Aird,
Basha,
Bourget,
Bourque,
Connolly
(*Ottawa West*),
Davey,
Duggan,
Fournier
(*de Lanaudière*),
Goldenberg,
Hastings,
Hays,
Lafond,
Langlois,
Lapointe,
Lefrançois,
Martin,
McElman,
McNamara,
Michaud,
Petten,
Stanbury—21.

So it was resolved in the negative.

Debate was resumed on the motion of the Honourable Senator Hays, P.C., seconded by the Honourable Senator Fournier (de Lanaudière), for the second reading of the Bill C-176, intituled: "An Act to establish the National Farm Products Marketing Council and to authorize the establishment of national marketing agencies for farm products".

The debate was interrupted, and—

The Honourable the Speaker having put the question whether the Senate do now adjourn during pleasure to reassemble at the call of the bell at approximately two o'clock p.m., it was—

Resolved in the affirmative. 1.15 p.m.

The sitting of the Senate was resumed. 2.05 p.m.

After further debate, and—
The question being put on the motion, it was—
Resolved in the affirmative.

The Bill was then read the second time.

The Honourable Senator Hays, P.C., moved, seconded by the Honourable Senator Fournier (*de Lanaudière*), that the Bill be referred to the Standing Senate Committee on Banking, Trade and Commerce.

The question being put on the motion, it was—
Resolved in the affirmative.

With leave,
The Senate proceeded to Notices of Motions.

With leave of the Senate,
The Honourable Senator Langlois moved, seconded by the Honourable Senator Bourget, P.C.:

That the names of the Honourable Senators Argue, Hastings and Molgat be substituted for those of the Honourable Senators Burchill, Gélinas and Giguère on the list of Senators on the Standing Senate Committee on Banking, Trade and Commerce.

After debate, and—
The question being put on the motion, it was—
Resolved in the affirmative."

Robert Fortier,
Clerk of the Senate.

24351—2

Minutes of Proceedings

Friday, December 31, 1971.
(69)

Pursuant to adjournment and notice the Standing Senate Committee on Banking, Trade and Commerce met this day at 3:45 p.m. to examine and consider Bill C-176 intituled:

"An Act to establish the National Farm Products Marketing Council and to authorize the establishment of national marketing agencies for farm products."

Present: The Honourable Senators Aird, Argue, Belisle, Benidickson, Bourget, Connolly (*Ottawa West*), Goldenberg, Grosart, Hastings, Hays, Lafond, Langlois, Martin, McElman, Molgat and Phillips—(16).

Present, but not of the Committee: The Honourable Senators Davey, Duggan, Fergusson, Forsey, E. E. Fournier, S. Fournier, Michaud, McNamara, Petten, Sparrow and Stanbury—(11).

In attendance: Mr. R. L. du Plessis, Acting Parliamentary Counsel.

In the absence of the Chairman and upon motion duly put, it was Resolved that the Honourable Senator Connolly (*Ottawa West*) be elected Acting Chairman.

The following witness was heard:

The Honourable H. A. Olson, Minister,
Department of Agriculture.

Present, but not heard:

Mr. S. D. Williams,
Deputy Minister,
Department of Agriculture;

Mr. C. R. Phillips,
Director General,
Production and Marketing Branch,
Department of Agriculture.

It was Moved by Senator Hays that the Bill be reported without amendment.

It was Moved by Senator Molgat, in amendment, that the Committee adjourn to a subsequent date.

After discussion both the motion and the motion in amendment were duly withdrawn.

At 6:30 p.m. the Committee adjourned until 11:00 a.m. Thursday, January 6, 1972.

ATTEST:

Georges A. Coderre,
Clerk of the Committee.

The Standing Senate Committee on Banking, Trade and Commerce

Evidence

Ottawa, Friday, December 31, 1971.

The Standing Senate Committee on Banking, Trade and Commerce, to which was referred Bill C-176, to Establish the National Farm Products Marketing Council and to authorize the establishment of national marketing agencies for farm products, met this day at 4.45 p.m. to give consideration to the bill.

Senator John J. Connolly (*Acting Chairman*) in the Chair.

The Acting Chairman: Honourable senators, the honourable H. A. Olson, the Minister of Agriculture, is present. Is it your pleasure that the minister come forward and discuss the bill?

Hon. Senators: Agreed.

Senator Grosart: We very much appreciate the presence of the minister. I am sure that he will not want to stay too long. I move that we receive a statement from the minister and then adjourn until an appropriate time in order to continue our proceedings. It is rather late in the afternoon to attempt to discuss the bill, and it is New Year's Eve. It seems to be a fairly general feeling that there are other witnesses whom we should call, at which time perhaps the minister might make himself available.

Senator Martin: The minister is familiar with the background of the debate, and we may wish to ask him some questions, particularly with regard to procedure.

The Honourable H. A. Olson, Minister of Agriculture: Mr. Chairman, I do not have a prepared statement, but I will be happy to make an opening statement with regard to the provisions of Bill C-176.

Senator Benidickson: As amended?

Hon. Mr. Olson: As amended and amended and amended.

Mr. Chairman, the history of Bill C-176 is based on a determination by both levels of government, provincial and federal, to try to find the means, under Canada's Constitution, whereby we could set up a legal structure, and the administrative machinery within that legal structure, to deal effectively with the marketing problems which have been faced by agriculture over a long period of time.

As honourable senators know, the federal Government has not assumed that it has constitutional jurisdiction to deal with intraprovincial trade in agricultural products. Further than that, the Government has never assumed that it has the power to deal with production controls or quota allotments based on that kind of jurisdiction within a province, whether the product were to move in intra- or interprovincial trade.

The consequence of this, in historical terms, has been that the provinces have set up marketing legislation in their respective provinces under their legislative competence. That is now true of all of the provinces of Canada. Their experience has been that while they have the constitutional right to make laws, rules and regulations respecting intraprovincial trade and to do other things to achieve that purpose, they do run into severe difficulties with respect to interprovincial trade as a result of these marketing boards either having failed to co-ordinate their efforts or, indeed, having failed so far to have it set up under a national scheme to which both levels of government could delegate their authority.

That, Mr. Chairman, is briefly the basis on which we have brought this bill before the Parliament of Canada. This bill has been carefully drawn so that we do not make any attempt to invade provincial jurisdiction in so far as law-making is concerned, but it has also been carefully drawn to make sure that the administrative machinery that is set up under the provisions of Bill C-176 is capable of both receiving and administering delegated powers from both levels of government in order to achieve the purposes that I outlined some time ago.

Part I of the bill, that is, clauses 3 to 16, are those sections that set up the National Farm Products Marketing Council, which shall have the power to inquire into the merits of establishing a marketing plan, that give them the right to do market research, and all other such things, to determine whether or not they wish to recommend to the minister and to the Governor in Council whether or not a market agency for specific commodities should be established.

There are other clauses that deal with marketing agencies themselves, but I should say very briefly that the National Farm Products Marketing Council, that will be in some respects overseeing all of the specific commodities agencies, is not permitted to recommend to the minister or to the Governor in Council that a marketing agency be established unless it is able, by a positive indication, to say that there is majority support of the producers of the particular commodity for the establishment of that agency.

There are, of course, clauses dealing with such things as the requirement to hold public hearings; this is dealt with in clauses 8, 9 and 10. Clauses 11 to 16 deal with the organization of a National Farm Products Marketing Council. Clause 17, in Part II of the bill, deals with what the Governor in Council is required to do before issuing

the proclamation setting up a marketing agency and the plan that it will administer. You will note in clause 17 that the Governor in Council must be satisfied that a majority of the producers of the farm product, or each of the farm products, in Canada is in favour of such an agency. Subclause 2 of clause 17 deals with the manner in which the Governor in Council shall determine whether a majority of the producers is in fact supporting the establishment of an agency.

Senator Martin: May I ask a question? What is the exact position of the provinces with respect to this bill? Senator Hays, in his excellent presentation today, stated that it was the wish of the provinces to have this bill passed. Can you tell us if this is in fact so?

Hon. Mr. Olson: I have sent for my file so that I can read it verbatim, but in the meantime I will try to recite it from memory.

Senator Benidickson: Some of us are particularly concerned about how the provinces feel about the amendments which came down yesterday and this morning, and their attitude to them.

Hon. Mr. Olson: I will deal with it from memory. At the meeting held in Ottawa on November 25 or 26 the provinces recognized the urgency, if I may put it that way, and the essential need for national enabling legislation. They went on to say, in the communique that was agreed to by all of the ministers, that if we were to amend the bill in a way that would require further action on the part of Parliament naming the commodities, that is, with the exception of poultry and poultry products, to be included in the bill, they would then urge the speedy passage of this bill. I did ask unanimous consent of the other place to introduce such an amendment to clause 18, and I received that consent. It was amended there yesterday to that effect.

Senator Martin: Mr. Minister, may I ask you this, pending the arrival of your notes containing the verbatim position of the provinces: Is it a fact that this bill, with its amendments, represents the wish of the nine provinces, subject to the one reservation of the Province of Manitoba?

Hon. Mr. Olson: Yes, sir.

Senator Martin: Is that unmistakably the position?

Hon. Mr. Olson: Yes, sir. For Manitoba, the minister, Mr. Uskiw, made it clear that Manitoba had a reservation. They had no reservations about the provisions that are in the bill. His one reservation was that there should be another amendment to the bill, which would require unanimous consent of all of the provinces for each marketing plan. My reply to him is that if you put it around the other way, that will also give each province a veto on each marketing plan, whether or not they were a significant producer of the commodity involved, and I informed him that I was not willing to accept that. In fact, the other provincial ministers were not willing to accept that either.

Senator Bélisle: May I ask a supplementary question to Senator Martin's? If you have this, have you got it in writing from the nine provinces, and was it as of this morning, when the alleged statement came out in the other place?

Hon. Mr. Olson: I think I can give you an unqualified "Yes" to that question, because I will give you the exact text of the communiqué that was agreed to by all provincial ministers. I am sure you will agree with me when you read the qualification to Bill C-176 that they put on an endorsation of that bill, recommending speedy passage, and that the amendment you have respecting clause 18 does in fact meet the request of the qualification in that communiqué.

Senator Forsey: That is subclause (3), is it?

Hon. Mr. Olson: Of clause 18?

Senator Forsey: Of clause 18.

Hon. Mr. Olson: Yes.

The Acting Chairman: It is the new subclause added to clause 18.

Senator Forsey: That appears to be subclause (3).

The Acting Chairman: Yes, that is right.

Senator Grosart: May I ask you a further supplementary question, Mr. Minister? We have had some discussion of the effects of clause 2(c)(ii). Does this mean that a province or provinces can veto a national scheme?

Hon. Mr. Olson: No, sir.

Senator Grosart: What does it mean, then, when it says that any other natural product and any part of that product is not a farm product within the meaning of the act unless there is a declaration by the provincial governments?

Hon. Mr. Olson: If you would not mind, Mr. Chairman, I will try to explain the meaning of the whole of that subclause.

As you can see, "farm product" for the purposes of Part I—which is clauses 3 to 16, that is, the functions of the council—means any natural farm product or any part thereof. Of course, that will be set out from Day 1 of the proclamation of this act.

After that, paragraph (c)(i) puts eggs and poultry in that category, so that there does not have to be a further declaration from the province.

Then, paragraph (c)(ii) says "any other"; so in regard to any natural product of agriculture, other than eggs, and poultry, and any part of any such product, that would be capable of being defined as a farm product under this interpretation clause, the Governor in Council would have to be satisfied, as a result of a declaration of provincial governments, following plebiscites or otherwise—and here I want to point out that we must not tell the provinces how they can determine this—that the majority of the producers thereof in Canada is in favour of the establishment of this agency. My interpretation would be, first of all, if we were going to set up a national marketing agency for the commodity involved, that we would have to be satisfied that the majority of the producers in Canada were in agreement.

It does not require that each individual province should make that declaration that they were willing to delegate their legislation.

Senator Grosart: It seems to state very clearly that it must be as a result of declarations by provincial governments—to become a farm product.

Hon. Mr. Olson: Yes.

Senator Grosart: To come within the definition of a farm product. This is part of the definition section. This clause would seem to say that one of the conditions is a declaration by provincial governments.

Hon. Mr. Olson: That is right. I think it says two or more governments.

Senator Grosart: No, it says by provincial governments.

Hon. Mr. Olson: Yes.

Senator Grosart: Does this mean that there must be two provincial governments to make this declaration?

Hon. Mr. Olson: Mr. Chairman, there would be no need to set up a marketing agency under the national legislation if there were but one province which wished to have it within that province—because, of course, clearly this would be within its own jurisdiction. So it has to be two or more, or there would be no need for the national legislation to apply.

Senator Grosart: Yes, but what I am asking, Mr. Minister, is this: Is a declaration by a provincial government a requirement or condition before one of these other products can be described as a farm product within the meaning of the act?

Hon. Mr. Olson: For purposes of this act, yes.

Senator Grosart: This is a fundamental change in the bill.

Hon. Mr. Olson: I would like to comment on that, very briefly.

Senator Grosart: Perhaps I should have said, "Is it a fundamental change . . .?"

Hon. Mr. Olson: It is not a fundamental change in the bill because there are other clauses that require the Governor in Council to be satisfied that a majority of the producers of that product—

Senator Grosart: Yes.

Hon. Mr. Olson: So what it is really doing is stating again what has been stated in the bill, in other places.

I refer you to clause 17(2), which was in the bill for several months, that the Governor in Council, in order to determine whether a majority of producers of a farm product are in favour of establishing an agency, may request that each province carry out a plebiscite of the said producers. That says they may request a plebiscite. But if there is this declaration, other than by plebiscite—and we cannot impose our rules on the provinces—it is essentially the same meaning.

Senator Grosart: But it has to be a declaration which is not technically a part of the bill until this amendment is made.

Hon. Mr. Olson: No.

Senator Goldenberg: May I say that Senator Grosart is rather confused by the word "declaration". Does not this word "declaration" really mean a report of that provincial government that a vote has been taken and that the result is such and such?

Senator Grosart: It means a declaration.

Senator Goldenberg: It means, as a result of the plebiscite.

Senator Grosart: It says "a plebiscite or otherwise".

Senator Goldenberg: "Or otherwise" means if there is no plebiscite.

Senator Grosart: But there must be a declaration by provincial governments—more than one—before anything other than eggs or poultry is a farm product within the meaning of the act. That is all I am concerned with.

Senator Martin: Could we just have the answer to that?

Hon. Mr. Olson: I have already answered yes to that. The other part of the question was whether this was something new in the act, and as far as I am concerned it is not.

Senator Grosart: "May" in clause 17 has now become obligatory. It was "may" before, but now it is an obligation.

Senator Martin: That is a matter of interpretation.

Senator Goldenberg: They both remain in effect because of the "or otherwise".

Senator Grosart: No, the "or otherwise" refers only to the alternative to the plebiscite.

Senator Langlois: No, it refers to the requesting of the plebiscite alone. Nothing else.

Senator Phillips: Mr. Chairman, as a supplementary, may I have a definition of the word "otherwise" when it comes my turn for questioning? And while we are on this clause, I wonder why the word "otherwise" has been included in here.

Hon. Mr. Olson: Mr. Chairman, the basic reason is that it is not competent, so I am advised, for the federal Parliament to pass laws that impose instructions or conditions on how the provinces administer law that is passed within the competence of their legislature. When you ask what is the definition of "or otherwise", there are three provinces in Canada, Quebec, Prince Edward Island and Alberta, that require a vote before they can set up any marketing agency under their own legislation. There are six provinces that have written their legislation in such a way that they can set up a marketing plan and an agency with or without a vote. Those provinces are Manitoba, Saskatchewan, Ontario, New Brunswick, British Columbia and Nova Scotia. The three that require a vote are Quebec, Prince Edward Island and Alberta.

So they have other means of determining whether there is a majority, and whether we agree with it or not in this case is irrelevant, because I do not believe we have the right to tell them how they should determine this. They do

it by public hearings. They do it by many means that are not strictly defined as a plebiscite.

Senator Molgat: Mr. Chairman, "producer" is defined by the province in every case.

Hon. Mr. Olson: Yes.

Senator Molgat: And can vary substantially from province to province.

Hon. Mr. Olson: Well, that is right. It does at the present time, Mr. Chairman, for the purposes of the provincial legislation. But remember that, if we set up a national farm marketing agency, all of the provinces will have to agree to the same plan—the marketing plan for the commodity. The provinces have already indicated that, if they are all going to delegate their legislation—and the definition of "producer" is, of course, done by regulation in any event for the various commodities,—they would have to agree to the plan that would be applied nationally. If that was done, then, of course, it would be uniform across the country.

Senator Molgat: But that would be after the plan was in effect.

Hon. Mr. Olson: Yes.

Senator Molgat: The decision to go into the plan would be made by producers defined by the province.

Hon. Mr. Olson: I think that it might be possible to define for the purposes of the National Farm Products Marketing Council something much different, but I have to draw to your attention here that there are different regulations in different provinces respecting the depth to which a marketing plan might go—that is, if it goes for a commission or if it goes for a one-desk selling agency, or if it goes even farther where it sets quota production, and so on. If we set up a marketing plan which the provinces may tentatively agree to, they would also have in some cases an obligation to go back to their producers if they intend to increase the powers of a marketing agency. And so I think that by the time we got to the point where we had a draft plan that was more or less tentatively agreed to, that we would use the terms and conditions laid down in that plan for other things, but more specifically for the definition of a producer so that the vote would be applied uniformally.

Senator Molgat: But in clause 2. (c)(ii), when you get a declaration from the province, that declaration is based on the definition that that province has established at that point what a producer is. When the province comes to you and says, "By plebiscite or by some other means, we say to you that the majority of our producers are in favour," the "majority of producers" means as defined by that province.

Hon. Mr. Olson: I would think that that is probably technically correct, but I should also draw to your attention that there is a great deal of work which the National Farm Products Marketing Council will do prior to having reached that position that you are now talking about, and that is where you take the vote. The National Farm Products Marketing Council has, of course, power to make inquiries and to do research and to do a lot of things to determine whether or not they wish to recommend that favourable consideration should be given to a plan. And, of course, the Governor in Council, or the Minister as a representative of the Governor in Council, would set in motion other requirements under this act, and one of them would be to devise a marketing plan which is provided for in clause 2 (e), where it says:

> (e) "marketing plan" means a plan relating to the promotion, regulation and control of the marketing of any regulated product . . .

And then it goes on in the other subsections and says that the marketing plan may do such things as is the determination of those engaged in the growing or production of the regulated product. And of course this would constitute the electorate or the voters' list, if you like. As I said, I think that once we had a marketing plan, and all the provinces were going to subscribe to it and it included the definition of producer, then it would be uniform across the country.

Senator Molgat: But that again would be after the plan was in operation?

Hon. Mr. Olson: Not necessarily, and in fact I think it would be very unlikely that that would be the case. There is an exception to that, of course. I suppose, for example, that where they already have provincial marketing plans that have been voted and supported by the producers, and they already have a full-scale marketing plan in each province, it may be ossible under those conditions for us to put together a plan that would simply co-ordinate the operations of those already there.

Senator Molgat: What would be the situation if there were three provinces, for example, opposed to the plan and the other seven were in favour, and those seven constituted a majority of producers?

Hon. Mr. Olson: If the seven constituted a majority of producers, that would satisfy the requirement under the amended clause 2(c). But here is a situation where we have to have the National Farm Marketing Council use some judgment and discretion. Certainly there is no point in embarking on a national farm marketing agency if there is enough of the product outside of the jurisdiction of the agency to bring about a high chance of failure before it started. So some discretion is required, and what I have consistently said throughout the public debate going on for many months concerning this is that if there was a province which did not wish to join the plan but was at the same time a significant producer in terms of the national production of the commodity that I would be very reluctant, if I did not completely refuse, to move forward with that plan until all of the provinces who had significant production of that commodity in question were agreeable.

I do not think that can be spelled out any more rigidly than that. We hope the Farm Products Marketing Council will exercise a certain amount of discretion in these matters.

Senator Molgat: But if a decision were made, there would be no opting out.

Hon. Mr. Olson: Clause 39 provides for opting out by a province.

The Acting Chairman: That is the dissolution of an agency in respect of which an order has been made.

Hon. Mr. Olson: Yes. That is right, but clause 32, which deals with federal-provincial agreements, provides that a province making an arrangement or entering into a contract for a period can designate the length of time for which they will delegate their authority and be party to such agreement. The province can put a terminal on it, as is the case with any other agreement or contract.

Senator Molgat: That is not how I read clause 32, which indicates the possibility of the federal Government making an arrangement with a province.

Hon. Mr. Olson: Mr. Chairman, if the province withdraws its delegated authority under its provincial jurisdiction, that is the power to deal with intraprovincial trade, market and production controls, then, of course, the function of the national agency is dead in that province.

Senator Molgat: Could that province market as it wishes? Would there be quotas, and could it sell throughout Canada?

Hon. Mr. Olson: The federal Government exercises that jurisdiction.

Senator Molgat: For example, if there were a hog marketing board established and the Province of Saskatchewan did not wish to participate, it would be free to produce all the hogs it wished and sell throughout Canada?

Hon. Mr. Olson: No, it could without signing the agreement, of course, and I suppose it would be given some access to its traditional market. That is included in another clause. In this example, if Saskatchewan would not sign an agreement but there was a majority and an overwhelming quantity of hogs produced in Canada subject to agreement, that province then could and would, perhaps, be given access to its traditional markets on the same basis as other provinces when that product was sold into other provinces.

Senator Molgat: But that is not written out in the bill.

Hon. Mr. Olson: Well, I am not sure what you mean by, "It is not written out in the bill." This act, of necessity, is based on an agreement to agree. If there is not an agreement to agree, then obviously we have to do the best we can to try to put some kind of marketing plan together, bearing in mind the various interests and the sovereignty and jurisdiction of provinces, which is like putting many pieces together.

Senator Phillips: I am not sure whether I understood the minister correctly. Senator Molgat has raised a very important point. If one province, which we will call Province A, has a surplus of hogs, and it then decides to withdraw from the marketing council, is that province free to ship into Province B which is still under the marketing plan?

Hon. Mr. Olson: I do not believe that the other provinces and the federal Government would agree to allow a province to wreck the marketing plan, but I think they would probably have access to the market place for their traditional supply.

Senator Benidickson: But the traditional supply may be responsible for the general chaos in the market.

Senator Phillips: How do you relate that to section 121 of the BNA Act, if the province is exercising its right in interprovincial trade?

Hon. Mr. Olson: I think the honourable senator is asking for a legal opinion on the Constitution of Canada, which I am not sure that I am competent to give.

Senator Martin: But you are competent to give to the committee details of what the provinces wired to you.

Hon. Mr. Olson: I will have to be guided by the Acting Chairman.

The Acting Chairman: I think the agreement was that the communiqué would be put on the record.

Senator Benidickson: It is not a telegram; it is a communiqué. Senator Martin referred to a telegram.

Hon. Mr. Olson: It is a communiqué that was issued following a meeting of provincial Ministers of Agriculture and the federal minister. Would the committee like me to read it in toto? It is dated Ottawa, November 23, 1971.

The Acting Chairman: Would the committee like to have the entire communiqué on the record?

Hon. Senators: Agreed.

Hon. Mr. Olson: It reads as follows:

> Agreement was reached today by the federal and provincial Ministers of Agriculture on the principles necessary to establish policies and programs aimed at assisting Canada's rural areas and provide improved opportunities for low income farm people.
>
> These principles draw upon basic documents prepared by the Canada Department of Agriculture and upon the report by the provincial ministers presented to the federal minister in Ottawa on November 22.
>
> The agreement includes principles which take into account the social as well as the economic aspects of the rural sector.
>
> Principles include provisions to enable farm people to more readily acquire the land and capital resources essential to improving their income. In addition, improvement will be made in existing information and advisory programs. Programs to be developed will aim primarily at assisting small family type farms.
>
> Further details of the program providing minimum acceptable levels will be developed immediately by a joint federal-provincial technical committee. Individual provinces will then be able to enter specific agreements with the federal Government in accordance with the particular needs of farm people in that province. Such agreements will be within an agreed national framework.
>
> Administration of the program by federal and provincial agencies within a province will be carried out

on the basis of the agreement and the program will be under continuing review by an advisory group drawn from federal and provincial officials.

The group also focussed attention on the immediate need of some producer groups for national marketing agencies including supply management systems for poultry to allow them to meet the demands of the market place and avoid the disastrously low prices resulting from surpluses. There was majority agreement that legislation was necessary to provide the legal framework for a coordinating agency and to ensure speedy passage of bill C-176. It was suggested that amendments be made to ensure that supply management features of the bill were not provided to producers of commodities other than poultry and poultry products without a new amending bill. In effect this would provide the opportunity for poultry and poultry product producers to utilize all features of the bill while other commodity producers would only have available to them, without further parliamentary action, the non supply management features of the bill.

It was noted that the Canada Grains Council has a study well under-way on the pricing of feed grains in Canada. When the report is available ministers will consider whether further study is required to arrive at a recommendation on equity of treatment across Canada.

Related problems including price stabilization, export development, farm and rural credit and the impact of low priced imports were discussed extensively and it is planned that further consultation be held next month to formalize proposals in these areas to ensure a strengthening of canadian agriculture and to improve producer income.

Senator Benidickson: Would you mind re-reading the section which you feel indicates that any changes made yesterday are not incompatible with the communiqué?

Hon. Mr. Olson: The significant part of the communiqué which deals with that is as follows:

> There was majority agreement that legislation was necessary to provide the legal framework for a coordinating agency and to ensure speedy passage of Bill C-176. It was suggested that amendments be made to ensure that supply management features of the bill were not provided to producers of commodities other than poultry and poultry products without a new amending bill. In effect this would provide the opportunity for poultry and poultry product producers to utilize all features of the bill while other commodity producers would only have available to them, without further parliamentary action, the non supply management features of the bill.

Senator Argue: When was that communiqué issued?

Hon. Mr. Olson: November 23, 1971.

Senator Argue: And we are still having speedy passage!

Senator Bélisle: I asked you a question a while ago supplementary to Senator Martin's question and you answered an unequivocal "yes". Did you only have the communiqué in mind when you answered my question, or did you have something else in mind? I believe my question was, "As of this morning, do you have something in writing?"

Hon. Mr. Olson: I think your question related to whether the provinces were satisfied that the two amendments passed last night in the other place were compatible with the wishes of the provincial government. I think that is what you asked. I answered, "Yes" to that question, because the request that is made here by way of the amendment is, I think, completely satisfied by the two, and I think it is fair to say the only two, amendments of significance that were made last night.

Senator Sparrow: I am not a constitutional expert, although we have some here. The minister has mentioned a couple of times that we cannot impose our rules on provinces, and that we have not the constitutional right to say how a province determines what its producers' wishes are. I think that is what he said. If that is what you said, and if that is what you meant, how can you relate that, when you that Parliament cannot dictate to the provinces? How in clause 2(c)(i) in the same bill can we dictate at this time that eggs, poultry and any part of such product can be in that. If paragraph (i) can be in that constitutionally, why cannot paragraph (ii) be constitutional as well, to say that it must be a plebiscite?

Hon. Mr. Olson: What clause 2(c)(i) says is that a farm product for the purposes of this bill is eggs, poultry and any part of any such product, and there is no qualification to that. That is all it says.

Senator Sparrow: So are we not then dictating to the provinces that those items are in it, regardless of how it is determined? They do not even have the right to determine.

The Acting Chairman: I would gather from the communiqué that the provinces wanted those two. They agreed.

Senator Sparrow: But the communiqué is not law. This bill happens to be law, if it is passed. I am concerned with the fact that the words "or otherwise" are in the bill. The minister used the word "impose". If we can impose paragraph (i) without a vote or any decision by the provinces, such as by legislation, why can we not impose the same thing, that a plebiscite be held in each province?

The Acting Chairman: I think what the minister is saying is that in respect of eggs and poultry the provinces have delegated, and for that reason the federal authority is assuming jurisdiction. It is part of an interprovincial agreement. In respect of the other, they write it quite differently to take into account the position, and the undoubted jurisdiction, of the provinces.

Senator Phillips: You say it is an agreement, Mr. Chairman. Has that agreement been tabled in Parliament at any time?

Hon. Mr. Olson: No. The communiqué has been tabled.

Senator Phillips: There is no reason why Parliament should not see the federal-provincial agreement. Why the secrecy? Why cannot we have it tabled?

The Acting Chairman: I do not think there is any question of secrecy, if you are taking that from what I said. All I said was that there was agreement. I did not say that there was a written agreement, and it is obvious from the communiqué that there is agreement, a meeting of minds between the federal and provincial ministers of agriculture. And that is as far as I would like to take it.

Senator Phillips: I do not think it is a signed agreement, then.

Hon. Mr. Olson: If I may answer that, Mr. Chairman, I do not know how you can have a signed agreement with the Government of Canada, which receives its authority from Parliament, before Parliament gives the authority under which it could enter into such an agreement.

Senator Sparrow: On the "majority of producers" aspect in (ii) again—and Senator Molgat touched on this—that is the basis on which each province will determine what a "producer" is. There may be an area in Canada, for example, in cattle,where they could produce a number of cattle, a greater extent in numbers, with less producers. So an area could supply the greater number of animals on the market, with less producers. How do you relate that to the "majority"?

As an example, if a province said that under its provincial regulations a "producer" would be one who has two animals on his farm, or 12 on his farm, at such-and-such a date, then you might have, in theory, 30,000 of those, or whatever the case may be, in an area, "producing". You might have 30,000 head of cattle and half of them would be owned by many producers, as against a few producers of 50,000 head of cattle. This would be the concern, I would suggest, for areas that are heavy producers in any commodity, where it is the lifeblood of the country that is involved.

Hon. Mr. Olson: Mr. Chairman, I am advised that all the provincial legislation calls for one man one vote. What they do from there on is to set out what qualifications are necessary for a man to vote. Once he has that qualification to vote, there is no further distinguishing between the weight of that vote. It is one man one vote. In some provinces, the requirement is that they sell $500 worth of the commodity in an area. In other places it is so many hogs and they must have so many acres of potatoes, whatever it may be.

I would not like to repeat what I have said—unless you wish me to do so—about the marketing plan. It is the responsibility of the national farm council to inquire into the merits of establishing a marketing plan for a commodity. Once they have done that and are recommending to me, as the minister—and of course also to the Governor in Council—that a marketing plan should be established, then we would have to go to the provinces and work out this marketing plan. As I pointed out, that marketing plan can, and in my view would be, applied uniformly across the country. That marketing plan would define or specify the qualifications on who is to vote. Just to use round figures, supposing they said you need to have 20 head of cattle or 100 head of cattle, and that that is applied uniformly across the country—even if a man is qualified to vote, because he has the minimum requirements for a vote, he does not get more than one vote because he has twice as many cattle.

Senator Sparrow: Mr. Chairman, may I pursue that for a moment? Assuming that that producer was someone with a thousand head of cattle, that would mean restricting it in certain areas of Canada with a great many producers. If the reverse were true, that they said ten head of cattle, then you relate it to the area of production, so that the production of a few producers then exceeded the production in another area with a lot of producers than would otherwise be the case. The bill says it is the "majority of producers". It is the importance of that market or that commodity to an area.

Hon. Mr. Olson: Mr. Chairman, I do not think that we can get into a position—nor would I like to get into a position either—where we distinguish between the votes of individuals. I am talking about people. Once they are qualified to vote it is one man-one vote. But in the area that you are talking about, where it may be significant, certainly all the people in that area would have a vote providing they had the minimum qualifications for a vote.

Senator Fournier (De Lanaudière): Mr. Chairman, although I am not a member of the committee, may I be permitted to make one little remark?

The Acting Chairman: Certainly.

Senator Fournier (De Lanaudière): A moment ago Senator Sparrow suggested that we were imposing something. We are not here to impose our will. Everybody is free. It will be the common desire or vote of the committee. I do not like the word "impose". If it becomes the law, it will be the law of the land. I am not prepared to accept that I am an imposer. Of course, I am not a member of the committee and what I say would have effect only in the Senate, but I should like Senator Sparrow to revise that expression.

The Acting Chairman: I believe Senator Sparrow was referring to the imposition of the view of the federal Government upon the provincial authority. I think the minister has corrected that point. He said that the desire was not to ride roughshod, even if the federal authority had the constitutional right to do so, but to co-operate and to fit in with the schemes of the provinces. Is that fair, Mr. Minister?

Hon. Mr. Olson: Yes.

Senator Fournier (De Lanaudière): I am happy with that.

Senator Goldenberg: Mr. Olson, was this legislation discussed with representatives of farm organizations and others?

Hon. Mr. Olson: Yes, sir, very extensively with hundreds of organizations.

Senator Goldenberg: With all of the principal organizations?

Hon. Mr. Olson: Yes, sir.

Senator Martin: Mr. Olson, in the light of the reply you have just given to Senator Goldenberg, am I right in saying that there was a parliamentary committee that

went among the farm organizations and ascertained their opinions?

Hon. Mr. Olson: Yes, sir. There was a parliamentary committee that sat for hundreds of hours. The figure was given for so many hundreds of hours, but I am not sure how many it was. They held extensive meetings here in Ottawa over quite a long period of time. In addition to that they held hearings in Halifax, Quebec City, Ottawa, Toronto . . .

Senator Martin: And Windsor?

Hon. Mr. Olson: I am not sure about Windsor, but they held hearings in Winnipeg, Regina, Edmonton and Vancouver.

Senator Argue: What year was that?

Hon. Mr. Olson: 1971.

Senator Argue: When did they finish those hearings?

Hon. Mr. Olson: I think the travelling hearings were completed in February of 1971.

Senator Phillips: And you found unanimity and support for the bill, of course!

Hon. Mr. Olson: No, I would not say we found unanimity for all the clauses of the bill, but I think it would be a fair statement to say that the major farm organizations, and I am talking now about the national ones like the Canadian Federation of Agriculture and the National Farmers Union and several others, agreed with the principles and concept of the bill and generally with the bill itself. We have stacks of telegrams from these organizations asking that it be passed, but there are, of course, some details that they made recommendations on, and we have tried very sincerely to reconcile the many conflicting recommendations to come up with the most acceptable bill possible.

Senator Phillips: Have you heard from the National Farmers Union today?

Hon. Mr. Olson: No. I have heard through the press, but not directly.

The Acting Chairman: Are there any other questions of the minister at this time?

Senator Martin: What I am concerned about, Senator Olson,—I mean Mr. Olson. I keep wanting to promote you, and I hope it will come to you after your continuous period of good service—is this: we have from you now the view that the provinces want this legislation.

Hon. Mr. Olson: Yes, that is right.

Senator Martin: And we have from you a statement that there has been an exhaustive committee examination of this bill by the other house of Parliament. We have the third statement that the amendments to this bill represent likewise the wish of the nine provinces, in fact of the 10 provinces with the exception of the one reservation that Manitoba makes.

Hon. Mr. Olson: Yes.

Senator Martin: Now what is your timetable? You have heard the debate today and you have heard the desire of senators to make an examination of the bill. How do you see your schedule in relation to the problems that face the provinces? For instance, in my province, and I suppose this is true of all the others, the Government would have to enter into arrangements with farm organizations, and this would be quite an extensive thing. We are meeting at an unusual time of the year, as did the other house, and all of us, regardless of our position, are actuated by the best of all possible motives; in other words, we want the best legislation possible. But what is your timetable? I ask that so that we can address ourselves to that in the light of our own situation.

Hon. Mr. Olson: Mr. Chairman, I will try to answer that question. It is very difficult to be specific that there is some critical date. As far as I am concerned, that critical date is somewhere behind us, because there has been a great deal of financial suffering in some commodity groups, and in this case particularly the poultry, eggs and turkey producer group, because we have been unable so far to accommodate them by setting up a national marketing agency. But at this point in time with every day that passes this continues to be the case, and as I said, or at least as I am advised, the producer organizations in all ten provinces respecting eggs, for example, have come to an agreement, but they do not have any legal structure on which to formalize and administer that agreement until this bill is passed. There is a further complication with respect to your province, Senator Martin, and that is that they are now in the final stages of attempting to obtain the majority producers' support that this bill talks about.

If I may put it in very concise terms, the public debate indicates that the Province of Ontario would probably wish to enter into a marketing arrangement provided they were satisfied that it would be administered on a national basis. They are not, however, so sure that they would wish to do that if it were to apply only to Ontario and not on a national basis. It is therefore critical that we can say to the producers of egg and poultry products, not only in Ontario, but particularly Ontario because of the timing, that if they come to an agreement with respect to a marketing agency we at least have the legal structure on which we are prepared to sign an agreement with them and the other provinces who have also agreed.

As I said, the provinces have indicated to me, if I may rephrase what they said, that they wish to see speedy passage of Bill C-176. I realize that was a month ago, but its urgency is just as acute today, if not more acute than it was then. I realize that the attempt to achieve, first of all, majority producer support, then agreements from the provincial and federal jurisdictions, involves many pieces which have to go together as a result of negotiation and agreement.

It therefore seems to me that if we are at that point in time at which there is a very high level of agreement and disposition to enter into a satisfactory arrangement, every day that passes is damaging to a very large part of the rural and agricultural sector of the economy.

Senator Benidickson: With respect to the question of urgency, when you answered Senator Martin you put first

the question of poultry and eggs. I am no farmer, but I am a consumer. I recall some months ago the papers contained many reports with regard to the chaos in this particular production field. I have not heard of it recently, but I know I am paying higher prices for all poultry products. I therefore wonder if it has settled down? There do not seem to be bargain prices for those products such as there were at a certain point in time. What has happened in the meantime?

Hon. Mr. Olson: There has been a kind of gentlemen's agreement, if you like, among the provinces in an endeavour to hold down some of this surplus production.

Senator Benidickson: Was it dumping?

Hon. Mr. Olson: It was to hold down the surplus production so that there were not great quantities of surplus eggs and broilers on the market at disastrously low prices. As a consumer, you probably refer to them as bargains, but it is a disaster to the farmer producing them. The federal Government took action on two occasions to assist in this situation. In July, for example, we entered into a program under which we brought 50,000-30-dozen cases of eggs. We took them off the market, dried them and included them in our world food program. That took some of the pressure off the market. It did not raise the price, but it helped the situation from becoming all the more disastrous.

On November 1, I announced a fowl slaughter program which hopefully would have taken off another 320,000 to 350,000 fowl, which would otherwise be recycled and put back into the laying pens. That was not so terribly successful, I have to admit. We hoped that if we could reduce production by something like 3,000 to 5,000 cases per week, we would stabilize the market to some extent.

These three things—the kind of agreement to stop cutting each other's throat, the program where whereby we took some of these eggs and put them in the world food program, and the fowl slaughter program to accelerate that slightly—have worked together to stabilize the situation somewhat.

I have to say that I am very, very fearful about what could develop two or three months ahead unless we are able to give legal status to the agreement which seems to have been reached.

Senator Argue: I am interested particularly in the role that farmers and farm organizations will play in this. I notice that the proposed council is to have between three and nine members. Perhaps the minister is in a position to tell us whether the number is likely to be three or nine. In other words, will the proposed council be as broad as nine might make it, or as narrow as three might make it?

Hon. Mr. Olson: There will be three to start with. There may be more, but there will have to be at least three.

Hon. Mr. Argue: Of which two will be farmers?

Hon. Mr. Olson: The bill says producers. I would be extremely anxious to obtain three highly competent people in this field immediately.

Senator Argue: Do you have anyone in mind?

Hon. Mr. Olson: Obviously we have done some canvassing of the prospects. Perhaps one commodity, such as poultry, might be enough to start with. However, let us assume that potatoes were to come in. They may not be very far behind poultry, and certainly I would want one person on the council who was thoroughly familiar with the marketing of potatoes. The council would expand in proportion to the number and variety of commodities that came in. I am sure that Senator Argue realizes that there is quite a significant difference in the marketing of various products that might come in. In other words, farm products are certainly not all marketed in the same manner.

Senator Argue: The proposed council seems to have an enormous amount of power, but it seems to me that there is not necessarily adequate assurance that the voice of the producers will be well represented. I know that could be argued.

Hon. Mr. Olson: The majority of them would be producers. We start out from that point. The National Farm Marketing Council is then responsible to the minister, the minister is responsible to Parliament, and the honourable senator knows to whom Parliament is responsible. There is a chain there. It is pretty important that the producers' interest be paramount.

Senator Argue: The word itself would denote a much larger body than this. I would have thought there would have been some formula whereby there was greater assurance that the producers themselves, in a fairly direct way, would be represented. So it will not be misunderstood I am in favour of the bill as it stands, in my opinion, a great deal of progress has been made, but, nonetheless, as a farmer I would like to see a greater voice at the grass roots level.

Correct me if I am wrong in my interpretation of this . . .

Hon. Mr. Olson: May I just say one thing?

Senator Argue: Yes.

Hon. Mr. Olson: I just want to make the point that the agencies themselves will be operating the marketing plan, and here again there is a requirement for a majority of producers on the board of each agency. There is a double situation where you must have 50 per cent of the producers on the council and you also must have 50 per cent or a majority, is the word that is used, of persons on the agency itself.

Senator Argue: What I was going to refer to was the clause that deals with advisory committees of the agencies. I must admit I get mixed up with all of the draft bills that we have received. I marked the earlier one because it was the only one I had, until this later one came in, and they are not exactly the same. In any event, in the one which was passed by the House of Commons last night, at page 19, subparagraph (g), it states:

> For the establishment of consultative or advisory committees—

that is of the agencies.

> . . . consisting of members of the agency or persons other than members or both; . . .

That would suggest to me, right off hand, that this provision is for the agency to be adviser to the agency, because members of the advisory committee can be members of the agency.

It would seem to me that if it were to be an independent advisory committee they would need to have members of the agency on the committee. I may be wrong in my interpretation.

Hon. Mr. Olson: Mr. Chairman, we have a number of these consultative or advisory agencies set up at the present time. For example, we have one with the Wheat Board; we have one with the Canadian Dairy Commission; and we have one with the . . .

Senator Argue: You have one with the Eastern Feed Board.

Hon. Mr. Olson: Yes. On every one of them there is one member of the agency who is also a member of the advisory committee, and they sit with them. We put them in there so that one of them, either the chairman or someone designated by him, could sit with the advisory committee. However, it is one member of the agency only. For example, the Chairman of the F.C.C. sits with the advisory committee, but all of the others are producers.

Senator Argue: If that is what it means, then I have no objection. As it is, it seemed to me that the agency was advising the agency. The other part I question is as follows:

> . . . consisting of members of the agency or persons other than members or both; . . .

It would seem to me that it might have been advisable to spell out that these would be representatives of producers or farmers or farm organizations, or whatever you want to call them. In other words, this would be a grassroots voice in an advisory capacity to the agency, rather than, as it would seem to me, giving the agency the power to select its own advisers, subject to the veto of the council.

The Chairman: Who else could they get?

Senator Argue: You would be surprised. They might load it with packers or directors of banks.

Hon. Mr. Olson: Mr. Chairman, there is certainly a great need and desire to have producers on these agencies. I am sure Senator Argue would agree with me that if we are going to set up advisory committees to marketing agencies it might be extremely useful to have someone who was competent in marketing, maybe domestically, maybe internationally, and so on.

Senator Argue: In the council, you said, they will be producers, but in the advisory agency it is left wide open. I would think you might strengthen it from the producers' point of view if it read a little differently.

Hon. Mr. Olson: I can assure you that has been the result of those committees that have been set up.

Senator Molgat: Mr. Minister, you referred a number of times to the vote after a plan is established. There is no provision that there must be a vote. The provision that I see is that you may ask for a plebiscite, but a plan could be set up simply if enough provinces indicate to you that they are in favour, and that this represents the majority of producers. Is that not correct?

Hon. Mr. Olson: I am not quite sure I get the gist of the timing of your question.

Senator Molgat: Let us assume that a sufficient number of provinces, say eight provinces, give you a declaration that the majority of their producers are in favour of a plan, and this represents the majority of the producers in the industry in your view, it can then proceed without a vote; the plan can be set up, can it not?

Hon. Mr. Olson: Three provinces—Quebec, Prince Edward Island and Alberta—cannot, because they require a vote under their own law. That varies, too. Quebec requires a 66 2/3 per cent majority; so does Prince Edward Island; Alberta requires a 51 per cent majority. I want to be practical here. If you try asking me to show you the exact legal terminology in the bill that calls for this, I will find it difficult.

Here is the sequence of what would happen. In the first instance, the provinces would come to the National Farm Marketing Council and suggest that they think there ought to be a national farm marketing plan for, let us say, potatoes. The council is required to inquire into the merits of that, to look into it and have proposals, and perhaps do some work on drafting a marketing plan that could be operated. That is about as far as that would go up to that point. If it were subsequently determined that the national council wanted to recommend that to the Governor in Council, I think the provinces would go back and, by agreement, look at the marketing plan that was proposed to be agreed to. They would apply the rules that were set out in that proposed marketing plan to their own situation within that province, including what you are concerned about, which is the definition of who can vote, the qualification of who can vote.

It would be at that point, which would be several stages after the initial consideration was taken into account, that they would then apply the terms and provisions of the proposed marketing plan in establishing whether the majority of those producers gave their approval. At that point, as I said, I am relatively certain that the provinces will have to agree that they are going to apply essentially the same criteria as other provinces in making that determination. Here we get into some difficulties about my trying to say, either in statutory law or otherwise, what exactly then provinces have to do, because they have to agree to agree. But once they have agreed to what the marketing plan is going to be, or the tentative marketing plan is going to be, then it would be my opinion that that would be applied uniformly in those provinces, and they would have to apply the same criteria in that uniformity.

Senator Hastings: The concern in the west is largely from the red meat producers. There seems to be agreement in so far as poultry and eggs are concerned. The people concerned in livestock groups, the cattlemen, have not seen these agreements, obviously. These came out during the course of yesterday's debate, did they not?

Senator Argue: They are part of the bill.

Hon. Mr. Olson: I do not think they saw the exact wording, but the representation that we have seen, is that they were aware that the provinces had made this representation some time ago, I am fairly sure.

You see, there is a difference of opinion here, I think, on what was in the bill prior to these two amendments going in last night. I have stated, and I am still of the same opinion, that in practical application of the law, what those two amendments do, with one or two exceptions, is a repetition of what was in the bill before.

I do not wish to try to mislead you in any way that all of the qualifications as to "a farm product" were in it, but I am saying that when you get to the point of setting up an agency all these steps would have to be taken in any event.

There is one difference in the amendment to clause 18, that is, it requires a further action by the Parliament of Canada to name a commodity after all the other measures have been taken. That was not in there before, but that means we have to bring in an amending bill, naming the commodity, and put it through both houses of Parliament, if we want "supply management" as a feature of the program.

Senator Hays: I wish to preface my question with an observation. It is only a little less than eight years ago that we had something like 450 million pounds of butter in Canada, with millions of pounds of powdered milk, and so on. The fact that this has been agreed to is, I believe, sufficient. I would like to move that we rise and report the bill without amendment.

Senator Bélisle: I object.

Senator Phillips: I object.

The Acting Chairman: I have a motion from Senator Hays, that the bill be reported without amendment.

Senator Argue: I wish to say a few words. It would be a great mistake to pass this motion, certainly with the minister here. He has been very competent and I wish him all the success in the world. He told us that the last time the farm organizations were heard was February of this year. We were told that by various people—not by the minister.

Hon. Mr. Olson: I do not want to leave any misunderstanding. I said, when the committee was travelling.

Senator Argue: Was that the last time the committee heard the farm organization representatives?

Hon. Mr. Olson: No. There have been meetings since then.

Senator Argue: I do not think they were heard for some months. I think this is one of the questions being asked. I do not believe the farm organizations have been heard for some months, and I believe the amendments before us are exceedingly important. I have not heard anything yet that would suggest that if this bill is not passed today this whole thing is going to collapse. I think there is a gentleman's agreement, based on speedy progress, speedy passage of required legislation. I think the Senate could bring about the speedy passage of this legislation after some further sessions of this committee, and after we have made the bill available to farm organizations and hear them, if they wish to be heard. Therefore, I feel that we would be doing a great disservice to the Senate and to the country by shutting off our deliberations by this means at this time.

Senator Phillips: Mr. Chairman, in the course of my remarks this afternoon I left out certain portions of my notes. Perhaps unwisely I accepted the word of the Leader of the Government in the Senate that we would be able to ask questions, that we would have all the time we wanted here, and that we would be in the hands of the committee. We have not been in here long enough to even hear a statement from the minister. And now we get a closure motion. It is absolutely ridiculous, and it is a double-cross of the worst kind.

The Acting Chairman: It is in the hands of the committee. There is no closure.

Senator Martin: No, there is no closure.

Senator Phillips: If there is no closure, then why the motion?

The Acting Chairman: Any member of the committee is entitled to move a motion at any time and the committee will decide it.

Senator Forsey: There are several of us who have questions to ask. I have two questions of importance that I want to put. I am simply staggered by this motion.

Senator Phillips: It is a double-cross of the meanest kind.

The Acting Chairman: Well, it is open to any member of the committee to amend the motion, if he so desires.

Senator Molgat: In the course of the debate this afternoon there was some feeling that the debate should be adjourned to some time next week or to some other date. From further discussion I understood that a compromise was reached and that Senator Langlois was prepared to move a motion that this committee adjourn to some time probably next week. At that stage I was not a member of this committee, and that is why he did that. But once I became a member of the committee Senator Langlois indicated to me that he expected me to do so.

Senator Hays: Mr. Chairman, if there are more questions, I would be glad to withdraw my motion.

Senator Martin: I would think so at this stage. It is difficult for me at this time because I am a colleague of Mr. Olson's, but this Senate is trying to do its job. It has spent a lot of time today in a general debate. It has this bill before it now. Obviously, the senators, as you can sense from their remarks, are anxious to have a full examination of this bill. If it could be established by you, Mr. Olson, now, that this bill must be passed now or there will be a disaster, then there is no doubt in my mind what senators would do. But some of them wish to have the opportunity of further examination of certain situations.

Can you help us in this, Mr. Olson?

Hon. Mr. Olson: Mr. Chairman, perhaps this will be a slight repetition of what I said a few moments ago, but my view is that a great deal of urgency has been expressed by

the Government, and by the governments of all ten provinces, but to put a date on which a disaster will occur if the bill is not passed and so on is not possible. I do know that there is a serious situation for producers of poultry. That situation applied to other provinces as well, but I confine my remarks solely to poultry for the moment because they are at the stages where they have advised me that they are ready to sign an agreement, if they can have the legal structure under which to do so. The situation is that they have suffered a great deal financially over the past few months. You know about the "chicken and egg war" as well as I do. With every day that passes there is going to be more damage to the industry.

I wish to say also, and I say it very sincerely, that I am fearful of agreements breaking down as more and more time passes. We have seen this happen in international agreements where there has not been an overall co-ordinating agency that has been agreed to. Inasmuch as the poultry producers are at that stage at least, they have been telephoning, wiring and telegraphing me and coming in to see me almost every week, pleading with us to try to do something to get this legal structure so that they can get on with the agreement they have been waiting weeks for.

The fault obviously is not with the Senate. This bill has not been to the Senate until today. The fault for that holdup lies elsewhere, as you all know very well.

Senator Martin: It certainly does not lie here.

Hon. Mr. Olson: But the point is that the urgency that I see not only for the whole of the national marketing plan that could be set up now is one thing. I do not want to repeat the situation in Ontario, but in my view and in the view of the Minister of Agriculture and Food in Ontario that is also critical, and so I do not know how I am going to convince you, but I tell you my own opinion.

Senator Martin: I am not asking you to convince me. I am asking you to help me.

The Acting Chairman: Perhaps I might intervene at this moment. It is obvious to the Chair, at least, that there are a number of questions that a number of the members of the committee have to ask, and at this stage the question which I put to the committee is this: Is this the appropriate time to do so? In considering that I think it is fair to say to the minister that the Senate, certainly this committee, has no intention of introducing any protracted delay in connection with the consideration of this legislation. But there may be some delay that is required for senators to satisfy their responsibility as legislators in this country. That, I think, is the idea that motivates members of this committee. It may be that that can be satisfied very quickly, but perhaps not now. Senator Forsey's remarks seem to indicate that. So I think we have a motion before us that the bill be reported without amendment. I have not had any contrary motion or amendment.

Senator Molgat: I was in the process of proposing the amendment that has been discussed this afternoon in the Senate. I regret the minister was not in the gallery at the time of that discussion because he would have heard the views of the senators, as expressed at that time, and what was said by Senator Langlois. The amendment I wish to propose is that the committee do not report but rather adjourn until Thursday, January 6.

Senator Belisle: I second that motion.

The Acting Chairman: There is no seconder required in committee.

Senator Hays: Mr. Chairman, if there are some more questions to be asked, I will be glad to withdraw my motion.

Senator Phillips: In support of Senator Molgat's motion, I am prepared to come back tomorrow or Monday, but I do not see how we can deal with it now. I have at least one hour's questioning of the minister, and I do not see how we can possibly come into a committee or ever accept the word of the Leader of the Government again if we are going to close . . .

The Acting Chairman: There is no question about that, Senator Phillips. I do not think you have to worry about that part. As to the question of the word of the Leader of the Government, I do not think we raise that here. Do not do that.

Senator Hays: I would be glad to withdraw the motion.

The Acting Chairman: Perhaps you would like to take a lead from the Chair on this point. Senator Molgat suggests Thursday.

Senator Benidickson: Senator Hays said he will withdraw his motion.

The Acting Chairman: I know, but Senator Molgat has an amendment. Let us take it that Senator Hays' motion is now withdrawn. Is that agreed?

Hon. Senators: Agreed.

The Acting Chairman: Senator Molgat, perhaps you would now care to introduce a motion? I would like to suggest that you consider a Wednesday sitting because of the fact that the work week in Parliament ends on Friday. It is not desirable that the Senate be constricted by any time factor which would prevent adequate consideration.

Senator Molgat: As was discussed in the house this afternoon, Mr. Chairman, my only concern is to be able to contact producer groups in my province with respect to the new amendments. In view of the long weekend that a number of them will take, there may be problems in contacting them in time for a Wednesday meeting. On the other hand, I recognize the minister's legitimate request to deal with this as quickly as possible. I do not wish to delay any longer than is necessary. As far as I am concerned, Thursday would be more suitable. If the following Tuesday is preferred, I do not care.

The Acting Chairman: Do you move, Senator Molgat, that the committee rise now and reassemble at 11 o'clock in the morning on Thursday, January 6, 1972?

Senator Langlois: 2 o'clock in the afternoon.

The Acting Chairman: We have to ascertain if our star witness can be present. Would the minister be available on January 6 at 11 o'clock, or at 2 o'clock?

Hon. Mr. Olson: Mr. Chairman, I would have to cancel some meetings, but I regard the passage of this bill as so important that I will attempt to do that.

The Acting Chairman: So you will be here?

Hon. Mr. Olson: Yes, I will.

Senator Phillips: Mr. Chairman, with respect to the hour of the meeting, we should bear in mind that members of the other house will probably be returning for royal assent. Therefore I favour the committee meeting at 11 o'clock, with the hope and expectation that we could complete our study on that day.

The Acting Chairman: On Thursday? I do not think Senator Phillips, we can anticipate that, and I consider it to be a very chancy business. If the committee is of the opinion that we could start at 11 o'clock in the morning, the Chairman will be here and, I hope, a quorum of the committee. The questioning can continue and go on into the afternoon and evening, if you so desire.

Senator Belisle: Will we be permitted to invite outside witnesses?

The Acting Chairman: That is up to the committee. I do not think we will cross that bridge before we come to it.

Senator Belisle: If the committee decides it will not, what is the use?

The Acting Chairman: Perhaps the committee is in a position to make a decision now. However, I do not think so, because there are still questions to come.

Senator Belisle: Senator Molgat said he would like to invite other witnesses.

Senator Langlois: It should be pointed out that it has been the long-standing practice of Senate committees to accept requests of witnesses to appear. I see no reason to change this.

Senator McElman: Mr. Chairman, is it practical to suggest to the minister that between now and the next meeting of the committee he could perhaps contact the provinces? I ask because there seems to be doubt in the minds of some senators, and we would like confirmation that the amendments are not in conflict, in any sense, with the agreed protocol.

Hon. Mr. Olson: Mr. Chairman, I will certainly have my office make an attempt to do that. I am aware that some provincial Ministers of Agriculture are away on holiday. I do not believe that I can get an opinion from anyone other than the ministers that would satisfy the request, but we can try.

Senator Forsey: You told us how urgent this was. You have been telling us that the sky would fall in if the bill did not go through in jig time. Tell them the same thing.

The Acting Chairman: In fairness to the minister, he did not say that.

Senator Forsey: But that was the sense of it.

The Acting Chairman: That is not what the minister inferred.

Hon. Mr. Olson: In reply to Senator Forsey, I say to him, without qualification, that what is in the bill now before you has the endorsation of all the ministers.

Senator Forsey: Why did you not say that to Senator McElman just now?

Hon. Mr. Olson: That was not the question. He asked me if I would contact them again.

Senator Forsey: He said some of us were uneasy about this.

Senator Benidickson: I think we have to take the minister's word on this.

Senator Martin: Mr. Chairman, before you put the question, I would like both yourself and Senator Langlois to address yourself to this point. How long the matter takes is, of course, for the committee to decide. A moment ago Senator Phillips thought that we had to take into account the other place if we were going to have royal assent. Senator Langlois and I have to know whether we must recall the full Senate. What do we do? Has Senator Langlois an idea? The members of the committee are not sufficient in number to constitute a quorum of the Senate.

The Acting Chairman: Perhaps I can help the honourable senator to some extent. The Speaker has the authority to summon the Senate at will. I assume that the motion to adjourn today will be to a date in January, certainly after January 6. If the committee should finish its deliberations on the 6th, perhaps it would be appropriate to recall the Senate for the 7th.

Senator Benidickson: You would have to consult the officers of the other house. It does not matter when we are recalled.

The Acting Chairman: Certainly the other house will have to be recalled, but the other house has it within its power, by an order made this morning, to be recalled for royal assent.

Senator Martin: But the point made by Senator Phillips is very important. He thought that the proceedings might be finished on Thursday; but I do not think it is clear that that will be the case. Can we, in fairness, ask others to come here when they have no immediate business?

The Acting Chairman: I do not wish to give advice to the Leader of the Government, but depending upon the result of the committee's first day of sitting, a decision could then be taken as to when the Senate should be summoned.

Senator Martin: That would clearly mean that it would not be until the following week.

The Acting Chairman: Not necessarily.

Senator Martin: How could we sit unless it were on a Saturday?

The Acting Chairman: As I understand it, under the rule that the Speaker now works on, the Senate can be summoned at any time and there is no notice required.

Senator Martin: We would have to give adequate notice, but it is not only the Senate that is affected; the other place is also affected if this bill is going to be made law after it has been dealt with by the Senate.

The Acting Chairman: That is their responsibility, but between the two houses there could be an accommodation worked out. In any event, I feel this is beyond the purview of this committee. While we would like to help the Leader of the Government, I think that the way is fairly clear for him to decide on what steps he should take following whatever disposition is made of this bill by this committee.

Senator Martin: I must say, with great respect, that I do not think there would be any chance, unless we pass the bill quickly on Thursday, of our being able to provide royal assent before the following week.

The Acting Chairman: That may be.

Senator Martin: I want Mr. Olson to be aware of the implications of this. In my opinion, we would not be able to give royal assent to this bill before January 10.

Senator Bourget: We are at the call of the chairman.

Senator Martin: Yes, but the chairman might not know Thursday night what to do.

The Acting Chairman: Senator Martin, I think we are all sympathetic to your problem, but so far as this committee is concerned it cannot decide . . .

Senator Martin: I realize that, Mr. Chairman, but I am just seeking advice.

Senator Phillips: See me after the meeting, and I will give you advice.

The Acting Chairman: I will put the question to the committee. Shall the committee rise now and reassemble at 11 o'clock on Thursday, January 6, 1972?

Hon. Senators: Agreed.

The committee adjourned.

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THIRD SESSION—TWENTY-EIGHTH PARLIAMENT

1970-71-72

THE SENATE OF CANADA

PROCEEDINGS

OF THE

STANDING SENATE COMMITTEE ON

BANKING, TRADE AND COMMERCE

The Honourable JOHN J. CONNOLLY, P.C., *Acting Chairman*

No. 54

THURSDAY, JANUARY 6, 1972

FINAL PROCEEDINGS ON BILL C-176

intituled:

"An Act to establish the National Farm Products Marketing Council and to authorize the establishment of national marketing agencies for farm products."

REPORT OF THE COMMITTEE

(Witnesses—See Minutes of Proceedings)

THE STANDING SENATE COMMITTEE ON

BANKING, TRADE AND COMMERCE

The Honourable Salter A. Hayden, *Chairman*

The Honourable Senators:

Aird	Hayden
Argue	Hays
Beaubien	Isnor
Belisle	Lafond
Benidickson	Lang
Bourget	Langlois
Buckwold	* Martin
Choquette	McElman
Connolly (*Ottawa West*)	Molgat
Cook	Molson
Desruisseaux	O'Leary
Everett	Phillips
* Flynn	Quart
Goldenberg	Sullivan
Grosart	Walker
Hastings	Willis

* *Ex officio members*

30 Members (Quorum 7)

Order of Reference

Extract from the Minutes of the Proceedings of the Senate, December 31, 1971:

"A Message was brought from the House of Commons by their Clerk with a Bill C-176, intituled: "An Act to establish the National Farm Products Marketing Council and to authorize the establishment of national marketing agencies for farm products", to which they desire the concurrence of the Senate.

The Bill was read the first time.

The Honourable Senator Hays, P.C., moved, seconded by the Honourable Senator Fournier (*de Lanaudière*) that the Bill be read the second time now.

After debate,

The Honourable Senator Sparrow moved, seconded by the Honourable Senator Molgat, that further debate on the motion be adjourned until Tuesday, 11th January, 1972.

The question being put on the motion,

The Senate divided and the names being called they were taken down as follows:—

YEAS

The Honourable Senators

Argue,
Bélisle,
Benidickson,
Fergusson,
Forsey,
Grosart,
McGrand,
Molgat,
Phillips,
Sparrow—10.

NAYS

The Honourable Senators

Aird,
Basha,
Bourget,
Bourque,
Connolly,
(*Ottawa West*),
Davey,
Duggan,
Fournier
(*de Lanaudière*),
Goldenberg,
Hastings,
Hays,
Lafond,
Langlois,
Lapointe,
Lefrançois,
Martin,
McElman,
McNamara,
Michaud,
Petten,
Stanbury—21.

So it was resolved in the negative.

Debate was resumed on the motion of the Honourable Senator Hays, P.C., seconded by the Honourable Senator Fournier (*de Lanaudière*), for the second reading of the Bill C-176, intituled: "An Act to establish the National Farm Products Marketing Council and to authorize the establishment of national marketing agencies for farm products".

The debate was interrupted, and—

The Honourable the Speaker having put the question whether the Senate do now adjourn during pleasure to reassemble at the call of the bell at approximately two o'clock p.m., it was—

Resolved in the affirmative. 1.15 p.m.

The sitting of the Senate was resumed. 2.05 p.m.

After further debate, and—
The question being put on the motion, it was—
Resolved in the affirmative.

The Bill was then read the second time.

The Honourable Senator Hays, P.C., moved, seconded by the Honourable Senator Fournier (*de Lanaudière*), that the Bill be referred to the Standing Senate Committee on Banking, Trade and Commerce.

The question being put on the motion, it was—
Resolved in the affirmative.

With leave,
The Senate proceeded to Notices of Motions.

With leave of the Senate,

The Honourable Senator Langlois moved, seconded by the Honourable Senator Bourget, P.C.:

That the names of the Honourable Senators Argue, Hastings and Molgat be substituted for those of the Honourable Senators Burchill, Gélinas and Giguère on the list of Senators on the Standing Senate Committee on Banking, Trade and Commerce.

After debate, and—
The question being put on the motion, it was—
Resolved in the affirmative."

Robert Fortier,
Clerk of the Senate.

24353—1½

Minutes of Proceedings

Thursday, January 6, 1972.
(71)

Pursuant to adjournment and notice the Standing Senate Committee on Banking, Trade and Commerce met this day at 11:00 a.m. to examine and consider Bill C-176 intituled:

"An Act to establish the National Farm Products Marketing Council and to authorize the establishment of national marketing agencies for farm products."

Present: The Honourable Senators Argue, Bélisle, Benidickson, Bourget, Buckwold, Connolly (*Ottawa West*), Goldenberg, Grosart, Hastings, Lafond, Lang, Langlois, Martin, McElman, Molgat, Phillips and Quart—(17).

Present, but not of the Committee: The Honourable Senators Haig, Forsey, McNamara, Michaud and Sparrow—(5).

In attendance: Mr. R. L. du Plessis, Acting Parliamentary Counsel, and Mr. Pierre Godbout, Director of Committees, Assistant Law Clerk and Parliamentary Counsel.

In the absence of the Chairman and upon motion duly put, it was Resolved that the Honourable Senator Connolly (*Ottawa West*) be elected Acting Chairman.

The following witnesses were heard:

Mr. Roy Atkinson,
President,
National Farmers' Union;

Mr. Charles A. Gracey,
Manager,
Canadian Cattlemen's Association.

Present, but not heard:

Mr. S. D. Williams,
Deputy Minister,
Department of Agriculture;

Mr. C. R. Phillips,
Director General,
Production and Marketing Branch,
Department of Agriculture.

At 12:55 p.m. the Committee adjourned.

At 2:35 p.m. the Committee resumed.

Present: The Honourable Senators Argue, Bélisle, Bourget, Buckwold, Connolly (*Ottawa West*), Goldenberg, Grosart, Hastings, Lafond, Langlois, McElman, Molgat, Phillips and Quart—(14).

Present, but not of the Committee: The Honourable Senators Haig, Forsey, Fournier, McNamara, Michaud and Sparrow—(6).

In attendance: Mr. R. L. du Plessis, Acting Parliamentary Counsel and Mr. Pierre Godbout, Director of Committees, Assistant Law Clerk and Parliamentary Counsel.

The following witnesses were heard:

Mr. Joe Hudson,
Lyn, Ontario;

Mr. J. Pringle, M.P.,
Fraser Valley East, B.C.:

Mr. David Kirk,
Executive Secretary,
The Canadian Federation of Agriculture;

The Honourable H. A. Olson,
Minister,
Department of Agriculture;

Mr. S. D. Williams,
Deputy Minister,
Department of Agriculture.

Present, but not heard:

Mr. C. R. Phillips,
Director General,
Production and Marketing Branch,
Department of Agriculture.

A brief submitted by the Consumers Association of Canada was ordered to be printed as an appendix to these Proceedings (See Appendix "A").

Upon motion duly put it was Resolved to proceed to a clause by clause examination of the Bill.

It was moved by the Honourable Senator Grosart that the comma after the word "plebicite" on line 25 of Section 2(c) be deleted.

The question being put on the motion, the Committee divided as follows:

YEAS—3 NAYS—10

The motion was declared passed in the negative.

It was moved by the Honourable Senator Phillips that in clause 3(1) the following words on lines 11 and 12 "to hold office during pleasure" be deleted.

The question being put on the motion, the Committee divided as follows:

YEAS—4 NAYS—9

The motion was declared passed in the negative.

It was moved by the Honourable Senator Phillips that paragraph (ii) in clause 18(1)(a) be deleted.

The motion was duly withdrawn.

It was moved by the Honourable Senator Argue that paragraph (g) in clause 26 be deleted and replaced by the following:

"(g) for the establishment of consultative or advisory committees consisting of members of the agency, primary producers, or persons other than members or primary producers; provided that a majority shall be primary producers."

The question being put on the motion, the Committee divided as follows:

YEAS—5 NAYS—8

The motion was declared passed in the negative.

It was moved by the Honourable Senator Phillips that the following be added as a new subsection (2) to clause 38 of Bill C-176, the remaining subsections being renumbered accordingly:

"38 (2) Every person who

(a) wilfully discloses or makes known directly or indirectly to any person not entitled to receive the same, any information submitted to the Council or an agency or required to be submitted to the Council or an agency pursuant to a requirement under subparagraph (iii) of paragraph (h) of subsection (1) of section 7 that might exert an influence upon or affect the market value of any regulated product, or (b) uses any such information for the purpose of speculating in any regulated product,

is guilty of an offence and is liable, on summary conviction, to a fine not exceeding three thousand dollars."

The question being put on the motion, the Committee divided as follows:

YEAS—3 NAYS—9

The motion was declared passed in the negative.

It was moved by the Honourable Senator Phillips that lines 40 to 43 in clause 39 of Bill C-176 be deleted and replaced with the following:

"but an order or proclamation under this section becomes effective only on the expiration of nine months from the date of publication thereof in the *Canada Gazette*, or such other period of time from the date of publication thereof in the *Canada Gazette* as is recommended by the Council."

The question being put on the motion, the Committee divided as follows:

YEAS—3 NAYS—9

The motion was declared passed in the negative.

It was unanimously Resolved that the Committee report Bill C-176 without amendment.

At 6:55 p.m. the Committee adjourned to the call of the Chairman.

ATTEST:

Georges A. Coderre,
Clerk of the Committee.

Report of the Committee

Thursday, January 6, 1972.

The Standing Senate Committee on Banking, Trade and Commerce to which was referred Bill C-176, intituled: "An Act to establish the National Farm Products Marketing Council and to authorize the establishment of national marketing agencies for farm products", has in obedience to the order of reference of December 31, 1971, examined the said Bill and now reports the same without amendment.

Respectfully submitted.

John J. Connolly,
Acting Chairman.

The Standing Senate Committee on Banking, Trade and Commerce

Evidence

Ottawa, Thursday, January 6, 1972

The Standing Senate Committee on Banking, Trade and Commerce met this day at 11 a.m. to give further consideration to Bill C-176, to establish the National Farm Products Marketing Council and to authorize the establishment of national marketing agencies for farm products.

Senator John J. Connolly (*Acting Chairman*) in the Chair.

The Acting Chairman: Honourable senators, we have with us this morning Mr. S. B. Williams, Deputy Minister, Department of Agriculture, and Mr. C. R. Phillips, Director General, Production and Marketing Branch, Department of Agriculture.

I should like to say a few words about some developments that have taken place since the last meeting. Although I ceased being Acting Chairman when that meeting adjourned, a number of inquiries have nevertheless been directed to me in connection with representations that are desired to be made to the committee. After discussing the matter with officials of the Senate Committees Branch, I informed those people making inquiries that, if they cared to appear here at eleven o'clock, the committee would consider whether or not they should be heard.

I may say that the practice has always been to hear witnesses appearing before the committee. Without presuming upon what decision the committee might make this morning, I thought you should know that all those people who made inquiries were told that the committee would certainly consider their request to be heard.

I should also like to inform the committee of two or three other developments.

Senator Grosart: Excuse me, Mr. Chairman, but will you tell us the names of those who requested to appear?

The Acting Chairman: I will come to that in a moment, Senator Grosart. First I should like to put on record some telegrams that I have received.

The first is a telegram that was addressed to me, which I received on January 4. It reads as follows:

> Senator J.J. Connolly, Acting Chairman Banking Trade Commerce Committee, The Senate, Ottawa, Ontario
>
> The consumer interest has been overlooked in the hasty passage by the House of Commons of Bill C-176. While denying the consumer the advantages which competition provides and the opportunity for free choice, the legislation fails to provide for consumer representation upon or public scrutiny of the agencies which may be established under this act. It also fails to provide for the right of appeal from any actions taken by such agencies.
>
> On behalf of the sixty thousand members of the Consumers Association of Canada I urgently appeal to you to grant us the opportunity of presenting to your committee the reasons for our strong opposition to this bill and our suggestions for amendments which would assist in safeguarding the public interest.
>
> Maryon Brechin, President Consumers Association of Canada, 100 Gloucester Street, Ottawa.

I directed the officials of the Committees Branch to inform Maryon Brechin that the Standing Senate Committee on Banking, Trade and Commerce would be meeting at 11 o'clock this morning. I do not know whether or not the lady in question is now present. In any event, I thought the committee should have that information.

I have just been handed a further telegram addressed to the committee, for my attention. That telegram is dated January 6, 1972. It comes from Woodstock, Ontario, and reads as follows:

> Banking Trade and Commerce Committee of the Senate Attention: John Connolly, Ottawa, Ontario
>
> We strongly urge you to delay passing Bill C-176. The public is unaware of its contents in its amended form. Strong opposition is being registered by Consumers Association of Canada. Negotiable quotas will add to food costs but not to farm income. Opposition by major farm groups and individuals has been well documented. This bill will decrease agricultural exports and raise agricultural imports due to artificially raised prices. Having a long look at this bill would enhance the public image of the Senate. We would be willing to discuss this in Ottawa at your request.
>
> Don Hart, Vern Kaufmann and Fred Cohoe.

This morning I had a telephone call from Mr. John R. Stewart, R.R. 6, Strathroy, Middlesex County. He describes himself as a dirt farmer, and is opposed to marketing schemes in general. He says he is a free enterpriser, and that he would be glad to come and in fact, he would be anxious to come to make a five-minute presentation, but he is up near London at the moment. I promised I would report his desire and view to the committee in the general way I have done.

This morning Mr. C. A. Gracey, Manager of the Canadian Cattlemen's Association, who lives in Toronto, came to my office and said that he would attend the committee meetings this morning and that he had a short presenta-

tion to make. Mr. Gracey informed me he was one of the witnesses who appeared before the Agriculture Committee of the House of Commons. I understand Mr. Gracey is here.

Mr. Roy Atkinson, President of the Farmers Union, is here and desires to make representations on this bill. I am also informed that a Mr. Joseph Hudson, an egg producer who lives in eastern Ontario in a place called Lyn—and I understand that is near Brockville—desires to appear before the committee. He cannot be here this morning, but I am informed that he could be here at 2.30 this afternoon.

Those are the only people whose interest in the work of the committee has been directed to me, and I wonder if there are any others present for the purpose of making representations.

Apparently there are not.

Now, honourable senators, what is your wish in respect of these people who desire to make representations?

Senator Molgat: I move that they be heard.

Senator Phillips: Before you bring that up, Mr. Chairman—and here I am deliberately trying to be careful in my remarks not to criticize you—

The Acting Chairman: You can criticize me if you like.

Senator Phillips: I fully realize the difficult position you are in, but I have here the unrevised version of the report of the last meeting, and I quote Senator Langlois where he said:

> It should be pointed out that it has been the long-standing practice of Senate committees to accept requests of witnesses to appear. I see no reason to change this.

A number of us had interpreted from that that witnesses would automatically be heard, and I hope that the fact that we had to refer the decision back to this committee did not discourage anyone from appearing.

The Acting Chairman: I do not think that is the case. Everyone I spoke to appreciated the fact that the committee ultimately had to make the decision. Now Senator Molgat has moved that those who are here should be heard. Is it agreed, honourable senators?

Hon. Senators: Agreed.

The Acting Chairman: I think it might meet with the views of all if we heard Mr. Atkinson first. I understand he has a plane to catch, and I think Mr. Gracey will not mind if we do that.

Senator Goldenberg: Do I understand that witnesses will be heard on the principles of the bill, that is, on all aspects of the bill, or only on the changes which were made in the House of Commons before Thursday last? There were three major changes which we discussed in the Senate.

The Acting Chairman: Perhaps we had better ask Mr. Atkinson specifically, and we can ask Mr. Gracey afterwards.

Is it your intention, Mr. Atkinson, to speak mainly to the amendments?

Mr. Roy Atkinson, President, National Farmers' Union: It was my intention to speak to the bill.

The Acting Chairman: But you will be mentioning the amendments?

Mr. Atkinson: Yes.

Senator Grosart: Before we hear Mr. Atkinson, may I ask if the minister will be here?

The Acting Chairman: I am sorry; I should have told you this earlier. I rather anticipated that the committee would take the decision it has taken to hear witnesses, and because I thought there might be questions of policy raised by the various witnesses it might be more appropriate if the minister were held in reserve so that he could deal with questions of policy, and the officials here could deal with questions of administration and detail.

Senator Grosart: Could I make the suggestion now that before we complete our consideration of the bill we should take it clause by clause? The reason I make that suggestion now is that I think it will simplify our discussion if we know that we are going to come to it *seriatim*, clause by clause, rather than questioning here and there and all over the place. So, if you will accept the motion, I move that we take the bill clause by clause.

The Acting Chairman: I do not think the committee normally has any objection to that. When Senator Hayden is here we do not as a rule move at an early stage to do this, for the simple reason that sometimes later in the development of the work we find there is no necessity to go over them all. Why not leave your motion until we have heard the witnesses? I think we could proceed in an orderly way if you did.

Senator Grosart: I am in your hands on that.

The Acting Chairman: In other words, let us keep it in mind that we will be calling the bill clause by clause before we adjourn.

Senator Phillips: And there may be further questions put before we begin clause-by-clause study.

The Acting Chairman: Certainly.

Now, Mr. Atkinson, would you like to make a statement?

Mr. Atkinson: Honourable senators, my submission this morning will be an oral one. I heard of the opportunity to appear before your committee and made the decision to appear yesterday, at noon, while I was at another conference, so I was not in a position to prepare any written material. I will attempt to keep my remarks brief.

The first item I would like to present for your consideration is what we deem to be an important principle which is contained on page 14, clause 19 of the bill which has to do with the appointment of the council members and their duration in office. Subclause (1) of clause 19 states that the members shall hold office at the pleasure of the minister or the Governor in Council.

When one examines clause 7, on page 6 of the bill, and the underlying subclauses, one finds that this council is given a great deal of responsibility, as a matter of fact a

very onerous responsibility, in reviewing and making decisions upon regulations and other regulatory matters having to do with the agencies.

In our view the appointment of council members during pleasure gives the Governor in Council and the minister extraordinary powers. It could possibly affect the decisions made by those responsible for operating the council. Therefore we believe that in order to give some independence to the council, and I say "some" independence, its members should be appointed for a definite period. Notwithstanding that proposition, council members should only be dismissed on the basis of a firm reason, which should be divulged.

Senator Grosart: Mr. Atkinson, in your opinion, should that apply also to clause 3, which provides for appointment to the federal council during pleasure?

Mr. Atkinson: It should apply to all clauses under which appointments, to arrive at very responsible decisions, will be made.

Senator Argue: For what length of time?

Mr. Atkinson: That is a matter of judgment. Five years would seem to be reasonable.

Senator Phillips: Should the appointment be renewable once during a term?

Mr. Atkinson: It could be renewed, depending on the performance of the members.

Senator Martin: Mr. Atkinson, will you please indicate the particular subclause of clause 7, or do you refer to the whole clause?

Mr. Atkinson: A number of clauses are involved.

The Acting Chairman: Clause 19(1) refers to agencies and clause 3(1) refers to the Council.

Mr. Atkinson: It applies in both positions.

Senator Martin: I do not understand your observation.

Mr. Atkinson: I say that the principle of appointment at pleasure applies in both positions.

Senator Goldenberg: No, Mr. Atkinson, it does not apply to agencies. Clause 19(1), at page 14, provides:

> The members of an agency shall be appointed by the Governor in Council to hold office during pleasure, or in such other manner including election by producers, . . .

Senator Forsey: "and for such term".

The Acting Chairman: Mr. Atkinson, are your comments directed to clause 3(1), rather than to clause 19?

Mr. Atkinson: That is correct.

The Acting Chairman: We can thank Senator Goldenberg for his wise legal counsel in this regard.

Mr. Atkinson: I am using clause 19 as the basis for speaking to other clauses.

Senator Forsey: But it is quite different.

Mr. Atkinson: I am also using clause 3(1).

Senator Phillips: Despite the wise counsel of Senator Goldenberg, I still feel that since the members shall be appointed by the Governor in Council and there is nothing to say that the alternative will be used, the Governor in Council can still appoint.

Senator Goldenberg: Of course, one or the other.

Senator Argue: But they cannot be appointed to stay in office longer than the life of the agency. It therefore seems that either they will have an indefinite period of time, which would be very long, or a period which would be the life of the agency. I suppose you would wish to appoint them for a longer period of time than the life of the matter with which they are dealing?

Mr. Atkinson: My concern is really that one clause provides that members of agencies shall be appointed at pleasure.

Senator Forsey: Clause 19(1) does not provide that, but for appointment "during pleasure, or in such other manner" and so on, surely.

Mr. Atkinson: My point is that the discretion contained in the clause should be removed.

Senator Grosart: In my opinion, Mr. Atkinson's point is well taken. As long as the Governor in Council has the right to appoint during pleasure, that may be done. In Mr. Atkinson's opinion the power to appoint during pleasure should not exist, regardless of any alternatives.

Senator McNamara: Mr. Chairman and Mr. Atkinson, it is my understanding, in which I may be wrong, that this is quite normal. Appointments to such marketing boards as the one with which I used to be associated were during pleasure. It used to be during good behaviour. There was always a definite weakness with regard to the setting of a period of time as the duration of an appointment. I know from my own experience that "pleasure" means pleasure and it did not in any way affect the operation of the Wheat Board.

There are two sides to the argument that it might be better for an appointee to be appointed during the pleasure of the Governor in Council rather than for a definite period of time. In the event that it was desired to remove a person from office, a definite period of appointment might prove to be too long.

Mr. Atkinson: I have presented the point for your consideration and will not debate it.

Senator Grosart: Do you know if any farm organizations with which you are familiar have strong feelings in this regard?

Mr. Atkinson: I can only speak for the organization which I represent. It does have strong feelings.

Senator Grosart: Do you see any dangers in it?

Mr. Atkinson: The opportunity is always open for excessive pressure on members to carry out the will of the Government, if you will, as an expedient measure of the time. That illustrates the reason for our position.

Senator Grosart: Have you seen any indication of that danger actually arising in connection with the many marketing boards which have been in operation in Canada?

Mr. Atkinson: Generally speaking, provincial marketing boards are producer boards, to which members are elected. In this case we are not referring to the board, but the council or the regulatory body. At times we have witnessed denial to a producer board of a decision made by it. An example is the white bean marketing board in Ontario, which in its wisdom decided to enter the marketing and storage aspects. A decision of the regulatory body prevented this.

Senator Grosart: Mr. Chairman, I wonder if we could ask the deputy minister to comment with regard to this, not as a matter of policy but as to why appointment during pleasure was included?

The Acting Chairman: Yes, Senator Grosart, he should be asked. However, in view of Mr. Atkinson's problem of time, perhaps the deputy minister would take note of this particular point, because we will deal with it. Perhaps Mr. Atkinson could complete his presentation, after which we will call on the deputy minister for point-by-point discussion.

Senator Belisle: Mr. Atkinson, is it your intention to make the same presentation to the Ontario Government when they are preparing their legislation?

Mr. Atkinson: We would have to examine the legislation. Certainly we are interested in making representation with respect to any new agencies, and have already done so in the case of those existing.

The Acting Chairman: Does your organization include representatives from the province of Ontario?

Mr. Atkinson: We operate throughout the country.

The Acting Chairman: Are appointments during pleasure made to any provincial boards?

Mr. Atkinson: I am not aware of any, but there may well be.

Senator Grosart: Did you say the majority are elected?

Mr. Atkinson: I would not make a judgment in that respect.

The Acting Chairman: Please continue, Mr. Atkinson.

Mr. Atkinson: The next item of concern is clause 24, on page 18, which has to do with market sharing. It says:

> . . . the marketing agency shall consider the principle of comparative advantage of production.

It seems to me that that is a rather discretionary clause. It is a matter of considering. But beyond that, the historical basis of judgment is based on production rather than a sharing of the market, which has been traditionally penetrated by a province outside the particular jurisdiction that this may happen in.

The question I raise concerns the historical aspect, of it being based on the market share rather than production.

Senator Forsey: You would prefer it to be based on the share of the market.

Mr. Atkinson: I would think that would be more appropriate, because production might not reflect the market share.

Senator Molgat: Do our statistics provide adequate information on market shares for all potential products?

Mr. Atkinson: I would say so; or if they do not, it is a matter of providing for those kinds of statistics. It is physically possible to do that.

Senator Forsey: Do I understand you to say that this has been done in other cases?

Mr. Atkinson: I have not said that this has been done. I am recommending that it be done in this instance.

Senator Forsey: I thought you said something about the historical way of doing it.

Mr. Atkinson: The historical pattern of marketing. I suppose you could say it was the historical way, because it was the pattern.

Senator Forsey: But not in regulation by marketing boards?

Mr. Atkinson: This is, in fact, a new concept, as a result of the bringing into being of national legislation, which impinges on the historical market practice of marketing in the country of a particular product or a group of products. Let us take, for example, one that you all know, namely, the matter of eggs, and the movement of eggs from Manitoba to eastern Canada—or in another direction.

Senator Martin: When the parliamentary committee of the other place was examining this problem, did you make representations there?

Mr. Atkinson: Yes, back in 1970.

The Acting Chairman: In the fall of 1970?

Mr. Atkinson: I am not certain.

Senator Grosart: We are dealing with a clause which is a last-minute amendment?

The Acting Chairman: Yes. This is one of the three amendments.

Senator Martin: Were you addressing yourself to your previous evidence or to the particular amendment?

Mr. Atkinson: To the particular amendment.

Senator Grosart: It does not matter whether it is to a particular amendment. He is dealing with a clause in the bill.

Senator Phillips: I intend to bring this up later, when we are doing our clause-by-clause study. I have considerable difficulty in deciding exactly what is meant by "comparative advantage of production." You, who represent a large group of farmers, can help us by giving us your interpretation of that.

Mr. Atkinson: I would say that classically an area of comparative advantage would be an area in which a product can be produced, giving a profit at least cost, given the resources at hand, between regions or even between farms.

Senator Phillips: In other words, if it is cheaper to produce hogs in Saskatchewan than in Ontario, you produce them in Saskatchewan?

Mr. Atkinson: That is the theory.

Senator Grosart: Can you give us an example of a possible major change in productive capacity between provinces? It might occur and it might make this clause very difficult to administer.

Mr. Atkinson: Again, this has to do with the principle of comparative advantage. The wording is "shall consider". It does not say "will" consider.

Senator Grosart: It says also, "shall allocate that quota on the basis".

Mr. Atkinson: Yes, but it does not say that that is the final basis for making the judgment. It says that it shall consider that as part of the basis of making the judgment.

Senator Goldenberg: Only in allocating additional quotas, not the original quota.

Mr. Atkinson: Right; but that is also an important element in the total proposition. As an example, at the moment Ontario is proposing to put a good deal of public money into the development of cow-calf operations which could well be a subsidy. As a result of that subsidy the production pattern may shift. That may be the only area in the country which introduces it, which means that it will disadvantage other areas in which cows and calves are being operated.

Senator Forsey: It appears to me that clause 24, taken in conjunction with clause 18(3) can apply only to eggs and poultry or parts of eggs and poultry.

Mr. Atkinson: At the moment.

Senator Forsey: Not at the moment, but altogether. It seems to me, if I read the legislation correctly, that the whole business of quotas can apply only to eggs or poultry or parts of eggs or poultry, unless there is a subsequent amendment to the act.

Mr. Atkinson: That is correct.

Senator Forsey: So your example of calves is not terribly relevant at the moment.

Mr. Atkinson: I will use a different example, that of poultry. I think the *Globe and Mail* had a story about the kind of buying and the kind of difficulty that the guy who does the work gets into. He owes the money to Maple Leaf Mills, which is really an integrator. You get that kind of subsidy being played with by integrators in order to get control of the market. Your point is very relevant and valid. It could have the effect of moving the production around through artificial means.

Senator Grosart: Do I take it that you are not objecting to the requirement that the quota be allocated on the basis of production, but only to the requirement that whoever makes up the marketing plan—presumably it will be approved by the council—must consider the principle of comparative advantage? You are not objecting to the first part of the clause?

Mr. Atkinson: No; but that has to be an important element, otherwise you get into the business of manipulation of the movement of production by existing growers subsidizing those who are manipulating.

Senator Argue: The result of this legislation, as we understand it, will be to bring poultry and eggs under the legislation at an early date. Since the egg marketing business in Canada is obviously in serious trouble today—and Mr. Atkinson referred to the article in the *Globe and Mail* which, in my opinion, pinpointed some of the difficulties—I am wondering whether Mr. Atkinson could give us a brief idea of the way in which he would like to see an egg marketing plant operated; how quotas should be set and, more specifically, whether or not he feels that there should be a maximum limit on quotas from individual producers. The article in the *Globe and Mail* points out that the Kaiser brothers produce 5,000 dozen eggs a day and the money is put up by Maple Leaf Mills.

Are you, as an organization, interested in having a board that takes the production or a percentage of the production of this type of company, and to what extent is the egg production business today in the hands of feed mills or packing companies, or other integrated operations? Would you want to see a ceiling, and do you want an egg marketing board for the ordinary rank and file producer solely, or will it also apply to these huge integrated producers?

Mr. Atkinson: Our position is documented in a brief which we presented yesterday to the inquiry on egg marketing in Ontario. We are recommending, in light of the situation, that quotas have a maximum level of 30,000 hens. The general feeling in that respect was a quota of around 100,000 hens. However, we took the position of 30,000 hens because that takes into account most of the individual hen or egg producers. Beyond that you get into these integrated operations.

An interesting sidelight to this is that in the income study in Ontario, "The Challenge of Abundance" which was conducted in 1968, I believe, it was recommended at that time that the quota be 5,000 to 15,000 hens, so you can see the type of disturbance there has been in the egg business since then, resulting in production increases from 5,000 to 15,000 up to an average of 30,000.

Senator Argue: Do you feel that a 15,000, 20,000, or 30,000 hen producer is as efficient an operation as a much larger producer, or more efficient?

Mr. Atkinson: You have to look at certain situations. Certainly in terms of use of management and capital, it is a more efficient operation.

Senator Argue: Which one?

Mr. Atkinson: The 30,000 hen producer or even down to 15,000. It seems to me that the larger operations are the

ones that are in real difficulty at the moment, and they are generally the ones being assisted by feed companies and other outside investors. Integrated operations are carried on either through subsidies, or the individual's capital is being transferred to the integrated company and he finally goes bankrupt.

Senator Argue: Would you say there is some sympathy for the point of view you put forward, or is the large integrated operation going to be in on it?

The article in the *Globe and Mail* states—and I feel badly that they are losing so much money—that if you had this type of system set up they would stand to gain $165,000. Now, as a member of the Government of Canada, I am not interested in doing something to rescue Maple Leaf Feed Mills, but I am interested in the ordinary producer and what the ordinary producer feels. Could the ordinary producer, if given the chance, produce at least as efficiently as the larger integrated operations?

Mr. Atkinson: The answer to that question, in my opinion, will depend on the nature of the agencies and the legislation that they function under. This very important item that I have raised is a factor in determining the net result.

Senator Molgat: Do you think this five-year time limt will work unfairly in certain commodity groups?

Mr. Atkinson: Well, I was only able to get hold of this this morning, so I really have not had much time to think it through. Inasmuch as it relates to poultry, it may well be an appropriate consideration, but if other kinds of production are brought in, it may well be that one would have to look at each one, bearing in mind the cyclical trend, and it may well be that a different type of time span may be required. I realize I am not answering your question with a straight yes or no. It is not that easy a question to answer.

Senator Goldenberg: This does not mean that there will not be a different time span; clause 24 clearly applies only to eggs and poultry. Amending legislation could provide for a different time span for cattle or any other farm product.

Mr. Atkinson: I think what you are really saying is that if other commodities are brought in under this legislation, this clause would require amendment.

Senator Goldenberg: Yes.

Senator Sparrow: It may not necessarily require amendment.

Mr. Atkinson: No, but it may.

Senator Forsey: Do you feel the five-year period is appropriate for eggs and poultry?

Mr. Atkinson: I would think the answer to that, because there has been quite a shift in the whole business of poultry and technology and development in recent years, is that it probably is an appropriate period.

Senator Sparrow: Would you suggest that the wording be amended to read "a minimum of five years", giving a discretion for a longer period should it be required?

Mr. Atkinson: I am not really certain on that. Rather than answer your question, I would just say I do not know.

Senator Grosart: Mr. Chairman, it should be stated that we should not consider these clauses at the moment on the basis of what amendments might come down if other products come under the act. These clauses relate to the whole principle of a national marketing plan that may take in any natural farm product. Therefore, I do not believe it is a valid argument to say that this now only applies to eggs and poultry. It is the fundamental concept in the bill that we should look at. Otherwise, we would have to look at every single clause and say, "Will this have to be amended if some other product comes under the Act"? The bill that is before us relates to all natural farm products, and I feel we should read the clauses, having in mind, of course, that they can be amended . . .

The Acting Chairman: I think that Senator Goldenberg and Senator Forsey—both of whom, I am sure, are experienced farmers!—follow that line of reasoning, Senator Grosart.

Mr. Atkinson: I have two more points to make. One of my points is that this legislation is inadequate in the sense that it accepts the proposition of maintaining existing marketing structures on a provincial basis. This, in my opinion, is an inadequacy, and it will prove to be one in the future. The time has come in this country to integrate provincial matters in this respect, and rather than operating autonomous provincial agencies that come under the umbrella of this legislation, I feel that the provincial agencies should be integrated into a national agency.

The Chairman: The problem is one of jurisdiction.

Mr. Atkinson: I realize it is a jurisdictional question.

Senator Goldenberg: You would have to amend the Constitution.

Senator Grosart: Is that not the whole purpose of the bill?

Senator Goldenberg: To co-ordinate, not to integrate.

Mr. Atkinson: I believe the weakness, if you will, in this is that it is an accommodation to do something, but the accommodation is not going to be effective because of these imperfections. I just want to make that point.

The Acting Chairman: It is a good point to be made, but it is a problem that besets any federal state. Is that not so, where you have these?

Mr. Atkinson: I think it could be accommodated in this way, and I recognize it requires the agreement of the various jurisdictions, to transfer power.

The Acting Chairman: I should tell you that at the last meeting there was some discussion about how far the provinces approved this proposal, and the minister undertook to canvass that situation. I understand that matter will be clarified at a later time. The problem remains that consultation is essential because of the divided jurisdiction.

Senator Martin: Apart from the constitutional problem, which is obviously a long one, I am sure Mr. Atkinson is aware of the provincial ministers' meeting, to which the minister referred.

Mr. Atkinson: Right.

Senator Martin: That provides an inevitable premise, I think, for us, does it not?

Mr. Atkinson: I think we need some real strong leadership in this respect, and I could see no more appropriate body for that leadership to come from.

The Acting Chairman: You flatter us. Senator Martin, of course, is not a farmer; he is a constitutionalist.

Senator Grosart: Mr. Atkinson, are you saying, in effect, that an established provincial marketing board, an intra-provincial marketing board, should be forced to integrate its activities, should be required by law to integrate its activities with other boards, with other areas or regions?

Mr. Atkinson: That is correct.

Senator Grosart: This is a new concept.

Mr. Atkinson: You used the word "forced".

Senator Grosart: They are required by law, by this bill.

Mr. Atkinson: I think this would help expedite the movement that is necessary.

Senator Argue: It could be required by provincial law too.

Mr. Atkinson: Yes, it could.

Senator Martin: Apart from the merits of your proposal, do you know of any provincial government, that takes that position?

Mr. Atkinson: I am not aware of any specifically. I think there is a lot of thinking in this country that feels that way.

The Acting Chairman: What about the situation in the States? It is a federal state. Is there anything comparable there?

Mr. Atkinson: No. They operate on marketing orders and things like that.

Senator Grosart: In making that remark, are you in effect expressing some concern about the possibility of balkanization?

Mr. Atkinson: I do not think it is a possibility. I think it is a probability. I think that kind of thing already exists. I do not think this bill will help that.

Senator Goldenberg: Would you not say that under this bill there would be less balkanization than there is now?

Mr. Atkinson: Well, I am from Missouri.

Senator Goldenberg: Is that not the intention?

Mr. Atkinson: Well, the road to hell is paved with good intentions. I am being serious now.

Senator Argue: But you are in favour of the bill as far as poultry and eggs are concerned. You would not like to see it defeated?

Mr. Atkinson: Let us put it this way. I would be in favour of the bill if there were some practical improvements made in it, much more in favour of the bill.

Senator Argue: You are not opposed to it now though?

Mr. Atkinson: I am opposed to it on the ground—and this is another factor involved—that there is really no effective collective bargaining mechanism between the farmers and the agencies. I know that we can get into an argument and say the agencies could be the bargaining instrument. Experience is that this is not necessarily so.

Senator Goldenberg: You know that the council, which is to recommend the setting up of these agencies, must hold public hearings; it is not done privately.

Mr. Atkinson: That is true.

Senator Goldenberg: The various parties will have an opportunity to be heard.

Mr. Atkinson: Right.

Senator Buckwold: We have heard a rather mild statement from you today, far different from what I heard on my local television station, when you heaped nothing but scorn on this bill.

The Acting Chairman: Let us say "reasoned" rather than "mild".

Senator Buckwold: All right, reasoned. What is worrying me is that here we are moving into a marketing bill, presumably a step forward in the relationship of farmers and their production, their price structures and adequately meeting the market demands; hopefully a progressive bill. You based your television comments at least, in quite a drastic statement, on the basis that (a) the farmer still has no collective position in bargaining with the agencies, and, although you did not say it, (b) the problem of integrating all the provincial bodies does not meet with your approval. What you do not say is what is the constitutional problem. With respect to collective bargaining, we have had it pointed out today that the agencies will be holding hearings. What other steps in this bill would you be proposing to try to meet the points you have raised?

Mr. Atkinson: I think the proposals I have made are the ones that would meet the points.

Senator Buckwold: The proposals you have made here so far?

Mr. Atkinson: Yes.

Senator Buckwold: Where does that help the collective bargaining position of the farmer vis-à-vis the price of his products?

Mr. Atkinson: I have not specifically outlined a section which would build into this the collective bargaining process, because obviously it will not happen. I just point this out as a weakness. The agencies that will emerge as a result of this legislation will be not unlike the ones that already exist. I think that is the point. There is the question of the inter-provincial conflicts, if you will, or the differences of interest, to start off from that proposition, because it is really what it starts with—they become conflicts of interest and then become really heated struggles—as long as producers, which is what we are now talking about, operate in that kind of structure, whether a pro-

ducer or anyone else, there is a decision-making process that takes place in terms of their needs in another jurisdiction, and the thing becomes a conflict of interest. What I am trying to point out is that in order to change that process, to get them making decisions together, that integration has to take place. It is pointed out, rightly, that we have a jurisdictional question. This then brings into focus the importance of resolving that jurisdictional question.

Senator Buckwold: I think we all recognize that.

The Acting Chairman: But you are not suggesting that integration should be forced from above?

Mr. Atkinson: I would put it this way. It would be nice to see some leadership taken.

The Acting Chairman: Leadership is different, though, from the imposition of a view.

Mr. Atkinson: Imposition is already here with many people.

The Acting Chairman: I think Senator Goldenberg just pointed out that here what was sought was co-operation, and if it had not been for some co-operation between the federal and provincial authorities we probably would not have this at all, so they are working in the direction you are pointing. Perhaps they are not going as quickly or as far as you would like, but that is the direction of the move.

Mr. Atkinson: Sometimes compromise is worse than nothing at all. That is the point.

Senator Goldenberg: Are you saying this bill is worse than the present situation? I thought you said a little while ago that it was an improvement, that there would be less balkanization.

Mr. Atkinson: No, I did not say that.

Senator Goldenberg: Well, the bill aims at less balkanization.

Mr. Atkinson: Yes. What I said was that balkanization is already taking place, and it was my view that this bill in itself would not overcome that problem. As a matter of fact, it may irritate that problem.

Senator Goldenberg: How would it irritate that problem?

Mr. Atkinson: I think some of the trade-offs that will be made between the provinces will be irritating.

Senator Molgat: Trade-offs, you mean between different products?

Mr. Atkinson: Yes, between different products produced in different areas, and between the same products produced in different areas. I think that is going to be difficult.

Senator Phillips: Mr. Atkinson, the fact that an area or a region can come under the agency, or even that, say, 7 out of 10 provinces can come under the council or agency and three remain outside, is this not going to irritate further the balkanization?

Mr. Atkinson: I am not certain. I do not know, in that respect. I am not certain.

Senator Grosart: Mr. Chairman, I think I heard Senator Buckwold say the agencies will require to hold public hearings. Is that your recollection? I do not find anything in the bill that says that this shall be so.

The Acting Chairman: Senator Buckwold said that this is an important distinction between the setting up of a board and the setting up of an agency. On the matter of collective bargaining raised by Senator Buckwold, I do not think there is any protection whatever with regard to the holding of public hearings on the setting up of an agency.

Senator Goldenberg: There is a protection for the setting up of an agency, because the council must approve the setting up of that agency, and the council must hold public hearings before it makes its recommendation.

Senator Grosart: But from then on the agency has powers, it could amend.

Senator Goldenberg: Subject to approval of the council—which holds public hearings.

Senator Grosart: But Mr. Atkinson's point is that it is not subject to approval by the members, and I think that is a very good point.

Senator Goldenberg: I have one final question. Mr. Atkinson, would you like the Senate to defeat this bill?

Mr. Atkinson: I would not like to take it on myself to make that judgment.

The Acting Chairman: Are there any further points?

Mr. Atkinson: Mr. Chairman, may I just add to that? It would be my hope that the Senate would see fit to improve the effectiveness of this bill, by taking into consideration some of the things I have said here today.

Senator Goldenberg: The most important thing you said—and I understand it very well, and I sympathize with you—is that there can not be integration; but, given the constitutional position, the decision of the Supreme Court re the National Farm Products Marketing Act, in the 1930s, that is not possible at this time. None of the provinces would agree. Therefore, I ask you whether, in the light of that, you would prefer that this legislation not be enacted, and leave the present system of balkanization, which you criticized?

Mr. Atkinson: My former answer still stands.

Senator Goldenberg: I beg your pardon?

Mr. Atkinson: I still go back to that former answer: it is a responsibility that Parliament will have to take.

Senator Grosart: Are you still beating your wife? That is the question.

Senator Argue: I wonder if Mr. Atkinson would comment on paragraph (g) on page 19 which deals with the establishment of consultative and/or advisory committees to the agencies. I am wondering if Mr. Atkinson is in favour of a change being made in this paragraph, that would require that a majority of the members of the advisory committee should be producers. According to the bill, the majority of

the members of the council must be producers; and the majority of the members of the agencies must be producers. It would seem to me to be important that a majority of the members of the advisory committee should also be producers.

Mr. Atkinson: I think that is important.

Senator Argue: You think the advisory committee is an important body, in the sense that it advises the agency?

Mr. Atkinson: Yes, and I think it is important, and I think they should be producers, because they are directly affected.

Senator Argue: Would you, as an organization, participate in the operation of this scheme, in the sense that if you were asked to suggest names of persons for an advisory committee, you would co-operate to that extent?

Mr. Atkinson: Because our people would be affected by any marketing agencies, and the effects of these activities, and so on, we would be prepared to do so.

Senator Martin: Mr. Atkinson has already got names in mind.

Mr. Atkinson: May I respond to Senator Martin in this way, that our policy is—and this would be the basis on which we would propose representation—that the representatives would be responsible to our organization and would report directly to that organization matters concerning what was going on in the advisory committee, and if the agencies in their wisdom accepted on that basis, we would make representation.

Senator Grosart: Would you suggest then, Mr. Atkinson, that in clause 26(g) there should be added "a majority of whom shall be producers"?

Mr. Atkinson: I would say so.

Senator Grosart: Mr. Atkinson, as I think you have almost finished your evidence, I might suggest to you, through the chairman—so that we can consider, as we go through the bill clause by clause, the suggestions you have made—that when you stand down, you indicate on a piece of paper the clauses and the specific amendments—not necessarily in legal terms—that you would propose, so that we could have them before us when we go through the bill clause by clause.

Mr. Atkinson: I am not a lawyer, but I would give you that information.

Senator Grosart: Could I suggest that, Mr. Chairman?

The Acting Chairman: Yes, certainly, that would be a good idea; and, Mr. Atkinson, I would ask you to do so.

Senator Molgat: In order to be crystal clear on one point, in regard to the jurisdiction question, is it the policy of the National Farmers' Union that where a national marketing board is established there be no provincial power?

Mr. Atkinson: That is our desire.

Senator Molgat: That is National Farmers' Union policy?

Mr. Atkinson: Yes.

Senator Molgat: Secondly, it is your view that the present bill will lead to more balkanization?

Mr. Atkinson: I will put it a little more delicately than that and say that our view is that it will not assist in debalkanizating the country.

Senator Molgat: Earlier, I thought that you felt it would increase balkanization.

Mr. Atkinson: I think the tendency will be there, yes.

Senator Phillips: Mr. Atkinson, you said the persons you would appoint to the advisory committee would be responsible to the National Farmers' Union. I would like clarification on two points: firstly, the time limit you would appoint them on; and, secondly, in what manner you expect them to be responsible to the National Farmers' Union.

Mr. Atkinson: In transmitting information. I would not make a judgment. It would depend on each particular situation, as to what kind of time limit there would be.

Senator Phillips: You would like freedom of movement in that respect, when they would be appointed?

Mr. Atkinson: Yes.

The Acting Chairman: Perhaps I might help on that point. You said in response to Senator Argue, in respect of clause 26(1)(g), that you would favour the establishment of a consultative or advisory committee, and that the majority of the members should be producers. There is nothing to prevent that happening at the present time, is there?

Mr. Atkinson: No. That is so.

The Acting Chairman: This can be done?

Mr. Atkinson: That is true. It is not explicitly stated.

The Acting Chairman: That is right. Is it likely in establishing an advisory committee that the candidates for membership would be more likely to be producers than otherwise?

Mr. Atkinson: Well, I would suppose so.

The Acting Chairman: Well, it seems to me that that is the inference.

Senator Phillips: Mr. Atkinson, what would be your attitude to having consumers on the advisory board?

Mr. Atkinson: I would have no real opposition to having a consumer on the advisory board as a matter of information.

The Acting Chairman: And that, too, is possible. Of course, a producer is also a consumer.

Senator Grosart: Would you also be in favour of consumer representation on the council and the agencies as well as the advisory board?

Mr. Atkinson: My answer to that would be no.

Senator Grosart: Why?

Mr. Atkinson: In the first place, I think that the agencies dealing with farm products should be responsible to that sector of the economy. You might ask me another question: Would we support the industrial representatives on the council or on the agencies? My answer to that would be no, unless they are prepared to open their boards of directors to farmers.

The Acting Chairman: Are there other questions for Mr. Atkinson? Thank you very much indeed for coming, sir. You will let me have whatever notes you have, will you? Thank you.

Honourable Senators, is it your pleasure at this time to hear from Mr. C. A. Gracey, the Manager of the Canadian Cattlemen's Association?

Hon. Senators: Agreed.

The Acting Chairman: Mr. Gracey, would you identify yoursel for the record?

Mr. Charles A. Gracey, Manager, Canadian Cattlemen's Association: My name is Charles Gracey. I am Manager of the Canadian Cattlemen's Association.

Senator Argue: Where is your head office?

Mr. Gracey: We have two offices, sir. We call either one the head office. We have one office in Calgary and one in Toronto. I am from the Toronto office.

Mr. Chairman and honourable senators, we are delighted to have the opportunity to appear before you. I am instructed by our president to do so and to point out to you at the outset that we are in your hands. Our purpose here is to clarify as clearly as we can our position with respect to Bill C-176 in order to justify to you, if we can, why we have taken the position we have and where we stand now in respect to the bill.

Like Mr. Atkinson, we also, necessarily, had short notice. Thus, I do not have a prepared brief to distribute to you. I am prepared, however, to put in your hands some documentation that we have available with respect to the bill.

Senator Goldenberg: Have you already made representations on this bill to the House of Commons?

Mr. Gracey: Yes. I was going to point out that I have in my briefcase copies of three separate briefs which we submitted to the Commons Committee on Agriculture in 1970 and 1971. I think I have sufficient copies to distribute to you.

In the interest of time I think I can be even briefer than I had originally thought by simply pointing out to you that our attitude with respect to this bill, when it first came out as Bill C-197 in the year 1969 or 1970, was that although the bill was interesting and might be useful to some commodities, it was totally alien and foreign to our philosophy, our objectives and our goals. At that time we read the bill and all its provisions very carefully and we found that the cattlemen and the people we represent in the great majority of cases, as evidenced by the fact that we are affiliated with provincial beef-producer organizations in aid of the ten provinces, supported our stand on the bill.

As you know from studying it, the bill contains within it the mechanism of coercive supply management—that is to say, regional quotas and so on and so forth, and the mechanism of establishing marketing boards and so on. And this is counter to the philosophy of the Canadian Cattlemen's Association and all of its provincial organizations.

However, we had a problem. We realized that in a free country other commodities might want this bill. Therefore, I want to say very clearly that at no time in the history of this bill have we opposed the bill. We have never opposed or sought the defeat of this bill. I want, Mr. Chairman, to go on record as saying that any claims that we have been associated with any campaigns to defeat this bill are not true. We did recognize that we had a dilemma, however. We did not like the bill or its provisions. We recognized some commodities did. We thought the cleanest way out of the bill for cattle producers would be simply to say, which we did many times to the agricultural committee, "Please exempt us. Exempt cattle, calves, beef and veal from the provisions of this act. It might be a good bill for some commodities, but it sure is not, in our view, for the cattle industry."

We thought that this was a democratic approach. We thought that, where legislation is proposed that cannot be demonstrated to be necessary to the public interest and cannot be demonstrated to be essential to a particular industry, such as the beef industry, and where the beef producers themselves do not want it, that we should have the right to be exempted from the bill. I would like to point out, Mr. Chairman, that it may not be generally recognized that the beef industry is by far the largest agricultural industry in this country. Twenty-two per cent of all agriculture is the beef industry. So we rather felt, in view of the fact that we did not like the provisions of the bill, did not agree with the philosophy, thrust and direction of the bill, that we should be exempted.

I just want to say in passing that I heard and was interested in the discussion that preceded my appearance here. I would say to Senator Goldenberg that the idea that this legislation will move in the direction of reducing balkinization is not in our view correct. We think it will legitimize balkinization.

We have to be very clear about this. Our view is that the whole legisaltion is completely irrelevant to the beef industry, because we do not accept in any way any idea of provincial boundaries for the beef industry. We are determined that all that is needed as the enabling legislation is the British North America Act. We are persuaded that beef should move freely back and forth across this country without any restrictions whatsoever. Therefore, if you appreciate this, you will understand why we say that most of the provisions of the bill—all of the provisions of the bill so far as we are concerned—are completely irrelevant. There is no thought in our minds about dividing up this country so that Manitoba can have X per cent of the beef market, whereas Ontario can have Y per cent and Quebec Z per cent. That is not in our minds at all. We believe that beef should be produced in the areas of economic advantage. This is another irrelevant issue discussed in the committee about apportioning production to the areas of economic advantage. We believe production will flow to the areas of economic advantage, if we let it.

I wanted to make those points, and I think I have made the quite clearly in trying to state the philosophy of the association.

The Acting Chairman: You also made them before the Commons agricultural committee.

Mr. Gracey: Yes, I have paraphrased the three separate briefs, sir, that we presented to the agricultural committee.

The Acting Chairman: Thank you.

Mr. Gracey: Before turning to the bill itself, I should like to make the point now that before all else the Canadian Cattlemen's Association respects the laws of the country and will live with whatever legislation finally comes into being. We will do all we can to represent our views before legislation is passed, but we will live with it afterwards. So, turning to the bill itself, I should like to make a couple of points. In the amendment to clause 2(c)—and here I am addressing myself to the amended bill—the amendment is of major importance to us because we feel that this form is infinitely better than the unamended form. We feel that this is superior to the original form because it does provide almost unmistakable assurances that a plebiscite will be held before an agency is established. We are happy about this because it is much more democratic than it was. But I want to take issue with some of the phrasing in it. Clause 2.(c)(ii) says:

> (ii) any other natural product of agriculture and any part of any such product in respect of which the Governor in Council is satisfied, as a result of declarations by provincial governments following plebiscites, or otherwise, that the majority of the producers thereof in Canada is in favour of the establishment of an agency under section with powers relating to that product;

The point I am raising is in connection with the two words "or otherwise". We are opposed to the inclusion of those two words and would seek to have them removed. To clarify my point, we have received the explanation that the term "or otherwise" is used because provincial plebiscites are only a requirement in provinces where the provincial marketing act requires one. It has also been argued that the federal Government may not require a province to hold a plebiscite, because that is a provincial matter. We quite agree. But we think the argument is wholly irrelevant. After all, Bill C-176 is, in our view, a piece of national legislation and surely it is within the sphere of authority of the federal Government to lay down a requirement that a plebiscite shall be held before the machinery of Bill C-176 is put into motion. Surely the federal Government can say to a provincial government that whether they hold a vote or not is the business of the provincial government, but that the business of the federal Government is to see that Bill C-176 is not put into motion in respect of any commodity until a plebiscite has been held.

There is a fine distinction here. We have argued it before. We believe it is fully within the authority of the federal Government to say that a plebiscite shall be held before implementing a federal act. This is not, in our view, tantamount to telling the province what it shall do, but it is in our view tantamount to saying that the federal Government will not do something until the province holds a plebiscite. It seems to be a difficult point that we have argued about before. But might I suggest a simple parallel? I might be negotiating with one of you to buy your car for a certain sum of money, and I may say, "I will buy that car for that sum of money if you put new tires on." Now I have not dictated to you that you shall put new tires on, but I have said that when you put new tires on them I will buy it. This is the same principle here. We do not like the inclusion of the words, "or otherwise". You may wish to question me on that.

Senator Grosart: On that point, Mr. Gracey, have you considered the possibility that the phrase "or otherwise" may nullify the whole possible effect of subparagraph (ii)?

Mr. Gracey: Of course, we recognize this possibility, and we would be very much incensed if this were to develop. We tend to take the word of the people in the government who said that this is their intent. But I do agree with you that this is quite possible and that they could say, "or otherwise".

Senator Grosart: The point I am making, and we may come back to this later, is that it does not seem to be clear from any point of view of English syntax whether "or otherwise" qualifies the word "plebiscite" or the declaration. The concern in my mind is that a court might, if it took the interpretation which would be the normal syntactical one because of the place of the comma, that the "or otherwise" gave the Governor in Council the right to be satisfied without a provincial declaration, and that the whole thing would be nullified.

Mr. Gracey: That is our point.

Senator Grosart: It is a very serious matter from the point of view of draftsmanship. My suggestion later will be that we take out the comma aftr "plebiscite" which would bring the intent, I think, into line with normal English syntax.

Senator Goldenberg: Mr. Gracey, have you read clause 17(2)? That says that the Governor in Council may request that each province carry out a plebiscite of the said producers.

Mr. Gracey: Yes. If I might continue my remarks and I will come to the point you are now making. We therefore urge most strongly that the words "or otherwise" be deleted from clause 2(c)(ii). Further, in respect of this same point of principle we suggest that clause 17(2) does not provide a clear enough indication to Canadian farmers that the will of the majority will be sought. We suggest, again on the basis of our former argument, that the term "may request" that each province carry out a plebiscite of the said producers should be amended to read something like "shall require that each province".

Senator Goldenberg: Why are you satisfied, Mr. Gracey, that that would be acceptable in a court of law?

Mr. Gracey: You are referring now to "shall require"?

Senator Goldenberg: Yes, that is the federal Government imposing a condition on a province in a field in which the federal Government does not have jurisdiction.

Mr. Gracey: This is exactly my point. I do not believe that those words would impose anything on the province. You are simply saying this to the province: "We have a bill, a national bill, under national legislation, and we will impose it only if you have a plebiscite." I think you have complete and utter authority to do that.

Senator Forsey: It is a "no tickee, no washee" proposition.

Mr. Gracey: That is right.

Senator Buckwold: Does that mean they do not come under the bill or that there won't be any bill?

Mr. Gracey: It would mean in my mind that there would not be any agency.

Senator Buckwold: If one small province, and let us say it is Prince Edward Island, did not want to have a plebiscite, it could in fact stop a complete marketing proposal?

Senator Phillips: May I point out that Prince Edward Island, by its provincial law, requires a plebiscite before having any marketing agency?

Senator Buckwold: I was only using this as an example.

Mr. Gracey: I think it is an interesting point that the other side of the coin is just as sharp, and that is that the way it is now could frustrate democracy and that one could have the establishment of an agency without a plebiscite. And I suggest that that is the worse of the two evils.

Senator Grosart: But surely that is not implicit in the bill. It merely says that in order for the Governor in Council to satisfy himself that a majority, an overall majority of producers want to come under an agency, he may use the plebiscite as a basis for the provincial declaration.

If a sufficient number of provinces to constitute a majority of producers made the declaration, there would not be a situation in which, for instance, Prince Edward Island could frustrate the whole marketing plan.

Senator Phillips: I do not like the idea of using Prince Edward Island as an example.

Mr. Gracey: I will say province "X". The only method by which the Governor in Council in a democracy can ever be satisfied is following a plebiscite.

The Acting Chairman: Well, now, is that right? I suppose that would be true of almost everything, but a plebiscite is not necessarily the be-all and end-all. The democratic process does not require a counting of heads to that extent. There is such a thing as majority government, which is the basis of the democratic process. If he wished to be sure in the case of each individual producer, that would be another matter.

Senator Grosart: Or if he wished to be sure that there was a majority.

Mr. Gracey: In our view the only method is by plebiscite of producers.

Senator Goldenberg: How is this done in provinces which do not now have a plebiscite?

Mr. Gracey: I do have some information with regard to that. I must say before giving it, however, that I do not have supporting material with me. Marketing agencies now exist in some provinces which have never had a vote. This is what sticks in our craw. We do not like this type of thing.

Senator Martin: Mr. Gracey, I believe your president issued a statement?

Mr. Gracey: Yes, he did.

Senator Martin: It was not very long; have you a copy?

Mr. Gracey: Yes, I have.

Senator Martin: Would you read it into the record please?

Mr. Gracey: Yes, I will, sir. I described the essence of the statement earlier, but I will read it. It is a press release of January 4, 1972, entitled "Cattlemen President Fox Approves Amended Farm Marketing Bill". It reads as follows:

> The controversial farm marketing bill, known as Bill C-176, is now "—in a form acceptable to Canadian beef producers". According to Jonathan Fox, of Lloydminster, Saskatchewan, the current president of the Canadian Cattlemen's Association.
>
> For the past two years the Canadian Cattlemen's Association has vigorously opposed the principles of coercive supply management and legislative production and marketing controls in the draft bill. While not opposing passage of the bill itself cattlemen requested the specific exemption of cattle, calves, beef and veal from the bill.
>
> Although the Government did not grant specific exemption for the beef industry the passage of two important amendments during the closing hours of debate really accomplishes the same purpose", said Fox.
>
> An amendment to clause two

—which we have been discussing—

> —provides that an agency may only be established for any farm product, except poultry and poultry products, after a series of plebiscites in each province across Canada indicates that a majority of producers approves the establishment of an agency.

May I just interrupt, to say—

Senator Martin: Please finish the statement, for the record.

Mr. Gracey:

> An important amendment to clause 18 also provides that a proclamation establishing an agency for any commodity, except poultry and poultry products, shall not grant an agency any power to introduce supply management. In order to establish supply management for the beef industry the bill would have to be amended and this would mean referral back to the agricultural industry and full debate in the House of Commons.

"We can live with this bill" commented Mr. Fox. While we would still prefer exemption for our products we have taken the motor out of this bill and it can only become operative again as a result of a majority vote of beef producers. "Thus beef producers have retained control of the direction of their industry in their own hands", continued Mr. Fox.

In commenting on this significant victory for cattlemen Mr. Fox expressed satisfaction that the Government and the House of Commons had agreed to amendments to the bill in accordance with the wishes of cattlemen and a great number of producers of other commodities. Mr. Fox noted particularly the tremendous efforts of a number of opposition members led by Jack Horner to make the bill more acceptable. "Without the strong and sustained efforts of Jack Horner and several other members the bill would have passed many months ago in its original form", said Mr. Fox. "In fighting for important amendments Mr. Horner has rendered Canadian agriculture an important service."

Senator Grosart: Mr. Gracey, you have asked for exemption from this bill. Is it not true that clause 18(3) exempts you completely?

Mr. Gracey: It exempts us from the supply marketing features of the bill.

Senator Grosart: Yes, you are quite correct; it exempts you completely from the supply management features of the bill.

Mr. Gracey: Yes.

Senator Grosart: It may come later in an amendment, but you now have the exemption which you requested.

Mr. Gracey: Yes, however the point to which I refer in no way differs from the press release which Senator Martin asked me to read. We take issue with one or two other aspects of the bill, which we do not consider to be quite proper. I have indicated throughout that we will live with whatever law is passed.

Senator Martin: Your president went further than that, which was the point of placing the release on the record.

Senator Forsey: Mr. Gracey, I have derived the impression from what I have heard that there are groups of beef producers in Ontario who do not take the same view as that of your organization. Am I correct in that impression?

Mr. Gracey: You certainly are, sir. The Canadian Cattlemen's Association is represented by organizations in every province. I doubt whether we will ever be in so healthy a state that we can say we represent the views of every beef producer. I can, however, say that we represent the views of the overwhelming majority.

Senator Forsey: Including those in Ontario?

Mr. Gracey: Definitely. There were allegations during the debate leading up to this that this is an east-west fight. It is ironic however, that at a recent meeting of the Ontario Beef Improvement Association Board of Directors, I was given instructions to do everything possible to make sure that cattle was deleted from the bill. Of course, I could not carry out their instructions fully, because our board is prepared to accept the amendments which were presented.

Senator Grosart: What percentage of beef production does your association represent?

Mr. Gracey: The answer to that question involves discussion of the structure of the organization.

Senator Grosart: What is the approximate percentage?

Mr. Gracey: We strive for 100 per cent representation.

Senator Grosart: What percentage does your actual membership represent?

Mr. Gracey: The membership is at the provincial level. In the Province of Ontario a member of the Canadian Cattlemen's Association is so basically because he is a member of the Carleton County Beef Improvement Association, which is a member of the Ontario organization with which we are affiliated.

Senator Grosart: What percentage of beef producers are not members of the Canadian Cattlemen's Association? Please include all beef production.

Mr. Gracey: I have attempted to explain our structure. I could say 100 per cent are members. That is our goal. Every beef producer in this nation, and that includes the dairyman, has the absolute and unqualified right to attend at the local beef association, state his views, vote on issues and so on.

Senator Grosart: Do they pay membership fees?

Mr. Gracey: The county associations in Ontario have a membership fee of $1. This varies between provinces.

Senator Grosart: But you must have in your mind an overall figure as to the percentage of beef production for which you, as an official of the association, are entitled to speak.

Mr. Gracey: I will give you a figure, which I will qualify by saying that we strive to represent 100 per cent of beef production. We are convinced that our views are supported by at least 75 per cent of beef producers in this country.

Senator Grosart: Is 75 per cent of beef production represented by your association, through affiliation, or otherwise?

Mr. Gracey: Yes. I would have to show you our constitution to explain the structure. It will illustrate how a beef producer in the Province of Saskatchewan, for instance, puts forward his views. That is the essence of it.

Senator Martin: I want to clearly understand that the president of the association supports the bill, and you yourself also support the bill.

Mr. Gracey: Yes, but I would turn the emphasis around. I would say that we will live with the bill. We find fault with a couple of things in it. That is why I am here.

Senator Grosart: In your objections, I take it that you are looking to the future rather than to the effect of the bill when it receives royal assent.

Mr. Gracey: We are quite happy with the fact that there is a plebiscite proposed.

Senator Grosart: That plebiscite is in the future. It does not concern you at the moment.

Mr. Gracey: We want the plebiscite to be properly structured when it comes.

Senator Grosart: that is right. You are thinking of the future, when an amendment to the bill may be made which might bring you within the terms of the bill.

Mr. Gracey: The other reason why I was sent here was to represent our strongest view, that any changes proposed in the bill not move further in the direction away from where we want to go. We would propose a withdrawal of the amendments which we have recently submitted.

Senator Forsey: Senator Grosart suggested that the changes Mr. Gracey has been suggesting referred only to something that might arise if there were an amending bill. That is not altogether correct. You would like to see this because, except for supply management, you could be brought under this legislation now. That is why you want to get the "or otherwise" struck out.

Mr. Gracey: Yes. It was suggested that some day we might have a vote to establish an agency even without supply management. We want to be sure, if such an event comes about, that it will be a proper vote.

Senator Forsey: It is not a question only of amending legislation. It is a question of what might arise under the legislation as it now stands.

Senator Grosart: Are you concerned with any other control aspects of an agency under the bill, other than supply management?

Mr. Gracey: I am not sure that I understand the question.

Senator Grosart: As Senator Forsey pointed out, you could come under this bill by provincial declaration and a proclamation by the council. Under 18(3), this would not bring you under supply management, but you could come under the bill. Are there any other control features, that would be set up as a result of the establishment of an agency, which you would object to, other than the supply management aspect?

Mr. Gracey: Once supply management is removed, about all one can do is establish an agency for promotion, research, and so on. The bill is completely irrelevant in this respect, because we already have a national organization, we already have a provincial organization, we are already working on product development, and we are already co-operating with the federal Department of Agriculture to change the grade standards.

Senator Grosart: There is no other control that you would object to.

Senator Sparrow: The bill does not define a producer. Can you define a beef producer, and how does your association define a beef producer?

Mr. Gracey: Obviously, that is a central question any time a vote is about to take place. I have personal views on it. The question has not been deeply discussed within the Canadian Cattlemen's Association. I think I can go so far as to say that the Canadian Cattlemen's Association would take the position that a beef producer is anyone who produces beef and derives a significant proportion of his income from a beef operation. There is a very real question as to whether or not a producer who markets 500 cattle should have one vote in the same sense as a producer who markets three cattle. That is a real question which has to be faced, on which we have not taken a position.

Senator Sparrow: Do you read into the bill that each province must define who a producer is in that province? There is no standard definition of "producer".

Mr. Gracey: There is not. It is a question that has to be honestly faced.

Senator Sparrow: With regard to beef producers, the bill refers to a majority of producers in Canada. Would you read into the bill that a region or area in Canada which might very well have a majority of producers, would not, in fact, represent the total production of the industry? I would like to quote some figures with which you might agree or disagree. In the four western provinces, there were, as of June 1, 1971, 4,804,000 head of beef cattle. You might want to record this figure. There were 35,703 producers. These figures are taken from the Dominion Bureau of Statistics. The cattle population in Ontario and Quebec was only 1,528,000, or 20 per cent or less than western production. However, they had 79,143 producers. They had double the producers and 20 per cent of the production. In the bill itself it would appear that they could come under the marketing legislation by a vote of Ontario and Quebec producers. Are my figures correct?

Mr. Gracey: Essentially, yes. I think that is a very good point. If you phrase the question as to how we would react on this, as I said before, the question is a very difficult one. The Canadian Cattlemen's Association has not expressed a view on this, but I have no hesitation in expressing my own view, which is that we have to give consideration to some kind of a balance between producers and production.

Senator Sparrow: Would you suggest that there is an area of change in the bill which would protect a region in Canada? Have you given that any consideration?

Mr. Gracey: As far as a region of Canada is concerned, that aspect is irrelevant. We do not care where the beef producer is. It does not matter whether all of the beef producers are in the Province of Prince Edward Island. This is one country, so that part is irrelevant.

I have already answered the first part, have I not?

Senator Molgat: Mr. Gracey, when we were discussing a vote by provinces, the objection was raised that if one

province refused to conduct a vote, that province could prevent a board. You reject the regional concept, do you?

Mr. Gracey: Yes.

Senator Molgat: Would you then consider a national vote?

Mr. Gracey: Would we, as an association, consider a national vote?

Senator Molgat: Yes, leaving aside any regional or provincial concept.

Mr. Gracey: I will answer that with the opening qualification that we do not support the idea of marketing boards and agencies to begin with, but if it appears that a significant number of producers want an agency, then we are on the side of democracy and if a vote is held we would definitely like to see a nationally conducted vote. If some provinces were being troublesome by not providing a plebiscite, then I feel there should be some means whereby a national vote could be conducted.

Senator Phillips: Mr. Gracey, I have two questions. You stated that the bill might be all right for certain products, but it was your view that beef should be free to move anywhere in Canada. Can you tell me the difference between hamburger moving freely anywhere in Canada and fried chicken moving freely anywhere in Canada? I cannot make that distinction.

Mr. Gracey: Nor can I. I see no reason why hamburger or fried chicken should be restricted in moving anywhere in Canada at all.

Senator Phillips: My second question is: Are you concerned that the bill does not provide any import quotas? I am assuming that beef production comes under the act.

Mr. Gracey: Yes and no. I want to explain that; it is important. I happen to be one who agrees that probably it would not be appropriate to have import controls vested in this bill. Perhaps this is not popular with the majority of beef producers, but I feel we need some import controls in some form under some legislation. The Canadian Cattlemen's Association has advocated a level of import controls. We have never supported imports completely, but we feel there must be a level of import controls.

The question you have asked identifies one of the main weaknesses in this bill. I believe it is the general philosophy that we are going to create an island of ourselves, to protect ourselves to an unlimited degree against imports. This is an impossible dream. We have to compete in the North American economy, and this is just another reason why we have absolutely no use for the principle of coercive supply management. I agree we must have some workable means of a sensible level of import controls in certain instances. For example, the oceanic beef imports can hurt us; they have hurt us. We have to have control at some level. We have never asked that imports be shut out completely, as is the case with respect to some dairy products.

Senator Grosart: Mr. Gracey, there seems to be a contradiction in what you just said. You object to Canada becoming an agricultural island in North America, but there is nothing in the bill to suggest that happening.

The question Senator Phillips asked, in effect, was: Would you like to see import controls written into the powers of the National Farm Products Marketing Council or a marketing agency?

Mr. Gracey: Let me answer that question again more clearly by saying that if this bill is going to work in the manner intended, it would have to have import controls.

Senator Phillips: That is specifically the point I wanted you to make.

Senator Grosart: On the question of a plebiscite or vote, the minister stated, and this appears at page L-3 in the "blues" of our last hearing:

> Mr. Chairman, I am advised that all the provincial legislation calls for one man/one vote. What they do from there on is to set out what qualifications are necessary for a man to vote. Once he has that qualification to vote, there is no further distinguishing between the weight of that vote. It is one man one vote. In some provinces, the requirement is that they sell $500 worth of the commodity in an area.

Would this indicate to you that it is at least the intent of the minister that any plebiscite should be on the basis of one man/one vote?

Mr. Gracey: I cannot say what the intent of the minister was. Again, I would say this is a tremendously difficult area. The only thing that I would be opposed to would be an arbitrary solution. In my opinion, the solution that says a man must sell $500 or $600 worth of a commodity is an arbitrary solution; the solution that a man must have a thousand hands is an arbitrary one. I think someone has to face the real question of principle as to whether it should be one man/one vote or one cow/one vote.

Some Hon. Senators: Never.

Senator Sparrow: One egg/one vote.

Senator Grosart: You might get a more intelligent vote.

Mr. Gracey: I heard some honourable senators say "Never," but it is my understanding that at a shareholders' meeting the shares owned vote.

Senator Goldenberg: If a man holds a thousand shares he has a thousand votes, and a man who owns one share has one vote.

The Acting Chairman: Are there any other questions for Mr. Gracey?

Thank you very much, Mr. Gracey.

It is now ten minutes to one. There is a possibility that Mr. Hudson will be here by 2.30. Would you prefer to adjourn at this stage for lunch, or do you wish the deputy minister to go over the points that have been covered? Policy matters, of course, would be reserved for the minister when he returns.

Senator Grosart: I wonder if I could make a suggestion, Mr. Chairman? Perhaps it would be better if the deputy minister gave his reply when we start to discuss the bill clause by clause. Most of the matters that have been raised refer to specific clauses.

The Acting Chairman: That might be a feasible way to deal with it. I see no objection to that.

Senator Martin: There have been some matters raised this morning on which we ought to have some reply.

The Acting Chairman: Well, let us deal with that as we come to the bridge.

Hopefully, then, we will have Mr. Hudson at 2.30.

Senator Molgat: Mr. Chairman, I understand there will also be a representative from the Consumers Association of Canada.

The Acting Chairman: They have been notified, but the Committees Branch has not heard from them.

Senator Molgat: I take it that if they appear this afternoon, or if others appear, they will be given an opportunity to speak.

The Acting Chairman: That is in the hands of the committee, and the usual practice is to give them an opportunity.

We will adjourn until 2.30.

The committee adjourned until 2.30 p.m.

Upon resuming at 2.30 p.m.

The Acting Chairman: Honourable senators, I reported to you this morning that Mr. Hudson wanted to make representations. I have also been informed that Mr. David Kirk, the Executive Secretary of the Canadian Federation of Agriculture, is here and would like to be heard. Is it the wish of the committee that both these gentlemen be heard?

Hon. Senators: Agreed.

The Acting Chairman: Perhaps we should hear Mr. Hudson first, because he said this morning that he would like to be heard at about 2.30 p.m.

Mr. Hudson, for the benefit of the committee, would you give us your full name and address?

Mr. J. Hudson: Mr. Joe Hudson of Lyn, Ontario.

Senator Martin: What organization does Mr. Hudson represent?

Mr. Hudson: Really just a fairly extensive group of farmers in Ontario, I guess, who have views and opinions on this. Nobody formally, sir.

Senator Martin: You do not represent an organization?

Mr. Hudson: No, no organization, that is right.

Senator Phillips: That is not absolutely necessary.

Senator Martin: No, but it is possible for me to put a question.

The Acting Chairman: Are you a producer?

Mr. Hudson: Yes, I am an egg producer.

The Acting Chairman: Where is Lyn, Ontario?

Mr. Hudson: I knew I would be asked that. It is near Brockville. You know where Brockville is. We are about four miles from Brockville.

Senator Goldenberg: Is the *Globe and Mail* correct when it describes your farm as the largest egg-producing farm in the Province of Ontario?

Mr. Hudson: Well, that is correct. I will explain that to you in a minute or two.

First I would like to say how pleased I am to be here. I certainly did not expect the privilege of appearing. I will tell you who I am and describe our operation fully before any of my compatriots who follow might do so.

I am a farmer. I guess you would still call us farmers. At least we do for municipal tax purposes anyway. We farm at Lyn, Ontario, my brother, my father and myself, and we operate an egge farm of approximately 270,000 hens. There are three of us involved. We have farmed all our lives. We started with milk way back and converted to beef cattle, broilers, got out of that and moved into eggs back in the early 'fifties, and have developed this. We also run a grading station, where we began grading our own product in about 1957, shipping it mainly into Montreal, to Steinbergs Limited. We are fairly successful at it with our own product. In 1960 we started to buy from other people and developed it into a fairly good operation, and now supply eggs into Ottawa and the Montreal areas. That is our background.

The only formal thing I can say is that I am an elected director of the Ontario Egg Board, one of the two directors who dissent with this quota business, controls and so on. However, I think I can safely say I represent the views of a good many farmers in the Province of Ontario who do not go along with the thinking that supply management, as they have it laid out today, and controls and the control of our agriculture is the only way to go. We proved that to Minister Stewart back in 1969 when they held the G.F.O. vote. It was defeated about 57 per cent to 43 per cent, and we have not had a really major vote since of any kind, to my knowledge. Certainly we have not had an egg vote yet, and he has had no further vote to my knowledge.

Senator Grosart: What is G.F.O.?

Mr. Hudson: That is supposed to be a General Farm Organization. Many of us have called the system before us the national G.F.O., but it was a General Farm Organization. Perhaps Mr. Kirk could explain it much better than I can. It was a General Farm Organization that checked off on all farm products. It had a compulsory membership for all farmers in the Ontario General Farm Organization. Many of us look on it as simply a way of getting democratic control of our affairs.

I have no formal presentation, but I am giving these items point by point and if senators have questions, they might throw them in as I go along, as otherwise I would probably forget what I have said.

First of all, you may wonder why I am here. I personally have had contact with many of my friends on this matter, not just in the case of eggs. I am very concerned with the way in which the bill was passed, in the last week or ten days, and with the effect it is going to have on the true farmer, and the general happenings.

Certainly, Parliament has debated this bill. I left my coat in Mr. Pringle's office. I hope I do not spoil his reputation as a parliamentarian.

Senator Phillips: But you may spoil your credibility as a witness, by leaving it there!

Mr. Hudson: Parliament has debated this bill off and on for about eighteen months or two years. They held hearings, but many of us feel that, even though the hearings were held, they did not hear.

Senator Martin: Were you at the hearings?

Mr. Hudson: Yes, we appeared before the hearings two or three times.

The Acting Chairman: That is, the hearings of the Agriculture Committee?

Mr. Hudson: Yes, the hearings of the Agricultural Committee in Ottawa, in Toronto and so on.

The Acting Chairman: When you say "we"?

Mr. Hudson: I appeared in Ottawa with another man. Three or four of us made appearances in Toronto also, representing a different point of view. I do not know whether the Farmers' Union has been in or not—

The Acting Chairman: They were here this morning, so you need not repeat their evidence.

Mr. Hudson: I do not know if they got what they wanted, but they stated quite openly on television that they did not get what they wanted.

Senator Martin: May I ask you a question? I have before me a statement of Mr. Atkinson of September 29, 1970. I want to know if you agree with this. He said, at page 4915:

> Bill C-197 should be further amended to provide a mechanism allowing annual production price reviews. Since the primary producer is accorded no policy role in the operations or marketing functions of the proposed marketing agencies, the only meaningful way in which farmer interests can be protected is through the assumption of a price and policy negotiation role, we should call it a bargaining role between the National Farmers' Union and the respective marketing agencies. We recommend that this provision be provided for in the bill.

You would not agree with that statement?

Mr. Hudson: I would not agree with it you say?

Senator Martin: I am asking you by way of question.

Mr. Hudson: Oh, this is what he would like. I am not so sure that that would be much better for the farmer than what he is being offered today.

Senator Martin: You do not think that his union should be the sole marketing union.

Mr. Hudson: The sole negotiating agency?

Senator Martin: Yes, the sole negotiating agency?

Mr. Hudson: I would have to debate that with Mr. Atkinson. I do not agree with everything put forward. I am not a member.

Senator Martin: I was just putting it to you now.

Mr. Hudson: I am not a member, and I am not prepared to comment on what he was saying. However, there were many things. For instance, beef and pork. Beef, in particular, wanted out. I think that was quite apparent at every hearing, and they did not really get out. Import controls were deemed necessary by almost all of our poultry groups, if this bill is to work in poultry, and we have no control over imports, under this bill.

A good many of us suggested that it would be democratic to have plebiscites on all products, and not just on some. We heard in Toronto that the consumers felt they should participate in the commission. Whether they should or not, is up to them to plead. There are many things that we feel that, even though there were hearings, were not heard.

Last spring the bill went again before parliament and a massive protest was launched. Mr. Olson accused some of the people participating in the program, of some possibly devious tactics. I would say they were, maybe, more like desperate tactics.

However, in a week's time we had some of the largest write-ins ever to Parliament, protesting the bill. I think I am right in saying that, not the bulk, but a good many of the farmers across Canada felt the issue was dead after that. It lay dormant until it came up as a Christmas package. It was rushed in at the Christmas recess; the M.P.s were literally dragged back at that time, when they did not want to be. We had compromises made. A good many amendments, of which only one or two, or two or three, were put through, I think, out of all the amendments. Probably, if you read and took to heart the *Globe and Mail* editorial last Monday—which I think probably most of you did—we would not have to say any more. I do not know whether the Chair can do this, but if you are making a transcript I think that it should be put in the transcript. I would hate to lose this copy, as I have only got one. I will not take time to read it now.

Senator Forsey: That was an editorial, not an article?

Mr. Hudson: That was an editorial. You could even put the picture in, because it is pretty good, where the turkey says to the farmer: "And, furthermore, where is your licence?" The lead editorial is the one I am talking about now.

Senator Forsey: That is the one that assumes that quotas would apply to all products, is it not?

Mr. Hudson: It assumes that quotas will apply, yes.

Senator Forsey: Which they do not.

Mr. Hudson: No, but they do apply to poultry products.

Mr. Forsey: Yes.

Mr. Hudson: That is what I am concerned about, mostly. The cattlemen would have to fight for themselves.

The Acting Chairman: They were here this morning.

Mr. Hudson: I figured that Mr. Gracey was here for something.

We feel that this was no way to pass this. I think you realize that this is the major piece of farm legislation that

will probably ever come before us in any of our time. No matter how young or how old you are, I do not think there ever will be a piece of farm legislation as major as this. We do not think this was the way to pass it. There was no possible time for farmer opposition to build, in the three days. Another thing that we feel was very bad is that, right from the hearings on, on this bill, we had hard party lines drawn and it ended up really not whether it was good or bad for Canada but simply that the bill was, we feel, pushed through and pushed through very drastically.

Senator Goldenberg: Mr. Hudson, are you suggesting that the house was rather taken by surprise and had only three days to consider this proposal?

Mr. Hudson: No, they had debated it a good deal before, there is no doubt, but it was brought back in—I do not know on which day it was—before the house, just before the house rose. I am not so familiar with Parliament, but I know that the major debate took place over three days.

Senator Goldenberg: I understand that the legislation was originally introduced in late 1969.

Mr. Hudson: Yes, I have mentioned before that it was introduced about two years ago, and there were hearings on it from one side of the country to another. But my feeling is that, when it reached the final stage, it was not thoroughly debated and the final amendments were not debated, and so on.

Senator Phillips: Mr. Chairman, in all fairness, following Mr. Goldenberg's remarks, you will recall that just before certain by-elections the bill was withdrawn. I think most of the parliamentarians assumed that a different bill would be introduced. I think this is a point that Senator Goldenberg has conveniently overlooked.

Mr. Hudson: I do not know about the parliamentarians, but I do know that a good many of the farmers assumed that a different type of bill would be brought forward.

Senator Goldenberg: My understanding is that that bill was not withdrawn. There was one piece of agricultural legislation that was withdrawn, but it was not this one.

Senator Forsey: It could not be withdrawn, unless the consent of the house was given to its withdrawal. The other side decided not to proceed with it, but it certainly was not withdrawn.

The Acting Chairman: These proceedings in the other place certainly should not unduly disturb us.

Mr. Hudson: They had it for fourteen months, without withdrawal.

Senator McElman: As a matter of record, the first reading in the other place was on October 26, 1970.

Mr. Hudson: Regardless of this, a tremendous number of farmers are dissatisfied with this bill. As I have said, the beef and a good deal of the pork wanted out. I do not know what Mr. Atkinson said. I am sure he spoke quite capably for himself. You have the dairy and the grains pretty well covered as it is. So, in effect, when you narrow it down, who really wants the bill?

Senator Goldenberg: Would you tell us, Mr. Hudson, why we understand that all the provincial governments want or are in favour of this measure? Are they so far removed from the electors that they all want to push this bill?

Mr. Hudson: I can only speak for one—and some of us think that he is.

Senator Langlois: Which one is this?

An Hon. Senator: Are you speaking for him?

Senator Goldenberg: You are speaking of the Minister of Agriculture in Ontario?

Mr. Hudson: We feel that about Mr. Stewart. The last vote he had was in 1969 and that vote was lost by 57 to 43. Many of us fought that campaign on quotas and supply management, because that is where we felt the General Farm Organization was going to lead, and it was soundly defeated. That is just two years ago.

Senator Martin: Much later than that, only last month, the Minister of Agriculture in Ontario along with other ministers of agriculture in the provinces said that they are in favour of this measure.

Mr. Hudson: Of course, you have to remember that it has been the policy of the agricultural department in Ontario for many years, rightly or wrongly. The quota marketing system has been promoted by the province of Ontario. Ontario had one of the first broiler boards, one of the first tobacco boards and so on. Rightly or wrongly they feel that this is good for the farmers.

Senator Martin: That is just your opinion.

Mr. Hudson: That is right, and I am talking only about the agricultural department.

Senator Sparrow: But the last vote that was actually held was not in favour of the marketing legislation.

Mr. Hudson: To the best of my knowledge no major farm product has been voted on since 1969. In 1968 we held an egg vote which was defeated. In 1969 we had a general farm organization vote which was also defeated.

Now, there seems to be a great urgency about this bill, that all kinds of terrible things are going to happen if it is not passed. Well, we know what the beef situation is. They have never had it so good. Pork is making a remarkable recovery. It is certainly getting better. A few years ago the Government actively promoted the idea that people should be in pork. I cannot put a year on that, but it was a few years ago. After that time there were considerable problems in the pork industry, but they are now coming back to the point where pork is a profitable item.

The chicken-and-egg war which apparently needs solving has already been solved. It was solved by the British North America Act at the end of June. Since then in Ontario and Quebec, and I can only speak for those provinces because they are the ones I am familiar with, there has been absolutely no interference with the movement of the product across the border either way. Mr. Stewart withdrew his controversial permits under Bill 10. Many of us called them illegal, not just controversial. Many of us

have seen fit to co-operate sufficiently with FEDCO that the system down there is working at this time to nobody's disadvantage.

So there does not seem to be any real problem in the chicken and egg industry. The egg industry is recovering from a period of extremely low prices which it brought about itself. The broiler industry is fairly healthy right now. The turkey industry is claiming that it is on the road to recovery via negotiations being made between Ontario and Quebec, the two major turkey producers.

So I would say that at the moment in eggs, for instance, regardless of what is done for the next six months or maybe more, we are going to be governed as we are today directly by the American product which sets our price. We have had to lower our prices on the loose markets, on the surplus markets, as much as eight and nine cents in the last week in order to stop American eggs from coming across the border, because they are available in large quantities at very low prices.

Those of us who are egg producers also feel, in spite of the fact that there are boards in these other products, that eggs will probably make the best recovery because there are not that many artificial conditions in the major egg-producing provinces. For example, in Ontario we have had, as some of the fellows have said, a real blood-letting. It has backed the feed companies off. I will explain in a minute where we feel the responsibilities were.

As some of you probably know, we are holding an inquiry into eggs in Ontario right now. I do not have the terms of reference here, but I am familiar with them, and the purpose of the inquiry is to look into the problems of the egg industry, to see whether quotas would be a necessity or would be of value at all, to look at the national plan in terms of what our participation in it would lead to, to look at the problems that have been had with Quebec, and to look at almost anything else that Judge Ross might bring out during the inquiry.

Senator Grosart: You say "we". Whom do you mean?

Mr. Hudson: I mean the egg industry. I will have to give you a bit of history on this. The egg industry was going to hold a vote last summer, and in respect of that there was a tremendous number of registrations. There was a large number of registrations of small producers. It became pretty apparent that that vote was going to be lost, that the smaller producers would not vote for it.

At that point in time the Government decided it wanted to review the whole subject, because there were all kinds of accusations of illegal registrations and that sort of thing. This happened in about July and the Government did not want too much fuss during that period so they put a judge on to it and put the inquiry into effect. We are now holding the inquiry.

Senator Grosart: What is the status of that inquiry? Under what act has Judge Ross been appointed?

Mr. Hudson: I have no idea. It is a judicial inquiry.

The Acting Chairman: It was probably under the Inquiries Act.

Senator Phillips: By way of a supplementary to Senator Grosart's question, was Judge Ross appointed by the provincial government?

Mr. Hudson: By the provincial government, yes.

Senator Phillips: I find that rather strange, in view of the fact that at our last committee meeting the minister told us that in the matter of urgency it was the desire of the Government of Ontario to have new legislation.

Mr. Hudson: Well, he does not even know yet whether Judge Ross is going to tell him whether we need the legislation or not.

Senator Grosart: That is the point.

Mr. Hudson: Maybe Judge Ross will say that this legislation will not work. He is getting some very enlightening information. I will give you a little bit of that information as I go along. If I gave it all to you we would be here for three days. It is becoming increasingly clear from these hearings, and I have been at most of them, that the problem has been caused by the producers themselves in the last three years. You must go back to 1968 and 1969 at which time we were in very high egg prices. A man could double his money very quickly. Two factors were involved: the producers were looking to make more money by raising more eggs and the feed companies were moving in.

There was an interesting article in the *Globe and Mail* yesterday. I might say the *Globe and Mail* seems to be promoting eggs these days. That article showed the degree of control the feed companies have in the egg business today, whether they like it or not, by the fact that the business has been over-promoted by the companies. It takes two people to make a deal. We cannot blame them. As one woman said in Ottawa the other day, "It takes the greedy feed company to put out the money and the greedy producer to take it." It takes two to close this deal.

It has been shown quite conclusively that many of these producers are non-farmers—men with a few acres of ground and a chicken house on it that they got by taking on a feed company mortgage. We are trying to find out how many are in that situation.

The proponents of the plan in Ontario, who also favour our national plan, are being shown to be a part of the problem. They themselves increased—or some of them—anywhere from 50 per cent to 500 per cent in the period in question. They are now saying that something is wrong with our industry and that we need to put quotas on and lock it up.

Rightly or wrongly, we feel that these quotas are not a lock-in of the farmer but are a lock-out of the farmer. That may sound ironic, coming from a producer as big as I am, but, as I told Senator Goldenberg on the telephone the other day, I am probably not the right man to come here and plead the case of the farmers. At this point I am probably the best the fellows have, which just shows what they lack.

However, in Ontario these low prices, as I have said, have solved the problem very quickly and decisively so that right now the feed people are starting to back off very

severely. I would suggest that you read that article in yesterday's *Globe and Mail*. You will see what I mean. I assure you that Maple Leaf mills who were one of the biggest promoters, who happen to be the people with whom we work for our feed, are no longer promoters of the egg business. They are demoters of the egg business. They are trying to get this business backed up to where it will make money. In many cases these people, who were very active, no longer want to be active.

If you want to define "farmer", and this is supposed to be farm legislation that we are getting, for our purposes a farmer is a man who has acres of ground and who farms that ground. We have had it shown to us that in many cases the farmer feeds his feed to his own livestock, especially in the east. What we are saying is that once you put these quotas on, especially on eggs, the bulk of the industry is already locked up financially with people such as the feed companies. These feed companies own mortgages and so on on the property and once you have locked this up there is no access for the farmer to get into this market. Besides this, it is coming up quite clearly at our hearings, and I have brought with me three or four samples which I can leave if you want to put them in the record, where farmer-feeders—that is a man who has his own farm, makes his own feed and feeds it—some of them have not lost money, and some of them claim they have made a little money, or if they have lost it has been very little. Whereas the people who are non-farmers or who are financed heavily by the feed companies are showing anywhere from $1.50 to $3 loss per bird in that 18-month period of bad pricing. The thing I think you have to remember is that in poultry, eggs and turkeys, poultry equals mill feed which equals feed company interest, and when you get a quota put on, if the feed people can get their hands on it, by contract, by financing or by direct ownership, they then own the right to feed the feed, and the feeder, the man who grows the feed, has no place to go. If he does not want to take the feed company's price, he now has to take that feed and sell it to them at the going rate, whatever it is.

It does not take very long to show that this legislation, especially in poultry—in milk it does not apply because what feed company wants to get their hands on a milk quota? They would not milk the cows morning and night even if they did have one. But this does not apply in poultry and what we say is that this quota in poultry—and this is what you will get nationally—protects only a favoured few and a good many of these people are non-farmers. It is being shown, as I said, that many of these people, particularly in Ontario, who expanded in these last three years are opting for this. We had a good example this morning of what it has done in turkeys in Ontario. I am reading now from a submission by Mr. Jack Walkie who is a turkey grower and I think he is a member of the Turkey Board, and this is what he put in the transcript this morning in Toronto in front of the judge at Judge Ross' inquiry. Remember this is farmer legislation that he is working under and that our provincial government is working under. He has this to say:

> In looking, at the quotas for heavy turkeys, the total quotas for Ontario approximate 98,000,000 pounds. However, of this total quantity, we have the following companies with quotas—Maple Leaf Mills-6,500,000 lbs. Ernie Hadler-6,000,000 lbs. Ralston Purina—4,300,-000 lbs. Harvey Beaty & Coldspring Farms— . . .

. . . our Egg Board Chairman . . .

> . . . 13,000,000 lbs. Canada Packers—4,000,000 lbs. Royce Packers—2,500,000 lbs. Wm. Knechtel & Parrish & Heimbecker Limited—3,500,000 lbs. Currah Mills—1,700,000 lbs. Cuddy Foods Limited—2,600,000 lbs. and Campbell Soup Limited—1,400,000 lbs. These figures are approximate and total 45,000,000 lbs., which means that the above companies hold over 45% of the heavy turkey production, . . .

Under their quotas. That is to say nothing of other contracts and so on besides this. His comment is:

> . . . so again I would have to ask the question "is this a turkey farmer producers board?".

Then there is a point made about broilers which I shall read to you. This is what he said about the directors of the former broiler industry and he says he is willing to back this up for the judge with hard facts.

Senator Martin: Do you think all this is relevant? We are considering a specific bill.

Mr. Hudson: I do.

Senator Martin: I am asking the chairman because we have a particular bill before us, and I think you should direct yourself to that.

Mr. Hudson: This bill advocates quotas on turkey products, on broilers and on eggs. We are telling you that half of Ontario's turkeys, which means 25 per cent of Canada's turkeys are tied up by ten companies. Now, that is just in Ontario, and you are about to pass farmer legislation to legalize this. We do not mind something going to the farmers, and we know that something needs to be done, but we do not consider that this is for the farmer. That is my whole point.

Senator Martin: I understand that, but I wonder if you should not address yourself particularly to the bill.

Senator Phillips: You want to apply closure, Senator Martin.

Mr. Hudson: Is not this what the bill is about, Senator Martin?

The Acting Chairman: Mr. Hudson, I think if you were to relate it to the bill as closely as you possibly can we should not take too long.

Senator Buckwold: How are the quotas established? By past performance?

Mr. Hudson: In a variety of ways. In the 30 quotas they took the biggest percentage of any one of three years, the biggest volume of three years, and that means they ended up with about 30 per cent more than they ever had in any one year. One thing that Mr. Walkie said in here was that the members of the original broiler board in Ontario in 1965 and 1966—very few of these men even exist today. The bulk have sold out and taken their dollar and a half per bird for their quota.

Senator Buckwold: Let us get back to the quota for a moment and you must excuse my ignorance. You are making an important point that the quota system is in fact freezing ten companies into half the market of Ontario. But so far as the balance is concerned, how would it be applied there?

Mr. Hudson: Well, it is applied to the other producers.

Senator Buckwold: Again on a sale basis?

Mr. Hudson: On what they had originally of what they bought. One man, Mr. Hadler—and I posed this question to the President of the Ontario Federation of Agriculture—this man Hadler has taken from three million to six million pounds out of a total of 90 million. I said to the President of the Federation, Mr. Hill, "What good is that to the Ontario farmer?" And he did not have too satisfactory an answer for me.

Senator Buckwold: But the fact is that this is based on performance or some established procedure or formula establishing a quota. I just do not know how it could be otherwise. Are not these people going to maintain their share of the market in any case whether you emphasize this or not?

Mr. Hudson: Well, the big do not always stay big. We stole most of the egg business we have from Canada Packers in Montreal. And I presume that if we get a little too big somebody will steal it from us.

Senator Buckwold: But this is an ongoing thing, and as you look at it now, I presume there will be changes even on the basis of quotas.

Mr. Hudson: The change that has become very evident is that when you have the quota and it is locked in, you can no longer get in there by ability.

Senator Buckwold: What is your quota?

Mr. Hudson: I do not have a quota and I do not want one. I am only saying this, that when you have the quota it does not matter how energetic the young farmer is and it does not matter how much ambition he has. We had 35 hens in 1942, and our egg board ruled that a man with less than 500 hens should not have a vote. It did not matter how much energy he had or how ambitious and ingenious he was. The only concern was whether he had sufficient money to purchase the quota.

Senator Grosart: What does a quota cost?

Mr. Hudson: About $1.50 in broilers.

Senator Grosart: What does the $1.50 purchase?

Mr. Hudson: Per bird. I have no idea what it is in turkeys.

Senator Grosart: What is the procedure for buying a quota?

Mr. Hudson: A deal is made with an existing quota-holder. For instance, in eastern Ontario there are no turkeys nor broilers, but plenty of farmers. How will we ever get turkeys and broilers in eastern Ontario under our present system? What God-given right have those in western Ontario to the total production of turkeys and broilers in Ontario?

Senator Martin: You have touched me on a sore point there. I ask you, did the integrators with the largest percentage of quotas in turkeys enter the business before or after the Ontario Marketing Board was established?

Mr. Hudson: They were in business when the plan was born, there is no doubt. The plan, however, has done absolutely nothing to stop this. Hadler doubled his volume under the terms of the quota system. It does not matter if limitations are imposed. Ways will be found to get around them.

The Acting Chairman: Mr. Hudson, perhaps you will move along. We have already been 40 minutes.

Senator Phillips: May I ask a question?

The Acting Chairman: Yes, certainly.

Senator Phillips: Mr. Hudson, you mentioned that you had been in beef and moved to broilers and so on. Does a young man wishing to establish a farming operation in poultry have to buy a quota? If so, can he obtain one? Can a person operating in, for instance, the dairy industry change to poultry?

Mr. Hudson: It can be done in eggs at present. In the other products they must be able to buy a quota, and one would have to be available.

Senator Phillips: They have to buy a quota?

Mr. Hudson: In order to make the change they must buy a quota. Farming is one industry and if it is continually frozen off it will turn total quota, regardless of what happens. As it is frozen off one at a time all the operators are driven into the remaining products. "X" number of products have been frozen off in Ontario and the producers are driven into those remaining. It is impossible to enter the broiler field today without buying a quota.

One ironic aspect is the proposal put before the federal Minister of Agriculture by the provincial ministers in November. One side of it suggested the farms be consolidated. On the other side the proposal was to impose quotas on poultry. What is the farmer to do with his consolidated farm if every product is under quota? The farms can be consolidated but still nothing can be done with them.

I repeat that farming is a total industry. There are many concerns which I will not go into, as we have been discussing quotas for quite a period of time.

Senator Grosart: Before leaving the quota, would you say that under this bill, once quotas are set by an agency no one can get into that particular farm product?

Mr. Hudson: Oh, no.

Senator Grosart: Without buying a quota?

Mr. Hudson: Arrangements might be made to set up new procedures. I am not aware of that, but it has not been the case in most of the other products. In some cases it has been the opposite. The quotas in poultry have gravitated to

the feed manufacturers or bigger producers. For instance, APM in Alberta and Pinecrest Poultry Sales own almost 50 per cent of the poultry quotas in that province. Is that not correct, Mr. Pringle?

Mr. M. Erwin Pringle, M.P., (Fraser Valley East), Chilliwack, B.C.: Do you wish me to answer that, Mr. Chairman?

The Acting Chairman: If you wish to do so.

Mr. Pringle: The integrated production of broilers in Alberta has not increased since the Marketing Board was established. The original producers have pretty well held their ground. Some small producers have sold out. This is true, but the APM have a large control of the secondary industries, such as hatcheries and processing. Their increase as an integrator was caused mostly by buying out other integrators in the province. Alberta has a plan under which 35 per cent of all new quotas issued must be allowed to new, young people or those who wish to start. There is no price permitted for broiler quotas in the Province of Alberta.

Mr. Hudson: I wonder, though, how much new quota they are issuing?

Mr. Pringle: The production has doubled in 10 years.

Mr. Hudson: We have many concerns regarding the bill. One is with respect to provinces being allowed to opt out.

Senator Grosart: Before we move to that, to continue with the quota, I am sure you have read the new clause 24 of this bill?

Mr. Hudson: No, I have not.

Senator Grosart: This is one of the three amendments made in the House of Commons, which we discussed this morning. It provides as follows:

> A marketing plan to the extent that it allocates any production or marketing quota to any area of Canada, shall allocate that quota on the basis of the production from that area in relation to the total production of Canada over a period of five years immediately preceding the effective date of the marketing plan. In allocating additional quotas for anticipated growth of market demand, the marketing agency shall consider the principle of comparative advantage of production.

In view of your comment regarding the apparent rigidity of the quota system, would it be your view that this clause would make the allocation even more rigid?

Mr. Hudson: It would lock it into the regions, regardless of the economics. For instance, western Ontario at one time produced half the demand of eggs in Ottawa. Now the producers in this part of the province have increased their production at a competitive price and satisfy all requirements here, plus shipping into Montreal. Over the last 15 years I would say eastern Ontario's egg volume has doubled.

Senator Grosart: Would a marketing plan established under the provisions of clause 24, to take specific example, make it impossible for a switch to take place in the total percentage of production, for instance, between western and eastern Ontario?

Mr. Hudson: It is very unlikely that it would switch between regions unless the quotas changed hands. No, under that, they could not, could they? It would have to remain as a quota base in the region.

Senator Grosart: So it would depend upon the dimensions of the region determined by the marketing plan?

Mr. Hudson: That is right.

Senator Grosart: But if western Ontario was designated as a region for turkeys, would they maintain under the provisions of clause 24 their quota percentage related to their five-year production?

Mr. Hudson: Legislation guarantees them the business for time to come.

Senator Forsey: Go on to the second sentence of clause 24.

The Chairman: I wish to ensure that Mr. Hudson has full opportunity to make his presentation. Perhaps we might allow him to finish, following which we can ask questions.

Mr. Hudson: There are many aspects of the bill. One is the concern over provinces opting out. The question was asked where does it say they can opt out, but where does it say they cannot?

Senator Goldenberg: Normally the legislation would provide that it can be done if that is so. It would not be said negatively. There is nothing in this legislation to say that a province can opt out.

Mr. Hudson: We are concerned by errors in judgment. For instance, British Columbia, with a very good marketing board, has over-produced eggs and shipped them to Ontario on a two-price system. That is really not very ethical in our estimation. What would happen if we were to do this nationally? I am sure that the Americans would not allow us to ship eggs in surplus on a two-price basis to them. Today we are worried with regard to the setting of quotas. What do you say with respect to the butter shortage in Canada today? Why should a country which has a vigorous dairy industry, as we have in Canada, have to import butter, as we are told we do? Nationally our boys were told by one government to grow wheat. We did so. We did not sell it, so we were told to grow hogs. But we grew to many hogs. We were told to grow beef last year. Some of us wonder what we will be told to grow next year. The most ironic part of the whole thing is that while all this is going on, we import American corn and turn it into products. Over the years we have imported a good deal of it, while our barley lies rotting out west. This does not make sense. We are also concerned over import controls. Will we artificially raise our prices? This will certainly add to bureaucratic costs. If it does and we have quotas, the quotas will add to costs. In Quebec, up until they put their quota system in, they bought their grain from the west or their corn from the States, or wherever they got it, turned it into broilers and shipped them clear back to British Columbia; and we heard great screams from British Columbia that they were being harassed with Quebec broilers. I do not know how they did that. They must have had some kind of magicians down there, turning these broilers over, because there is no way they should be able

to back-ship them to British Columbia and harass anybody.

We feel that imports will roll in and that the Americans will drive us into a corner in poultry products. We get an American price now plus a nice little premium. We will get American price plus the cost of this machine. The consumer will simply buy or import a substitute if we do not get a tariff increase. I told Mr. Olson in 1968—I went in to see him personally. I was concerned about this, and he was good enough to give me a hearing—that many of us would buy the deal if he would give us import control, if he would give us legislation against synthetics, and get consumers to stop their approval of the bill. I do not think he has done anything yet. We say that the better this bill works, the sooner the consumer will get angry and destroy it. She will not take artificial prices very long. She will want competition and she will buy the US product unless you are willing to put the tariffs on.

We talk about plebiscites. We feel there should be plebiscites. I read some of the things that happened in the Senate. Some of you talked about differences in plebiscites, differences in the definition of producers, and so on. To finalize this very quickly, why does Canada need a poultry bill? I will put into your transcript an article written by a Mr. Roytenberg who is the marketing man for Steinberg's Montreal. It was written up in one of the farm publications, *Country Guide*. This man flatly states the point that if we do not produce it at a price at which the consumer will buy it, the consumer will force them to import. I will give this to you.

The Acting Chairman: What is the date of that?

Mr. Hudson: It is on there, *Country Guide*, December 1971.

The Acting Chairman: This is a monthly publication?

Mr. Hudson: Right.

The Acting Chairman: It is entitled "A Marketing Strategy for Agriculture". The author is Don Baron.

Mr. Hudson: No; the editor is Don Baron. The author is Max Roytenberg.

The Acting Chairman: Is it the wish of the committee to have this appended as an exhibit?

Senator Martin: I have no objection to that. We have been very patient. Any witness can appear before the committee and put in any kind of supporting material, but . . .

Mr. Hudson: It is not necessary to be put in. Perhaps I can read just one paragraph. It says:

> There's no room in the merchandising scheme, he says, for "supply management", the philosophy that better prices can be obtained by artificially limiting supply. "Supply management doesn't solve the agricultural problem because it is a flight away from the mass markets of the world. It dooms us to be content with a shrinking share of the market at prices that become increasingly vulnerable with time."

I think this is only too true. I will not put that in the record.

The Acting Chairman: In other words, the author objects to marketing schemes of this kind, and you agree with him.

Mr. Hudson: He does not object to marketing schemes. He objects to the supply management as being self-defeating. He says that it is self-defeating.

The Acting Chairman: And you agree.

Mr. Hudson: I agree with him; absolutely, yes. I feel that if you analyse your bill, you will find that there is a good deal of coercive legislation in there. We find, for instance, that the council or producers can be appointed. It does not have to be elected. They sit at the minister's pleasure, whatever that means. The agencies can be appointed or elected, you do not have plebiscites for all producers, and so on. There were a good deal of amendments. I will not take time to go through them. About four or five of those amendments were good ones. We suggest that there should at least be a careful review of this bill. In regard to poultry, it will assist the non-farmer more than it will assist the farmer. We feel that poultry should be excluded rather than included.

It is possible that if a farm bill is needed, it should be reviewed as a farm bill for farmers. I heard from one of the boys this morning that the premiers are pressing the Senate to get it through. Somebody said the agriculture ministers were, and I am sure the MPs are. But this is not their bill. It is a farm bill, and it is for farmers. If enough farmers want it, fine, but I question whether this is so.

Gentlemen, whe whole system is withdrawing, it is regressive, it is a policy for the retired. It would make, in the words of one of our farm leaders, a giant public utility out of farming. I state this in closing: what is wrong with a vigorous, competitive Canada, and what is wrong with a vigorous, competitive, aggressive, prosperous system for Canada? We have to compete with the Americans, whether we like it or not. Some of us, believe it or not, still hope to sell to the Americans and not to sell out to them. We feel that too many Canadians are just trying to get big enough to sell out to the Americans, or we are withdrawing and letting the Americans come in the door, such as will happen to our poultry products under the bill.

If this bill has to be passed, then pass the bill for the farmer, but not this bill in the name of the farmer. Put up major amendments. Do what needs to be done. Make it a good bill and put it back to the Parliament. It had only one day of debate. If you read what the Honourable Mr. MacEachen said in the opening of the debate on the last day, you will find they had one day of debate and two days of wheeling and dealing. We feel that is not good enough.

I thank you very much for letting me appear. Do not get me wrong. I realize that you need legislation for the farmer, but we do not think it is this legislation.

The Acting Chairman: Thank you.

Honourable senators, Mr. David Kirk, the Executive Secretary of the Canadian Federation of Agriculture is here. Is it your pleasure to hear him?

Senator Molgat: May I ask Mr. Hudson a question before he leaves? You have dealt with the over-production that

occurs, for example, in the case of poultry, by letting the free market situation drive out those who cannot stay in.

Mr. Hudson: If you have not read yesterday's *Globe and Mail* I would urge you to read it. If you read that editorial you will see that the feed companies, looking to corner a share of the market, put into business far more people than they should have and they are now suffering because of that and they will continue to bear the brunt of it one way or the other.

We feel that if you allowed a young farmer the opportunity to produce he could produce cheaper than, for instance, Mr. Beatty, with his 13-million-pound quota. We are saying that the young farmer should have the opportunity to do so. What is needed is access to the market.

Senator Phillips: Your remark to the effect that you hoped to export to the United States rather interested me. Do we export eggs or poultry products to the United States at the present time?

Mr. Hudson: Eggs were going last year, but this year they are coming back. The pattern seems to be a process of exporting and importing. What we are saying is that if we had the grains at a competitive price many of us feel we could increase our production.

Senator Phillips: You also mentioned, Mr. Hudson, that we imported a substantial amount of American corn. I was rather surprised at that statement, and I am wondering why we do not use western feed corn as opposed to American corn.

Mr. Hudson: I have no idea how much American corn comes into Canada. I know some does, but we would like to use western feed corn if we could. I believe the United Grain Growers has more or less put their stamp of approval on this trend.

Senator Phillips: So you would use western corn if you had a reasonable transportation price and access?

Mr. Hudson: Well, we are now promoting more corn growing in Quebec and Ontario, so there is really no need to grow more corn.

Senator Sparrow: Would this legislation meet with your approval if the supply management features of the bill, as far as your industry is concerned, were deleted? In other words, just a marketing agency.

Mr. Hudson: If it was a marketing agency which would genuinely try to help us in exporting our products, and so forth, certainly. There is absolutely no reason why we would not want this. However, any time we have bowed down to this, they take our money and they get us one at a time. Do you follow me? In other words, we would have to be guaranteed that supply management would not come in.

Senator Sparrow: Under the supply management feature in the legislation, your feeling is that the bigger producer has the greatest opportunity to get bigger because he would have the financial resources to buy up the smaller quotas. You have mentioned ten of the largest producers and the possibility of them picking up all of the quotas. In other words, the bigger producers could pick up the smaller quotas much easier than could a new farmer just starting in the business.

Mr. Hudson: Four of the biggest producers are feed companies and one is Campbell Soups, so they have unlimited financial resources. It is not a matter of whether they can produce cheaper, but whether or not they have access to the market, and they do not have this access if they do not have the quota system.

Senator Grosart: Mr. Hudson, you have made a strong plea for the average producer, but are you not satisfied with the requirement that the council cannot recommend a marketing plan or the formation of an agency unless it is satisfied that a majority of the producers of that farm product in the region to which the farm marketing plan would apply is in favour? Is this not a protection for the majority, particularly in view of your statement with respect to the domination by certain large producers, and the minister's statement that this will normally be a one man/one vote decision? Does this not protect the majority?

Mr. Hudson: It does to an extent, but if you arrive at a situation similar to what we have had in poultry where you have so many people who have been pushed into the industry and then the cookie is held out one or two years hence. This is what has happened in Ontario. The feed companies have a good deal of control of the industry by reason of the amount of financing they have put into it. They did this with reckless abandonment and now they are suffering because of it.

Senator Grosart: What percentage of individual producers would be under the control of feed companies?

Mr. Hudson: Individual producers of eggs?

Senator Grosart: Yes.

Mr. Hudson: In Ontario, I would say most of them are independent, but eggs have not been moving and as a result many individuals are heavily in debt to the feed companies.

Senator Grosart: What percentage would be under the control of the feed companies?

Mr. Hudson: Man for man?

Senator Grosart: Yes.

Mr. Hudson: Less than 30 per cent of the producers, but probably 75 per cent of the hens. This is why we are having this inquiry in Ontario. Any time they allow enough small producers to vote, it is voted down because the small farmer does not want it, and we contend it is small farmer legislation.

Senator Grosart: Would the small farmer who is under some financial obligation to the feed company vote for an agency, in your opinion?

Mr. Hudson: It depends on what you call a small farmer. If you are talking about a man with a couple of thousand hens, he probably is not under that heavy an obligation; if you are talking about a man with 20,000 hens who has a heavy financial obligation to a feed company, he would

probably view this as a solution and he could probably sell his quota for $40,000.

Senator Grosart: What percentage of the total quota would the $40,000 involve?

Mr. Hudson: Well, broilers trade at $1.50 a bird, and they consume about 25 pounds of feed a year, so we are saying a hen is worth $2.00; $40,000 would be a 20,000-bird quota.

Senator Grosart: Yes, but I would like to know what the relation of $40,000 is to the total quota. Is it one per cent, 1/10th of a per cent, or what?

Mr. Hudson: There are 10 million hens in Ontario, so you immediately create a quota of $20 million to $30 million if you put the quota system in.

Senator Grosart: So $40,000 would be what?

Mr. Hudson: It would be one-fifth of one percent.

Senator Grosart: One-fifth of one per cent of the quota would be worth $40,000?

Mr. Hudson: Yes.

Senator Buckwold: Mr. Hudson, to get back to the poultry industry in Ontario, you have spoken as a rugged individualist and I admire that, but is there such an organization as the Ontario Poultry Association?

Mr. Hudson: The Ontario Egg and Fowl Board.

Senator Buckwold: And are you a member?

Mr. Hudson: I am a director.

Senator Buckwold: And has that organization made any representations or raised any objections against this marketing bill?

Mr. Hudson: The organization is in favour of the bill. That is why we are having this inquiry. It is a battle fetween the producers of Ontario.

Senator Buckwold: And are the majority of the people in that association producers?

Mr. Hudson: The majority of the directors are, but the last time we had a vote which was in 1968, they lost.

Senator Buckwold: But nevertheless we are now talking of today. I am just trying to get your personal views as against the position of the industry as a whole. Your views and opinions do not in any way coincide with the opinions of that association?

Mr. Hudson: No, they disagree with me; not the industry as a whole, but the board itself disagrees with me. Two directors of the board have now indicated they are against it. When we held our last vote in 1968 I was all alone. There was one against it and eight for it.

Senator Goldenberg: You made some progress.

Mr. Hudson: We have got twice the strength.

The Acting Chairman: A 100 per cent increase.

Mr. Hudson: A 100 per cent increase.

Senator Sparrow: I am sorry to hold this up, but I should like to ask two further questions. Mr. Hudson, you did define what you thought a producer was who was a farmer. I am very interested in that. We have been trying to define what a producer is. You seem to define it in the broad sense of a producer in any agricultural product. Would you repeat that for us?

My second question is this. We have referred to the Ross inquiry. Do you know when they are expected to report, if there is any time they are expected to report, and if in fact that inquiry would have some relevance to this bill?

Mr. Hudson: There are two or three questions there. Let me answer the last one first and then go backwards. The Ross inquiry is over on Monday. I do not know how long it takes a judge to report; maybe a month, maybe two or three months, with the piles of stuff that Judge Ross has on his desk. If he reports, he is reporting to our Department of Agriculture. Of course, they do not have to listen to his report unless they want to. The Department of Agriculture will then decide what they will do relative to his report. If they decide quotas are not for Ontario, I presume this will make it difficult to have a national egg marketing bill. Ontario has over 40 per cent of the eggs in Canada.

Turning to your first question, I will give you three briefs that I have. If you think they are worth looking at, Senator Sparrow, you can pass them around to the other senators. By my definition I am not a farmer. Remember, my brother, my father and myself stand to pick up $750,-000 or a little better for a quota, so we should be on the other side of the fence really. If I were 60 years old I probably would be.

The Acting Chairman: Don't knock the sixty-year olds!

Mr. Hudson: No, no. There is nothing wrong with being 60, or more. A farmer is a man who has acres of ground, who grows crops on that ground. If he lives east of Manitoba, in many cases he feeds it into his animals and puts it into the marketplace. West of Manitoba, many of the fellows do not, as you know. In Eastern Ontario there are very few straight corn farmers; most of them grow the corn and put it through hogs. For instance, in the hog industry, they do not opt for quotas in Ontario, and there are over 20,000 farmers. Every time the integrators move in the industry to contract hogs, they run a low price cycle and drive them right back out again. The farmer feeder does this. I have good briefs here from at least one or two farmer feeders. I have one from George Morris, who is a very well known cattle man, and so on. I will give them to you, Senator Sparrow, and you can pass them around if you see any merit in them.

Senator Molgat: Do I understand you to say that the hog producers in Ontario do not want quotas?

Mr. Hudson: They have not got them. They do not have quotas, no. They have a marketing plan, but no quotas. They have a sales agency only.

The Acting Chairman: Thank you very much indeed, sir.

Mr. Hudson: Thank you again for hearing me.

The Acting Chairman: We will now hear from Mr. Kirk. Mr. Kirk, would you identify yourself, please?

Mr. David Kirk, Executive Secretary, Canadian Federation of Agriculture: My name is David Kirk. I am the Executive Secretary of the Canadian Federation of Agriculture, and recently acquired the responsibilities of Secretary to the Canadian Egg Producers Council.

The Acting Chairman: Where are your headquarters?

Mr. Kirk: In Ottawa.

The Acting Chairman: Have you some representations to make in respect of this legislation?

Mr. Kirk: Yes. I appreciate very much being here. The remarks I have to make will, I think, be brief, but perhaps there will be some questioning following my remarks that you would find useful.

The position of the Canadian Federation of Agriculture all through the debates on this legislation has been one of being in favour of the legislation, and continues to be so, as a piece of enabling legislation that provides the capability for in some cases the better management, and in others the better development of agriculture, of many commodities in this country.

The provisions that have been arrived at by the House of Commons are that supply management, the quotas, can only be introduced without further amendment to the bill in the poultry and egg field. That accommodation, to bring in quotas for commodities other than in the poultry industry, is one that I am quite sure the Canadian Federation of Agriculture would accept.

If you check through our submissions, we never did feel that it made much sense to exclude any commodities, because this is a piece of enabling legislation, and there are many things that can be done under it. We made it clear in our representations with respect to hogs and beef that we did not anticipate, and we did not see the producer support for, an early, or perhaps ever, introduction of a system of quotas. Therefore, we have no quarrel at all, although when the time comes for further commodities to be introduced, if it does—probably not hogs or beef, probably something else than poultry or hogs or beef—it is necessary that the organization has been done, the producer discussion has taken place, the examination of the needs of the industry has taken place, and we hope that, if and when the time comes for the introduction of amendments to introduce further commodities into the bill for supply management, the momentum and drive that will obviously have to go behind such a move will not be held up by the circumstances of the House and the work of the House, and all that kind of thing. That was really the only reason that we favoured, on the whole, leaving the supply management capability in the bill for all commodities. As I say, we are not quarrelling with that.

However, we do support the immediate introduction into the bill of supply management for poultry products, because our thorough understanding is that the great majority of poultry producers and egg producers in this country in fact want the provisions of federal legislation that enable an agency to conduct a supply management system; they want that power in there. That certainly is true of the Canadian Egg Producers Council, and very strongly so.

That is the main proposition. Really what I am saying is that we would like to see this bill go through. Unquestionably in particular details, between my organization and, perhaps, others, and within my organization, there are many sometimes quite difficult questions of what is the very best way to word this bill. Our position is that we think it should be passed. We think that bills can be amended in the future if real difficulties arise with respect to the satisfactory nature of any particular clause. For instance, in a particular commodity that is to be introduced into supply management, it is possible that the mandatory five-year base provision might not statistically lend itself to the right answer. That might raise the question of amending the act. But our position is that we would like to see it passed.

Perhaps that is all I can say, as a start. When I say I would like to see it passed, I say that with all respect, of course, to this Senate, and I would point out that the Federation has always been aware of that and has not been anything less than frank about the fact that it is a legislative power that is being provided here. There is a public interest involved, and I would say for the future that the Senate as well as the House of Commons would have not only an interest but a responsibility to review and pay attention to how this whole thing works.

Times change, developments occur and problems arise, and it is a very legitimate public responsibility to pay attention to the operations of any such legislation.

Finally, on the general question that Mr. Hudson was discussing, I am not going to get into the in and outs of the integration question, except to say that there are at least a great many producers I know who would say that, on the whole, they think that the fundamental drift in the poultry industry is towards integration and non-producer control.

Senator Grosart: Is that a good thing?

M. Kirk: They would say it is a bad thing. They would say that this bill and the marketing plans have within them the capacity for precisely seeing that that does not happen. If in a particular plan the regulations are so formed that it does happen or start to happen, you can have an argument whether that is desirable or not, and so on. But the capacity is there to do much more what you want to do, than without the bill.

Senator Grosart: In view of the importance of the organization which you represent, I should like to ask you a few questions. Would you be in favour of the inclusion of consumer representatives on the Council or agency boards?

Mr. Kirk: I think my organization's position would be that they would not be in favour of that. They would be in favour, I am sure, of its inclusion in the advisory structure or structures that might be set up.

This relates, in part, back to the point I was making about the fact that this is public legislation and the responsibility of public bodies such as the Senate is to review this. This is a public interest question. We really question how meaningful it is, to introduce into these

bodies that you mention a consumer interest as such. We are not exactly sure what it might be, always. This is with all respect to the organizations that take the consumer name. We do not think that that would be a useful thing. What we do support is the very best continuing examination and the raising of issues that exist in the operation of marketing boards and we have no objection to the public interest being recognized thoroughly.

Senator Grosart: The bill requires agencies to consider the consumer interest. Would you agree that it might be a useful way of implementing that, to have at least one consumer representative on an agency board? If not, why not?

Mr. Kirk: I think the best way for the consumer interest to be represented is to have a very good examination of the industry and of the issues that are involved in marketing boards, and the right kind of work done to clarify those issues and to expose them. I do not think that a consumer representative per se ensures that that kind of examination is done, and without it the criteria for acting would be difficult. I do not see the situation as an adversary situation, and it should not be so.

Senator Grosart: I am not suggesting it should be an adversary situation, but that there should be some feed in of data of the dimensions of the consumer interest when this kind of legislation is proposed whose main effect, in terms of Canadian citizens, will be on consumers.

Mr. Kirk: I am not sure that that is right, that its main effect will be on consumers. It is not clear to me, and it is far from self-evident, that an egg marketing board would result in either higher or lower prices for consumers. You have now a cycle, and it is the cycle you are modifying with high or low prices. You would have to know in fact what the results were in relation to the price policy of the board, to know what the effect was on consumers, and it could well be beneficial.

Senator Grosart: Is not one of the main functions of the marketing board to prevent extremely low prices for a farm product?

Mr. Kirk: Yes, the main function of a marketing board is to prevent at a given time—

Senator Grosart: I said "one of them".

Mr. Kirk: At a given time, to prevent extremely low prices, but more properly looked at, it is to avoid extreme instability and the insecurity to the producer that is involved in that and the waste to the economy that is involved in the production cycle, because there is a very significant economic waste in large swings of production.

Senator Grosart: I will leave that point. Do you agree that members of the council and of the agencies should be appointed at the pleasure of the Governor in Council, or would you favour a specific term of office?

Mr. Kirk: I do not think that our people have very strong feelings about it. I am not sure that I could validly speak as a reflection of the views of our people on that particular point.

Senator Grosart: What has been the situation with respect to other marketing boards with which you may be familiar? Are the appointments largely at pleasure, or for a term of office?

Mr. Kirk: The marketing boards of the type that is largely conceived in here are essentially producer representative boards, of course, at the provincial level. That is a different situation, and those producer boards mostly have elected representatives.

Senator Grosart: That is why I asked the question.

Mr. Kirk: The boards we have had nationally have been federal boards. We have had the Wheat Board and the Canadian Dairy Commission. I do not think it is a parallel situation in either of those institutions.

Senator Grosart: Would not this be parallel, let us say, to the council, but not to the agencies, if as you say the majority of agency directors are now elected. Would you not be afraid that the introduction of this appointment of agencies at pleasure is a novel and perhaps dangerous innovation?

Mr. Kirk: I think our people would favour, on the whole, a term of office arrangement, probably with renewal; but I do not think they consider this an essential question.

Senator Grosart: It is not obligatory under the act. The other alternatives are open. But, from your experience, would you say that the CFA would, all circumstances being equal, in general favour elective agency boards?

Mr. Kirk: Well, if you are speaking of the national agencies—

Senator Grosart: I am speaking of the agencies, not the council. Leave that out for the moment.

Mr. Kirk: The national agencies under the legislation?

Senator Grosart: Well, at least intra-provincial, if not national.

Mr. Kirk: I know that a lot of our people see very severe difficulties in a meaningful elective procedure for a national board.

Senator Grosart: So do we all.

Mr. Kirk: The majority of them—the egg producers at the present time, for example—feel that the board should in fact be made up of the named provincial representatives of the provincial boards. That is what they feel.

Senator Grosart: Who feels this?

Mr. Kirk: The Canadian Egg Producers Council feels this. They feel that essentially a board should be that kind of a group. That is how they feel at the present time.

In our discussions in our organization we did not have concensus on this. I can tell you that quite frankly. This is quite a difficult question. We were in fact in favour of a provision that would require a procedure for orderly and mandatory examination of that particular question, with rules promulgated in each case, after having a thorough

hearing of producers' views, because we think that the situation can vary from product to product and from plan to plan.

Senator Grosart: Which is, in effect, provided for in the bill.

Mr. Kirk: Yes, which is, in effect, provided for in the bill.

Senator Molgat: Mr. Kirk, Mr. Hudson just indicated the situation vis-à-vis turkey production in Ontario. Did I understand correctly that you feel that under a marketing plan it would be easier to protect the farmer element than without a plan?

Mr. Kirk: What I am saying, and this is in respect of Ontario, of course, is that if, without a plan, the basic drift is to integration, then, of course, with a plan you can in fact stop it. You can in fact reverse it. My point is that you can do what you want to do. I do not say that this is a simple question. I am saying that you can do it.

Senator Molgat: But has there not, in effect, been a plan in Ontario?

Mr. Kirk: There has. I am not as familiar as I might like to be with the details. I do not know how much additional integration has been created during the period of the Ontario turkey plan. I just do not know. I do not have direct information about how that plan has gone.

Senator Molgat: But there is a plan and the result has been that almost half of the production is in the hands of ten producers.

Mr. Kirk: I am saying that I do not know whether that is the result of the plan.

Senator Molgat: But it exists.

Mr. Kirk: It exists, yes. That is what I heard this afternoon.

Senator Molgat: If I understood correctly, both Mr. Gracey and Mr. Hudson made the statement that import controls would be necessary if the plan were to work properly. Do you share that view?

Mr. Kirk: Well, if you have a plan that is designed to stabilize the price and if you set a price that is higher than the lows of the cycle in the country next door—in the United States, let us say—then it is perfectly clear that, if they do not have a plan, then the price will at the low points of the cycle dip below the stabilized price. I think that is fairly clear. Therefore, there will be a threat to the plan. We have always said that the question of import policy will have to be dealt with and the plan protected. But that is a matter for negotiation. It does not have to be in the act to be a governmental capability. It can be done. It is legal under the GATT agreement under Article 11, I believe. But we have not pressed for its inclusion as a power of the agencies. One of the reasons is precisely on this consumer question. That would be an exercise of public interest judgment, would it not? It is not built into the act. Many of our producers would, of course, like to see it in the act from their standpoint, but we have not pressed for this because our understanding was that the Government felt quite strongly that, first of all, public interest was involved in that question in a special way, and, second of all, that so were their trading interests involved in terms of negotiation, you know, in particular types of arrangements. So we said, "Okay, but it has to be recognized," and I think it is recognized, and we hope that the import trade arrangements will certainly be involved in the operation.

Senator Grosart: But you can hardly give to a marketing agency the power to set up international tariffs.

Mr. Kirk: Well, we had not expected to.

Senator Grosart: Senator Martin might object to that.

Senator Molgat: For those of us who represent regions or provinces which are normally exporters of agricultural products, the whole question of free access to the whole Canadian market is very important. This morning Mr. Atkinson gave me the impression that he felt that a plan would, in fact, lead to greater balkanization. Has the federation looked at this question of access to the Canadian market?

Mr. Kirk: On this question I always go back to the Canadian Egg Producers conference that the Canadian Federation of Agriculture sponsored, which I think had a lot to do with a large part of the genesis of this whole thing. At that conference these problems were intensively discussed. The conclusion the conference reached then, and I believe the concensus of producers now, is that the overriding need is for stability, security and proper management of the industry. That is the overriding need, and the other problems will have to be worked out.

And therefore, in that sense, it would not be balkanization. In that sense it would, in fact, be management with a very large element of federal authority in that management.

I do not know whether you can properly call that balkanization. That there would be management under an egg-quota plan is clear. There would. It is not clear to me that that is the same thing as balkanization.

Senator Michaud: As a representative of the province of New Brunswick I would first like to say that I was pleased to hear that the Ministers of Agriculture from the Maritimes had, as a whole, approved this legislation. I do hope that it will eventually prove to be of some benefit, first of all, to the poultry and egg producers, then to the hog producers, and then particularly to the main crop producers in New Brunswick—the potato producers.

As far back as I can remember, the potato industry, when it came to marketing conditions, was always faced with a condition of morass, let us say.

I was just wondering if Mr. Kirk would care to comment in what respect or in what way this legislation might enable the potato industry to be put into a more stable situation.

Mr. Kirk: Well, if the industry moved towards some system of national or regional quotas, then that would require an amendment to the legislation, but it is very possible that many constructive things could be done short of that. There is the capability in this legislation, first of all, for studying through the Council the problems of the industry and examining them with care and reporting on

the problems in a context that has not existed to date. That might be extremely useful. There is a capability for setting up, if I am not wrong, not only regionally based agencies through which a particular sector of the industry, a group of provinces, could manage their affairs in many ways, with respect to quality, with respect to export market development, with respect to orderly movement of the product by agreement short of quota management; but I am not sufficiently expert on the potato industry, sir, to spell out an answer for the potato industry just offhand beyond that.

Senator Phillips: Mr. Chairman, I wonder if Mr. Kirk could tell us what percentage of Canadian farmers belong to the Federation of Agriculture.

Mr. Kirk: Well, sir, when we add up the membership of our member organizations, which is a duplicating membership, we get way more than 100 per cent, but I am quite sure that if it was in strict terms of affiliated membership through all organizations you would get a good 80 to 90 per cent of the farmers of Canada belonging to some organization affiliated through the federation.

Senator Phillips: All right. Let us put it on the one-man, one-vote principle. On that basis, what percentage do you have?

Mr. Kirk: That is my answer.

Senator Phillips: You rather surprise me, Mr. Kirk, in that you come out so strongly in favour of this legislation. Recently the Federation of Agriculture in my province held meetings, and when this bill came up, after four hours of debate, the directors voted on the question of supporting it, and the vote was 12-12. What is your relationship to various organizations such as that that are not as wholeheartedly in support of the bill as you are?

Mr. Kirk: Well, our relationship is that they are bona finde members of our organization. I do not know which specific organization you are referring to.

Senator Phillips: The Prince Edward Island Federation of Agriculture.

Mr. Kirk: The situation is, of course, that this bill has given rise to an enormous amount of debate, and a lot of that debate was really on the issue of supply management for each commodity. That is why I said I think our people would support it. But in fact I have not had a full-scale, general meeting on this accommodation which has been reached in the house, so I am just giving you my judgment and the judgment of my president with whom I have discussed this. My judgment is that now that the question of supply management has been dealt with in the way it has been, so that it is no longer possible to identify the whole of the bill with quotas for every commodity, our people would very much support this bill as it is.

Senator Phillips: I find it very interesting that you have not had any meetings either of your directors or with any organizations since the bill was amended in the House of Commons, and yet you come in and support it. Now I noticed in your remarks, if I interpret you correctly, you said that one of the possible ways to deal with farm legislation is to have a hearing and then have publication of regulations. What form of appeal would you suggest for an individual who is going to be harmed or hurt under the regulations?

Mr. Kirk: For an individual who is going to be harmed or hurt, as opposed to a legality question?

Senator Grosart: Somebody who objects to it.

Mr. Kirk: Well, the fundamental provision in the bill now, of course, is really the one dealing with the council, is it not?

Senator Phillips: But I am asking you, as a representative of the Federation, what form of appeal you would favour, and not what is in the bill.

The Acting Chairman: Does that matter? We are really talking about the bill and we are not examining the witness with respect to his own personal views.

Senator Phillips: Then I am asking for those of the Federation.

Mr. Kirk: The Federation is in favour of some procedure. I do not think they would favour a full judicial procedure but I think they would favour some review of individual complaints. I doubt if they would favour a straight ministerial or Governor in Council fiat on it. However, I am not sure about that. I must confess I have forgotten what exactly the bill says on this point precisely. But could I just refer back to the first point you made about your surprise that I would have the temerity to assess the views of my organization without having had a formal meeting on it. The reason I do that is, first of all, I know my organization rather well, and especially in view of the uniform support which I gather has been publicly expressed, of the accommodation that was reached, and I know the general British Columbia, Ontario, Quebec and other positions, and I am quite sure my board of directors, and I admit it is a matter of judgment, would support this accommodation.

Senator Phillips: I would have been much more impressed by your brief, Mr. Kirk, if you had had a board of directors' meeting.

Senator Argue: Might I ask a supplementary question on that point? I wonder if Mr. Kirk had any communication at all with the President of the Saskatchewan Federation of Agriculture or anyone out there? They were meeting this week, and I was pleased to be there myself. I learned that they were in support of the Senate's giving this further study.

I wonder if Mr. Boden expressed to Mr. Kirk the feeling he conveyed to me? It was that the Saskatchewan Federation of Agriculture, in general, was in favour of this bill as the Senate now has it.

Mr. Kirk: No, unfortunately I have not had that conversation with Mr. Boden. I have discussed it with a number of other officers of the group.

Senator Argue: That their support is quite clearly solidly in favour of the bill?

Mr. Kirk: That is right.

Senator Forsey: Relating to the question of Mr. Kirk's judgment in this matter, it would be worth while putting on record how long he has been connected with the Federation of Agriculture. To my personal knowledge it has been a very long time. I could not say offhand how many years. Therefore, it is a very good basis for his judgment.

The Acting Chairman: Without dating him, let us ask him how long he has been there.

Mr. Kirk: Eighteen years come May.

Senator Martin: Did you succeed Herb. Hannam?

Mr. Kirk: No, I held that position under Mr. Hannam.

Senator Martin: He became president after being director.

Mr. Kirk: He was president, and Mr. Munro has become president since his death.

Senator Martin: And Mr. Munro, the president, is a farmer from Embro, in Ontario?

Mr. Kirk: That is right, and I discussed this with him before coming here.

The Acting Chairman: Is Embro near Windsor, Ontario?

Senator Sparrow: Mr. Kirk, you mentioned that you represent probably 80 per cent of the farmers in Canada?

Mr. Kirk: That is right.

Senator Sparrow: Is the National Farmers' Union a member of your organization?

Mr. Kirk: No.

Senator Sparrow: Is the Canadian Cattlemen's Association a member?

Mr. Kirk: No, the Canadian Cattlemen's Association is not a member. Its constituent members are, for the most part, members of our provincial organizations.

Senator Sparrow: Is the Canadian Stockgrowers' Association a member?

Mr. Kirk: No.

Senator Sparrow: Do you have direct memberships in the Canadian Federation of Agriculture?

Mr. Kirk: No, we are a federation of organizations, some of which, of course, are very important direct membership institutions, if that is an issue. The Union Catholique des Cultivateurs in Quebec is a member organization. I would estimate that it is far and away the largest direct membership organization in Canada, whether all-Canada or provincial. We also have others.

Senator Sparrow: Approximately how many farm organizations would be affiliated with the CFA?

Mr. Kirk: We have 13 members, the membership lists of which fill approximately 14 pages. It is a very large group of organizations.

I should say that when I say I represent them, I mean that they hold and continue to hold membership in the Canadian Federation of Agriculture. They do that in light of their knowledge of the procedures and processes of the federation and its activities. It does not mean that within the organization there is a total unanimity of views every time I, the president or the board of directors speak on a policy decision, nor could it mean that.

Senator Sparrow: So you are not saying that your views today represent 80 per cent of the producers, or farmers?

The Acting Chairman: It is sufficient for this committee to say that Mr. Kirk is the Executive Secretary of the Canadian Federation of Agriculture.

Senator Sparrow: Thank you; I will ask another question. Clause 2(c)(ii) of the bill provides:

> ... as a result of declarations by provincial governments following plebiscites, or otherwise ...

That means that a provincial government can opt in without a plebiscite. What is the view of your federation in that regard? Should plebiscites take place in each province or is the "otherwise" aspect in the bill sufficient?

Mr. Kirk: My view is that a great deal of reliance should be placed upon the action that has been taken at provincial levels with respect to the formation of boards. In the case of an existing board, for example, attempting to group together other boards, there could be circumstances where the board and government of that province would consider it simple nonsense to hold a plebiscite. There are other circumstances, in which the council could raise the question and ask for some processes up to and including a plebiscite in order to satisfy themselves of producers' views. There is provision for that, which I do not consider to be improper.

Senator Sparrow: In other words, you deem there to be sufficient safeguards in the bill?

Mr. Kirk: That is right.

Senator Phillips: Perhaps I am projecting into the future, Mr. Chairman. Mr. Kirk, what would be the attitude of the federation if in future an amendment were made to include other farm produce, such as beef?

Mr. Kirk: That is an exceedingly hypothetical question.

The Acting Chairman: It is purely hypothetical.

Mr. Kirk: It would depend primarily upon the wishes of the beef producers.

The Acting Chairman: Honourable senators, I think that is about as far as anyone could go. Shall we thank Mr. Kirk very much?

Senator Grosart: I would like to pursue the question of the right of appeal. I know you have read the bill very carefully, Mr. Kirk. It does not seem to include any provision for appeal. It has been stated, of course, that clause 7(1)(f), provides that the Council may inquire into any complaint and take action.

Under a marketing plan, clause 2(e)(v) provides the power to cancel or suspend any licence—that is, presumably, to deprive a person of the quota. My interpretation of

the bill is that the Marketing Council could inquire into this. They do not seem to be required to inquire into it. Do you think that a complainant who feels that he has been unjustly treated, for instance, by the cancellation of his licence, should have an appeal other than to the agency or to the Council? I am not asking the type of appeal, but should he be able to go beyond the Council and the agency in it?

Mr. Kirk: It would depend partly, I am sure, upon the definition of matters which could be appealed. Let us take integration as an example. The decision under a regulation that certain types of feed companies should no longer be licensed, would be a matter of policy.

Senator Grosart: Let us stay with my case of the cancellation of a person's licence. It is cancelled. He is notified by the agency that his licence is cancelled, that he is out of business. I do not care whether he is right or wrong. I am asking whether he should have some recourse, other than to the council or to the agency.

The Acting Chairman: I stand to be corrected on this, but perhaps the prerogative writs would be available to a man in such a position. I would defer in this matter to some of the other legal counsel here.

Senator Goldenberg: You are right, Mr. Chairman.

Senator Grosart: I would like a little explanation on this matter.

Senator Phillips: We have legal counsel. Could we have his opinion as to whether that would apply? Not that I distrust my friends in the committee. I have seen too many lawyers in court to know that there are always four sides to every question. Probably we could have a definition from our legal counsel.

Mr. R. L. du Plessis, Legislation Section, Department of Justice: I do not profess to be an expert on this matter. I think there is a possibility that an appeal could be made to the courts.

Senator Grosart: You say a possibility; but does a right exist?

The Acting Chairman: One could always issue a prerogative writ. I do not think there is any question about that.

Senator Phillips: What would be the effect of issuing it?

The Acting Chairman: That would be dependent upon the courts. It would depend upon the character of the issue that is presented to the court under the writ.

Senator Grosart: Could that issue go beyond the fact that the agency or Council might have exceeded its powers?

The Acting Chairman: It could certainly go that far.

Senator Grosart: Could it go beyond that?

The Acting Chairman: I do not know whether you could go beyond that. If the council had exceeded its powers, presumably the court would find that the exercise of its powers in excess of those conferred by the statute was not proper.

Senator Grosart: I refer the committee to clause 23(f) on page 16, which says:

> (f) where it is empowered to implement a marketing plan, make such orders and regulations as it considers necessary

What is the use of a prerogative writ if the act says if the agency considers this necessary?

The Acting Chairman: The court, being seized of a question under a prerogative writ, would probably address itself to the adequacy of the reasons which moved the board to issue or make an order under (f). If it were an unreasonable exercise of power, the court would have authority to nullify the order.

Senator Forsey: There is no privative clause here, such as you find in the Labour Relations Act, which clause, in my experience, has been totally ineffective against the use of the prerogative writ.

Senator Grosart: The Senate must consider whether it should pass an act which does not specifically provide for the right of appeal. I suggest the committee look at subclause (n) on page 17, which says:

> (n) do all such other things as are necessary

When we come to the clause I will suggest that we amend subclause (f) to read:

> (f) where it is empowered to implement a marketing plan, make such orders and regulations as are necessary

The wording in subclause (n) is a very essential protection. There is a triple delegation to the agency. It has delegation of power from the federal Government, from the provincial government, and, in effect, a delegation from the marketing council. You have a triple delegation of parliamentary authority, and then you say that the agency may do whatever it thinks necessary. I think this is a fundamental abrogation of the essential right of any person to require that any such agency have the power to do only what is necessary to implement the act, and not to do what it thinks is necessary.

The Acting Chairman: I should think, Senator Grosart, that if the worst happened under the exercise of its delegated authority, the issue of a prerogative writ would correct it. Am I right on that?

Senator Grosart: It is a very expensive process. That means Federal Court, does it not?

The Acting Chairman: It may be done by the superior court of a province, certainly.

Senator Grosart: I do not want to make you a witness, Mr. Chairman, but you are an eminent lawyer. Can a prerogative writ be effective where an agency or board is acting within its powers under the act?

Senator Goldenberg: If it exercises its powers unfairly.

The Acting Chairman: Yes, and unreasonably. That is the purpose of the prerogative writ.

Senator Forsey: Surely, we have had that in labour relations cases, where the Supreme Court of Canada, in one

case, declared that the Nova Scotia Labour Relations Board had neglected the rule to hear both sides and sent the thing back. I should have thought the same would apply here. I think there was a privative clause saying the courts were not to review the decisions of a board.

The Acting Chairman: There is nothing in the act to that effect. If there are no further questions, we have finished with this witness.

Honourable senators, I have a letter from the Consumers Association of Canada signed by Maryon Brechin, saying:

> Enclosed are copies of submissions presented by the Consumers Association of Canada on Bill C-197 and Bill C-176, the acts dealing with the establishment of a National Farm Products Marketing Council.

The letter is dated January 6:

> The Consumers' Association of Canada wishes to present to the Senate our suggestions for amendments to Bill C-176 which we believe will assist in safeguarding the public interest under such legislation.

I take it that Mrs. Brechin is not in the room. Has the committee any directions for me? I understand that everyone has received a copy of this letter.

Senator Martin: I understand that she sent the brief, which she submitted earlier, to every senator. I received mine this morning.

Senator Langlois: Is it lengthy?

The Acting Chairman: It is fairly lengthy. It is dated October 1, 1970. There is a memo attached to it dated March 15, 1971 addressed to members of Parliament from Jean Jones, the National President. The brief is in English and in French.

Senator Martin: She also sent a memo dated today reiterating the submissions contained in the brief.

The Acting Chairman: Yes.

Senator Langlois: It should be printed as part of today's proceedings.

The Acting Chairman: Is it the committee's direction that the material submitted be printed as part of the committee's evidence?

Hon. Senators: Agreed.

See Appendix "A"

Senator Grosart: Is there a suggested amendment, Mr. Chairman?

The Acting Chairman: I have not read the brief because it has just reached me.

Senator Grosart: I would suggest, Mr. Chairman, that if there is a suggested amendment from the Consumers Association of Canada, it should be read into the record. We should have it before us when we come to the clause-by-clause examination of the bill.

The Acting Chairman: It has been suggested to me that the proposed amendment was contained in the telegram which I read this morning, but I do not seem to be able to identify anything in there as an amendment. I do not see any specific reference to an amendment.

Senator Goldenberg: I suggest you start at paragraph 13, Mr. Chairman, page 5, of the brief.

The Acting Chairman: Thank you. Perhaps I should read page 5, paragraph 13, of the material submitted. It reads as follows:

> Part I, Section 6 of Bill C-197 . . .

That is not the bill before us.

Senator Goldenberg: That is the original bill.

The Acting Chairman: Yes.

> . . . should include as a duty the periodic assessment of the work of the council and its agencies, to be reported to parliament.

Senator Grosart: That is in the bill now.

The Acting Chairman: Yes. Paragraph 15 states:

> In Part I, Section 8, paragraph 2, this paragraph should be changed to read "A public hearing *must* (not may) be held."

Senator Grosart: I wonder if I might ask the deputy minister what section that comes under now?

Senator Goldenberg: It is clause 8, subclause (2) on page 9.

Senator Grosart: It now reads "shall be held . . .".

Senator Goldenberg: The suggestion is that it should read "must" instead of "may".

Senator Grosart: But it now reads "shall be . . .".

Senator Goldenberg: That is clause 8 subclause (1). Clause 8 subclause (2) reads "may . . .".

The Acting Chairman: There may be a technical point with respect to this which perhaps can be dealt with by the deputy minister.

Mr. Phillips points out the following portions of the telegram which came from Mrs. Brechin yesterday, and I quote from the telegram: . . . the legislation fails to provide for consumer representation upon or public scrutiny of the agencies which may be established under this act. It also fails to provide for the right of appeal from any actions taken by such agencies.

We have had discussion on both of those points. What is the view of the committee with regard to these representations? Does the committee feel we have dealt with the issues put forth by Mrs. Brechin?

Senator Grosart: Perhaps we can take them up when we deal with the bill clause by clause.

The Acting Chairman: Yes, certainly.

I referred this morning to the fact that I had received a telephone call from a Mr. John R. Stewart of R.R. 6, Strathroy, Middlesex County. He described himself as an independent dirt farmer and suggested he would like to make a five-minute presentation to the committee. What

are the views of the committee with respect to Mr. Stewart's representations?

Senator Buckwold: I would suggest, Mr. Chairman, that if he wishes to make representations to the committee he should do so in writing as soon as possible.

The Acting Chairman: I will have the Clerk of the Committee convey that message to Mr. Stewart.

Senator Grosart: It might be pointed out to Mr. Stewart, so that he will not think we are making it impossible for him to get his views before this committee before our decision is made, that if he has views which were found acceptable they could be discussed on third reading, in the event that this committee has reported in the meantime.

The Acting Chairman: That is on the record, and the clerk will convey that message to Mr. Stewart.

Senator Buckwold: I wonder if a telegram could be sent to him to that effect.

The Acting Chairman: Yes.

What is the committee's views as to further proceedings? The minister, the deputy minister and Mr. Phillips are now present. Shall we now proceed to clause-by-clause consideration?

Some Hon. Senators: Agreed.

The Acting Chairman: The copy of the bill that we will deal with is the copy as passed by the House of Commons on December 31, 1971, and I understand that all senators have a copy of that bill.

Senator McElman: For the record, Mr. Chairman, it was passed on December 30, not December 31.

The Acting Chairman: It should read December 31, not December 30. That was a typographical error and Senator Langlois corrected it.

Senator Grosart: Also corrected was another typographical error on page 2, the third line, where the number "17" was omitted.

The Acting Chairman: Yes.

Senator Langlois: That was corrected by amendment in the other place.

The Acting Chairman: Yes, and it was not reflected in the printing.

Senator Langlois: It was in the insert of the bill.

The Acting Chairman: Yes.

Mr. Olson, do you have any opening remarks you wish to make to the committee?

The Honourable H. A. Olson, Minister of Agriculture: Mr. Chairman, I do not think there are any other general observations that I wish to add to the comments that I made when I was here last.

The Acting Chairman: Shall we consider the bill clause by clause, then?

Some Hon. Senators: Agreed.

The Acting Chairman: Clause 2, paragraph (a), "agency"?

Hon. Senators: Agreed.

The Acting Chairman: Paragraph (b), "Council"?

Hon. Senators: Agreed.

The Acting Chairman: Paragraph (c), "farm product"?

Senator Grosart: I should like to put the first question to the minister. First of all, our thanks to you for coming before us again, Mr. Olson. We appreciated your enlightenment on New Year's Eve, and I am sure we will be in a position to appreciate the enlightenment you will give us today. What is your interpretation of the word "natural" in "natural product" in clause 2(c)?

Hon. Mr. Olson: My interpretation is that it is an agricultural product in the form before it is processed.

Senator Grosart: But this would include beef and animal products as well as products of the soil.

Hon. Mr. Olson: Yes, of course.

Senator Grosart: I ask that because there seemed to be some confusion in the other place.

Hon. Mr. Olson: That is why we put in the words "and any part of any such product", because I suppose it is, in practical terms, far more usual for parts of animals to be cut up and sold rather than parts of most other agricultural products. Usually when grain, field crops or fruits and vegetables go to the stage where there are parts of them, there is other processing involved. Quite often, for a very large part of the trade it is done without further processing, except taking it apart.

Senator Grosart: I cannot quote the clause immediately, but the bill would seem to provide for control over processing.

Hon. Mr. Olson: Yes, it does. Further on that can be provided under what the marketing plan is capable of dealing with, in clause 2(e).

Mr. S. B. Williams, Deputy Minister, Department of Agriculture: It is in the definition of "marketing plan".

Senator Grosart: Would it be correct to say, Mr. Minister, that a natural farm product is what is normally meant by a farm product?

Hon. Mr. Olson: I would think so.

Senator Grosart: In its natural state?

Hon. Mr. Olson: Yes.

Senator Grosart: But the bill does provide that a plan can control the processing at some later stage.

Hon. Mr. Olson: Yes.

Senator Grosart: Mr. Minister, I am still very much concerned with this "or otherwise" phrase.

Senator Phillips: Before we come to that, might I ask the minister again to interpret for us what is meant by "the Governor in Council is satisfied"?

Hon. Mr. Olson: In this respect the words "Governor in Council" are put in there because before a marketing plan can be approved under the provisions of this bill, there would of necessity, under clauses, 17 and 18, I believe, need to be a proclamation by the Governor in Council to establish that marketing plan for the commodity involved. Therefore, the Governor in Council, under clause 2(c)(ii), must be satisfied prior to making that proclamation that the provisions contained in that clause have been complied with.

Senator Phillips: I am more concerned with the word "satisfied" than with the words "Governor in Council". If you will allow me to ask the question in a somewhat facetious manner: what would satisfy this Governor in Council?

Hon. Mr. Olson: The Governor in Council would have to be satisfied that, as a result of declarations by provincial governments, either by plebiscite or otherwise, a majority of the producers were in favour of the marketing plan for the commodity involved.

Senator Grosart: Mr. Minister, my concern about the phrase "or otherwise" is purely a matter of draftsmanship. I am not going into its implications at all. It seems to me the intent was that "or otherwise" should qualify "plebiscites". I think that was your evidence before.

Hon. Mr. Olson: Yes.

Senator Grosart: My concern is that this might be interpreted, and probably would be in the normal syntactical interpretation, as qualifying the whole phrase "as a result of declarations by provincial governments following plebiscites". If the comma was taken out after "plebiscites" I would have no problems. What concerns me is that the whole intent of clause 2(c)(ii) might be upset by a court if it said that this means any natural product of agriculture and any part of any such product in respect of which the Governor in Council is satisfied, as a result of declarations by provincial governments following plebiscites, or if satisfied otherwise, in another way. I hope honourable senators will look hard at this, because it is surely one of our functions as a Senate to make sure, to the extent that we can, that there should be no ambiguity in the wording. Would you object to that comma coming out?

Hon. Mr. Olson: I am not sure that I would object to it coming out if people learned in the law are having any difficulty with it. However, i should like to draw to your attention that all of the words "as a result of declarations by provincial governments following plebiscites" are contained within the two commas. Therefore, the "or otherwise" contained between the next two sets of commas would, in my view, and could modify that which is contained between the previous two commas. It seems to me that if the comma were to be moved so that the modifier was specifically for the word "plebiscites" and not what is contained now in total between those two commas, we would have to take it out and move it perhaps to between the words "governments" and "following".

However, I would like to draw this to your attention, because I think it is extremely important. When we are talking here about a majority of producers and relating this to the supply management features that would be the imposition of quotas on production or access to markets within intra-provincial trade, and so on and so forth, all of that constitutional jurisdiction, in my view—and it is the view of the Government—lies within the provincial jurisdiction. Therefore, whether it modifies "declarations" or not, certainly there is no way that the federal Government can impose quota control or access to market control without a delegation of authority to the marketing agency set up coming from the provincial government.

It seems to me, therefore, to follow that it is somewhat less important whether the communication to the Governor in Council, to their satisfaction, comes as a result of a declaration or a plebiscite, or any modification of those. For example, instead of a declaration a provincial government may, if they choose, provide us with a complete detailed result of the vote they have taken, or a complete detailed result of such things as a series of public hearings and so forth. The essential point here is that there could be no action taken in any event unless the provincial government itself was prepared to delegate the authority that is required to make those clauses of this bill, or the provisions of any marketing plan with supply management features, operative.

My problem is this. This bill, as I have pointed out, was drawn very, very carefully, so we must first of all satisfy the Governor in Council that there is a majority of all of the producers, an overall majority of the producers in Canada, that there is majority support for a marketing plan, and, indeed, the terms and conditions of that marketing plan in so far as the provinces are concerned. Once we have established that there is an overall majority, then we have to go back again and examine the ambit of the provincial jurisdiction, which would require those provinces also to be satisfied, for the delegation of their own authority under their own statutes, that there was a majority of the producers of the product in their province in favour of it. That is why we believe, and I have been so advised by the Department of Justice, that we must not attempt to write into a federal statute terms and conditions under which provinces administer their own law. That is the problem that I have when attempting to modify this particular clause in that respect. I understand your problem. You are wondering whether the "otherwise" could modify only "plebiscites" or the determination by plebiscite.

Senator Grosart: That is right.

Hon. Mr. Olson: Or Wheter it could modify the word "declarations".

Senator Grosart: That is right.

Hon. Mr. Olson: I really cannot see the importance of that, and I say that with all respect. However, they communicate it, their indication that there was a majority of the producers in favour of the plan. It would also have to follow that the province itself, through its own legislation, is obliged to delegate the authority for supply management to the national marketing agency. So I fail to see the significance of it.

Senator Grosart: Mr. Minister the significance that I see is in two parts. The first is that the House of Commons, in its wisdom, thought it was necessary to make this amendment. It does not seem reasonable to say that it does not matter whether it is ambiguous or not. The second reason is that, surely, we have a duty here.

The Acting Chairman: That is not what the minister said. He did not say it did not matter that it was ambiguous.

Senator Grosart: The minister said, as I understood him, that whether my point was valid—that it is ambiguous, or not—was not important because the act as a whole removed any problem. That is my understanding of what he said. Surely, this is not a principle of the drafting of legislation. I suggest that if there is any ambiguity—and I think the minister agrees that there may be ambiguity—it is our responsibility here to remove that ambiguity. The minister, as I understood him, said today, that he felt that "or otherwise" qualifies the whole phrase "as a result of declarations by provincial governments following plebiscites". I understood him to say that—I may be wrong—and I also understood him to say the very opposite, when he was before us on New Year's Eve. I am only speaking to the point of unambiguity here.

Let me quote it. I said to the minister:

> Yes, but what I am asking, Mr. Minister, is this. Is a declaration by a provincial government a requirement or condition before one of these products can be described as a farm product within the meaning of the act?

And the minister's reply, as reported, is:

For the purposes of this act, yes.

If that is so, surely "or otherwise" cannot qualify that whole phrase. If the minister agrees that a declaration by a provincial government is a requirement or condition, then surely we have an ambiguity. I will ask him again. In his view, is his answer to my question correct?

Hon. Mr. Olson: Well, Mr. Chairman, certainly it is correct, I would like to draw to Senator Grosart's attention that what is written in clause 2(c)—he referred to the House of Commons having felt it necessary to amend the bill—in this particular part of it, was not really an amendment to the substance of the bill. I made that very clear, I think, on New Year's Eve when I was here, that what was written there was really a repetition of what was already in clause 17.

Senator Grosart: This is what worries me. My suggestion is that it is not a repetition of what was in clause 17, because clause 17 would not, as I read it, provide that a declaration by a provincial government is a requirement before one of these products can be described as a farm product within the meaning of the act, and those are the minister's words.

Hon. Mr. Olson: Mr. Chairman, clause 17 says, firstly, that the Governor in Council may by proclamation—I will not read all the words, but the operative words get down to, after the word "act" in line 21—"where he is satisfied"—and referring to the Governor in Council—that the producers of the farm products, of each of the farm products in Canada, is in favour of the establishment of an agency. You have to read that also with clause 17(2), where the Governor in Council, in order to determine whether a majority of producers of the farm product are in favour of establishing an agency, "may request"—and I was very careful to put "may" there, not "shall", demand or impose on provinces ways and means by which they administer their legislation—that each province carry out a plebiscite. It seems to me that these words in clause 17(2) were words that are permissive, that they may request, that it is not mandatory that they demand of the province, that it is completely consistent with what is in clause 2(c).

Clause 2(c) is essentially the same in practical terms, except that it deals with it at a different stage, on the procedure for setting up a marketing agency, that is, the definition of a farm product. I am really not very concerned about whether or not we can define a farm product for the purposes of this act, if we have not already complied with the requirements of setting up a marketing plan which is contained in the provisions of clauses 17(1) and 17(2) which, in my view, are exactly the same.

It satisfied some members of the House of Commons and some other people that we wrote the same provisions in practical terms in two or three places. In my view, not only in practice but in law, what it means is a repetition of the same thing that was there before.

Senator Martin: That is the position taken by your lawyers?

Hon. Mr. Olson: Yes.

Senator Grosart: Mr. Minister, I am afraid I have to say that I do not agree with you that it is not a fundamental change, but I will not argue it at the moment. The observation that this was the position taken by your law officers does not impress me, either, because otherwise we would not have had the hundreds of cases before the Supreme Court trying to interpret statutes. Our job here is to try to make the statutes unambiguous.

May I ask you again, then, Mr. Minister, in your view does clause 2(c)(ii) make it mandatory that there be a declaration by a provincial government before a product, other than eggs and poultry, can be a product within the meaning of the act?

Hon. Mr. Olson: It does, and what is even more important, the provincial government under its own law, must be satisfied of that position, before they can delegate the authority to a national marketing board to operate a plan wherein a farm product is defined and acceptable under the provisions of this bill.

Senator Grosart: I am not concerned with that aspect of it. I am concerned only with whether a declaration by the province is now mandatory before any other farm product can be brought under this act.

Hon. Mr. Olson: In my view, it is, yes.

Senator Grosart: Which would seem to be—if I may finish—at variance with what I thought was your statement that "or otherwise" qualifies the whole phrase "as a result of declarations by provincial governments following plebiscites".

My suggestion is that what you now say makes it very clear that it qualifies the word "plebiscites" only, and I will say no more.

Senator Forsey: Mr. Chairman, if I am not mistaken, in the absence of clause 2(c)(ii), clause 17(2) would not require any declaration by a provincial government at all. I understood the minister to say that clause 2(c)(ii) really just said again what clause 17 says, but it seems to me that in fact it says something rather different because it says in clause 17(1), "where he"—the Governor in Council—"is satisfied". There is nothing about declarations. In clause 17(2) there is provision for a request to the provincial government to hold a plebiscite. But there is not a word about declarations in that whole clause, as it seems to me. Therefore, it seems that clause 2(c)(ii) does contain something new in mentioning declarations.

The Acting Chairman: Would you hear Mr. duPlessis on that?

Mr. duPlessis: However, the words "farm product" are use in clause 17(1) and, therefore, the whole of the meaning of the words "farm product" is incorporated in subclause (1) of clause 17.

Senator Forsey: Quite, but my point is that I understood the minister to say that clause 2(c)(ii) did not add anything, did not change anything, but that it merely said over again what was in clause 17. It seems to me that it does not simply say over again what it says in clause 17.

Hon. Mr. Olson: There was one other qualification to my comment, Senator Forsey, and that was "in practical terms". I am not a lawyer; I am a dirt farmer.

Senator Grosart: Mr. Chairman, I move the deletion of the comma after the word "plebiscites". I hope the minister will accept that. I do not believe under our practice that it would be necessary for this to go back to the House of Commons. I think it could be regarded as a typographical change just to clarify the meaning.

Senator Langlois: That is a new concept to me.

Senator Grosart: No, we have had that before.

Mr. duPlessis: I have just one comment to make in that connection, Senator Grosart. It is my understanding that it is a generally accepted principle of the interpretation of statutes that punctuation does not form the basis of the interpretation of statutes.

Senator Grosart: That is a principle which has many qualifications in its application. It is a long time since I spent any time on the interpretation of statutes, but that is a rather bald statement that would require a great deal of qualification, because there are cases that I know of, although I cannot recall any specifically, where the whole case revolved around punctuation. Surely, punctuation is one of the ways in which we make our meaning unambiguous. That is one of the purposes of punctuation.

The Acting Chairman: It helps the structure of language, but I think the problem is the effect in law, and Mr. duPlessis, as a representative of the Department of Justice, has given his opinion, which the committee will have to assess in its approach to this.

Senator Grosart: What is his opinion?

The Acting Chairman: That the punctuation does not affect, in law, the interpretation of this clause.

Senator Grosart: I would ask Mr. duPlessis if he makes that statement without qualification as to the rules of the interpretation of statutes.

Mr. duPlessis: It was not a considered opinion, Senator Grosart. I would be glad to look into the matter and report back, just to confirm it.

Senator Grosart: Would the minister accept the amendment? If, as you say, punctuation does not affect the interpretation of statutes, can we have an opinion as to whether, if the minister accepted this amendment, it would be necessary for the bill to go back to the House of Commons? I am asking for a legal opinion.

Senator Martin: It changes the meaning. Obviously, it has to go back.

Senator Grosart: But our expert says that it does not change the meaning.

The Acting Chairman: Order, please. I would hate to see this Senate committee flounder on a question of whether a comma should or should not be in this clause, in view of the opinion given by the representative of the Department of Justice. I think I should point out that the minister is pretty well bound, as a member of a government, by the legal advice tendered by the Department of Justice, by the Attorney General of Canada and by the law officers of the Crown.

You may ask the minister if he would accept the opinion, Senator Grosart, but I think the minister, on a technical point like this, probably has to look to his advisers, and his advisers tell him that this is the way the thing should be written. This is the way it has been written. I think it is up to the committee to decide, then, whether the clause should be changed.

Senator Grosart: Well, there is a motion to that effect.

The Acting Chairman: All right. Let me put the motion. Senator Grosart moves that the comma after the word "plebiscites" on line 25 of the first page of the bill be deleted. What is the view of the committee? Those in favour of the amendment please raise their hands. There are three. Those against the amendment please raise their hands. There are ten. I declare the amendment lost.

Senator Molgat: Mr. Chairman, on the overall question of subclause (c) I have some questions to ask for the purpose of clarification. I had undertaken to speak to a number of people in Manitoba, and in the west generally, who were interested in the bill in order to get their points of view. A number of questions arose with respect to this clause, and I should now like to have some clarification from the minister on subclause (c).

A number of rapeseed growers were interested to know whether this clause 2(c) would include rapeseed.

Hon. Mr. Olson: Yes, under Part I, as has been pointed out to me, for the purposes of making inquiries and that sort of thing, it would, because rapeseed would be a natural product of agriculture. But, of course, rapeseed could not be included for the other clauses of the bill unless and until there was, first of all, as I pointed out, a majority support of the growers and then a further action by Parliament to name that commodity.

Senator Molgat: But rapeseed under clause 2(c)(ii) is a farm product.

Hon. Mr. Olson: I think so, yes.

Senator Molgat: Fair enough. The next question I was asked was what effect, if any, did this have in so far as the Wheat Board is concerned?

Hon. Mr. Olson: The Wheat Board is specifically excluded from this entire bill under clause 17(1).

Senator Molgat: My next question has to do with the definition of "producers." We had some discussion about this last week when we were in committee, but the association and groups to whom I spoke were concerned about this matter of definition of producers. They were concerned with the idea that various provinces, individually, would have the right to determine what a producer is, because that could lead to some very difficult problems when trying to ascertain what is in fact the national point of view of the producers.

Hon. Mr. Olson: Here we run into essentially the same problem that we were discussing a few moments ago, that is, that the producers for the purposes of voting, for example, and the qualifications of individuals, are determined under the provisional regulation. I am sure that the specific definition of each producer is not contained in the provincial legislation, but there are provisions so that they may set down the qualifications of who is a producer for the purposes of voting and that sort of thing. We are in the position where we do not believe that it would be proper for the federal Parliament or the federal Government to attempt to set the qualifications for a plebiscite, for example, that would be carried out under provincial law. But I want to say, too, that there is broad general agreement among the provinces that when we reach the stage where we write a marketing plan for a commodity they would move to have, if not complete uniformity, reasonable uniformity of the definition of the producer for those purposes.

Senator Molgat: Because of the objections and the expressions of concern which I had from most of the people with whom I spoke on this, I thought it necessary to point out the objections at this time. It will probably help later to refer back to the discussion which was held today.

Hon. Mr. Olson: We can do that, but I really very seriously question whether, if we did refer back to it and tried to write a law which would impose qualifications on the administration of provincial law, that would be constitutional. I am afraid it would not be.

Senator Molgat: I will come back to it again on 17(2) anyway. There was also considerable concern expressed by a number of the associations about the expression "otherwise". I know what the minister's explanation is since he has made it, and I shall not ask him to repeat it. But I want to point out that the group for whom I spoke is concerned about that term and by and large would definitely prefer a clear-cut plebiscite.

Hon. Mr. Olson: Are they aware of the constitutional difficulties? I simply want to repeat that I do not believe it would have any effect, even if it was mandatory in this law, as an imposition on how the province should administer its laws.

Senator Molgat: Then there is a question of clarification of the term "majority of the producers". Would that mean a majority of the producers and not necessarily a majority of those voting?

Hon. Mr. Olson: Well, a majority, under ordinary democratic procedure, is of those voting, is it not?

Senator Molgat: There is a very great difference between a majority of producers and a majority of those voting. This is a very important point so far as this bill is concerned. We had exactly that problem in Manitoba when setting up our marketing board legislation there. Originally, we were operating on the basis that there had to be a 66 2/3 per cent majority of those voting. But here you say "a majority of the producers", and on that basis I assume you mean that we register in a province all of the producers and then when the votes are cast it must be a majority of the producers and not just a majority of those voting.

Hon. Mr. Olson: Of course, this would be contained in the communication we would receive from the provinces because they would be conducting whatever procedures they decided on making a communication to us that a majority of the producers in that province are in favour of it.

Senator Molgat: Well, I want to be sure we are talking about the majority of producers and not the majority of those voting.

Hon. Mr. Olson: I understand very clearly the point you are making, but here again, if a province advises us that a majority of the producers is in favour of a marketing plan for that commodity, I think that is about as far as the federal Government can go.

Senator Molgat: I presume that the provinces would have to adhere to this clause which says "the majority of the producers", and possibly legal counsel can address himself to this. It is my interpretation that the majority of producers would not necessarily be the majority of producers voting. This can be a very important distinction.

The Acting Chairman: It seems to me that the clause speaks for itself, and I think Senator Molgat's interpretation—and this is only an opinion—is the one that would govern because it does say "majority of producers".

Senator Goldenberg: It says the same thing in clause 17(1).

The Acting Chairman: Shall subclause (c) carry?

Hon. Senators: Carried.

The Acting Chairman: Then we come to subclause (d).

Senator Phillips: Mr. Chairman, this, to me, gives the council authority to establish packaging plants. Now, for the moment, I shall deal with eggs. Is it necessary to give the council authority to set up grading stations when producers such as our witness this afternoon and many others have their own grading stations, and these grading stations are constantly under inspection by the federal Government?

Hon. Mr. Olson: Well, Mr. Chairman, I would like to draw to your attention that what we are talking about in clause 2(d) is a definition of marketing, and in that particular context it is very clearly stated in line 6 that this definition is in relation to any farm product that is not a regulated product. Any regulated product, of course, and the terms and conditions and all the other parts that would be administered—that is, parts of the marketing system—would be provided for within the marketing plan which comes under the next clause. This does not deal with regulated products in so far as defining what marketing means for the purpose of interpretation under this bill.

The Acting Chairman: Shall subclause (d) carry?

Hon. Senators: Carried.

The Acting Chairman: Then we come to subclause (e).

Senator Grosart: I have a question, Mr. Chairman. I would like to ask the minister, in view of the very extensive powers granted under a marketing plan which can be proclaimed by the Governor in Council, if there is any recourse by a complainant—and I am aware of clause 7(f)—other than to the agency or to the Counsil? Where a complainant feels he has been unfairly treated in the matter, let us say, of the exemption of persons under subparagraph (i) or the cancellation of a licence under (v) or under (vi) or any other matter, has he any recourse other than to the agency or to hope that the council will make an inquiry under 7(f)? Has he any other recourse, in law, if he feels he is unfairly treated by an agency?

Hon. Mr. Olson: There are several here, Senator Grosart, and I am advised that in clause 8(1)(c) the minister may order them to hold a public hearing.

Senator Grosart: "May".

Hon. Mr. Olson: No, it says "shall" in clause 8(1), and that is in the first instance of making inquiries for the purpose of setting up, but I think you have to read that along with 8(1)(c)—

Read altogether, it provides:

> A public hearing shall be held by the Council
>
> (c) in connection with any other matter relating to its objects if the Governor in Council or the Minister directs the Council to hold a public hearing in connection with such matter.

Of course, that is broad enough to include appeals by individuals who may feel that they have been aggrieved. Of course, clause 7(1)(f) specifically spells out that within the powers of the Council the following is provided:

> shall make such enquiries and take such action within its powers as it deems appropriate in relation to any complaints received by it—

The wording is "any complaints received by it from any person who is directly affected". If all those are read together, firstly, anyone who feels they have a complaint can appeal to the marketing board. If they are dissatisfied with the result they can appeal to the National Council, which has an obligation to supervise and keep under constant review all the orders. If a complainant still feels he has not received justice, he has an appeal to the minister, who has the power to order an inquiry on any other matter relating to the operation of the marketing agency.

Senator Grosart: I was aware of those provisions of the bill. My question, however, was: Has a complainant recourse, other than to the agency and the Council—in which I will include the minister because he has the power to order an inquiry, but the decision would still be made either by the Council or the agency—has he recourse other than to the agency or the marketing board?

Hon. Mr. Olson: I suppose you are referring to recourse to the courts?

Senator Grosart: Yes.

Hon. Mr. Olson: I do not think there is anything in the bill that bars recourse to the courts. Although I am not a lawyer, I think that anyone has recourse to the courts with regard to any statutory matters unless it is specifically prohibited or prevented in the act. Therefore, obviously, he would have recourse to the courts.

Senator Grosart: Very good.

Senator Phillips: We are overlooking the fact that the farmer could lose two crop seasons while the court case is being heard.

Hon. Mr. Olson: Well, I am sure you would not expect any comment from me with respect to the administration of the judiciary system.

Senator Phillips: No, I am pointing out the difficulty of the farmer under the present system.

The Acting Chairman: Is clause 2(e) carried?

Senator Phillips: No, I have a question. Clause 2(e)(iii) gives the Council authority to establish class, grade and price. On New Year's eve the minister stated that he hoped that potatoes would soon come under this bill. Traditionally, New Brunswick and Prince Edward Island potato producers have received a higher price for their products than those in central Canada. I wonder how the present system will work and if that differential can be maintained?

Hon. Mr. Olson: We must bear in mind that we are considering the definition of a marketing plan. The marketing plan itself, obviously, could take all those traditional differentials into account. It would, of course, have to be agreed to by the provinces in any event before it could become operative.

Senator Phillips: In other words, the provinces to which I referred would have to approve the price structure before the marketing plan could go into effect?

Hon. Mr. Olson: Yes, and also the other provisions, because they would have to delegate their authority under provincial law to be administered by the National Marketing Board or agency established for the purposes of administering the agreed upon marketing plan.

The Acting Chairman: Is clause 2(e) carried?

Senator Grosart: I have one question. This being the definitive section, I wonder if I could ask the minister if consideration was given to including a definition of producers?

Hon. Mr. Olson: Yes, there was some discussion regarding that, but we decided, or concluded that it would probably be duplication, involving the risk of it differing to some degree from the definitions set down by the provinces and we should leave the definition to them.

Senator Grosart: In your view, would that aspect of the dedication of authority be exclusively within the provincial jurisdiction?

Hon. Mr. Olson: In so far as the supply, management, control and all other items within provincial jurisdiction, the answer is yes.

The Acting Chairman: Is clause 2(e) carried?

Hon. Senators: Carried.

The Acting Chairman: Is clause 2(f) carried?

Hon. Senators: Carried.

The Acting Chairman: Clause 2(g).

Senator Forsey: Is there a definition of the word "region"? We find elsewhere the word "area". Is there a definition in the bill, or is there a judicial definition?

Hon. Mr. Olson: I cannot answer as to whether there is a judicial definition. Our concern is that in the matter of setting out or delineating geographical regions, political boundaries do not always and, in fact, very seldom do delineate the production regions of a commodity which would be involved. It seemed that region would be broad enough that it could be an area that would transcend provincial boundaries in the event there is production on both sides of borders. It must always be borne in mind that provincial jurisdiction covers up to and only up to their borders.

The Acting Chairman: Is that clause carried?

Senator Grosart: Could I ask a supplementary question of the minister? Is there any significance in the fact that the word "area" is used rather than "region" in one of the amendments, which now appears as clause 24?

Mr. Williams: A different word was chosen for clause 24 in the event that you might not wish to have the geographical, and I am going to have to use one of those words, areas or regions coincide under these two separate parts. In other words, you might wish to use a different area for the allocation of quotas to the region that was used in this portion of it.

Senator Grosart: Good, I am satisfied.

The Acting Chairman: Shall clause 2(g) carry?

Hon. Senators: Carried.

The Acting Chairman: Honourable senators, this morning Mr. Atkinson, who appeared before the committee, promised to leave a memorandum with regard to his views. I notice that the first clause to which he refers in the memorandum is clause 3(1), which we are now approaching. I have had his suggestions copied and will ask Mr. Coderre to have them circulated to the members of the committee.

Part I. Shall clause 3(1) carry?

Senator Molgat: Mr. Chairman, this morning a request was made of the deputy minister that he comment on certain points made. I wonder if he has anything further to say with regard to Mr. Atkinson's memorandum?

Mr. Williams: No, I do not have anything to add. In fact, Senator McNamara covered very well what I would have said; that is, that there are arguments on both sides of this question. The position in recent years, in most legislation at any rate, has been in favour of this particular wording.

One question was asked with respect to what is done in provincial legislation. We have researched that and the boards, that is the parent body within the province's equivalent to the Council, are always appointed by the Lieutenant Governor in Council. I do not have a complete text of the terms of office, but certainly some are during pleasure. I am talking about the parent board, not the agencies themselves. The body within the province that is equivalent to the council is invariably appointed by the Lieutenant Governor, and at least in some cases the wording says during pleasure. That was part of the other question.

Senator Grosart: May I draw to the attention of the minister the fact that we have had representtions suggesting that there should be consumer representation on the council. What is the minister's view on whether there should be consumer representation?

Hon. Mr. Olson: I would think that every person in Canada is a consumer, to begin with. Therefore all the members would be consumers in the literal definition of the word. I think, perhaps, that what you are referring to more specifically—correct me if I am wrong—is a representative of an organization of consumers. If that is so, and that is what you are referring to, I would have some concern on why it would be necessary to give special consideration to this only in farm or agricultural legislation.

I say that because I do not believe that an organization or even the law with respect to other organizations in Canada specifically provide for representation of some other group setting up the legal status on which they organize themselves to sell their services to the rest of society. I do not know, for example, that labour unions, who will be doing essentially the same thing for their

members as this bill will be doing for agriculture, specifically require the consumers of their services to be represented on their councils. Nor do the other professional societies. I do not believe that doctors, lawyers or anyone else have delegated representation from the consumers of their product or their service administering their organizations.

Senator Martin: That is the point of view of Mr. Kirk.

Hon. Mr. Olson: Therefore I have a great deal of difficulty in seeing why you single out farmers to have people from the other side of the table represented on their side of the table. If we want to have something for the farmers that is consistent with all the other laws and practices that we have had in Canada for years, I do not think they have any more right to be on this council than anyone else. Furthermore, I believe that this bill has enough safeguards in it that the people who are elected to represent the public interest, such as the Governor in Council and Parliament, and so on, are adequately provided for in this bill.

Senator Grosart: My reason for raising the question is that we are dealing with a federal act which will set up control over a product which is most vital in terms of consumer interest, particularly low-income consumers. That is one reason why it seems to me to differ from labour unions, which are not set up under any statutory authority, as such, or provided with this kind of control over their product. Your argument might apply to some professional organization.

Hon. Mr. Olson: Almost all of them, I think.

Senator Grosart: We are dealing here, for the first time in history, with a mechanism for the control of food, which will affect prices, distribution and packaging. That is why I raise the question. This is a different situation. We have had representation by mail and wire from the Consumers' Association asking us to bring this matter to your attention. Those are the reasons why I raise this question.

Senator Goldenberg: Clause 3(1) says that at least 50 per cent shall be primary producers. Is it not likely that if you are going to appoint somebody who was not a primary producer, he would be a consumer?

Hon. Mr. Olson: It is almost mandatory that he shall be a consumer.

Senator Molgat: In respect of the other 50 per cent, they could all be from the Civil Service.

Hon. Mr. Olson: I suppose that legally and technically they could be, but I think it highly unlikely that they would be. This 50 per cent is written in so that a majority will be of the primary producers. If a National Farm Products Marketing Council is to operate effectively, we may also have to look to the people who have great knowledge and trade in the marketing of farm products, who may not necessarily qualify as primary producers but who could make a very valuable contribution to the effective functioning on the marketing side.

Senator Molgat: The intention is to have other people who are knowledgeable in the farm aspect, but not necessarily from the Public Service.

Hon. Mr. Olson: We want the most competent people we can obtain for these positions. Some of these people may not be in the Public Service and not primary producers, but they may have expertise in the marketing of farm products.

Senator Phillips: During my remarks on second reading I stressed some concern that the members would hold office during pleasure. These views have been discussed in committee today, and I do not need to elaborate on them. I still hold my original views in that regard. I therefore move that clause 3(1) be amended by striking out all the words after "office" and substituting therefor "for a period of ten years."

The Acting Chairman: Honourable senators, are you ready for the question?

Senator Grosart: This is one matter that appears in Mr. Atkinson's suggestions.

The Acting Chairman: Yes.

Senator Forsey: May I ask a question of Senator Phillips? Would he not think it advisable to have some provision for removing people who were demonstrably incompetent? It is customary to have something of the kind.

Senator Phillips: I agree with Senator Forsey. Perhaps he wishes to make an amendment to that effect.

Senator Forsey: I am not a member of the committee. I cannot make amendments. I can only ask questions.

The Acting Chairman: Those in favour of Senator Phillips' amendment, please raise their hands.

I declare the amendment lost. Subclause (1) is therefore carried.

Does subclause (2) carry?

Hon. Senators: Carried.

The Acting Chairman: Subclause (3) deals with regional representation.

Senator Molgat: I think this is one that was an amendmentt from the original act, which was a vast improvement so far as we are concerned in western Canada. We would prefer to have the words "try to" in line 23. I hope I can understand the intentions of the minister that the words "try to" will be considered as a clear indication of the wishes of both the House of Commons and the Senate.

Senator Argue: What is a third of a third?

The Acting Chairman: Shall subclause (3) carry?

Hon. Senators: Carried.

The Acting Chairman: Shall subclause (4) carry?

Hon. Senators: Carried.

The Acting Chairman: Shall subclause (5) carry?

Hon. Senators: Carried.

The Acting Chairman: Shall clause 3 carry?

Hon. Senators: Carried.

The Acting Chairman: Shall clause 4 carry?

Hon. Senators: Carried.

The Acting Chairman: Shall clause 5 carry?

Senator Molgat: A question, Mr. Chairman. This is the individual who is to be the executive director or manager, or what-have-you, is it?

Senator Grosart: No, this is a member of the Council.

Senator Molgat: It is a member of the Council that shall be paid a salary. That means one only, I presume.

Hon. Mr. Olson: No. Any member of the council who is not an employee of the Public Service.

Senator Molgat: I was wondering about the use of "a" in that line and "each" in the next line.

The Acting Chairman: Shall clause 5 carry?

Hon. Senators: Carried.

The Acting Chairman: Shall clause 6 carry?

Hon. Senators: Carried.

The Acting Chairman: Shall clause 7 carry?

Senator Grosart: A question, Mr. Chairman.

The Acting Chairman: There is a question on clause 7.

Senator Grosart: Clause (7)(1)(a), the restriction to a written request from an association; Mr. Minister, has consideration been given to the fact that there might be an interest in requesting an agency by a group who are not members of an association? The written request to initiate proceedings to set up an agency seems to be limited to an association. Is there any reason for that?

Hon. Mr. Olson: Discussions as to whether or not an agency ought to be set up is, of course, a matter that is generally the subject of a great deal of public debate and discussion among members or producers over a long period of time. Inasmuch as there are associations respecting a great many farm products and certainly all major farm products, until and unless they persuade at least one association that they should make a request, it would not be particularly widespread. Line 17, Senator Grosart, states that the council may, on its own, initiate an inquiry into the merits, so it is covered in any event.

Senator Grosart: But such a group wishing to initiate proceedings would have to form themselves into an association, would they not?

The deputy minister is shaking his head, but would they not have to form themselves into an association to come under clause 7(1)(a)?

Hon. Mr. Olson: Yes, but my point is that those associations already exist. For example, swine producers have an association, poultry producers have an association, and so forth.

The Acting Chairman: Shall clause 7 carry?

Senator Grosart: Not all of clause 7, no.

Senator Phillips: Mr. Chairman, could I have an explanation on clause 7(1)(a)(ii)? I am concerned with the broadening of the authority, and whether any additional products can be taken in under the act in this regard?

Senator Grosart: Mr. Chairman, I have a question and an amendment before we get to subclause (2).

Senator Phillips: I yield.

Senator Grosart: Clause 7(1)(f) . . .

Senator Phillips: I am on paragraph (a)(ii) of clause 7(1), Senator Grosart.

Senator Grosart: I am sorry; I thought you were going on to subclause (2).

Hon. Mr. Olson: The explanation to Senator Phillips' question respecting subclause (1)(a)(ii) is that a marketing agency or plan can, of course, be set up with limited powers, limited to such things as promoting the sale of a product, taking fees for the financing of such an agency or commission, and so forth. There are a wide variety of limitations that would be much short of a complete supply management and quota controlled plan. Therefore, if an existing agency is to broaden its authority it must come back to the council for approval, if you will, and the rest of the procedures under clause 2.

Senator Phillips: Yes, but I have some concern, Mr. Minister, with this clause granting the agency authority to expand without coming back to Parliament, which, as I understand it, was the intention of the act.

Hon. Mr. Olson: If a plan was set up that did not include supply management control in all of its aspects without the expressed determination by Parliament that it should have those powers, then, of course, it would not be legal. If Parliament had granted those powers in the first instance and the plan was even more limited than the extent of those powers, then I do not suppose they would have to come back to Parliament to ask for reaffirmation of what it has already said. However, if you set up some type of commission or agency which fell short of the limitations that are provided for under clauses 2, 17 and 18, then, of course, you could not expand the powers to include supply management without an action by Parliament.

Senator Grosart: Just to clarify that: In the statement you just made, Mr. Minister, is your interpretation of this that if an existing agency wished to broaden its powers to take in a farm product not originally under the agency it would then require a declaration by the province?

Hon. Mr. Olson: It would depend, in most cases, on what the delegation of authority from the province was in the first instance. Certainly, they could not presume to administer authority that they had not been given by the provinces.

Senator Grosart: So that they would require a declaration if they were to bring a product . . .

Hon. Mr. Olson: Not only a declaration, but a delegation of authority.

Senator Grosart: Well, the declaration would assume the delegation.

The Acting Chairman: Shall clause 7 carry?

Senator Sparrow: Under clause 7(1)(a), Mr. Minister, the phrase "significant number of persons" is used. What does "significant number" mean?

Hon. Mr. Olson: This is a significant number of persons who are represented by an association. In other words, to give a hypothetical example, if you had 100,000 people who were growing a product and you had 50 members in the association that would probably not be significant, but if it was substantially more than 50, then it would qualify under a significant number of persons.

Senator Forsey: There would be some discretion in that regard, then? In other words, how many grains make a heap?

Hon. Mr. Olson: Yes, that is right.

The Acting Chairman: Senator Grosart, I believe you had an amendment you wanted to make?

Senator Grosart: No.

The Acting Chairman: Shall clause 7 carry?

Hon. Senators: Carried.

The Acting Chairman: Shall clause 8 carry?

Senator Grosart: We were asked to draw to the attention of the minister, by one of the witnesses, the word "may" in clause 8 (2). The Consumers Association of Canada, in a communication to us, asked that that should read "shall be held . . .". Personally, I would not argue that because the wording of the rest of the subclause puts the discretion with the council. The council must be satisfied, so even the word "shall" would not, in my view, really strengthen it. I just draw it to the attention of the minister.

Hon. Mr. Olson: I think, Mr. Chairman, if I may, I will say that I was present in the room when the submission was placed before the committee with respect to this "shall", and I think that was referring to Bill C-197 of the last session of Parliament. It occurred to me when that was going on that the words now contained there, "shall be held", in line 38 on page 8, satisfied that request completely.

Senator Grosart: But it was pointed out at that time that the "shall" in clause 8(1) refers to an entirely different situation. I am not pressing the point, but we were asked to bring it to the attention of the minister.

Hon. Mr. Olson: The essential point here, I think, is that in connection with an inquiry into the merits of establishing an agency, or even of broadening the authority of an existing agency, and so on, a public hearing shall be held.

The Acting Chairman: Shall clause 8 carry?

Hon. Senators: Carried.

The Acting Chairman: Clause 9, "Public Notice".

Hon. Senators: Carried.

The Acting Chairman: Clause 10, "Rules of Procedure".

Hon. Senators: Carried.

The Acting Chairman: Clause 11, under "Organization", "Head Office".

Senator Sparrow: I should like to ask the minister a question, which he may not be able to answer. Has he at this point given any consideration to where the head office may be located? Is he at liberty to state that?

Hon. Mr. Olson: I think in the initial stages it will probably be in the national capital region.

Senator Martin: You never thought of North Battleford?

The Acting Chairman: In the old days this would include Kingsmere, and perhaps at that time it might have been thought an appropriate place.

Senator Sparrow: When you say it will probably be in the national capital, it sounds from your statement that it will therefore be located in the national capital. I personally would like to see it located outside the national capital.

Hon. Mr. Olson: I think there are a number of reasons. We are not talking about the specific agencies here; we are talking about the national council. There is some significance to a national agency being in the national capital. That is one thing. Clause 13 also states that the council, wherever possible, shall utilize the services of employees within the Public Service of Canada. For keeping the costs down and that sort of thing that would be useful. Furthermore, I think even if you look at Canada, from Newfoundland to Vancouver Island, geographically it is about as convenient as anywhere .

The Acting Chairman: Shall clause 11 carry?

Hon. Senators: Carried.

The Acting Chairman: Clause 12, "By-laws".

Senator Grosart: May I ask the minister his understanding of the word "duties" in clause 12(b), in the fourth line. Is it his understanding that that does not authorize the delegation of powers, only of duties?

Hon. Mr. Olson: I think this is the standard, usual wording respecting the way in which the council must conduct itself while it is making by-laws. I do not think it does anything more than that.

Senator Grosart: I just want it for the record, that it refers only to duties; that it does not give them the right to delegate powers to a committee.

Hon. Mr. Olson: I think that is right.

Senator Grosart: There is one exception, where certain powers are given to two members but they are not designated as a committee.

Hon. Mr. Olson: That is right.

The Acting Chairman: Shall clause 12 carry?

Hon. Senators: Carried.

The Acting Chairman: Carried. Shall clause 13 carry?

Hon. Senators: Carried.

The Acting Chairman: Carried. Shall clause 14 carry?

Hon. Senators: Carried.

The Acting Chairman: Carried. Shall clause 15 carry?

Hon. Senators: Carried.

The Acting Chairman: Carried. Shall clause 16 carry?

Hon. Senators: Carried.

The Acting Chairman:

Part II, "Farm Products Marketing Agencies." Shall clause 17 carry?

Senator Molgat: On clause 17(2), I wonder if I might ask the minister a question. Was there any discussion with the provinces as to whether, in a case like this, where a decision is made to hold a national plebiscite, instead of doing it on a provincial basis that it be in fact a national plebiscite?

Hon. Mr. Olson: I would like to answer the question in this way, that the provinces have been over this bill, I am sure, with a fine-tooth comb, so they are apprised of all of it. To answer that question specifically. I go back to the answer I gave some time ago, that I do not think it came up that it was a desirable thing to do, because we should not try to write a law at the federal level that would fail in so far as the division of powers under the Constitution is concerned. Therefore, in the kind of organization that we have in our country, where we have this division of powers, it was desirable that the provinces should do this and we should be guided by their determination of results.

Senator Molgat: The term "may request," then, means that any or all provinces could turn it down and say they would not do it. They could defy the federal Government and say they would not carry out a plebiscite, and they issue a declaration. Then, what?

Hon. Mr. Olson: They issue a declaration that the majority of their producers are in favour?

Senator Molgat: Yes.

Hon. Mr. Olson: There are at least three provinces whose laws would prohibit them from doing so—Quebec, Alberta and Prince Edward Island. For the rest of them, it is a matter of policy, that they do in fact carry out plebiscites when they move to a marketing plan that includes all the supply management features. I think it is very unlikely that it would happen and indeed in most provinces it could not be operative anyway, because they could not delegate their power without having satisfied themselves that a majority supported it.

Senator Molgat: Is it still left here, even where a request comes from the federal Government that the producer be defined by the province, that it can vary from province to province?

Hon. Mr. Olson: I have to repeat what I said a few moments ago, that it could vary; but, as I said, there has been broad general agreement that there would be very little, if any, variation when it was being put to the producers that this would result in a national plan.

Senator Molgat: My last point comes back to the one I was making on clause 2(c)(ii), that if we are talking about a majority of producers, we are not talking about a majority of those voting?

Hon. Mr. Olson: I think the same discussion that we had a few minutes ago again is applicable.

Senator Molgat: I merely want it on record, because I suspect that this will arise at a later date, and I want it very, very clear at that time what it was that this committee agreed to.

Senator Sparrow: It states, "if the Governor in Council is satisfied that a majority of the producers". To have this satisfaction, you, or the Governor in Council, would be better off, and it would be easier for them to decide, if in fact a plebiscite were held in every province, and that would be a greater assurance for you than having a straight declaration? Is that true?

Hon. Mr. Olson: Mr. Chairman, we are getting back into the area of our trying to interpret how the provinces administer their legislation.

Senator Sparrow: No, I said that for the Governor in Council to be satisfied that, in fact, the request would come under this bill, it would be easier to be satisfied if the Governor in Council knew that a plebiscite had been held. Then, in fact, you would know it was representative of the majority of the producers. If that is the case, then, constitutionally, I would see nothing wrong with saying "shall request" instead of "may request" in clause 17(2), because, in turn, in the rest of the bill they do not have to conform with that. You are not insisting they do, but we are insisting in the bill that you ask them to and, if they say no, that is fine. They can still come under the bill, because they say, "No, we do not want to conform with that." But, at least, then we would be satisfied that the Governor in Council had asked them to have that plebiscite.

Hon. Mr. Olson: Mr. Chairman, all the provinces are familiar with the requirement of what is necessary here for the Governor in Council to be satisfied. If we get a declaration from a province that the majority of their producers are in favour of such a plan, I do not really see that we have any right to challenge it. How can we challenge a bare-faced statement passed to us by the government of a province? The requirement is here. They must advise us of that. We do not set down the terms and conditions of how they reach that determination, but, if a duly-elected government advises us that this is so in their province, I think we have some obligation to accept their word.

Senator Phillips: But, Mr. Minister, you told me earlier that the provinces had a right to agree to the plan. Surely it is not unreasonable for the federal Government to ask them to do certain things before you enter into an agreement with them? If you were buying a house you would

ask that the title be clear. That is not an unreasonable attitude. I do not think it is unreasonable to ask the provinces to have a plebiscite.

Hon. Mr. Olson: Mr. Chairman, that is provided for. It says that the Governor in Council may request such a plebiscite.

Senator Grosart: Mr. Minister, are you not really saying that the declaration that a majority of producers are in favour can be made by a declaration by the province which you will accept, whether it is made by plebiscite or otherwise?

Hon. Mr. Olson: That is right. Exactly.

The Acting Chairman: Shall clause 17 carry?

Hon. Senators: Carried.

The Acting Chairman: Clause 18 deals with the contents of proclamation, alteration and limitation.

Senator Phillips: Mr. Chairman, as I interpret clause 18(1)(a)(ii), it allows the council to designate the amount of the product that can be shipped from one region to another. Again referring to the statement of the Minister that he hoped that potatoes would soon come under this bill, I would point out to the members of the committee that Prince Edward Island and New Brunswick depend to a very, very great extent on potato production, and their largest market is in central Canada. We have an export market for seed, but our largest table stock market is in central Canada. I very much fear that our sale of table stock potatoes in central Canada could be reduced if put on a quota basis under this section. I draw this to the attention of my two colleagues from the Maritimes; and with this in mind, Mr. Chairman, I move that clause 18(1)(a)(ii) be deleted.

Hon. Mr. Olson: Mr. Chairman, I think the conclusion that the proclamation could contain this is, of course, hypothetical and indeed not only is it hypothetical, but it is completely prohibited under subclause (3) of clause 18 except for eggs and poultry products until there is a further amendment by the Parliament of Canada to name any other product including potatoes. Therefore until and unless there was a marketing plan that was agreed to, and under the spirit of this whole act, agreed to by the provinces producing the major part of that product, then of course it could not be done. And Parliament would have to pass an amendment including that commodity.

Senator Phillips: But the amendment could be simply one to define the product it will apply to. The amendment could be made under subclause 2(c) and nothing else changed in the act.

Hon. Mr. Olson: You would have to change clause 18(3) and you would also have to have a provincial agreement to the terms and conditions within the marketing plan which is provided for in clause 2(c) as well as clause 2(e). All of those provisions would have to be met by the provinces involved. Neither the marketing council nor the Governor in Council could of course achieve the situation you describe without the endorsation of the provinces involved and without an act of Parliament.

Senator McElman: Mr. Chairman, is it not a fact that the share of the central Canadian market held by the Maritime provinces has in fact been eroded in very recent years by production from other provinces? And do the provisions of the act not in fact provide some protection for that share as it now exists?

Hon. Mr. Olson: Yes, Mr. Chairman, that is correct. There is, of course, some variation from year to year, but in percentage terms your contention is correct. This bill provides that written into the statutory provisions now, of course, is what would have been done in any event. That is that the traditional marketing patterns would be taken into account over a five-year period in determining the allocation of quotas if a marketing plan arrives at that point.

The Acting Chairman: Senator Phillips, do you propose to press your amendment?

Senator Phillips: No, Mr. Chairman. I will be quite content to have it on the record indicating my concern. I know the amendment would be lost anyway.

The Acting Chairman: Shall clause 18 carry?

Senator Molgat: Mr. Chairman, clause 18(3) is of primary concern to the cattle and hog producers. It ultimately gives them the protection that they will not end up under a quota system. The question was asked of me as to what else could be done to them, apart entirely from the quota consideration? Could they be forced to market to a single agency? Could the whole system of handling be changed by the plan?

Hon. Mr. Olson: Clause 18(3) must be read in conjunction with clause 2(c). That provides that, until and unless we have a majority, farm products could not even be defined for the purposes of this act except for the inquiries section contained in Part I. I would rather doubt that anything beyond that could be done without action by Parliament under clause 2 to arrive at the definition of a farm product with respect to any other product than the exceptions contained therein. Clause 18, which refers to the supply management features, would also require amendment. My interpretation is that very little more than making inquiries would be allowed without amending either one or both of those provisions.

Senator Molgat: So the cattle and hog producers who are concerned by this can be assured that nothing can happen to them under these two clauses until such time as a vote or action under clause 2(c) takes place? Even if that were to occur, they could not be brought under a quota system without a further amendment?

Hon. Mr. Olson: A further amendment to clause 18(3).

Senator Molgat: They would have a double action.

The Acting Chairman: Shall clause 18 carry?

Carried.

The Acting Chairman: Shall clause 19, "Membership of Agencies," carry?

Senator Grosart: Because Mr. Atkinson put down his suggested objections, I want to call to the attention of the

minister that he objects agin to the appointment of members of agencies. I am referring to clause 19, subclause (1), the appointment of members of agencies during pleasure. I think we have disposed of that.

Hon. Mr. Olson: This is a little different, because we are talking about the membership of agencies that would be related very directly to the marketing plan and the provisions of the marketing plan. The marketing plan could easily call for appointment for a specific period of five years or any other period, or indeed during pleasure; but when we get to the appointment of membership of agencies, it is slightly different than the council. When we are talking about agencies there is even a far greater input of provincial jurisdiction than on the council itself.

Senator Grosart: There are other options here.

The Acting Chairman: Shall clause 19 carry?

Hon. Senators: Carried.

The Acting Chairman: Shall clause 20 carry?

Hon. Senators: Carried.

The Acting Chairman: Shall clause 21 carry?

Hon. Senators: Carried.

The Acting Chairman: Shall clause 22 carry?

Hon. Senators: Carried.

The Acting Chairman: Clause 23, "Powers."

Senator Grosart: This concerns the objection I made earlier to clause 23(1)(f), where the agency is empowered to make such orders as it considers necessary. I made the point earlier that it was giving far too much power and was, in effect, removing a legitimate complaint from recourse to the courts, because the answer that could be given is that the agency considered the powers necessary. However, I will not press it.

Hon. Mr. Olson: The answer to this is that the agency does get some discretion here of what it considers necessary, but quite obviously the agency could not exceed, firstly, all the statutory provisions of both provincial and federal law, and, secondly, it could not exceed the delegation of authority granted to them under the terms and conditions of the marketing plan that was agreed to by both levels of government. So they could not really consider it necessary to do anything that would exceed this delegation of authority.

Senator Grosart: This would apply to the delegation in (n) on page 17, where the wording is much better, namely, all such other things as are necessary. Why the two different phrases?

Hon. Mr. Olson: I do not know what to say about that, except that there is a little more redundancy in this bill than in only those two places.

The Acting Chairman: From an abundance of caution, they may have put in more than is required. You find it in the Corporations Act, where we talk about the powers that companies shall have, and we often wonder why. They are basket clauses.

Senator Grosart: I object, on principle, to all such clauses that give any organization or institution which exercises delegated powers the power to decide what they consider necessary.

The Acting Chairman: Shall the clause carry?

Hon. Senators: Carried.

The Acting Chairman: We now come to clause 24.

Senator Molgat: In checking with consumer groups, I find considerable concern about the five-year period, particutahly when it ehhties enross the boerd to etl commodities. The feeling expressed to me was that this might turn out to be of some serious disadvantage in certain commodity areas. Even a group which we have been told is quite anxious to have this bill passed, the broiler chicken group, to whom I spoke yesterday, expressed some concern about this five-year period. They indicated, for example, that if you went on a five-year average with regard to broiler chickens you might put Newfoundland, Prince Edward Island and Saskatchewan in a bad position, because they did not really get into the broiler chicken business in any significant way until the past three years. This could also affect other provinces. Some provinces such as Quebec cut their production substantially as a result of overproduction, and they might end up in a bad position as a result of that.

I spoke to the national president as well as the Manitoba president, and they gave me some figures which I thought were interesting. For example, Newfoundland's production has gone up by 75 per cent; Saskatchewan's production has gone down by 18.3 per cent; ONtario's production went down 2.7 per cent; Quebec went down 14.2 per cent, and so forth. They were concerned that a straight five-year average might put certain provinces at a disadvantage, and, in any case, they felt it was not fair to put a five-year average on all commodities.

Hon. Mr. Olson: I accept all of your arguments, senator, but I reach a different conclusion than you do or do the people from whom you received those representations. If you were to shorten the period, I suggest, it would be even more disruptive. For example, if you took only a one-year average and in the preceding year there was a large increase or decrease, that would not be fair to the traditional marketing patterns. You could also take a longer period. The five-year period is more or less an arbitrary figure, but it seems to me that it is more appropriate than any other. It is the space of time that people who are experts in the business look at, and my conclusion, to avoid even greater disruption in those provinces which may have had a significant decrease or increase in any particular year, was that it would be better for everyone if you took the five-year span.

The next question that comes up—and I certainly do not wish to take too much time on this—is that if you do not use the traditional marketing patterns which, of course, reflect also the traditional producing patterns in various areas of Canada, then what else can you use? There is nothing else to base it on. Frankly, I do not believe you can

take any single year and do justice to the people involved. You may argue that five years is not the right period, but I think it is probably the most appropriate period under the circumstances.

Senator Molgat: It was their feeling that it would be better to leave it to be determined for each commodity, depending on what happened in that commodity and its development in the various provinces.

Hon. Mr. Olson: I do not believe that I can add anything more to what I have already said. You have to try to be fair to people who would be on either side of that argument.

Senator Grosart: That could be dealt with in the amending legislation, bringing in other farm products under the bill.

Hon. Mr. Olson: That is right.

Senator Grosart: It is interesting that the minister used the phrase "marketing patterns", because in his submission to us Mr. Atkinson suggested that that should be the phrase. I think he said "historical marketing patterns" rather than "production". Is there a substantial difference here, in the practical working out of the bill, between basing this five-year average on production and on marketing patterns?

Hon. Mr. Olson: It seems to me that the two are so closely related that obviously if there is a traditional production pattern, if you like, production has found its way into a marketing pattern throughout this traditional period, and they are very closely related. The other problem, of course, is that we do not have data on marketing patterns, if you like, between provinces, but we do have rather carefully compiled data on the production patterns.

Senator Grosart: I just say that Mr. Atkinson seemed to think there was an essential difference. I do not know enough about it to pursue it.

The Acting Chairman: Shall clause 24 carry?

Hon. Senators: Carried.

The Acting Chairman: Clause 25, "Employment of staff".

Hon. Senators: Carried.

The Acting Chairman: Clause 26, "Agency may make by-laws".

Senator Argue: On clause 26, I would like to move an amendment. My amendment would be consistent with the other parts of the bill, namely, that as the bill now stands a majority of the members of the council must be producers, a majority of the members of the agencies must be producers. My proposal is that a majority of the members of the advisory committee should be producers.

I move that paragraph (g) of clause 26 be deleted, and that the following new paragraph (g) be substituted therefor:

> (g) for the establishment of consultative or advisory committees consisting of members of the agency, primary producers, or persons other than members or primary producers, provided that a majority shall be primary producers.

Hon. Mr. Olson: Mr. Chairman, may I speak to that?

The Acting Chairman: Yes.

Hon. Mr. Olson: I would think that inasmuch as these consultative committees or advisory committees will be appointed by the council and agencies that are set up, where there is a requirement that a majority there be producers it is somewhat redundant to require them, who are already producers, to do this.

The other problem, which is more important, is that these agencies or the council may wish to set up, for exemple, technical committees on research and that sort of thing. This is not limited to one committee for each agency; it says "consultative or advisory committees". They may be set up for very specific purposes, to do some examination of a highly technical nature. Therefore, I do not think it would be appropriate that they be required to comply with whatever the interpretation of "producer" is in the event that they were doing a technical study that required people with expertise in that area. Secondly, I think there is ample protection of the producer interest, when in fact a majority of the body appointing them are producers.

The Acting Chairman: Senator Argue, do you press your amendment?

Senator Argue: Yes, I press the motion. All I would say is that if it is a technical committee, a highly technical committee, a sales committee, you name it, I would think there are people in Canada who are producers who are expert in this field. We have had members of the Canadian Wheat Board who are producers, and I think experts, so I still press the amendment.

The Acting Chairman: Is the committee ready for the question?

Hon. Senators: Question!

The Acting Chairman: Those in favour of Senator Argue's motion please raise their hands—Five.

Those against Senator Argue's motion please raise their hands—Eight.

I declare the amendment last.

Shall clause 26 carry?

Hon. Senators: Carried.

The Acting Chairman: Shall clause 27 carry?

Hon. Senators: Carried.

The Acting Chairman: The financial clauses. Shall clause 28 carry, "Conduct of financial operations"?

Hon. Senators: Carried.

The Acting Chairman: Shall clause 29 carry, "Payment by the Minister of Finance"?

Senator Grosart: I wonder if I might ask the minister a question, through you, Mr. Chairman. In clause 29(1), line

3, where the Minister of Finance may make, on requisition of the Minister, grants to an agency, would that include loans?

Hon. Mr. Olson: It could. I suppose it does not say loans, but we have provided here for a payment out of the public treasury for a non-recurring grant for the purposes of meeting the initial operating cost of establishing the agency. In fact, we have another act under which we can guarantee loans to these agencies, which could be for far greater amounts, under a loan basis, than the limit of $100,000 here for the initation costs of setting up an agency.

Senator Grosart: The limitation, then, is as to grants on initiation of an agency?

Hon. Mr. Olson: Yes.

The Acting Chairman: Shall clause 29 carry?

Hon. Senators: Carried.

The Acting Chairman: Shall clause 30, "Audit", carry?

Senator Phillips: Is there any particular reason why this audit should not be carried out under the Auditor General?

Hon. Mr. Olson: It is not normal for an agency—and we are talking about the agencies now, not the council. They will be set up to spend their own funds, not public funds, after the initiation costs. It is not normal that it be mandatory that they do so under the Auditor General of Canada, because they will not be dealing with public funds.

Senator Phillips: For instance, Polymer did not involve a great deal of public funds but it also was under the Auditor General.

Hon. Mr. Olson: But Polymer was a crown corporation. This would not be a crown corporation.

Senator Grosart: It was a crown corporation and it was then subject to the Auditor General. I do not think it is now so subject, since it ceased to be a crown corporation.

The Acting Chairman: Shall clause 30 carry?

Hon. Senators: Carried.

The Acting Chairman: Clause 31, "Report to Parliament". Shall clause 31 carry?

Hon. Senators: Carried.

Senator Buckwold: Mr. Chairman, on Part III, I wonder whether I could move approval of the general clauses, unless any member wishes to deal with a particular question. I think these are basically technical clauses.

Senator Grosart: Mr. Chairman, we have a clause-by-clause motion. Let us stick with it.

Senator Phillips: And I have a couple of amendments.

The Acting Chairman: Shall clause 32 carry?

Hon. Senators: Carried.

The Acting Chairman: Shall clause 33 carry?

Hon. Senators: Carried.

The Acting Chairman: It is carried. Shall clause 34, "Inspectors", carry?

Hon. Senators: Carried.

The Acting Chairman: Shall clause 35, "Powers of inspectors", carry?

Hon. Senators: Carried.

The Acting Chairman: Shall clause 36, "Obstruction of inspector. False Statements", carry?

Hon. Senators: Carried.

The Acting Chairman: Clause 37, "Licence fees, levies and charges". Shall clause 37 carry?

Hon. Senators: Carried.

The Acting Chairman: Clause 38, "Offences and penalties. Punishment". Shall clause 38 carry?

Senator Phillips: Mr. Chairman, in my remarks on second reading I indicated concern that there is no limitation on the type of question that can be asked under clause 7, and that there is no protection provided for the people being asked those questions. After consultation with the legal advisers I have been advised that this would be the most appropriate place in which to move an amendment. The amendment I intend to move is rather lengthy. I have made copies, which I will distribute, if I may, Mr. Chairman.

I now wish to move the following amendment to Bill C-176:

> That the following be added as a new subsection (2) to clause 38 of Bill C-176, the remaining subsections being renumbered accordingly:
>
> "38 (2) Every person who
>
> (a) wilfully discloses or makes known directly or indirectly to any person not entitled to receive the same, any information submitted to the Council or an agency or required to be submitted to the Council or an agency pursuant to a requirement under subparagraph (iii) of paragraph (h) of subsection (1) of section 7 that might exert an influence upon or affect the market value of any regulated product, or
>
> (b) uses any such information for the purpose of speculating in any regulated product,
>
> is guilty of an offence and is liable, on summary conviction, to a fine not exceeding three thousand dollars."

The Acting Chairman: You wish that amendment to be added as a new subclause to clause 38?

Senator Phillips: Yes.

The Acting Chairman: So there is no amendment to subclause (1) of clause 38. Shall subclause (1) of clause 38 carry?

Hon. Senators: Carried.

The Acting Chairman: It is now proposed in amendment by Senator Phillips that clause 38 have added as a new subclause (2) the amendment which Senator Phillips has just read. We will then come to the renumbering of the present subclause (2) as subclause (3). Is that your proposal, Senator Phillips?

Senator Phillips: Yes.

The Acting Chairman: Senator Phillips, do you care to speak on this amendment?

Senator Phillips: I do not think there is very much I can add, Mr. Chairman, other than that I did express concern that various members, particularly of an agency or an advisory board, may come into possession of certain information and that, as the bill now stands, they are under no obligation to keep that information secret. This amendment is, in effect, an application of the Statistics Act or the principle of secrecy of the Statistics Act to this clause.

Senator Grosart: Mr. Chairman, may I point out that Senator Phillips' amendment refers specifically to the requirement in clause 7 that any person may be required to give this information. This would mean that any farmer would be required to give certain information, and it would appear that the purpose of Senator Phillips' amendment is to protect the security of that information that is now required under the bill. That is a fairly drastic requirement. I am not saying that it is not necessary, but it is a fairly drastic requirement that any farmer should be required to give any information at all that an agency asks for.

Senator Phillips: And that information could in fact be his net income for the year, which most people would not care to have fall into other people's hands.

Hon. Mr. Olson: Mr. Chairman, clause 7, of course, deals with the power of the council. And there it is specifically stated in paragraph (h), subparagraph (iii), at the top of page 8, that anyone is required to submit information only "relating to the production or marketing of the farm product by them as it may reasonably require". It does not say anything else, and there remains the interpretation of those words "as it may reasonably require" for the purpose of this act. So there is a very severe limitation.

In addition to that, the members of the council would be appointed by the Governor in Council, and I am not quite sure of this, but I think it is a fact that all appointees of the Governor in Council come under the official secrets requirements on appointment, and that being the case they are already prohibited from doing some of the things under the law that Senator Phillips has referred to.

The Acting Chairman: Surely, there must be some general provision in law with respect to the disclosure of official information? Can you help the committee in that respect, Senator Phillips?

Senator Phillips: Mr. Chairman, I have been trying to help the committee all afternoon, very unsuccessfully, and I wish I could be successful in this case but, unfortunately, I do not think I can.

The Acting Chairman: Would any of the learned counsel members of the committee have any views on this point?

Senator Martin: It would come under Official Secrets Act.

Senator Phillips: Not every employee is governed by that.

Hon. Mr. Olson: Appointees of the Governor in Council are.

Senator Grosart: I would suggest on that, Mr. Chairman, that this is to be found in clause 7(1)(h)(iii) which refers to the powers that may be given under a marketing plan. So these powers could then be given to an agency, and I very much doubt if any existing statute would extend any security regulations to employees of an organization which was so far down the line of delegation as this one is. This does not just refer to the members of the council. If I read the clause correctly, it refers to the powers conferred under a marketing plan. It says in (h): "may, for the purpose of implementing any marketing plan, require persons . . . ." and so on to submit to the Council for the purposes of the marketing plan. So if the council requires it for the purposes of the plan, the plan is the operative instrument of the agency. Certainly I would suggest that this power would, through the marketing plan, be granted to the members of the agency.

Senator Phillips: And the clause specifically states that they will keep books, records, and so on, containing such information as the council requires. It all depends on the type of question required by the questionnaire as to whether or not the information is revealed. We do not know that at present. Therefore I feel it is essential to protect the information given by the individual.

The Acting Chairman: To protect the secrecy of the information.

Senator Phillips: That is right.

The Acting Chairman: Those in favour of Senator Phillips' amendment to clause 38 please raise their hands?

The Clerk of the Committee: Three.

The Acting Chairman: Those against Senator Phillips' amendment please raise their hands?

The Clerk of the Committee: Nine.

The Acting Chairman: I declare the amendment lost. Is clause 38(2) carried?

Hon. Senators: Carried.

The Acting Chairman: Is clause 38(3), "Time limit" carried?

Hon. Senators: Carried.

The Acting Chairman: Is clause 38(4), "Evidence as to geographical origin", carried?

Hon. Senators: Carried.

The Acting Chairman: Shall clause 38 carry?

Hon. Senators: Carried.

The Acting Chairman: Shall clause 39, "Winding up of an agency", carry?

Senator Phillips: Mr. Chairman, I again have an amendment. This will be the last one. I am concerned by the wording of clause 39, wherein is provided:

> The Governor in Council may order any agency established pursuant to this Act to wind up its affairs and may by proclamation dissolve any agency . . .

et cetera.

My objection is that there is no provision, firstly, for the provinces to be consulted. It is a strictly one-sided privilege of the Governor in Council. Parliament does not even have to be consulted. Secondly, I object to the 90-day period. I point out to the members of the committee, Mr. Chairman, that in many cases in which a quota has been established an individual may have, limiting it for the time being to poultry, reduced his flock considerably, and the 90-day period would not afford him time to rebuild it and return to a competitive, free market. On the other hand, if another product, such as potatoes, did come under the act, 90 days would certainly not allow the individual time to resume the position he formerly held before a quota system was established.

Therefore, I move that lines 40 to 43 in clause 39 of Bill C-176 be deleted and replaced with the following:

> but an order or proclamation under this section becomes effective only on the expiration of nine months from the date of publication thereof in the *Canada Gazette,*

The Acting Chairman: That is the gestation period.

Senator Phillips: Yes:

> or such other periods of time from the date of publication thereof in the *Canada Gazette* as is recommended by the Council.

I might add, Mr. Chairman, that the council, if consulted, may be agreeable in certain cases to have periods less than nine months, or it may wish to have a longer period.

Hon. Mr. Olson: I should like to make three points with respect to the proposed amendment. Firstly, the marketing council is obliged under its duties ties and powers in the section 6(2), on page 5:

> (2) In carrying out its duties the Council shall consult, on a continuing basis, with the governments of all provinces having an interest in the establishment or the exercise of the powers of any one or more agencies . . .

Secondly, the period of 90 days is not a mandatory minimum or maximum. It could be more than 90 days. It shall become effective only on the expiration of 90 days. Obviously, it could be much longer than that, even up to what the amendment calls for.

What is more important is that after this obligation to consult with the provinces, the power ultimately rests with the same agency that made the proclamation, which is the Governor in Council. It follows therefore that only the agency or the body, which in this case is the Governor in Council, may undo what it has the power to do; and therefore the power has to be back to the same agency to undo a proclamation it has made.

Senator Grosart: A declaration by the province implies only that the majority of producers are in favour of it.

Hon. Mr. Olson: I think that is right. In putting in this amendment, it would set down terms and conditions that a province could direct what the Governor in Council may do, which is, in fact, to withdraw a proclamation which was set out by the Governor in Council. I am sure you recognize that would not be a suitable wording in a statute.

The Acting Chairman: Those in favour of Senator Phillips' amendment please signify in the usual way . . . I declare the amendment lost.

Shall clause 39 carry?

Hon. Senators: Carried.

The Acting Chairman: We now come to clause 40. Shall clause 40 carry?

Hon. Senators: Carried.

The Acting Chairman: Shall clause 41 carry?

Hon. Senators: Carried.

The Acting Chairman: Shall the title carry?

Hon. Senators: Carried.

The Acting Chairman: Shall the preamble carry?

Hon. Senators: Carried.

The Acting Chairman: Shall the bill carry?

Some Hon. Senators: Carried.

Senator Grosart: On division.

Senator Molgat: I have one further question for the minister, Mr. Chairman.

Mr. Minister, I believe you were to check with the provincial Ministers of Agriculture regarding their acceptance of the wording of the amendments.

Hon. Mr. Olson: The deputy minister has his notes in that respect, and I will ask him to answer the question.

Mr. Williams: Mr. Chairman, I contacted all deputy ministers, with one exception where there was an acting deputy minister. I asked them the question that was put to the minister, and I asked them to check with their ministers in that regard. All whose ministers were available checked with their ministers; there was one who did not have an active minister, and there were two who were unable to reach their ministers. We have positive replies from seven ministers via the deputy ministers, and in the other three cases the deputy ministers gave me their assurance that in so far as their understanding was concerned, and they all attended the meeting, the amendments implemented were in accordance with the commitments that were made and the understanding that was given at the meeting in Ottawa on November 23.

The Acting Chairman: Shall I report the bill without amendment?

Hon. Senators: Agreed.

Senator Langlois: Mr. Chairman, before we adjourn I would like to inform honourable senators that arrangements have been made with the Speakers of both chambers to reassemble the chambers on Tuesday next at 2 p.m. How long we are going to sit next week will not be known until we know how the Senate is going to handle this piece of legislation.

Senator Grosart: A long debate!

Senator Langlois: We will have to play it by ear. We will have royal assent next week, if at all possible.

The Acting Chairman: Thank you, Senator Langlois. The committee is adjourned.

The committee adjourned.

*APPENDIX "A"

CONSUMERS ASSOCIATION OF CANADA

ASSOCIATION DES CONSOMMATEURS DU CANADA

NATIONAL OFFICE—SIÈGE SOCIAL

100 RUE GLOUCESTER STREET, OTTAWA, ONTARIO,

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TELEPHONE (613) 236-2383

January 6th, 1972

Honourable J. J. Connolly,

The Senate,

Parliament Buildings,

Ottawa,

Ontario

Dear Senator Connolly,

Enclosed are copies of submiss ons presented by the Consumers' Association of Canada on Bill C-197 and Bill C-176, the acts dealing with the establishment of a National Farm Products Marketing Council.

The Consumers' Association of Canada wishes to present to the Senate our suggestions for amendments to Bill C-176 which we believe will assist in safeguarding the public interest under such legislation.

Sincerely,

Maryon Brechin,
(Mrs. W. A.)
National President.

MEMO TO: Members of Parliament

FROM: Jean Jones, National President

DATE: March 15th, 1971

The Consumers' Association of Canada, the voluntary organization representing the interest of consumers in Canada is deeply disturbed that Bill C-197 regarding the establishment of a National Farm Products Marketing Council was unchanged when re-introduced as Bill C-176 and that, despite extended committee hearings, no substantial amendments have been approved.

Bill C-176 is phrased in broad, all-encompassing terms which would allow complete control of all sources of a commodity, at any or all stages of its production or distribution to any Agency set up under the Act.

These terms allow for monopoly control which would affect the entire Canadian food industry. This represents a danger to consumers since the Bill contains no provision for representation of consumers or other segments of the food industry nor is a means of appeal from decisions of an Agency easily available.

You will have noted the many other responsible organizations which have voiced opposition to Billl C-176. These voices must not be ignored! Since so many commodity groups and a number of provinces are so strongly opposed, the Bill could prove to be a deeply devisive force, with serious results to our future as a Nation as well as to our food supply. Surely this is too high a price to pay for controlled production of agricultural commodities!

CAC considers the cost to our economy of setting up such a complex food monopoly will be too great. Bill C-176 is completely unacceptable to consumers, especially since there already exists, in provincial legislation, the means for voluntary co-operation between provinces to rationalize production.

We include a copy of CAC's submission to the Standing Committee on Agriculture regarding Bill C-197, which applies equally to its unchanged version Bill C-176. We would urge you to give your serious consideration to the possible effects of the implementation of this Bill, not only on our domestic food supply, but on Canada's position in our export markets.

SUBMISSION

by the

CONSUMERS' ASSOCIATION OF CANADA

to the

STANDING COMMITTEE ON AGRICULTURE

of the

HOUSE OF COMMONS

Consumers' Association of Canada,
100 Gloucester Street,
Ottawa 4, Ontario.

October 1st, 1970

Preamble

The Consumers' Association of Canada is the national organization representing and serving the interests of Canadian consumers. It is a non-government, non-sectarian, non-profit association of volunteers.

CAC's four main objectives are:

1) To unite the strength of consumers to improve the standards of living in Canadian homes.

2) To study consumer problems and make recommendations for their solution.

3) To bring the views of consumers to the attention of governments, trade and industry, and to provide a channel from these to the consumer.

4) To obtain and provide for consumers, information and counsel on consumer goods and services.

II. *Statement of CAC position on NATIONAL Marketing Boards* to the Honourable Mr. H. A. Olson read as follows:

For the past year, the Consumers' Association of Canada has been most concerned about marketing boards, their structure and their operation. The association presented its views to the Canadian Agricultural Congress and we would now like to present these views to you for your consideration. The points following represent specific concerns of the consumer in regard to marketing boards.

1. There is a danger that regions will become protectionist and in so doing may prevent areas where production is highly efficient from getting the greater share of the market. Consumers feel that goods should be produced wherever it is most economical, provided there is still a fair profit to the original producer.

2. Marketing boards tend to protect the smallest and most inefficient producers and prices can be set too high - this may discourage the adoption of new advances in technology which would tend to put Canada at a disadvantage in world markets.

3. Marketing boards must *not* be allowed to short supply the market in order to increase prices. This fact was mentioned in discussion at the Canadian Agricultural Congress and could certainly work to the disadvantage of consumers. Consumer consultation on any decision of a marketing board relating to the consumer interest is therefore essential.

The Consumers' Association of Canada feels that national marketing boards are not in the consumer's interest.

III. *Discussion on Bill C-197*

1. The purpose of this submission is to place before the committee some of the deeply felt concerns of consumers on the subject of national farm products marketing agencies in general, and to comment on the provisions for their establishment as set out in Bill C-197.

2. That those responsible for developing farm policies are concerned has been often demonstrated. The Ontario Farm Income Committee and the Federal Task Force on Agriculture are but two of the most recent groups to study the problem.

3. Consumers too, are deeply concerned, for all Canadians are dependent on our agricultural industry for the provision of a stable supply of high quality food products.

4. The development of marketing is, we realize, a means of presenting a united post and developing a countervailing power in the market in an effort to halt this erosion of the producers income. Unfortunately price control has been the major tool to be used. This is made possible by the provision in marketing acts which exempt such boards from the requirements of anti-combines legislation. We find the same provision for national marketing agencies in Part III, Section 2. This removes a basic protection from the consumer and is prejudicial to his interest.

5. The term marketing boards has proven to be a misnomer. Although much activity in the areas of market and product improvement is allowed, in their myopic concentration on price many boards have been completely production-oriented and have overlooked the marketing responsibilities they should bear. Market planning should begin with the consumer and work back to production needs. Consumer research in all agricultural commodities is almost non-existent and boards have done little or nothing in this respect.

6. Where the operations of plans were effective only on products produced within provincial boundaries, safeguards for consumers could exist. When, however, a provincial board feels itself able to interfere with interprovincial trade to the extent that all sources of a commodity are controlled by it, as has happened recently in the case of FEDCO (Federation des Producteurs des Oeufs pour Consumption) in Quebec and in the retaliatory action taken by the B.C., Ontario and New Brunswick Broiler Boards against imports of broiler chickens from Quebec and Alberta, the helpless consumer, lacking representation, alternative sources of supply or a court of appeal can only voice his opinion through the political process - a time-consuming and unsatisfactory way of solving consumer problems yet frequently the only one available.

7. Consumers know that farmers cannot remain in business without an adequate return. They are anxious to be assured of a supply of high quality products, clearly and adequately graded and labelled. Some are willing and able to pay higher prices for the addition of optional convenience features but many consumers must buy on the basis of price alone. Any action taken by government to increase returns to growers *must also ensure that adequate competition* exists either from imported supplies of the regulated commodity or available alternate products.

8. The consumer is no longer willing to tolerate a situation in which his needs are ignored. Efforts by any group, even producers, to establish a monopoly over which the consumer has no control will meet with determined opposition.

9. The concentration of control of a given commodity in the hands of a single agency when no representation of consumer viewpoint is allowed, nor any effective safeguards inserted in legislation to protect the consumer interest, is intolerable.

10. Consumers are opposed to the establishment of any system which increases costs without adding to the value of the goods they purchase. The provisions of Bill C-197 which set out the structure of a National Farm Products Marketing Council and the agencies it is empowered to establish, appear to us to detail a system which will be redundant, costly and totally unnecessary to the orderly marketing of farm products. It completely ignores the contribution made by other participants in the marketing chain.

11. CAC contends that one of the omost effective ways of protecting the consumer interest is through competition.

Yet in spite fof the statement in Part I, Section 6 of the Bill, that the duties of Council shall be to "advise the Minister—with a view to maintaining and promoting an efficient and *competitive* agricultural industry", the provisions of the bill tend to negate any form of competition and to create a monopolistic situation. Our feeling that this will be the effect is reinforced when we read in Part II, Section 23 (a) that an Agency may, when established:

> "Purchase any farm product *wherever grown or produced* that is of the same kind as the regulated product". We are concerned that the phrase "wherever grown or produced" is intended to control foreign imports.

12. The extent to which control over imports is given to a national marketing agency can determine much of its strength. As sole supplier of a product its ability to raise prices will be uncontrollable.

13. Part I, Section 6 of Bill C-197 should include as a duty the periodic assessment of the work of the council and its agencies, to be reported to parliament.

14. A periodical assessment of the work of the Council and its agencies by an independent agency such as the Economic Council of Canada or the Canadian Consumer Council to provide an overall view of objectives and performance in order to protect the public interest, should be included.

15. In Part I, Section 8,paragraph 2, this paragraph should be changed to read "A public hearing *must* (not may) be held."

16. If the committee decides that yet another regulatory agency is necessary, CAC is convinced that the regulating bodies must be properly representative of all segments of the industry. Bill C-197 states in Section 6(2) "In carrying out its duties the Council shall—(b) "have regard to the interest of consumers of farm products and of those engaged in the marketing thereof, as well as to the interests of producers of farm products." In order to ensure adherence to that general principle then Section 3 (1) "There shall be a Council to be known—etc." *must* be more explicit and specify that at least two representatives of the ultimate consumers of the National Products Marketing Council be appointed by the Governor-General in Council and in Part III, Section 19, paragraph 1, specify at least two representatives of the ultimate consumer be included and that the term of office for all appointees be for specified time periods.

17. CAC feels the provisions of Bill C-197 to be unnecessary to the orderly marketing of agricultural commodities, that the Bill itself is much too vague and general in outline and that insufficient time has been given for consideration of its effect on agriculture and its partners, the food industry and consumers.

18. As it stands, CAC believes Bill C-197 is contrary to the consumer interest.

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THE SENATE OF CANADA

STANDING SENATE COMMITTEE

ON

BANKING, TRADE AND COMMERCE

The Honourable SALTER A. HAYDEN, *Chairman*

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OF PROCEEDINGS

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