THE CANADIAN BAR ASSOCIATION
L'ASSOCIATION DU BARREAU CANADIEN

September 7, 2007

Mr. Jean-Jacques Lefebvre
Director, Aggressive Tax Planning Division
International & Large Business Directorate
Compliance Programs Branch
Canada Revenue Agency
344 Slater Street
Ottawa, ON K1A 0L5

Dear Mr. Lefebvre:

Re: OECD and FTA Tax Intermediaries Study

I am writing on behalf of the National Taxation Section of the Canadian Bar Association (the CBA Section) in response to your letter of August 3, 2007, requesting comments on draft Working Papers 4, 5 and 6 prepared by the OECD's tax intermediaries study team. In view of the short timeframe for response, the comments in this letter are limited to a few matters of particular concern or interest to members of the CBA Section.

Risk Profiling of Tax Advisers

Working Paper 5 proposes, in paragraphs 31 to 42, that revenue bodies could create risk profiles for tax advisers, and use those risk profiles as a factor in determining which taxpayers to audit. We are strongly opposed to the application of risk profiling to lawyers.

The assumption underlying the risk profiling of tax advisers is that there is a correlation between the advisers used by the taxpayer and the degree to which a taxpayer is aggressive in its tax affairs. We submit that such a correlation, if it exists at all in Canada, is likely to be very weak, at least when the tax advisers in question are lawyers. A lawyer's role is to provide advice, which clients may or may not follow. In general, the risk tolerance of clients will determine their appetite for taking on tax risk, not the advice provided by lawyers. Thus, we do not think that an attempt to develop risk profiles for lawyers would serve any useful purpose.

Furthermore, assuming that in theory it is possible to develop such risk profiles, it is not apparent to us what the CRA would use as a basis for doing so. The primary role of lawyers in tax planning and compliance is to provide advice to their clients. Thus, risk profiling would have to

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involve some sort of subjective assessment of the advice provided. However, for the most part, this advice is subject to solicitor-client privilege and so is not available to the CRA. Consequently, the CRA would not have the necessary information from which to develop risk profiles.

In the face of this problem, the only other approach to risk profiling that we can see would be to assign lawyers to risk categories based on the risk profiles of a selection of their clients. This approach also faces a very practical impediment. In general, the CRA will not know who has provided advice to a taxpayer with respect to particular matters. Thus, the CRA will have no way of establishing a link between a taxpayer's tax positions and particular advisers. More fundamentally, it would be highly unfair to tax lawyers and their clients to place a particular client in a high risk category on the basis that other clients of the lawyer are high risk taxpayers.

A further serious problem with the risk profiling of tax lawyers is that a lawyer given a "high risk" profile would generally not be able to provide the CRA with information to establish that the profile is inappropriate. The information required would concern the tax affairs of particular clients and the advice given by the lawyer to those clients. However, because of the strict professional duty to keep client matters confidential, as well as the constraint of solicitor-client privilege, a lawyer could not provide such information to the CRA.

For these reasons, we urge the CRA to take a strong stance against any recommendation that there be risk profiling of lawyers.

Solicitor-Client Privilege

Appendix Three to Working Paper 6 makes it clear, in paragraphs 11 to 13, that participation in the enhanced relationship would not require taxpayers to disclose information that is subject to legal professional privilege (referred to as solicitor-client privilege in Canada). In other words, the enhanced relationship is not intended to be a back door way for revenue bodies to obtain, on a voluntary basis, information that they cannot obtain on a compulsory basis.

Solicitor-client privilege is of fundamental importance to our legal system, as has been emphasized by the Supreme Court of Canada in several decisions. It would be completely inappropriate to attempt to undermine it by offering advantages to taxpayers in exchange for their willingness to hand over material protected by solicitor-client privilege. Thus, we urge the CRA to endorse the above-noted position of the study group.

Incentives for Enhanced Relationship between Taxpayers and Revenue Bodies

Working Paper 6 identifies five things that consultation has suggested revenue bodies need to demonstrate in order to provide taxpayers with an incentive to engage in the enhanced relationship: (i) commercial awareness; (ii) an impartial approach; (iii) proportionality; (iv) disclosure and transparency; and (v) responsiveness. The paper contemplates, however, that the dealings of a revenue body with taxpayers may not always reflect these characteristics. For example, it notes that a taxpayer who is not willing to engage meaningfully in the enhanced relationship will be less likely to receive the reciprocal benefits of that relationship.

We submit that, in general, a revenue body should exhibit these characteristics in its dealing with *all* taxpayers, regardless of the extent to which a particular taxpayer is perceived by the revenue body as having an enhanced relationship with the revenue body. We find it particularly inappropriate to suggest that taxpayers may have to enter into the enhanced relationship in order to benefit from impartiality on the part of the revenue body.

The final report should make a clear distinction between the conduct that all taxpayers have a right to expect from their revenue body, and the particular considerations and benefits for taxpayers who enter into the contemplated enhanced relationship.

Relationship between Tax Advisers and Revenue Bodies

Working Paper 6 observes that there should be scope for tax advisers and revenue bodies to develop their own form of "enhanced relationship". It sees the principal benefit to tax advisers as arising from the greater understanding that revenue bodies will gain of their businesses and of the impact that tax advisers have on their clients' tax-related decisions. As a result of this greater understanding, tax advisers and revenue bodies are more likely to collaborate on such matters as the early production of explanations of new laws and there is likely to be greater consultation in respect of law reform proposals. Conversely, tax advisers should gain an understanding of revenue bodies, their decision-making processes and their general areas of concern in relation to tax planning. As a result, they should be able to anticipate the revenue body's likely response to particular tax positions, and should have access to revenue officials in order to obtain advance clearance in respect of particular transactions. (Paragraphs 50 to 53 of Working Paper 6)

We have the following comments with respect to the relationship between the CRA and Canadian tax advisers in general and Canadian tax lawyers in particular.

First, there is nothing mysterious about the nature of legal practices and the interaction between tax lawyers and their clients. We fail to see what further understanding the CRA requires of these matters.

Second, the greater collaboration and consultation envisaged by the study team assumes that the revenue body is the primary entity that develops and explains legislative proposals. That is not the case in Canada. The responsibility for tax legislation lies with the Department of Finance, which often releases draft legislation for public comment and also prepares explanatory notes. Canadian tax advisers have for many years engaged in extensive dialogue with the Department of Finance regarding proposed legislation, often at the request of the Department..

Third, the CRA has been reasonably open about its internal procedures, although there is, of course, always room for more disclosure. We do not think that there is or should be any connection between the extent of the CRA's disclosure about its procedures and the adoption of the enhanced relationship concept.

Fourth, the CRA has an advance rulings process, and a procedure for providing non-binding technical interpretations in some circumstances. Rulings and technical interpretations are released (in redacted form) to commercial publishers, who make them available to the tax

community. The CRA publishes its positions on technical issues in Interpretation Bulletins and Income Tax Technical Newsletters, and responds to questions at tax roundtables sponsored by organizations such as the Canadian Tax Foundation. Thus, arrangements are in place to inform the public of the CRA's positions. In our view it is important that the CRA devotes sufficient resources to these activities to ensure that they continue on a broad and timely basis.

The discussion of an enhanced relationship between revenue bodies and tax advisers ends with comments on who the revenue bodies should approach to engage in a dialogue, having regard to the costs and benefits of the exercise (paragraph 54). The study team envisages that there could be direct dialogue between revenue bodies and (i) larger firms of tax advisers, (ii) others where there are particular reasons, and (iii) professional associations representing the remainder. It appears that the dialogue contemplated is to enable the revenue body to gather information about tax advisers. We question whether there would be any significant benefit to the CRA of entering into such a dialogue with Canadian law firms, individual lawyers and the professional associations that represent lawyers such as the Canadian Bar Association (or indeed the law societies that regulate the profession). Anything that law firms or individual lawyers might say about the provision of tax advice to clients will likely be quite generic, common knowledge and probably already known to the CRA. Furthermore, the professional associations are not in a position to comment on the practices of individual lawyers or any category of law firms.

Since it is germane to the discussion of the relationship between revenue bodies and tax advisers, we would point out that the Canadian Bar Association and the Canadian Institute of Chartered Accountants have a long-standing committee—The Joint Committee on Taxation—that regularly provides input to, and engages in dialogue with, the CRA and the Department of Finance. The Joint Committee is comprised of approximately a dozen members from each of the two sponsoring organizations. As examples of its dealings with the CRA, the Joint Committee discusses the interpretation of *Income Tax Act* provisions of general interest to the tax community, comments on draft publications, and discusses the operation of the Rulings Directorate.

Thank you for the opportunity to comment on the Working Papers. If you would like to discuss any of the comments in this letter, please do not hesitate to contact me at (416) 863-2697.

Yours truly,

(original signed by Paul Tamaki)

Paul Tamaki
Chair, National Taxation Section