Certified General
Accountants Association
of Canada

Harmonizing the Caribbean Tax Laws

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Check against delivery

Good morning.

I'm very pleased to be here in St. Kitts & Nevis to share your hospitality and learn from the excellent speakers assembled for this conference. In fact, it's been a most enjoyable week. Last Saturday I was in Barbados where I had the pleasure of welcoming 16 newly certified CGAs into membership in our association.

Over the past week, I've met people from all parts of the Caribbean and heard about some of the successes and the challenges of integration within CARICOM. The challenges are not unlike those facing many other parts of the world. In fact, even within the country of Canada, we are having some of the same debates around harmonization.

For this discussion of tax harmonization, I will defer to my two colleagues – Mr. Seaton and Ms. Eduardo – for their expertise in taxation and law, as well as their familiarity with CARICOM.

My presentation will focus on harmonization in a broader context in order to illustrate the opportunities and challenges harmonization presents.

The benefits of harmonization can be summed up by saying that harmonization promotes economic growth. It facilitates mobility in goods and services, labour and capital. Essentially it allows countries to put into practice Adam Smith's theory of comparative advantage. It encourages countries to specialize in the goods and services they are most efficient at producing, while trading for those which they produce less efficiently.

Markets naturally want to cross borders. Yet it is equally natural for governments to regulate their borders. Different rules, regulations, barriers and tariffs between countries inhibit trade and investment.

But when countries come together to establish common rules and regulations, whether through trade agreements or common market arrangements, trade between those countries is stimulated.

Harmonization reduces the bureaucracy and uncertainty of trading across borders. It leads to standardization of the interpretations of rules and clear processes for the resolution of disagreements. It can reduce development costs and lower training and education costs. And it reduces the incentive for countries to compete by undercutting each other in standards and tax rates.

But perhaps most importantly, by setting clear agreed-upon rules, it promotes fair competition. This is important because, while competition is an essential element of free markets, countries are not created equally. They are different sizes and at different stages of economic development.

For example, the dollar purchasing power of the world's largest economy, the United States, is 36,000 times bigger than that of here in St. Kitts and Nevis.[1] Even between CARICOM countries there are inequities. But harmonized standards and regulations create a level playing field to enable all participating countries to gain from increased trade.

When discussing harmonization, one of the most obvious points of reference is the European Union. In March of this year, the EU celebrated its 50th anniversary. The EU today is much larger and much more integrated than was imagined when the Treaty of Rome was signed in 1957. Yet, after 50 years, the European Union is still very much a work in progress. As the Economist newspaper noted recently, the EU faces several problems including ratification of its constitution, public disenchantment with the union, and relatively poor economic performance in recent years.[2]

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[1] Wolf 79
[2] The Economist. Fit at 50? 4-6

Yet despite the current malaise, the successes of the European Union are many and significant. Especially when one considers the diversity of the region. The EU itself functions in 23 officially recognized languages. (There are a number of other languages either recognized or widely spoken in EU member-countries.) The cultures of its 27 member countries are distinct and well entrenched. And the region has a long history of bloody conflicts.

With so many differences, it is hard to imagine how the EU countries could agree on economic and social policy. But it has forged agreement on a great many things, and it has done so by focusing on shared values such as democracy, freedom and social justice.[3] The EU's focus on shared values leads to clear policy objectives. These objectives help the EU to deal with the most difficult challenge of economic unions – finding the balance between the benefits of union and the need to protect national sovereignty.

[3] http://europa.eu

Taxation is a good case in point. The EU's policy on taxation preserves governments' responsibility for setting levels of direct taxation. However, the EU taxation policy ensures that tax rules are consistent with the goals of job creation, the EU's competitiveness, the single market and free movement of capital.

In other words, the policy ensures government's sovereign right to establish the types and levels of taxes required to fund spending, as long as they are consistent with the goals of a single market.[4] As a further protection of national sovereignty, decisions on tax matters require unanimous approval of all 27 member states, not just a majority of votes.

Still, the fear that harmonization means a loss of national autonomy – and eventually national identity – remains the biggest concern about harmonization.

[4] http://europa.eu

It is a legitimate concern in the sense that if a country cannot raise the revenue it needs through taxation, it will be unable to continue to operate.

However, as the EU example makes clear, harmonization has not hurt the ability of individual countries to make their own policy decisions. Tax rates and structures vary between EU member-countries. And overall, countries in the EU have seen a steady rise in tax revenue over the years since the union was formed. That rise has been in both absolute terms, but also as a percentage of gross domestic product.[5]

Still, many people have concerns that harmonization prevents countries from capitalizing on or compensating for their differences. Perhaps that is why some EU member countries remain cautious about some aspects of integration.

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[5] The Economist. Globalisation and its Critics 14

For example, only 13 of the 27 member countries have adopted the Euro, the European common currency.[6]

Those same concerns about autonomy can even be found within the borders of a single country – at least they can be found in my country. Tomorrow, Canada celebrates its 140th birthday. Yet after all these years, there is still considerable debate within the country regarding trade barriers between provinces and multiple levels of regulation.

Canada is a federation of 10 provinces and three territories. The constitution divides powers between the federal and provincial levels of government, giving the provinces a fair degree of political autonomy. This enabled protectionist policies to be implemented over the years that hindered trade between Canadian provinces.

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[6] Europa.eu

For example, a truck carrying bales of hay from the province of British Columbia to the neighbouring province of Alberta would have to pull off the highway at the border and restack the hay to comply with different regulations in Alberta. Major brewers such as Labatts and Molsons had to establish breweries in each province because they were prohibited from selling beer brewed in one province to customers in the adjoining provinces.

In July 1995, Canada adopted the Agreement on Internal Trade – essentially a free-trade agreement negotiated by the federal and provincial governments. The AIT removed the most contentious barriers to trade, but it had its own weaknesses, the main one being that it has proven to be unenforceable. And improving the AIT is difficult because of a lack of consensus among provinces.[7] Recently the provinces of British Columbia and Alberta signed their own bilateral trade deal, a move that has prompted further debate on the issue.

[7] CGA-Canada, Establishing an Open Domestic Market for Canada, 3-5

Securities regulation is another such issue between Canadian provinces. Regulation of capital markets is a provincial jurisdiction and, as such, companies raising capital in Canada may have to comply with as many as 13 different securities regulators. This has become an issue of much debate within the business community and the political arena.

Several consultation processes have taken place, but there is still no agreement in sight. The federal government and Ontario, the largest province, support the creation of a single national regulator. British Columbia, Alberta and Quebec are strongly opposed to a national securities regulator. Most of the provinces have agreed to a “passport” system for harmonizing securities regulations, but Ontario has refused to sign on to this program.

As a result, the issue of securities harmonization is at an impasse. Once again, the perceived need to protect provincial autonomy is at the root of the problem. And there is a good argument for protecting regional differences. The economic base is quite different from one province to another. The western provinces are resource-based, while central Canada is dominated by manufacturing. Some provinces argue that regional securities regulators are needed to ensure these regional economies continue to attract capital. The issue of securities harmonization in Canada will continue to prompt debate, but a resolution to the issue remains elusive.

When we talk about the rationale for protecting different standards in different jurisdictions, one of the fears commonly raised is that harmonization promotes a “race to the bottom”. Yet, another example of harmonization demonstrates that just the opposite is likely to occur. As professional accountants, we are well aware of the efforts to harmonize accounting standards internationally. That process has certainly not resulted in fewer or lower standards.

In fact, keeping up with "standards overload" is perhaps the biggest challenge professional accountants face at this time.

Harmonization of standards is happening at the same time that standard-setting boards are raising and tightening all standards that apply to the profession. This is driven by the need to protect public confidence. But what the example shows is that if there is a public interest in having certain regulations or standards, they will continue to be maintained.

International accounting standards serve as an excellent example of what is required for the harmonization process to be successful. First of all, the participation of member countries is needed both to reflect the countries' different needs and to ensure the legitimacy of the process. That participation can happen in different ways and may not necessarily include a direct vote in the decision process.

For example, the International Accounting Standards Board, which sets international accounting standards, is governed by a board made up of independent directors. The IASB does not have member-countries, as such. But the independence of the board, along with a thorough consultation process, is intended to ensure that decisions are made in the best interests of all or the majority of stakeholders.

The International Federation of Accountants, which through its various boards sets auditing and professional standards, offers a slightly different model. IFAC is made up of 155 members and associates in 118 countries. Each member body is represented on the IFAC council, giving them some direct input into the overall direction of the organization.

However, each of IFAC's four standard-setting boards is comprised of only 18 members meaning that very few member-bodies have a direct vote on IFAC standards.

There are a number of checks and balances in place though to ensure that the boards retain independence and transparency. There is a rigorous nomination process for appointments to the boards, each board includes public members, and their work is overseen by another independent body, the Public Interest Oversight Board.

Most important though is the amount of input obtained throughout the standard-setting process. Both IFAC and the IASB have established policies for developing standards and seeking input. Generally speaking, the process follows this approach:

- An issue is introduced through a discussion paper intended to spark dialogue on the issue within the profession. Interested parties are invited to comment.
- Then, research is conducted and direct consultation with stakeholders may be undertaken to gain a better understanding of different perspectives. For example, the IASB established a working group for its SME project that reflected a variety of interests.

- Next, an exposure draft of the proposed standard is released for public comment.
- Those comments guide the revision process, and in some cases prompt further consultation. After revision of the exposure draft, a decision is made on whether to issue a second exposure draft for comment.
- When it is determined that due process has been completed, the final standard is approved by a vote of the board at a public meeting.[8]

Not all member-bodies are always happy with the end result. But the process allows for considerable input from all stakeholders and ensures the necessary transparency.

I'll conclude my comments today with one more example of harmonization – the example of my own association, CGA-Canada. Regulation of the accounting profession in Canada is another area of provincial jurisdiction.

[8] International Accounting Standards Committee Foundation

That means the ultimate responsibility for certifying members rests with each of the 12 provincial and territorial CGA associations in Canada. CGA-Canada also has affiliates in Hong Kong, China, Bermuda and here in the Caribbean. If each affiliate set its own standards for certification, education and professional conduct, it would lead to uncertainty over how those standards compared to each other. That would severely impact peoples' confidence in the designation.

As a result, the affiliation agreement signed by all CGA associations gives CGA-Canada the authority to set national standards for certification, education and professional conduct. These are minimum standards to which all provincial, territorial and regional affiliates must adhere.

Standards are set by two committees of CGA-Canada: the National Education Committee and the National Professional Standards Committee.

Each affiliate is represented with a member on these committees. The development of standards includes appropriate consultation and opportunities for input from each affiliate. The final standards must be passed by the CGA-Canada board of directors, made up of representation from each affiliate.

I began my remarks today by mentioning that I welcomed 16 new members in Barbados last weekend. As a result of CGA-Canada's national standards, the public can have confidence that those 16 new CGAs have met the same rigorous certification requirements demanded of CGAs in Bermuda or Hong Kong or any jurisdiction in Canada.

That is the value of harmonization in general – the confidence that comes from comparability, transparency and clarity.
Harmonization takes time, as we've seen with the 50 year example of the European Union and the 140 year example of the Canadian federation. In fact, it's a process that never really ends.

But the benefits of harmonization are clear and the process is well worth the effort.

Thank you very much.

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