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## Standing Committee on Finance

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**Thursday, February 3, 2005**

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**Chair**

**Mr. Massimo Pacetti**

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## Standing Committee on Finance

Thursday, February 3, 2005

• (1535)

[English]

**The Chair (Mr. Massimo Pacetti (Saint-Léonard—Saint-Michel, Lib.)):** Good afternoon.

[Translation]

If everyone is ready, we can begin.

[English]

Today we have, from the Office of the Auditor General of Canada, Mr. Lennox and Mr. Hood. Pursuant to Standing Order 108(2), we are doing a study of chapter 6, “Canada Revenue Agency—Resolving Disputes and Encouraging Voluntary Disclosures”, of the 2004 Report of the Auditor General of Canada to the House of Commons.

We'll start with ten minutes of opening remarks and then we'll pass the microphone over to the members.

The floor is yours.

**Mr. Andrew Lennox (Assistant Auditor General, Office of the Auditor General of Canada):** Thank you, Mr. Chairman.

Thank you for this opportunity to appear before the committee to discuss our audit of the Canada Revenue Agency's Appeals Branch. The results of the audit were reported in chapter 6 of our November 2004 report.

The Auditor General sends her regrets, as she is unable to attend today. I am the Assistant Auditor General responsible for our audit work at the Canada Revenue Agency. Joining me at the table is Jamie Hood, the principal responsible for this audit.

[Translation]

This audit dealt with two key functions in the Agency's Appeals Branch. The first is the resolution of objections to income tax and GST assessments and reassessments. The second is the administration of the Voluntary Disclosures Program. I will address each of these separately.

[English]

Taxpayers and GST registrants who disagree with assessments by the agency on income tax, GST, and excise tax matters can file an objection with the agency. Affected parties who disagree with the agency's rulings and assessments on Canada Pension Plan and employment insurance can appeal. These objections and appeals are reviewed by the agency's appeals branch.

We found that the branch is resolving most of the income tax and GST objections it receives and is doing so in a way that is fair and impartial. I should note that we are encouraged by this positive conclusion. The same findings also apply to appeals of Canada Pension Plan and employment insurance rulings and assessments.

We also found that over half of the objections the branch receives are resolved within the timeliness goals the agency has set. However, under the legislation, taxpayers can appeal their case to the Tax Court of Canada if they have not received a decision from the appeals branch 90 days after filing their objection. While we noted that most taxpayers appear willing to wait for the administrative decision before appealing to the courts, we are concerned that many of the branch's timeliness goals for income tax objections exceed 90 days by a large margin.

Let me now turn to the voluntary disclosure program. The program allows taxpayers and GST registrants to correct past errors or omissions without penalty or prosecution, and sometimes with reduced interest. For example, a GST registrant who has collected GST for a number of years but never remitted it to the agency can request a voluntary disclosure. If the request is accepted, the registrant would remit the GST and some interest, but would avoid the penalties and possible prosecution that would follow if the agency had discovered the omission.

Taxpayers and registrants have responded well to the program; in the last four years, the number of requests has more than doubled.

Administering the program is a difficult balancing act. On the one hand, officers want to encourage taxpayers and registrants to correct past errors or omissions and become compliant. On the other hand, they need to ensure that the program is fair to compliant taxpayers and registrants and is not seen as a free ride or a reward for non-compliance. This calls for a lot of judgment on the part of the officers and solid support from headquarters. We found that the program is not administered consistently across the country, and we are concerned that the balance is not being maintained. Taxpayers and registrants who make a voluntary disclosure have a right to expect equal treatment across the country.

• (1540)

[Translation]

We also raised a concern about a contradiction between the information given to Parliament regarding the intended uses of the legislative authority supporting the program and the way that authority is actually being used. This issue may be of particular interest to this Committee.

[English]

Let me say at the outset that the agency is not doing anything illegal. The wording in the Income Tax Act and the Excise Tax Act is very clear: the Minister of National Revenue has the authority to waive or cancel all or any portion of any penalty or interest otherwise payable under the acts.

However, we found that when the relevant subsection of the Income Tax Act was introduced in 1991, the Department of Finance told Parliament in its technical notes that the minister's discretion to waive or cancel penalties and interest would generally be used in cases where taxpayers had encountered extraordinary circumstances that were beyond their control, such as floods, fires, strikes, etc. Further, Parliament was told that the minister would not use the provision unless the taxpayer had taken a reasonable amount of care in attempting to comply with the requirements of the act.

In the case of the voluntary disclosure program, many of the disclosures relate to income that was intentionally never reported. Using the relevant subsection of the Income Tax Act to waive the penalties and some of the interest on those disclosures is inconsistent with what Parliament was told in the technical notes. However, it is up to Parliament to decide whether the agency has gone beyond what Parliament intended the subsection to be used for.

Mr. Chair, that concludes my opening statement. We would be pleased to answer any of the committee's questions.

**The Chair:** Thank you, Mr. Lennox.

Mr. Pallister.

**Mr. Brian Pallister (Portage—Lisgar, CPC):** Thanks very much for being here today for your presentations and for working with your report.

It might seem a bit of a contradiction for a representative of a political party that is advancing the idea of lower taxation to be concerned that it should be higher in some cases, but in reality our concern is that there be a system that is fair and seen to be fair.

This voluntary disclosure issue in particular concerns us. Obviously we recognize there's a balancing act, but if people are being forgiven on their taxes without justification or beyond the scope of what Parliament meant when it approved the process, that creates a concern, certainly in my mind.

First of all, on what basis did you make that observation? Can you quantify how you arrived at the observation that the department was going outside the original intention? To what degree is it going outside the original intention? Is it just one or two cases? Is it half the time? What's the magnitude of the greater latitude that's being given?

**Mr. Andrew Lennox:** Going back to 1991, the actual technical notes that were provided when the legislation was passed contained

very specific statements as to what this section of the act would or would not in theory be used for, going forward. We are simply raising the contradiction that existed—

**Mr. Brian Pallister:** I'm sorry to interrupt, but I'm clear on the background of what you're talking about. What I'm concerned about is that you must have had some statistical basis for making the observation that the department was going beyond those original intentions. In what percentage of cases, for example, has voluntary disclosure resulted in the forgiveness of interest or resulted in the forgiveness of penalties under the broader interpretation that would not, if you follow me, have been the case under the original instructions?

**Mr. Andrew Lennox:** Jamie, maybe I'll call on you to.... Jamie is the principal who did the detailed work—

**Mr. Brian Pallister:** He takes the tough questions.

**Mr. Andrew Lennox:** He takes the tough questions, yes.

I'll call on him to see whether in doing our audits we actually got into the amounts you're referring to.

**Mr. Brian Pallister:** Good. Thank you.

**Mr. James Hood (Principal, Office of the Auditor General of Canada):** The short answer is no, we did not get into the amounts where this would take place; it comes back more to the overall intent. When the legislation was put before Parliament in 1991, the explanatory notes talked about exceptional circumstances—beyond the taxpayer's control—and used fires and floods and those kinds of things.

In point of fact, in the voluntary disclosures program most of the disclosures relate to either income that has not been reported—sometimes intentionally, sometimes unintentionally—or GST that has not been remitted, again sometimes intentionally, sometimes not. But no, I don't have an absolute breakdown as to when. It would really come down more to what was intentional and what was unintentional.

• (1545)

**Mr. Brian Pallister:** You said “most” in your answer. Looking at the increasing number of disclosures, on the one hand I suppose we should be happy: these are streams of revenue that are being reintroduced that might otherwise not have been. When I see 2,500 in 2000-2001 and 6,100 in 2003-2004, I suppose part of me is happy to see that.

However, if the increase in the number of these disclosure requests is a result of a broader latitude being given on forgiveness of penalties, there is of course a part of me that says that's not a great idea: we're sending a message here that isn't conducive to the timely reporting and accurate reporting of income and of data that would give a fair tax result.

This is why I'm getting into the specifics of this. I'm very concerned that we not send the message that there's a free ride here and you can be honest later, because everybody else will pay for that. The people who are honest today don't deserve to have to pay more because someone else has decided to be honest later on.

I guess I'll just ask you again. You've said you think most of the cases fall outside the specific parameters that were mentioned initially in the technical notes, being natural or human-made disasters, flood, fire, strike, recent serious illness or accident, and so on. You must have reviewed the rationale in your audit—I would assume you did, since you would have had to do it in order to make this observation—for why these voluntary disclosures resulted in the settlements they did.

Is there any further light you can shed on this, apart from just the general observation that there's more forgiveness going on than was originally the intention? I'm looking for more detail from you.

**Mr. James Hood:** There may be two issues here.

First, it's very clear from what the courts would say that the intent of Parliament is put in the words passed by Parliament. In this case, the words are very broad. The minister can waive or cancel any penalty or interest under the act—period.

What we're doing is simply flagging to you, as your auditor, that when that legislation was introduced and you passed it, here's how you were told it would generally be used.

**Mr. Brian Pallister:** I understand that, but let me then ask you this. In flagging this, are you communicating a concern as to what I've just said; that by a broader interpretation of the rules than was originally communicated we are potentially opening the door to an abuse of the system, or potentially encouraging—I don't know a nice word to use here—people to be less than forthright initially?

**Mr. Andrew Lennox:** One of the recommendations we also had for CRA was for them to do an evaluation type of work that would allow them to determine whether or not the voluntary disclosure program was indeed meeting its goal of improving compliance. That's something we have asked CRA to do, and it's our understanding they're committed to do it.

**Mr. Brian Pallister:** Right. You observe in your report on page 17 of chapter 6 that the agency is gathering the information, that officers are reporting the number of cases—these are the questions I'm asking, I suppose, in a sense—the types of issues disclosed, and the amount of additional tax assessed; however, they're not using the information in any detail to determine whether the program is meeting its objectives or to help manage the program. I guess the obvious question, then, is why gather the information?

Your recommendation and their concurrence in your recommendation tells us that something will happen with CRA. That's probably a very good idea.

You mention a number of cases in your report. Do you have any idea of the total dollar value of those cases?

• (1550)

**Mr. Andrew Lennox:** Cases of...? I'm sorry.

**Mr. Brian Pallister:** The number of voluntary disclosure requests, you said, increased from 2,500 to 6,100 in 2003-04. I'll just read from the report, on page 12: "...the associated federal income tax and GST (or HST) assessments increased from \$140 million to an estimated \$459 million." It goes on to say, "The \$459 million is unusually high, due to two large disclosures."

Is it your observation that there is an upward trend, or is it, in terms of the dollar amounts, just due to these two large cases?

**Mr. Andrew Lennox:** It's our understanding there's an upward trend.

**Mr. Brian Pallister:** The cases have gone from 2,500 to 6,100. What was the number of cases in 1996-97? Do you have any idea of that?

**Mr. James Hood:** No, but it would be considerably fewer than the 2,500. There is no question that the program has grown over the years, and particularly since it was moved from the special investigations division into the appeals branch.

**Mr. Brian Pallister:** Other people will have questions, and I don't want to dominate this, but I know with a number of other issues concerning CRA there is a concern, in some respects, that we balance awareness among taxpayers with people understanding too much about how the system works so that they are able to work it to their advantage.

How much promotion is done of the voluntary disclosure system? Can you share with us any idea? Is it simply a function of its becoming better known among Canadian taxpayers? Is that why this system is receiving so much increased input?

**Mr. James Hood:** It would be speculation, of course, but there is no question that the agency, through its appeals branch, has gone out to associations, particularly of professionals and taxpayer representatives, to talk about the voluntary disclosures program.

I think you'll notice in just the last two days there have been a couple of examples, when they have a prosecution for tax evasion, where at the end of the news release they talk about the voluntary disclosures program. You know: if you want to get back on stream, here is a way to do it.

Particularly as taxpayer representatives become more aware of it, they tell taxpayers as well.

**The Chair:** Thank you, Mr. Hood.

Monsieur Bouchard.

[Translation]

**Mr. Robert Bouchard (Chicoutimi—Le Fjord, BQ):** In approximately 50 per cent of all cases, the Canada Revenue Agency's Appeals Branch resolves GST objections and related questions within the time frame set. You also mentioned that in 2003-2004, the percentage of appeals resolved within this timeframe, that is within 90 days, increased to 62 per cent.

What kind of timeframe are we talking about for the delays exceeding the 62 per cent?

[English]

**Mr. James Hood:** Exhibit 6.2 on page 8 of the report gives you the timeliness goals for various types of income tax files. For example, for initial assessing or post-assessing, which is just a quick audit type of work done after an initial assessment of a tax return, the timeliness goal is 88 days, but by the time you get down to large business audit, the timeliness goal is 332 days, which is considerably more than the 90.

[Translation]

**Mr. Robert Bouchard:** I have another question. Can these delays be attributed to the lack of resources within the Canada Revenue Agency?

[English]

**Mr. James Hood:** What the agency has tried to do is balance its workload with the resources it has and its desire for a quality decision. At the moment, this is the result of that effort.

• (1555)

**The Chair:** Monsieur Hubbard.

**Mr. Charles Hubbard (Miramichi, Lib.):** Thanks, Mr. Chair.

I'm always intrigued by some of these lines Mr. Pallister referred to. You have what they call "two large disclosures". I was rather intrigued. You can see people making small mistakes—and I know you can't allude to them too directly—but how could there be two "large disclosures" that might indicate here something in the millions of dollars? Can you give the committee a little glimpse of what this type of disclosure would be, when people for ten years, for example, never reported income? How would you describe a "large disclosure"?

**Mr. Andrew Lennox:** As you mentioned, obviously we can't get into the specific taxpayer side of things. In paragraph 6.47 we list the main reasons for when somebody comes before CRA and says "I want to do a voluntary disclosure". What the typical types of incomes are that come to be disclosed is listed in paragraph 6.47.

As far as these individual cases are concerned, I could ask Jamie, but I'm not sure whether we know which of these lines those particular cases dealt with.

**Mr. James Hood:** I can make a comment on that. Some of the larger cases, I believe, have to do with GST. They would be in large corporations. Sometimes it is simply a matter of a computer coding error that has gone on for a number of years, and when they come to revise their systems they realize, "Uh-oh, this hasn't been recorded properly", and in order to not pay the penalties on this non-remittance they would come in for voluntary disclosure. That would be one example.

**Mr. Charles Hubbard:** So really we're not thinking of individuals, in that the revenue agency has a group of people who simply don't file—the so-called underground economy, or whatever—and haven't filed for ten years, and who suddenly have a conversion such that they have to become good Canadians, and they do all that and come with their disclosures. It's more in terms of technical problems...?

**Mr. James Hood:** It's a complete mixture. The agency sees all types of taxpayers and registrants coming forward, from individuals who simply in some cases, for example, have offshore income they didn't understand, for whatever reason, was supposed to be reported on their Canadian income tax returns—somehow they've become aware of that, and they want to fix it up—to situations where people die, and they haven't been reporting income, either intentionally or not, and the estate wants to get that cleaned up, so they come forward on that. And yes, you get businesses that are part of the underground economy but now want to set the record straight, either on the income tax side or the GST side. Then it goes right up to large corporations that have just made a technical error.

**Mr. Charles Hubbard:** Occasionally in our major newspapers we see ads where either lawyers or smart tax auditors or chartered accountants or whatever will say: "Come to me; I'll fix it all up and see that you don't get penalties or interest." You probably see those ads every so often. Is there really an attitude that there are people who have special ways of dealing with this to avoid penalties and interest, or are people being misled by those ads that you see in even some of our major Canadian newspapers?

**Mr. James Hood:** I'm not sure I know how to answer that.

**Mr. Charles Hubbard:** It seems like an industry that somebody has, and I sense that any chartered accountant should be able to deal on an equal basis with some other chartered accountant, or an accountant of any kind, to deal with Revenue Canada. But somehow every week or every month you see this kind of ad, and I wonder about it.

Finally, Mr. Chair, I'd like to refer to this tax court business. I know it's beyond the scope of our two witnesses, but people without a great deal of money and a great amount of assets, and often without too much education, are—with EI especially—referred to the Tax Court of Canada.

I took the liberty a couple of weeks ago to inquire a little about this. It's quite a complicated process. To say any Canadian can simply walk in or go.... They sent me a bunch of documents about six inches thick. They told me I needed \$50 to file on behalf of a constituent. If you were late, there was another penalty. There was all sorts of legalese that the average Canadian really couldn't deal with.

Just for the record I would say, Mr. Chair, that for some poor guy who's trying to live on EI and who gets into difficulty with the system about repayments, it's literally impossible to go through that process. I would hope that sometime maybe our own EI or human resources department can have a better system of assessing and dealing with people in need, rather than saying go to the tax court. It sounds so easy, but it's really so difficult.

Thank you, Mr. Chair.

• (1600)

**The Chair:** Would someone like to comment on that?

Was any of your work tied in to dealing with the tax court or appeals division? Might it be that a number of cases were dropped because of the complexity of some of the cases?

**Mr. Andrew Lennox:** In the report we give you an idea of the proportion of cases that are settled administratively in the appeals process. I think we talk about 93% in the case of income tax, which would lead to 7% going on to the tax court. I think we talk about 65% for EI and CPP. The main reason there is that there are many more parties involved, and many more parties can appeal. For every decision that goes one way, there is someone who is not happy with it and can appeal. It becomes a higher number who ultimately go through to the tax court. But there are large percentages that are settled within the appeals process within CRA; however, especially on the EI and CPP side, a large number do go forward to the tax court.

**The Chair:** Thank you.

Ms. Ambrose is next, and then Ms. Minna.

**Ms. Rona Ambrose (Edmonton—Spruce Grove, CPC):** Thank you, and thank you, Mr. Hood and Mr. Lennox, for coming to the committee today.

I have quite a specific question respecting what I hear in my constituency office from constituents concerning CPP complaints. Obviously these are very urgent calls, because many of the people who rely on CPP are on fixed incomes, and they have to go without income for months.

I know the Auditor General's report says the appeals branch isn't working well or in a timely way to deal with these. I am wondering, in your estimation, what sorts of changes need to be undertaken, and what you see as the most glaring inefficiencies.

**Mr. Andrew Lennox:** We highlighted that CRA should look at the efficiency aspect of processing CPP and EI appeals.

The main issue is that once a ruling is made one way or another with respect to CPP or EI, the appeals officer really re-does a lot of the work that was already done by the rulings officers in the first place. We are suggesting CRA have a look at that, because it appears to us to be a very inefficient process to go through.

Having said that, once you start an appeals process, as we've outlined in the chapter, the timelines are very long. There is a huge backlog, huge numbers that are coming in. I think we highlighted the fact that the inventory in these cases is still growing.

**Ms. Rona Ambrose:** As a follow-up question to that, from what you've said—and there is a comment also in the report about the appeals officers being impartial, obviously, when they're making their assessments—you suggest that the system is inefficient primarily because, as you just said, the appeals officers seem to be duplicating the work of the rulings officers.

I am wondering whether, having looked at the appeals process and what you just said about the CRA, you have any recommendations or any opinion on how much money actually could be saved by the suggestions you've made, and how it might be saved by the new measures you've suggested be implemented.

•(1605)

**Mr. Andrew Lennox:** We have suggested that CRA take a very good look at the efficiencies that could be gained. They've committed to do that. At this stage we're awaiting CRA's completion of that analysis, and we'll have a look at it going forward.

**Ms. Rona Ambrose:** Am I to understand, then, that it's up to them to come up with the plan and identify where the savings and efficiencies would be created?

**Mr. Andrew Lennox:** They've agreed with our recommendation, so they will indeed do a review of the processes involved with a view to identifying improvements in efficiency along the lines we have suggested. They are in the process of doing that.

**Ms. Rona Ambrose:** Is there a deadline or a timeline for it?

**Mr. James Hood:** In the case of CPP and EI, they agreed to do a preliminary report by the end of 2004. We have not gone back, but my understanding from talking to them is that the report has been drafted. They'll be doing some work internally to satisfy themselves

on it; we'll see it in due course, and they will as well start working on it.

**The Chair:** I have Mr. Bell, then Ms. Wasylycia-Leis, and then Mr. McKay.

**Mr. Don Bell (North Vancouver, Lib.):** I have two quick questions. One is on paragraph 6.47; you commented on it already. Just further to Mr. Hubbard's question, you indicate that these assessments increased from \$140 million to an estimated \$459 million. You say: "The \$459 million is unusually high, due to two large disclosures", and you've mentioned those disclosures. How much of that increase from \$140 million to \$459 million...? Am I reading that correctly, that you're saying in effect that about \$300 million was those two? In other words, what I'm wondering is, if you subtract those two anomalies, how much of an increase are you seeing?

**Mr. James Hood:** I'd have to go back to look at the numbers to be absolutely sure. I don't have them with me. All we were trying to stress was that the numbers have gone from 2,500 to 6,100, a little more than doubled, so you'd expect the \$140 million to go to around \$280 million or \$300 million—that kind of number—but it actually went to \$459 million. It was a little high because of those two big ones. That's all we were trying to point out.

**Mr. Don Bell:** So it might have gone from \$140 million to \$300 million, or something like that?

**Mr. James Hood:** Something like that.

**Mr. Don Bell:** You're then talking about two of them that added up to \$150 million between the two. Is it fair to say that in the increase from 2,500 to 6,100 there would be an "in kind" or corresponding increase?

**Mr. James Hood:** I think that's what one would expect. We were just trying to highlight the fact that—

**Mr. Don Bell:** Okay.

The other question concerns paragraph 6.49. You make reference to "no-name" disclosures and then refer that to paragraph 6.59, in which you just define what the program is. My question is, what is the nature of the inconsistency that you find?

**Mr. James Hood:** The problem there is when the protection begins against the penalties and possible prosecution. It's inconsistent across the country. Some would offer the protection essentially from the moment the taxpayer or the taxpayer's representative phones the agency and says: "We have a problem. We want to make a voluntary disclosure. We'll be in to see you with some details soon." The offices don't have a taxpayer name at that point, of course; they're just dealing with a representative, usually. Some offices will perhaps get the business the taxpayer is in, and I think maybe part of a postal code or something, but that's about the extent of the information.

Other offices will wait until they have more facts—not necessarily the taxpayer's name, but the types of income we're talking about, or whether we are talking about GST or income: some more information to at least have a sense whether or not this might even be a voluntary disclosure. Sometimes it turns out there's no penalty involved, and there's no "voluntary disclosure": it's just a normal requested adjustment.

Then, although I don't believe any offices are doing it, other officers are of the view that the protection shouldn't start until the taxpayer is actually named.

**The Chair:** Thank you.

Ms. Wasylycia-Leis.

**Ms. Judy Wasylycia-Leis (Winnipeg North, NDP):** Thank you very much for appearing before us today.

This is an example of an area where you did an audit and were generally satisfied with the results, so there's not a lot to be critical about in terms of the specific issues you investigated about how decisions were resolved and whether they were impartially resolved and on how timely a basis. But it seems to me, reading between the lines, that you're fairly critical about the timelines, and I want to know what you expect from the department to deal with that concern. Have you set a certain timeframe by which they need to resolve this? Or how do we check to see whether they've acted on this, to see whether they're going to improve the timelines at all?

• (1610)

**Mr. Andrew Lennox:** In due course we will be going back in to CRA and doing some work on following up on our recommendations. CRA has agreed with all of our recommendations, with the one exception, I'd say, with respect to their concern on the issue of voluntary disclosure. The inconsistency with their view on that particular one was that the legislation speaks for itself as to what was granted by Parliament.

On all other recommendations, CRA fully agreed and committed to act upon them, and thus we will be going in due course to review their actions on each of those recommendations. In due course we'll be able to report back on them.

**Ms. Judy Wasylycia-Leis:** What would be a reasonable timeline for us to expect action?

**Mr. Andrew Lennox:** Normally we'll begin to do a review in a two-year timeframe, and about two years out we will do a follow-up of issues on it. We give the departments and agencies about a two-year timeframe to show results with respect to our recommendations.

**Ms. Judy Wasylycia-Leis:** Do they say they need more staff, or just need more efficient processing, or what's the root of the problem?

**Mr. Andrew Lennox:** I think they would argue that it varies with each particular case. In some cases, it might require legal help from within their own agency or from the Department of Justice. They have time quotas for each one of these phases. If it has to go to legal services, then another six months—I forget the exact timeframe—gets added, but they have different timeframes involved depending on what has to happen with each case. They use that as a way of monitoring their timeliness. I think we've mentioned that even though they're within their timeliness goals, some of the time goals are very long. From a taxpayer's perspective, to say it's going to take a year or more to settle—that's a long time. Even though it might be within the time goals they have set, nonetheless it's a long time.

**Ms. Judy Wasylycia-Leis:** Aside from the length of time it's taking to resolve these issues, do you have any comments on how consumer-friendly the operation is, vis-à-vis taxpayers trying to get their problems addressed or trying to get into the system? Sometimes

we hear from constituents about how hard it is to get into the system, and they get in and, sure, they're addressed on an impartial basis, but then it takes the time to get the answer at the other end. Do you have any sense of that? You probably weren't equipped to deal with that.

**Mr. Andrew Lennox:** I think the only reference we made was that the CRA is required as part of their procedures to send a letter to the taxpayer within 30 days of receipt of an appeal. That is done in most cases. We made a comment that while it's done, it doesn't really address the substantive nature of the appeal. In other words, it's not done by an appeals officer who has had a close look at the issues that are implied in this particular appeal. It's more of a general letter that says your appeal has been received and we'll look at it in due course, etc. We're suggesting it would be more useful for a taxpayer to have a more substantive type of response.

**Ms. Judy Wasylycia-Leis:** Do you get a sense of whether or not there is an inordinate number of disagreements with assessments or appeals, vis-à-vis CPP and EI, and could that possibly explain the problems they have in dealing with issues on a timely basis? In other words, is there something more fundamental at stake here? Is there an automatic or "more likely than not" tendency to reject an application, or quarrel with...? I don't know. I'm just trying to get a sense whether there's a bigger volume at the front end than should normally be the case for a bureaucracy of this nature.

• (1615)

**Mr. James Hood:** In the case of an income tax or GST dispute, you're dealing with the taxpayer and the agency. It's just a disagreement over an interpretation of the law, usually. But when you get into CPP or EI, often you're dealing with an employer, you're dealing with a worker, and you're dealing with the agency that is making a decision on whether you have an employer-employee relationship or a contractor relationship. No matter what the agency decides, one of those parties is not going to be happy. It's just a more difficult sphere in which to work.

**Ms. Judy Wasylycia-Leis:** Thank you, Mr. Chair.

**The Chair:** Thank you.

Mr. McKay, and then Mr. Pallister.

**Hon. John McKay (Scarborough—Guildwood, Lib.):** Thank you, Mr. Chair.

How many tax filers are there for income tax and GST?

**Mr. James Hood:** Coming from the agency's 2004 annual report.... I'm just trying to find the number here.

**Hon. John McKay:** I think there are about 14 million tax filers for income tax, but I don't know how many there are—

**Mr. James Hood:** I think it's more than that.

Here we are. There are 23 million individual and trust tax returns and 1.5 million corporate tax returns processed.

**Hon. John McKay:** Really.

**Mr. James Hood:** Yes.

**Hon. John McKay:** That's the better end of 25 million. Would I understand correctly if I were to say we have 47,981 objections out of that almost 25 million? Is that fair to say?

**Mr. James Hood:** Yes, I believe so. That's the number of objections, isn't it? Or is that the...?



**Hon. John McKay:** I was just looking at page 6 of your chapter. There are roughly 50,000 objections on 23 million filings.

**Mr. James Hood:** Yes.

**Hon. John McKay:** I have no idea whether that's a good number or a bad number. Is there any basis for comparison with anything else—any other country or any other international comparison?

**Mr. James Hood:** We didn't look at comparable countries in this case.

**Hon. John McKay:** Paragraph 8 of your speaking notes says on the one hand that you want to encourage taxpayers to correct past errors. Then you say in the next sentence that on the other hand you want to ensure the program is fair to compliant taxpayers. Then you say this calls for a lot of judgment on the part of the officers. And then you say the program is not administered consistently.

I wonder whether you are asking for two contradictory things. You are asking for judgment and you are asking for consistency of application. Judgment almost by definition, certainly if it resides in an individual officer, may well be inconsistent with that of another individual officer. The two of you may look at a set of facts and make a different assessment.

It was important enough to put into your speech, and I'm not quite sure what it is you are driving at here.

• (1620)

**Mr. Andrew Lennox:** What we're suggesting is for CRA to provide more guidance to their people in the field with respect to those types of decisions. As Jamie mentioned, in the case of voluntary disclosure it's as to when the starting point for voluntary disclosure should occur. Should it occur as soon as the very first phone call comes in? I think we have a little case in the chapter that describes a GST type of issue, where it was several years between the actual first phone call that came in to talk about the possibility for a voluntary disclosure right through to the time when they actually disclosed the name of the corporation.

The question is when that clock should begin to tick. We are suggesting that CRA should provide more guidance to people out there who have to make those judgments.

**Hon. John McKay:** Is the issue in that particular instance the date of the file opening, or is it the judgment the officer applied?

**Mr. Andrew Lennox:** We're saying that in practice we have seen an inconsistency across the country as to when, in this particular case—there are various other ones—the clock would begin to tick. We're suggesting that in order to deal with those inconsistencies, because taxpayers would expect everybody to be treated on the same basis, maybe some more guidance should be provided to those who have to exercise judgment, rather than leaving it totally to the individual judgment of each individual person.

**Hon. John McKay:** Don't the officers regularly receive bulletins on matters such as that?

**Mr. Andrew Lennox:** There is a web-based training program for officers, and that's a relatively new process, but certainly additional training and additional written guidance would be useful in these particular cases.

**Hon. John McKay:** Is it a question that the officers aren't reading the material, or is it a question that they're not encouraged to read it?

**Mr. James Hood:** Maybe one of the other issues also is the level of officer. It varies considerably across the country. I would think some offices are in some cases using lower-level officers who simply do not have the experience to apply the judgment required in a program of this type.

**Hon. John McKay:** My final question is with respect to paragraph 9. You raised a concern about a contradiction between the information given to Parliament regarding the intended use of the legislative authority and the way the authority is actually being used. Could you be a little more specific about that?

**Mr. James Hood:** That's what's described in paragraphs 10, 11, and 12.

**Hon. John McKay:** Oh, I'm sorry. I was thinking that was a stand-alone paragraph.

**Mr. James Hood:** No, it's just the introduction to the next section.

**Hon. John McKay:** Okay. Thank you very much.

**The Chair:** Thank you, Mr. McKay.

Mr. Pallister.

**Mr. Brian Pallister:** Thanks, Mr. Chairman.

I have just a couple of quick questions. Do appeals officers have the ability to forgive tax owing?

**Mr. James Hood:** I don't believe so, no.

**Mr. Brian Pallister:** Then is that up to collections guys later on, or a separate section of Revenue Canada?

**Mr. James Hood:** I'm not sure of the answer. That really should be addressed to the department. I'm sorry, but I just don't have the answer to it.

**Mr. Brian Pallister:** What I'm trying to ascertain is what latitude appeals officers have to set the level of tax owing. It's a negotiation process, I suppose in part, with the taxpayer. I am curious as to how they would go about arriving at that amount.

**Mr. James Hood:** Oh, all right, I understand. I have a better sense of the question now.

Appeals officers must—and as far as we could tell do—resolve disputes within the law; there's no question. If the law says “this is the amount of tax you pay on this”, there's no latitude to them there.

Obviously, however, they get into situations such as the example we cited in the chapter, where I might say I have a business, but I didn't keep a log of my travel. I know I drove my car mostly for business, but there's no real proof of that. The auditor comes in, audits my business, and says: “You have no log; you have no proof. I'm going to disallow all your travel or car expenses.” Then I object and dig out an awful lot more information and can convince the appeals officer that obviously I'm doing some travelling. We will saw it off at some point; there's no question. And I could have done that with the auditor in the first case, too.

**Mr. Brian Pallister:** So there's some grey area, leaving room for interpretation by the appeals officers?

**Mr. James Hood:** Not of the law, but on the facts; in that case, it's just on the facts.

**Mr. Brian Pallister:** Such as we're familiar with in the House: it's just a dispute over the facts when we disagree. Is it like that?

Okay, good.

Later on you allude to the issue of interest forgiveness, indicating there's some inconsistency in applying that interest forgiveness—I think in respect of 4% or something. Can you give me some clarification on that interest relief issue?

•(1625)

**Mr. James Hood:** The inconsistency we were concerned with there is between the voluntary disclosures program, which in certain circumstances will just automatically reduce the interest rate by four percentage points, and the fairness program, which is really the one that deals with the extraordinary circumstances taxpayers find themselves in. In those cases they look at every case individually and determine a reduction in interest.

**Mr. Brian Pallister:** As in some cases recently during the strike; would it be that kind of thing?

**Mr. James Hood:** Yes, it's that kind of thing. It's a much more one-off determination in the fairness program.

**Mr. Brian Pallister:** I can understand the issue in paragraph 6.23 better now, thank you: "We expected the Branch to keep track accurately of how the amounts in dispute were resolved, but we found it has not done so." I guess when I was reading that, it was rather a surprise to me. Was it a surprise to you?

**Mr. James Hood:** Very much so.

**Mr. Andrew Lennox:** It was our expectation going in that they would be doing that.

**Mr. Brian Pallister:** Yes. This gets into one of these resources questions again. There's always a question of resources required to keep track of anything. This is a massive issue. Mr. McKay alluded to it earlier. What are we talking about here? Of 59,000 objections in 2003-04, 93% of them—it seems impressive on the surface of it—were resolved: the appeals officers' decisions were accepted by the taxpayer.

This is what you're talking about keeping track of, isn't it?

**Mr. James Hood:** That's right. And they are keeping track of the numbers. They're keeping track of how many cases there were where they confirmed the assessment, how many where they overturned the assessment, and how many where they varied the assessment. We're saying they should keep track of the dollars as well.

**Mr. Andrew Lennox:** And it's important to note that they've agreed to do that going forward.

**Mr. Brian Pallister:** Yes. This gets into another issue and another chapter for another time, I suppose. That's on the collections side, where there's more latitude given for forgiveness of interest and so on, where that would seem to be even more important.

Let me ask you this closing question. Is the voluntary disclosures program encouraging compliance and protecting the tax base—yes or no?

**Mr. Andrew Lennox:** That's a question we asked CRA as well. We've encouraged them to do an evaluation of whether the voluntary disclosure program is indeed meeting its goal of improving tax compliance. Again they've agreed to do that. Based on their

evaluation, we'll have a look at it and see what the result is. We did not do that evaluation ourselves.

**Mr. Brian Pallister:** No, but it was one of the objectives of your audit to determine that, and you failed to achieve one of the objectives of your audit. Is that correct?

**Mr. Andrew Lennox:** We have made a recommendation to the agency. The agency is responsible to do evaluations of its programs. We suggested that it in fact do that for the voluntary disclosure program, and we'll look at those results at that stage.

**Mr. Brian Pallister:** There's serious room for improvement. That's self-evident.

**Mr. Andrew Lennox:** We think it's important to know whether the program is achieving its goal.

**Mr. Brian Pallister:** Good. Thank you very much.

**The Chair:** Thank you, Mr. Pallister.

Ms. Minna.

**Hon. Maria Minna (Beaches—East York, Lib.):** Let me pick up a couple of things. One is on the fairness appeals. Is the only reason for reducing interest rates from the fairness process undue hardship, meaning the inability to pay because of income problems or what have you, or are there other criteria, other reasons? Is it strictly to do with hardship situations? Are there criteria in the fairness provisions to reduce interest rates and/or give other breaks strictly based on hardship, or are there other reasons for them to do that?

**Mr. Andrew Lennox:** I have a couple of comments. One is we mention the fairness provisions in the chapter, but the focus of our audit was not on the fairness program. A number of years ago we did an audit that covered the fairness provisions, so purposely we excluded it from this particular case.

Having said that, yes, hardship is one aspect, but there are others with respect to things that have occurred beyond the taxpayer's control, such as if CRA made a mistake itself and messed something up and as a result delayed the taxpayer's knowing he or she was supposed to pay something. That's another reason to grant the forgiveness. There are a number of criteria that are used beyond hardship.

•(1630)

**Hon. Maria Minna:** The reason I was asking is that I've had a few constituents come in who felt the mistakes were made by the CRA, which is why they were not caught in the first place. But they weren't getting anywhere because nobody was admitting to them.

**Mr. Andrew Lennox:** If that's the case, technically that is also a reason for granting forgiveness.

**Hon. Maria Minna:** So it's a question of proving that and having the person who dealt with it at CRA admit the fact that there was a mistake made. That's another struggle.

I'm curious about the appeals on CPP. Are they on disputes of moneys to be paid or on whether or not one is eligible for CPP at all? Are appeals of CPP done at HRDC, as I thought, or at CRA?

**Mr. Andrew Lennox:** They're done at CRA.

**Hon. Maria Minna:** Are they really? I used to always think it was over there. So this is eligibility—

**Mr. Andrew Lennox:** As far as eligibility as to whether, in the case of CPP, the employment is pensionable is concerned—is it employment or is it contracts—

**Hon. Maria Minna:** —or whether they are fully disabled or not.

**Mr. Andrew Lennox:** In the case of whether employment is eligible for CPP contributions as pensionable employment, it is CRA. There are other aspects that the—

**Hon. Maria Minna:** It's just that I for some reason thought the CPP appeals were being done somewhere else in terms of eligibility, which then brings me to another question on—

**Mr. Andrew Lennox:** As far as I know, the only thing in CPP or EI that CRA deals with is determining whether or not you have an employer-employee relationship, and therefore whether the earnings you're talking about are pensionable or insurable. The other aspects of CPP are not dealt with by CRA.

**Hon. Maria Minna:** You don't deal with appeals of disability, in terms of whether—

**Mr. James Hood:** No, that's over in....

**Hon. Maria Minna:** Okay, so there are two pieces here. That's what I wanted to clear up.

Were you able to determine what was causing the difficulty in resolving issues in a timely manner?

**Mr. James Hood:** Do you mean in the case of CPP and EI? I think it's primarily just the nature of the dispute, because you have two parties involved: you have the employer and you have the worker.

**Hon. Maria Minna:** Is it a matter of maybe extending the period so that it is timely, because we're being too demanding? Is that what you're saying?

**Mr. James Hood:** I'm not sure whether that's the issue or whether it's just a workload issue for CRA to deal with.

**Hon. Maria Minna:** Okay. Thank you, Mr. Chairman.

**The Chair:** Monsieur Bouchard.

[Translation]

**Mr. Robert Bouchard:** I had an opportunity to visit a taxation data centre in my region several months ago. A number of employees shared with me their frustration about certain things, specifically the centralization in Ottawa of services that used to be provided at the regional taxation centre. I got the impression that centralization might be impeding the efficiency of tax return processing operations.

Can you tell us whether cooperation between the central Agency in Ottawa and the regional taxation centres is good? Obviously, I can't speak for all centres, but I got the impression that the situation could potentially impede the efficiency of operations at the taxation data centre in my region.

[English]

**Mr. Andrew Lennox:** That particular question was not part of the scope of our audit this time around, so it's difficult for me to comment on that particular question. It simply wasn't part of our scope.

Jamie, is there anything you wanted to add?

**Mr. James Hood:** Not really.

[Translation]

**Mr. Robert Bouchard:** Thank you.

• (1635)

[English]

**The Chair:** I have a quick question. I'm a little concerned about these going past the appeal dates, not only for the CPP and EI, but for the GST and for the income tax in particular, especially when we have the big large-business audits going to 332 days. With Revenue Canada going in late, they are already going in at a disadvantage, because they are already in default, are they not? They're not in a positive negotiating position if they're already in default, so obviously when it comes to negotiating they've already pretty well given up their hand, I would think. Doesn't that cost money to the Canadian taxpayer?

**Mr. Andrew Lennox:** Do you mean the long delay?

**The Chair:** Yes.

**Mr. Andrew Lennox:** Overall we looked at the time delays in all of these cases and we certainly recommended to CRA to review.... I guess the general message was we're not all that pleased with the timing side of things. We certainly were happy with the independence and objectivity and the fairness of their views. But from a timeliness perspective, what we did was look at the time goals CRA themselves had set for these categories. We then compared how they were doing in relation to their time goals. I think the key test on all this is that the taxpayer has a right to go forward to the tax court after 90 days, and clearly very few do so. They are not happy about the long process, but they seem to be willing to wait.

**The Chair:** Obviously—they don't want to antagonize the CRA. But if I have a dispute, I'm going to wait for CRA to take its time, and when I'm sitting down at the table I'm going to say, "Listen, you guys are late." If there's legislation that requires them to answer an appeal or an assessment or a notice of objection by a certain date or time, they have to respect that. If not, then are they not in default already when they're approaching a file, or when they're trying to assess or reassess a file?

**Mr. James Hood:** The legislation simply is permissive in this case. It allows the taxpayer to go forward to the tax court if he or she hasn't received a response within 90 days. But the taxpayer does not have to go forward and can in fact wait as long as necessary. In fact, in many cases that wait is necessary because there is a similar case in the courts already, so you're just going to wait to see what the result of that case is, and then yours will be decided.

**The Chair:** But the taxpayer has a certain number of days—I think it's 90 days—to appeal his assessment. Revenue Canada has a certain number of days to answer that objection, does it not? It's not unlimited time. Once you've passed that time, they're in default.

**Mr. James Hood:** No, it has unlimited time. It's just that after 90 days the taxpayer has the right to go ahead, but doesn't have to go ahead. So no, the legislation does not say Revenue Canada must provide an answer by 90 days. The legislation turns it around and puts the onus in that case on the taxpayer, to say, "If you want to go to the tax court now, you're free to go." You can't for the first 90 days.

**The Chair:** So the onus is on the taxpayer both times, to make the appeal and then to wait for—

**Mr. James Hood:** That's correct.

**The Chair:** I'm not sure whether I agree, but anyway...

I want to thank you for appearing before the committee.

We're going to suspend for two minutes. The meeting is suspended.

• (1638) \_\_\_\_\_ (Pause) \_\_\_\_\_

• (1645)

**The Chair:** Good afternoon, Mr. Timmins and Mr. Zafiriou. You will have a ten-minute intervention.

Pursuant to Standing Order 108(2), this is a study of chapter 2, "Implementation of the National Initiative to Combat Money Laundering", of the report of the Auditor General of Canada to the House of Commons.

**Mr. Douglas Timmins (Assistant Auditor General, Office of the Auditor General of Canada):** Thank you, Mr. Chairman. I'm very pleased to appear before the committee today to discuss our recent audit of the implementation of the national initiative to combat money laundering.

As you've mentioned, I'm accompanied by Basil Zafiriou, the principal in the office who led the audit team that conducted this audit.

[Translation]

We appeared before this Committee in May 2003 to present the main findings of a study that described money laundering and identified key challenges to combating it. This audit follows from that study and focusses on the National Initiative to Combat Money Laundering that the government launched in 2000.

[English]

Financial institutions and other providers of financial services are now required to report certain financial transactions to the Financial Transactions and Reports Analysis Centre, called FINTRAC. FINTRAC analyzes these reports for links to money laundering or terrorist financing activities and discloses pertinent information to the police and other authorities. In 2003-04, FINTRAC received some 10 million transaction reports. It made 197 disclosures to law enforcement and other agencies, up from 103 the year before.

Our audit found several factors that impede the national initiative's overall performance. To safeguard privacy rights, the legislation limits the information FINTRAC may disclose to so-called "tombstone" data: when and where the transaction took place, the value of the transaction, the account numbers, and the names of the parties involved.

We found that these restrictions limit the value of FINTRAC disclosures to law enforcement and security agencies. Law enforcement agencies told us the tombstone information they receive is too limited to justify launching investigations. The exception is when a disclosure is related to an ongoing investigation. In these cases, the information disclosed can help corroborate findings or provide new leads. This is a serious criticism of a system set up

expressly to add value to the financial information provided by reporting organizations.

An additional limitation on the effectiveness of the national initiative is the exemption from reporting requirements that lawyers obtained as a result of successful legal challenges to the legislation. It means that individuals can now do banking through a lawyer without their identity being revealed, bypassing a key component of the anti-money-laundering system.

Insufficient cooperation is another impediment to the national initiative's performance. The national initiative to combat money laundering involves a partnership among several federal departments and agencies, provincial law enforcement agencies, and industry regulators. Cooperation among these partners is crucial to the initiative's success.

We found that the necessary cooperation was not always present. For example, we noted that FINTRAC and the Canada Revenue Agency had not agreed upon criteria for identifying money-laundering transactions that could be related to tax evasion. We also noted that reporting organizations received little feedback on the quality of the reports they submit to FINTRAC and on how or to what benefit the reports are used.

[Translation]

To improve cooperation, the audit report recommends that an effective management framework be established to provide direction and to coordinate anti-money laundering efforts at the federal level as well as with stakeholders at other levels of government and in the private sector.

• (1650)

[English]

Finally, the audit found that FINTRAC is using an incomplete system to measure and report the impact and performance of the national initiative. Information needed to measure performance has been limited so far. The performance indicators FINTRAC currently uses are mostly measures of operations, such as the number of reports received, disclosures made, and memoranda of understanding signed.

There is no formal mechanism for tracking the use of FINTRAC disclosures and measuring their effects. Without a comprehensive system for monitoring the use of its disclosures, it's impossible for FINTRAC to assess the value of the intelligence it provides and the impact it has on money laundering and terrorist financing.

The Proceeds of Crime (Money Laundering) and Terrorist Financing Act calls for a parliamentary committee to review the administration and operation of the act this year. We hope our findings will be useful in that review.

Mr. Chairman, we would be pleased to respond to the committee's questions.

**The Chair:** I think I did it in private, but just to put it on the record, I want to thank you for appearing before the committee.

Mr. Penson.

**Mr. Charlie Penson (Peace River, CPC):** thank you, Mr. Chairman.

I am wondering if you gentlemen can tell us if you've looked at any other countries that have a system that would work better or is more effective than what we are currently using.

**Mr. Douglas Timmins:** We didn't look at other countries' systems extensively. FINTRAC has certainly been involved in discussions with a lot of the other countries, and in our discussions and reviews we have some intelligence about what those other systems would look like.

Perhaps Mr. Zafiriou would add to my comments, but generally we have put in a system that now brings us pretty close. The lawyers' exemption I mentioned may be a bit of an exception to our meeting more or less the international standards. We are one of the few countries that collect so much information electronically. We are one of the largest ones, in terms of the size of the operations of the system we have.

Some of the other countries—such as, I believe, Australia—would be very comparable in some of the things they are trying to do. The United States would be much bigger in terms of its activities, but not necessarily doing all of the same things we would do.

Would you like to add, Basil?

**Mr. Basil Zafiriou (Principal, Office of the Auditor General of Canada):** That's quite right. Actually, countries have their own financial intelligence units that are tailored to their own circumstances. When we put our own initiative in place, privacy concerns were a major factor in establishing it in the way we did, as an arm's-length agency separate, say, from law enforcement and also with all these restrictions on disclosure.

Most other countries allow easier access, say by law enforcement, to the data the agency collects. In that sense we are, I would say, almost unique. But those countries that have established financial intelligence units have certain common elements, in that they collect information—but what kind of information and how extensive it is varies—and in that they analyze it and report back to law enforcement. Again, the relationships between law enforcement and the agencies vary.

**Mr. Charlie Penson:** I'm sure you've had discussions with FINTRAC about the shortcomings you see in their operation. Did they tell you they could bring in measures that could fix these shortcomings? What sorts of discussions did you have in that regard?

**Mr. Douglas Timmins:** I believe that in each of the cases in our report we've made recommendations. There are eight of them. Four of them were directed specifically to FINTRAC, and in our discussions they've responded relatively positively, in our view. There's a commitment to take them into account and take action, I think, on all of them.

The one aspect of the report in which we recommend having broader performance measures may be a little more difficult. They're not the only player in that, but that is the one that might be more challenging. For the others, I believe they've indicated quite positively that they intend to respond.

• (1655)

**The Chair:** Mr. Loubier.

[*Translation*]

**Mr. Yvan Loubier (Saint-Hyacinthe—Bagot, BQ):** Thank you, Mr. Chairman. Thank you as well to Mr. Timmins and Mr. Zafiriou.

I have a few questions for you, Mr. Timmins, concerning your presentation, and for you, Mr. Zafiriou, concerning your account of how things are done elsewhere.

You maintain that the tombstone data collected at the centre is too limited, given its very nature, to be of assistance to agencies doing investigations. This data is too general and does not make the fight against money laundering any more effective, except in cases where investigations have already been launched.

What type of information do you think should be collected and passed along to other investigative agencies to ensure that the process is truly effective? Have you looked to investigative bodies for suggestions on how to make operations to combat money laundering more effective?

[*English*]

**Mr. Douglas Timmins:** Let me first correct the assumption. What is provided is accurate. It is not an issue of inaccuracy; it is the question that there's not sufficient context for the police or law enforcement authorities to see what led FINTRAC to conclude they suspected money laundering.

[*Translation*]

**Mr. Yvan Loubier:** That's the gist of my question, Mr. Timmins. What additional information is needed to make this process work? If we continue to collect tombstone data, which is truthful and accurate — I've never doubted that — and if investigators and law enforcement agencies maintain that this kind of information is too limited, we'll merely be collecting this information for no good reason.

[*English*]

**Mr. Douglas Timmins:** All I'm saying is primarily FINTRAC does an analysis that leads them to believe there's money laundering involved. When they have provided the raw information I described, the police would have to go through the same analysis. They have no access to the analysis that has led FINTRAC analysts to conclude that money laundering may be suspected in this case.

The police are basically given a raw file and have to start an investigation themselves and come to the same conclusion as FINTRAC, which has already done that analysis. It is the sharing of the analysis that FINTRAC did that would lead them in seeing what pieces of information they were connecting, one to the other, and why they were then suspecting.

The reason this is not being done, as Mr. Zafiriou said, is to protect the privacy of the individuals, because the worry, I think—and I wasn't involved in the establishment of the original legislation—is to protect the people who might be innocent from being accused, or because of concern about how the police might use that information.

As Mr. Zafiriou said, in other countries it has not been as much of a concern as it has been here, and it certainly, from our point of view, is something that needs to be considered by the parliamentary committee that is reviewing the legislation this year.

[Translation]

**Mr. Yvan Loubier:** Therefore, if we take into account the fact that tombstone data is fundamentally weak and of little value, except in a few rare cases, to law enforcement officials, for instance, and if furthermore, we consider the exemption from reporting requirements obtained by lawyers, who, for the most part, engage in either criminal or legal transactions, we see that these provisions to combat money laundering operations may have appeared very bold indeed in the legislation to establish this initiative, but that ultimately, we're no further ahead, because of these two restrictions.

Earlier, Mr. Zafiriou told us — as you yourself may have done as well — that he had read about a different approach being taken elsewhere. To your knowledge, is Canada the only country where lawyers benefit from an exemption and where gathering information about transactions is such a risk-averse process?

• (1700)

[English]

**Mr. Douglas Timmins:** No.

First, let me respond to one of the earlier comments you made. We would point out that even the tombstone information is viewed as useful by the police enforcement agencies in the case where they have an ongoing investigation. It adds information, and they would certainly say it adds value from that point of view.

Part of the issue may be as well that the other information may be very useful to them but they don't have the resources to do the analysis. That's why we're suggesting that if there were a way around that, it would allow them to deal with more cases.

To get to your point about the exemption for lawyers, they are included in most of the six or seven or eight larger countries we've checked. The one that is similar to us would be the United States. They're exempt in the United States.

[Translation]

**Mr. Yvan Loubier:** Did I understand you correctly to say that no other country, with the exception of the United States, grants this kind of exemption?

[English]

**Mr. Douglas Timmins:** Lawyers are included in countries such as Australia, New Zealand, the United Kingdom, the Netherlands, Germany, France, and Belgium. There may be some limitations in those countries as to the types of transactions for lawyers. It doesn't have to be everything, which may be part of their concern, but many countries like those have....

[Translation]

**Mr. Yvan Loubier:** Thank you, Mr. Timmins.

**The Chair:** Thank you.

Mr. Cullen.

[English]

**Hon. Roy Cullen (Etobicoke North, Lib.):** Thank you, Mr. Chair, and thank you to the officials.

I was very much involved in the implementation of the proceeds of crime legislation and the establishment of FINTRAC, so I

understand some of the background. Now in my new responsibilities I've seen it being handled through the RCMP and the integrated proceeds of crime units and I've taken some time to see how it works on the other end as well.

I think it's not that accurate to talk about the tombstone data being inaccurate or incomplete. The tombstone data are designed in a way that will walk the fine line between what is allowed under the privacy rules and what the RCMP or other law enforcement can use.

The idea is that they look at the tombstone data, and there are certain patterns that FINTRAC sees. Then the law enforcement people can have a look at it from their perspective, and if they think there is sufficient scope to do a review, then they would go to a judge to get a warrant. If they can convince a judge of that, they can get all the data they want.

So the idea of the tombstone data being incomplete or inaccurate, I think, is.... It was designed to be sufficient for the RCMP to look at trends, but not to invade the privacy rights of Canadians.

That's why, with reference to identifying criteria with the Canada Revenue Agency for tax evasion, the government was very careful at the time to have as the primary focus money-laundering activities with the focus on major crime—where a good chunk would be drug money—and others. Many Canadians were concerned, in fact, that people would be checking up on a deposit over \$10,000 and trying to nail them for some kind of tax evasion. The idea was to have the focus clearly on proceeds of crime, and there might be some ancillary work that could be done on tax evasion if there were a case to be made. So I'm not surprised that there are no discrete protocols.

I'll just come to two questions, then, one on the question of the lawyers. Of course the idea at the time was to scope in everybody, because leaving a chink would create a problem, and while 98% of lawyers are honest citizens, there is the small percentage who aren't, and if you leave that door open, the money laundering could proceed through there. But the reality is the lawyers have launched a lawsuit under solicitor-client privilege. I know the Department of Finance is trying to negotiate something through that. I don't know if you've followed up or if you know, but maybe you could tell us where those negotiations are with respect to that.

The other question is, while you seem to acknowledge there are privacy rights for Canadians, you flag an item to which there doesn't seem to be much of a solution unless the government decides to invade the privacy rights of Canadians.

Maybe you could comment on those two points.

• (1705)

**Mr. Douglas Timmins:** Mr. Chairman, first of all I would like to correct. I never said the tombstone data was inaccurate; I was trying to comment that it wasn't. I think the concern is that it was felt to be incomplete by the law enforcement authorities. Mr. Zafiriou may be able to add something here.

In the concern about the process you described, you're describing what were called production orders, where they would get the information. There have only been two cases of that used. I go back to the point that the law enforcement people are very busy and have many other investigations that are ongoing. They don't have the time to initiate a new investigation and go through all that analysis. That's the point we're trying to raise and that they're raising with us.

**Hon. Roy Cullen:** Just on that point, I want to pick up. I have visited the RCMP and visited their proceeds of crime units. I'm quite curious because of being quite involved in FINTRAC and what they do. They took me through a few cases where they actually plot out all these various relationships. They may have some data from FINTRAC that show some relationships, so they map it, and they also have other information through leads, through informants, through good police work, and they put it together. What they told me was that often it helps them to corroborate the case they're building and reinforce whether they're on the right track or not. Whether they actually go back to get all that information is not necessarily, in my judgment, a sign that it's not useful.

The other point is, I think you're right that they are swamped. They made that point to me as well, that if you're dealing with some tombstone data and some interrelationships and you have the phone ringing with someone saying "I just saw someone drop off ten grand at Thomas Cook in U.S. dollars", you follow the really fun lead. I don't think you're trying to create the impression that the information's not useful, but all of government is under resource constraints, and unfortunately they can't follow up on everything.

I didn't mean to interrupt, so carry on.

**Mr. Basil Zafiriou:** Just to possibly add to what Mr. Timmins said about the disclosures FINTRAC provides to law enforcement when they relate to an ongoing case, you're absolutely right: these could corroborate information they have, or they could provide new links—they have proven useful. But when they get into situations where they have a cold case and all they get is this so-called tombstone data, what we were told is that it doesn't provide them with sufficient grounds to then launch an investigation of their own.

You're right in saying they could go to a court and ask for a production order to get the analysis behind that data, but they would have to convince the court that they have reasonable grounds to believe a crime has been committed, and the information they get from FINTRAC in that tombstone data is not sufficient. In other words, they would have to launch an investigation to decide whether to convince the judge to allow them to go after the additional information.

What they're saying is that perhaps in those cases where individuals have been identified as having committed or having been involved in money laundering or terrorist financing, FINTRAC should provide some context: what were the reasons that led FINTRAC to suspect?

**Hon. Roy Cullen:** My understanding, though, is that it was never meant that this was all supposed to be cold data. My understanding is that the way it was meant to work is that FINTRAC would provide this tombstone data. That would show that there are some strange deposits going on and there are some characters who seem to be involved, etc. Then the police look at it and say, "These are some

strange deposits going on in these areas where we know we have a problem with drugs"—or whatever—"and there are some similar characters involved", so they start to piece it together. Then, if they have something that seems to be meshing and want to pursue it further, they go to get more data.

I don't think it was ever envisaged—maybe from time to time—that this would just be cold information, that it wouldn't be matched with anything the law enforcement has. That's my understanding.

• (1710)

**Mr. Basil Zafiriou:** But they do get cases where they don't have anything themselves going on. If they do, you're right: when there is something already going on, they find it useful because it adds additional information.

**Mr. Douglas Timmins:** We're not intending to be negative here, but if FINTRAC is producing a number of disclosures, those are things they're initiating. There's not an interaction between FINTRAC and the enforcement agencies. If there were that and if there were a way....

You asked the question about whether we were advocating something that would have an impact on the privacy of citizens of Canada. I don't think that's what we're advocating. We're advocating, really, the case that this has been flagged to us as a problem when we did this review. It's up to Parliament now to consider, as they review this legislation, whether they want to make a change.

**Hon. Roy Cullen:** I'm not trying to be too defensive here either, because I was involved, but when you flag something like that.... This was clearly part of the challenge in designing FINTRAC and the proceeds of crime legislation: to find the fine balance so that it wouldn't be attacked and we wouldn't invade the privacy rights of Canadians. So while you can flag it, understand that.

I think you're right, in a sense, that because FINTRAC is relatively new, and because resources are stretched, and because everyone is feeling their way, there probably could be better cooperation, especially given the kinds of resources that would be needed to do everything. Of course, we can't do everything in government.

Just on the solicitor-client privilege point, do you know where those negotiations are? I guess you don't follow these things on a day-to-day basis.

**Mr. Basil Zafiriou:** No, but we've talked to the Department of Finance, and they've told us that they are progressing well. They are trying to bring them in and at the same time allow some carve-out for the solicitor-client privilege. They haven't concluded yet, but they expect possibly this spring that they might arrive at some solution.

**The Chair:** Thank you, Mr. Cullen.

Ms. Wasylycia-Leis.

**Ms. Judy Wasylycia-Leis:** Thank you very much for being here today.

I want to focus on one part of the report. It has to do with the section starting on page 17 of the chapter, dealing with unregulated money businesses.

I am wondering if it's ever possible for us to really put in place an effective mechanism or program to deal with money laundering if we continue to have in this country a totally unregulated money-business sector, where we don't have a clue how many such money businesses exist, never mind require them to be registered.

**Mr. Basil Zafiriou:** It's very difficult. That's how we flagged it. There are no easy answers.

Registration is one option that has been suggested by the FATF, the financial action task force, as a possible means of trying to get at it. It's not a panacea, but at least it will give the authorities some indication of who is out there. We heard from the major financial institutions that it would also provide them with some comfort that the entities they deal with are abiding by some controls that would allow them to put confidence in the transactions they are asked to do on behalf of these other financial intermediaries.

It would give the government a better handle on knowing who is out there and also, as I say, comfort to major financial institutions in dealing with them. On the other hand, it's not easy, because you can make money transfers today through all sorts of means. All it takes is a telephone call, and you could make it. How do you regulate everything?

Even, in other words, when you ask for registration, you will have to hope that most of these entities will register, but possibly not everybody will. So it's not a panacea, but it is an option that has been suggested.

• (1715)

**Ms. Judy Wasylycia-Leis:** You are right, it's not a panacea, but it seems to me it's an area we have to look at carefully because of the huge explosion of these money-lending services, these fringe operations that have sprung up like wildflowers as banks have pulled out from communities. We don't have any kind of clue what they do or what they're involved in.

You mentioned the argument you've heard, and I have heard the same, that in fact if you start to regulate and require registration of these outfits, you might just drive the transactions underground. But often these are dubious organizations to begin with. They are sometimes charging people 1,000% or 2,000% interest on loans.

I guess I'd like to ask you: wouldn't we be better to err on the side of some sort of knowledge about who they are and what they're up to than to believe that if we act we are going to have a bigger problem?

**Mr. Douglas Timmins:** I think you are right. I think there are certainly the two sides. I think there's a side that would say maybe some of them wouldn't mind being regulated and registered in some sense, because then it gives them some credibility and their image is enhanced. So there are two sides to the fence.

I think certainly it may not be a uniform solution. There may be certain areas where it makes sense to go by the regulation and restriction route. I'm not sure. It's not for us really to recommend specifically which way. We are flagging the issue, and I think it's something that requires some greater debate. There are, as I say, the

two sides. But some movement in this regard seems to make sense to us.

**Mr. Basil Zafiriou:** And the Department of Finance is looking at this.

**Mr. Douglas Timmins:** Yes.

**Ms. Judy Wasylycia-Leis:** Pardon?

**Mr. Basil Zafiriou:** The Department of Finance is looking at this right now.

**Ms. Judy Wasylycia-Leis:** Do you have any sense of how in the U.S., which does regulate or require registration of all of these money-lending outfits or fringe banking services, it has made a difference in their ability to deal with money laundering, or whether it has made it worse?

**Mr. Basil Zafiriou:** They've adopted it in response to some analysis they did, obviously. They have put out guidance as to how to register. It's hard to say, but obviously they believe it is helping. As I say, it's also a recommendation by the FATF, who believe it would be useful.

**Ms. Judy Wasylycia-Leis:** When was the final financial task force report done?

**Mr. Basil Zafiriou:** The FATF meets annually to discuss these things, and this is one of the—

**Ms. Judy Wasylycia-Leis:** Oh, the financial action task force on money laundering meets annually.

**Mr. Basil Zafiriou:** That's correct—well, actually, even more frequently. This is part of their 40 recommendations. One of them is that these money exchange houses be registered.

**Ms. Judy Wasylycia-Leis:** To what extent is this problem unresolved because it gets all tangled up in the federal-provincial jurisdictional stuff?

**Mr. Basil Zafiriou:** That's an issue. Obviously, a lot of these entities would be provincially registered or incorporated, but the legislation could apply to them. It would be under the Criminal Code, I suppose. I don't know.

**Ms. Judy Wasylycia-Leis:** Okay.

The last question would be just the question I asked on the previous issue. How do we measure change and how do we know, aside from your going in in another two years' time or so to monitor progress, what timelines to watch for? What specific commitments have been made by the government? What's the best way for us to be vigilant on this front as a committee?

**Mr. Douglas Timmins:** I can't remember whether there were specific commitments on dates in their response. I'm not sure.

This is an area where we did a study in 2003. We did this audit as a follow-up to that when we said we would. We knew the parliamentary committee would be reviewing the legislation this year. This is not something we will necessarily go back to do unless we feel or somebody signals that there's a major problem and that we should.



I guess we will monitor the recommendations and the responses to the recommendations in terms of both the Department of Finance's giving us an update and FINTRAC's giving us an update, because some of them were directed to the Department of Finance and some were directed to FINTRAC. We will monitor that. If we have major concern, then we might go in to do follow-up.

I would think the results of the parliamentary committee's review of the legislation and whatever changes they might make would maybe set out a basis for future follow-up.

We would hope this committee could be interested in this. One of the major things we've recommended is having better performance measures, rather than just the operational production statistics. Hopefully, that could go in one of their reports that would be public. That might be a reason for you to call FINTRAC to the committee to have a hearing. You could play a role, I would think, in that way if you wanted to.

• (1720)

**The Chair:** Thank you.

Ms. Ambrose.

**Ms. Rona Ambrose:** I had a question about FINTRAC's annual report with respect to money laundering. They've suggested that the almost 200 cases in the 2004 year, involving \$700 million in suspect financial transactions that were investigated in 2004, involved a significant rise from 2003, when they investigated \$460 million worth of suspect financial transactions. Of that \$700 million, their report shows that 10% is thought to be linked to terrorist activity and financing, so there's obviously an increase in that component as well.

I'm just wondering whether the increased investigation is a sign that things are working better, that they're tracking more, or is it that, as some speculate, more of these organizations are seeing Canada as an opportunity or a haven for money laundering?

**Mr. Basil Zafiriou:** It isn't easy to say. The full reporting under the legislation only came into effect in January 2003, so the previous year wouldn't have all of the reports they receive now. For instance, in fiscal 2003 they received 2.2 million reports or something like that. In the last year they received 9.5 million reports. So they receive a lot more reports now, and as they receive their reports, they have them in their data bank. When they get new information, they relate it to what they already have. As that data bank grows, they may find more links, and this may be related to that. It's hard to say what it implies about the extent of money laundering or terrorist financing.

**Ms. Rona Ambrose:** You say it's a matter that this is something that's new. Will there be a point when there can be a link made between the quantitative information you have and a thought about whether or not there is an increasing number of organizations using Canada as an opportunity to do money laundering?

**Mr. Douglas Timmins:** You'll note we didn't put that kind of information in our report. We focused on the number of transactions they looked at and the number of disclosures. The next logical thing would be prosecutions, and there are none. It's early days, and that's where we think the connection should be, because when they make the disclosures, the disclosures go to the police agencies, and they should be initiating investigations that would lead to prosecution. It's

more that side that would tell you whether the operation is being successful.

If your intention is only to determine whether there's more or less money laundering going on in Canada, then maybe their statistics will eventually tell you that. But as Mr. Zafiriou said, the volume of transactions and how much analysis they put into it is a factor. They're still developing some of their analytical skills and procedures. As they develop them, the amount they identify would go up.

• (1725)

**Ms. Rona Ambrose:** I have one other question with respect to privacy, because it has come up quite often with regard to FINTRAC's being able to disclose just tombstone data, as you mentioned. I wonder what privacy legislation oversees these transactions. Is it PIPEDA, the Personal Information Protection and Electronic Documents Act—the federal legislation? Does it involve the provincial privacy legislation?

I'm wondering also—you alluded to this legislation being amended or changed—whether you have suggested any changes to the legislation to facilitate these kinds of transactions.

**Mr. Basil Zafiriou:** The restrictions on what FINTRAC may disclose are provided in the Proceeds of Crime (Money Laundering) and Terrorist Financing Act, the act that set up the agency itself. So it's from part of the initial legislation setting up FINTRAC that those restrictions come.

In terms of recommendations we've made, as Mr. Timmins said earlier, what we've done is flag the impact these restrictions are having on the intelligence value of the disclosures FINTRAC makes. It is obviously up to parliamentarians to decide on the balance between privacy and security and make appropriate changes if necessary.

The Department of Finance has set up a committee that's looking into this issue right now, together with FINTRAC and law enforcement, in anticipation of the review Parliament will be making over the next few months. They may come up with recommendations.

**Ms. Rona Ambrose:** My understanding was that the electronic documents act would also have an impact on this kind of information and these types of transactions. Is that not the case?

**Mr. Basil Zafiriou:** I'm not sure. I don't think so. As I say, I think the original restrictions were placed in the act itself, and they emanated from charter rights concerns about privacy.

**The Chair:** Thank you, Ms. Ambrose.

Mr. Cullen.

**Hon. Roy Cullen:** I want to come back to this notion of measuring results. I know it's a significant challenge for FINTRAC and for the government generally, because once data is given to law enforcement, a long time could elapse. There could be charges laid; there might not be. If charges were laid or there were convictions, to what extent was the data from FINTRAC key in accomplishing that?

Then there's the other aspect of deterrence. If we ask how much money laundering is coming through Canada, how much money laundering would there have been without this legislation and without this agency? Who knows? Maybe it's had no impact. I doubt it, but how do you measure that? I know it's a significant challenge.

Do you have any ideas for them about how they might measure their effectiveness over time, or are they working on it? I'd like some concrete ideas.

**Mr. Douglas Timmins:** Certainly, as an organization ourselves who may be considered a deterrence factor, we'd agree with you and support the view that there is that.

In terms of actual measures, they have agreed this is an area on which they need to take action, so we've had discussions. They seem quite comfortable that this is something they can move forward on.

I agree with you that it will take time for it to come through. We're not looking necessarily for measures that are only identifiable to FINTRAC; they may only contribute to something. That is a useful analysis. But if they're not contributing, then they may want to do something different.

I don't know whether Mr. Zafiriou has anything to add to this in terms of the specifics of what they might do.

• (1730)

**Mr. Basil Zafiriou:** Only that FINTRAC has been working with law enforcement and security agencies to arrive at arrangements for getting feedback as to how they use the disclosures they give them, because obviously FINTRAC needs to know itself if it is to assess how it is performing.

They have been discussing with the RCMP and CSIS and provincial law enforcement putting in place arrangements to receive feedback as to how they use the information and what impact it has, but those arrangements are not yet fully in place.

**Hon. Roy Cullen:** In international cooperation, the same sort of rule applies: the chain is as good as its weakest link.

I note that through the financial action task force and other initiatives there are efforts being made to coordinate and to make sure that jurisdictions around the world have anti-money-laundering regimes in place. To what extent has that been successful? Has there been an increase in the number of countries that have been bringing in this type of program, or are there still a lot of countries that are pretty lax?

**Mr. Douglas Timmins:** Again I don't know whether Basil has something to add, but I listed earlier a number of the countries that include the lawyers, and those are some of the bigger countries. Those are the ones we looked at most. I don't know more broadly than that.

Do you have anything to add?

**Mr. Basil Zafiriou:** The members of the FATF have been increasing. There are sanctions for countries that will not comply with certain requirements. That's an incentive to bring more countries in, so in that sense there has been a greater coverage of countries that comply with the 40 recommendations of the FATF concerning anti-money-laundering efforts. Beyond that, we'd just be speculating on how effective these measures have been.

**The Chair:** Thank you, Mr. Cullen.

I want to thank the witnesses for appearing. Thank you for your time.

That's it. The meeting is adjourned.

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