



TEEKAY CORPORATION

Teekay Shipping (Canada) Ltd:

The Marine Midstream Company

Submission/Briefing Note

Pre-Budget Consultations

House of Commons

Standing Committee on Finance

August 12th 2011



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RECOMMENDATION

That the Government of Canada recognize the economic benefit of modernizing and amending the *Income Tax Act* (section 250(6)) with respect to International shipping companies who base their operations in Canada.

The amendments we recommend will result in the following:

- Sharpen Canada's competitive edge to keep and attract new international shipping companies to base their operations in Canada;
- Provide certainty to the international shipping community and allow our ports to capitalize on Canada's many other advantages; and
- Promote economic and employment growth with spin-off benefits such as additional maritime service enterprises such as ship brokering, marine insurance, shipping finance and maritime legal sectors

EXECUTIVE SUMMARY

- Teekay Corporation is a global leader in international shipping, serving as an essential link in the global energy supply chain, transporting approximately 10% of the world's seaborne oil.
- With a fleet of over 150 vessels, operated and managed by 5,500 sea-going and 850 shore-based employees, Teekay Corporation provides marine services to the world's major oil and gas companies.
- Changes made in 1991 and 1995 to the federal *Income Tax Act* were designed to attract international shipping companies to locate their head offices in Canada.
- These changes deemed a shipping company to be resident where it was incorporated, if the company carried on sufficient, strictly defined international shipping activities.
- This allowed a foreign incorporated company to move its *mind and management* to Canada while keeping non-Canadian sourced income exempt from income tax in Canada.
- The current rules are unduly restrictive, allowing a company to satisfy the residency deeming rule only if virtually all of its income is from international shipping or share investments in 100% owned subsidiaries that earn virtually all of their income from international shipping.
- Despite their limitations, the changed rules resulted in 14 shipping companies - one of which was Teekay Corporation - moving its head offices to Canada within the first five years after the rules were enacted.
- In 1991, Teekay Corporation established Teekay Shipping (Canada) Ltd. as its operational headquarters in Vancouver. Over 220 employees now live and work in British Columbia, including most of Teekay's senior management team, including the chief financial officer, chief strategy officer, general counsel, head of corporate resources and three presidents of the company's five business units.



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- The presence of Teekay Corporation and other international shipping companies contributes to the growth of maritime service enterprises such as ship brokering, marine insurance, shipping finance and maritime legal sectors.
- Teekay Corporation believes the current Canadian tax legislation must be modernized to address the challenges faced by the shipping community in order to keep pace with the more favourable shipping tax regimes available in other countries such as the USA and Singapore with whom Canadians compete with for shipping business.

SUBMISSION

This Submission aims to suggest that legislative changes to Canada's *Income Tax Act* to amend the rules applicable to international shipping operations by foreign corporations operating in Canada, are required to improve Canada's competitive position as a destination for international shipping company head offices by accommodating the business models and structures widely adopted by the international shipping industry.

OVERVIEW

Since the set of changes adopted by Canada in 1991, the nature of international shipping industry has become more expensive, more complex and more competitive.

Shipping assets require major capital investments, with a shipping vessel costing between \$70 to \$250 million. As a result, joint venture corporations and partnerships are often utilized to finance the capital costs, share the assumption of risks and operate and maintain the shipping vessels. Canada's current tax rules (deeming rule) do not recognize these common facets of modern shipping business.

International shipping activities are very mobile, and because they are carried on trans-nationally they can be operated from any nation which offers the necessary supportive infrastructure, competitive tax laws and political stability.

Jurisdictions such as Singapore and US have adapted to this reality by providing companies with the needed tax certainty and flexibility to manage and finance their fleets.

Singapore continually refines and implements incentives for international shipping to attract international shipping and has reaped greater economic benefits from international shipping than Canada. In 2009 alone, 26 new companies agreed to invest in Singapore. Shipping is a key pillar of the Singapore economy employing 100,000 people and making up 7% of the gross domestic product.



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The USA provides simple rules for international shipping companies to provide operation flexibility and tax certainty. For instance the US determines residence by place of incorporation and does not apply stringent deeming tests required by Canada.

Unlike these other jurisdictions, Canada's tax legislation has not kept pace, putting Teekay Corporation and other foreign international shipping corporations, established in Canada as well as Canadian ports, at a competitive disadvantage.

IMPORTANCE OF CLOSING THE GAP

Canada's current shipping income tax legislation, does not fully address the business of international shipping and the evolution of company structures and practices which shipping companies have adopted over the past 20 years. The legislation does not provide a clear definition of the business of international shipping and therefore, does not account for modern shipping activities like shuttling, production or storage.

The existing residency deeming rule does not consider modern business structures, joint assets or integrated business practices carried on by affiliated organizations. In fact, the *Income Tax Act* is not equipped to properly handle the industry's modern partnership structures. As a result, companies like Teekay Corporation cannot move the head offices of their publicly traded daughter companies to Canada because the existing tax regime does not properly recognize these modern organizational structures and it leaves revenues earned through non-Canadian sourced activities vulnerable to Canadian taxation.

Teekay Corporation has developed low-cost proposals that are consistent with the Government of Canada's stated policy objectives which, if enacted, will modernize Canada's outdated Canadian international shipping tax regime, thereby closing the gap between the Canadian regime and the regimes of other competing countries. Teekay's proposals are broadly supported by the Canadian shipping industry and supporting industries, including the Chamber of Shipping of British Columbia.

The modified international shipping tax rules would make changes to the definitions in Section 248, Subsection 250(6), and Section 253.1 of the Federal *Income Tax Act*:

- The current *Federal Income Tax Act* lacks a clear definition of the meaning of international shipping. This means important concepts determining whether a company is a shipping company can be left to interpretation, creating significant tax risk for shipping companies operating in Canada. Teekay proposes a clear definition of international shipping activities which would include the following in the definition of international shipping:
 - inter-company charters;
 - pooling activities;



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- ancillary transactions within an integrated shipping business;
- certain service activities including transfer and storage of goods being shipped;
- Teekay proposes the modification of the determinants of residency of a shipping company to reflect modern day business structures and integrated business carried on by more than one entity:
 - The proposals modify the asset composition and gross revenue tests of subsection 250(6) to make the changes; and,
 - The proposed test would take into account these modern business structures by allowing joint venture and partnership investments (current rules only allow investments in 100% owned subsidiaries), and by accommodating integrated businesses carried on by more than one entity.
- Modify rules to allow non-residents to invest in shipping limited partnerships without being subjected to Canadian taxation (current rules allow corporate investment, but not partnership investments);
 - Modify section 253.1 to ensure that a non-resident of Canada who invests in a shipping limited partnership having operations in Canada, will not be considered to be carrying on business in Canada, solely because of the investment in the partnership.

THE BENEFITS OF TAX MODERNIZATION:

Teekay Corporation has embarked on a growth strategy with the creation of three new companies developed to meet the growing demand for secure shipping of natural gas, crude oil and other petroleum products. The proposed amendments will permit Teekay Corporation the chance to establish these leadership teams in its Vancouver Headquarters.

The implementations of these changes will in turn also create local, regional and national benefits by encouraging the international shipping community to consider Canadian ports as ideal locations for their activities and strengthening Canada as an international shipping hub. Ultimately these changes will:

- Sharpen Canada's competitive edge to keep and attract new international shipping companies to base their operations in Canada;
- Provide certainty to the international shipping community and allow our ports to capitalize on Canada's many other advantages; and
- Promote economic and employment growth with spin-off benefits such as additional maritime service enterprises such as ship brokering, marine insurance, shipping finance and maritime legal sectors



CANADA'S COMMITMENT TO GLOBAL COMPETITIVENESS

The Government of Canada has a strong history of recognizing the important role that competition plays in improving the productivity of our society. In 2008, the Government of Canada introduced its economic plan – *Advantage Canada: Building a Strong Economy for Canadians, a Long-Term National Economic Plan Designed to Make Canada a true World Economic Leader*- establishing a strategic, long-term economic plan designed to improve Canada's economic prosperity both today and in the future.

The Advantage Canada plan is focused on creating five Canadian advantages that will help this country improve its quality of life and succeed on the world stage: a Tax Advantage; Fiscal Advantage; Entrepreneurial Advantage; Knowledge Advantage; and an Infrastructure Advantage.

Advantage Canada was founded on four core principles aimed at guiding policy decisions to improve Canada's quality of life and making Canada a world leader for today and for generations to come. These four core principles include: focusing on government; creating new opportunities and choices for people; investing for sustainable growth; and freeing businesses to grow and succeed.

The Advantage Canada Plan is evidence that the federal government understands that improving competition in Canada will not only improve our quality of life here at home, but it will also increase Canada's competitiveness in the larger global economy.

Relative to the Advantage Canada Plan are the proposals we have made regarding the *Income Tax Act*. Canada's tax legislation must be modernized to address the challenges faced by the international shipping community to reposition foreign international shipping corporations established in Canada as well as Canadian ports, at a competitive advantage. By not keeping pace with the modern shipping tax regimes adopted by other countries, Canada will fail to consolidate the gains made in 1991 and miss out on the opportunity to grow an important and strategic industry sector.

RECOMMENDATION

That the Government of Canada recognize the economic benefit of modernizing and amending the *Income Tax Act* (section 250(6)) with respect to International shipping companies who base their operations in Canada.

As evident by the progress and success that was achieved following the changes that were made in 1991 and 1995 to the federal *Income Tax Act*, a recommendation in support of our proposals will put Canada one step closer to repositioning itself as a world leader in the international shipping community, Canada would once again become a competitive and attractive location for international shipping companies to locate their head offices.