

Perspectives on Tax Law & Policy aims to provide a variety of perspectives on important policy-related issues in the tax system, with the goal of fostering informed, accessible commentary that bridges the gap between tax professionals, policy makers, and the general public. The views expressed in the articles in this newsletter by any particular author are solely the personal views of that author. They should not under any circumstances be construed as reflecting in any way the views of the organization with which such author is affiliated or of any other person or entity.

Aligning Our Tax Policy with Our Economic Strategy

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This issue of *Perspectives* focuses on the appropriate Canadian tax policy directions for the new world order.

Amid the well-documented rupture in global geopolitics, Canada finds itself at a fascinating inflection point regarding both economic policy in general and the role of tax policy within that broader context. Canada's economy has been underperforming for some time. Our tax system should be aligned with our broader economic strategy, and the tax measures we prioritize should address our most pressing economic problems. Getting our economy on the strongest possible footing as quickly as possible should be Canada's number one tax policy objective, if our aim is to preserve our sovereignty and the values that make us Canadian.

What Have We Seen?

The events of the past few years are instructive. Only if we are clear-eyed about the world we live in and how it might differ from the past can we develop realistic solutions to today's problems.

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International Developments

Internationally, the last two years have witnessed remarkable fiscal conflict. The US president launched a beggar-thy-neighbour tariff war (economically equivalent to a de facto national sales tax) against the rest of the world while threatening to deploy "revenue taxes" (discussed in Robin Morgan's [September 2025 article](#) in this newsletter) against countries he sees as treating America unfairly. Robert Goulder described the situation succinctly in a [July 2025 article](#):

In the end, pillar 1 progressed no further than Treasury would allow.

Today, we have two new agreements to digest—one regarding the future of pillar 2, the other involving the Canadian digital service tax. They follow the same script. I claim no joy in saying this, but both deals were capitulations. The United States gave away next to nothing and, in return, gained exactly what it wanted.

We can talk all day about the shared benefits of multilateralism and cooperation—themes many readers find appealing—but the events of recent days demonstrate that fiscal sovereignty, deployed unilaterally, often has the upper hand. The rest of the world, it seems, shall receive only as much tax harmonization as Washington is willing to tolerate. These days, that's not much.

The United States proceeded to turbocharge its economy with a barrage of business-friendly tax measures in the [One Big Beautiful Bill Act](#). These measures included (1) the extension of expiring corporate tax rate reductions, (2) the permanent reinstatement and expansion of immediate expensing for certain qualified property and for research and experimentation performed in the United States, and (3) the expansion of tax benefits for investors in shares of a "qualified small business."

Like tariff policies, these tax measures aggressively seek to boost US economic activity, often at the expense of other countries. Welcome to the new age of bare-knuckle fiscal policy.

Domestic Developments

At the same time, domestic developments have increased the pressure on Canadian businesses to become more competitive.

“Pitiful” Productivity

Canada continues to lag behind its G7 peers (particularly the United States) in labour productivity. According to a recent [Statistics Canada report](#), Canada’s labour productivity, relative to US labour productivity, has fallen 26 percent since the late 1990s, with much of that drop occurring in the past five years.

The primary culprit in this shortfall is underinvestment in productivity-enhancing assets, “most notably investments in information and communications technology (ICT) assets, like the computer hardware and software that underlie the digital economy” (see [Globerman, *Canada’s Productivity Performance: An Historical Perspective, 1981-2024*](#) (Vancouver: Fraser Institute, 2025)). Little wonder that Bank of Canada Governor Carolyn Rogers described this phenomenon as a “break-the-glass” emergency.

“Unprecedented Capital Recession”

A recent report (Brennan and Panahov, “Capital Gains: How Canada Can Unlock the \$1.8 Trillion It Needs for Growth,” *RBC*, April 14, 2026) cites 2015-2024 as a decade of weak business investment. The report notes that “Canada now ranks last among G7 nations in investment in both machinery and equipment . . . and intellectual property.” Canada’s last-place ranking has been accompanied by a historic outflow of capital:

Over the past decade, Canada’s net outflow of investment exceeded \$1 trillion, the most significant capital exodus in modern Canadian history. For every dollar invested in Canada from abroad, two dollars exited. Canada accounted for nearly 10% of global outward foreign direct investment over the past decade, having exported more capital than any country on Earth save the U.S. and China.

The problem has not been a shortage of investable capital in Canada. As Brennan and Panahov note: “Between pension funds and asset managers, Canada is sitting on nearly US\$10 trillion in capital.” Rather, the problem is that investment opportunities outside Canada are more attractive than those within the country.

Innovation Economy

Canada punches below its weight in the digital economy, which is the tax base of the future. According to a report by the Information Technology and Innovation Foundation, it fares especially poorly when it comes to commercializing intellectual property (IP) developed in Canada. Most notably, early-stage ventures face a shortage of investor capital: in the first quarter of 2026, new venture capital investment in Canadian growth-stage companies amounted to a single \$1 million deal. Persistent deficiencies in our capital markets have resulted in a loss of talented young companies, with promising Canadian innovation businesses (such as [Internet Backyard](#)) relocating to the United States as part of a larger [brain drain](#). We are losing the race we most need to win.

What Has Been the Focus of Recent Tax Policy?

The past five years have seen many tax initiatives in Canada. These measures have focused on tightening the system and preventing base erosion. The most notable of these are the following measures, inspired by the [OECD/G20 base erosion and profit shifting \(BEPS\) project](#):

- major interest deductibility limitations in the form of the [EIFEL rules](#) (BEPS action 4);
- two rounds of rules dealing with [hybrid mismatch arrangements](#) (BEPS action 2);
- [mandatory reporting rules](#) (BEPS action 12);
- the “modernization” of Canada’s transfer-pricing rules to align them with [OECD guidelines and standards](#) (BEPS actions 8-10);
- [global minimum tax rules](#) enacted in 2024 as part of the pillar 2 initiative (BEPS action 3);
- [country-by-country reporting requirements](#) (BEPS action 13); and
- a particularly ill-advised digital services tax (DST) (BEPS action 1), which Canada plowed ahead with (ignoring repeated warnings from the business community) until finally [capitulating](#) in the face of US demands.

Tax initiatives with domestic origins include the “modernization” (again) of the general anti-avoidance rule, rules targeting “substantive CCPCs,” and measures aimed at “[limiting aggressive tax avoidance by financial institutions](#)”—all introduced as part of a “tax fairness” package in the 2022 federal budget.

General revenue-raising measures have also featured prominently. The most infamous of these is the 2024 proposal to increase the capital gains inclusion rate. Its design and implementation appeared politically motivated and (not coincidentally) [very poorly handled](#), and the proposal was eventually abandoned. This debacle created a [powerful disincentive](#) for venture capital investment generally and for [innovation-sector investment specifically](#), in part by tarnishing Canada’s reputation for stability and certainty. Other notable measures include the special taxes on financial institutions introduced in 2022 (see [Kronick and Robson](#) in the [March 2023 issue](#) of this newsletter), the share buyback tax announced the same year, and the 2024 expansion of the alternative minimum tax.

Relatively few of Canada’s tax initiatives could be described as economically stimulative. While the [clean economy ITCs](#) certainly constitute a major tax expenditure (and one that serves Canada’s best interests), their primary purpose is environmental rather than commercial. The most significant stimulative measures in recent years are the [2025 federal budget proposals](#) to (1) allow immediate expensing for certain capital assets and (2) modestly enhance the SR & ED rules. These are definitely steps in the right direction. The [accelerated depreciation rules for patents](#) announced in 2024 are also stimulative.

To date, however, there has been no progress on the government's proposal to create a patent box regime to support the commercialization of IP in Canada, nor on proposals in the 2025 Liberal Party election platform to extend flowthrough share financing to Canadian innovation startups or to introduce a new AI deployment tax credit for small and medium-sized businesses. The enactment of an employee ownership trust regime and the modest expansion of the capital gains deferral rules for transfers of eligible small business corporation shares are welcome changes, but their practical impact is limited.

What Should We Do?

The most critical step is to make tax policy an integral part of a national economic strategy. We should view the tax system as supporting a larger strategic framework—not merely as a way to raise money but also as an economic driver, and a potential source of competitive advantage in itself. This will require reframing our current system around Canada's economic goals, rather than designing tax policy in the abstract. The tax system's primary objective should be to foster a strong economy with more commercial activity and a broader tax base. Without that, our tax revenues will not be sustainable or sufficient, no matter how perfectly drafted or leakage-free.

A complete review of all the possibilities is beyond the scope of this article, but several general principles should guide the discussion.

We Could Think Big

There exist tax systems designed at the macro level to stimulate overall economic activity rather than passively raise revenue from whatever activity occurs. One example is the distributed profits tax in Estonia, which both I and others have suggested as a model for Canada. The Estonian regime essentially defers the taxation of corporate business profits until they are distributed to shareholders, providing an effective incentive to reinvest business profits. Latvia has adopted a similar system.

The US Tax Foundation recently ranked these two countries as having the most competitive tax systems among the 38 countries reviewed (Canada's corporate tax system was ranked 22nd). In a recent article in the December 2025 issue of this newsletter, Jack Mintz explored how a Canadian version of this model could work, and he continued this exploration in a recent, more detailed C.D. Howe Institute study. That study also proposed broader reforms to personal taxation and the overall tax mix, concluding that Canada could implement these reforms on a revenue-neutral basis. Canada can think big if it chooses to.

Adjust the Mix

A more modest reform could keep the existing income tax regime but adjust the balance among the different types of taxes. The US Tax Foundation reported in 2025 that, by global

standards, Canada relies excessively on income taxes and underutilizes consumption taxes. Consumption taxes tend to discourage commercial activity and investment less than income taxes do (see Baylor and Beauséjour, *Taxation and Economic Efficiency: Results from a Canadian CGE Model* (Ottawa: Department of Finance, 2004), at 30). This sort of reform would be relatively simple to implement and could encourage business investment, along with the jobs and tax revenue that it produces.

Design for Canada's Situation

We must focus on solutions designed for Canada's actual situation, not solutions based on abstract tax policy theory. No other country shares Canada's relationship with—and proximity to—the world's largest economy. And few countries, if any, have Canada's endowment of natural resources, social cohesiveness, and legal stability.

Brennan and Panahov, in the report cited above, propose \$1.8 trillion in investment across six strategic and capital-intensive segments of Canada's economy, funded largely or entirely from existing Canadian capital pools. Our tax system should be geared toward supporting exactly this kind of investment activity. Without it, our best cards remain unplayed. A number of measures—for example, broader immediate expensing, reducing or eliminating tax on reinvested earnings, more permissive interest deductibility rules, and investment tax credits to help de-risk major projects—would strengthen Canada's ability to compete in areas where it holds natural advantages over other countries. Policy makers should also consider asking tax-advantaged Canadian capital pools, such as pension funds, to play a larger role—perhaps through a dual-mandate system similar to Quebec's (see Curry and Bradshaw, "Pension Funds Should Invest More in Canada, Senate Finance Committee Chair Says," *Globe and Mail*, May 6, 2026). We have the tools we need to compete. We just need to pick them up and get on with it.

In a 2025 paper, I explored at length the ways the tax system could support improved productivity and the innovation sector in Canada. The problem most often identified by those working in this area is the shortage of risk-tolerant capital willing to make the necessary investments. As John Ruffolo has observed, "Canada has built one of the most powerful tax incentives in the world for housing—and one of the weakest for innovation." There is much more we could be doing: providing appropriate rewards for risk taking (and thus promoting all of the spinoff benefits that risk taking creates); reducing the after-tax cost of commercial investment; removing disincentives for firms to scale up; and unlocking Canada's tax-exempt investment capital, including funds held in TFSAs and RRSPs.

Our unique proximity to the US economy exacerbates the challenge we face. Canada is more exposed to US competition than other countries are, so our tax policy must be especially competitive relative to US policy (see Marotta, "Ottawa Should Change Tax Regime To Attract Investment, Citibank Canada

CEO Says,” *Globe and Mail*, April 22, 2026). Overall, Canadian tax incentives for investors are not nearly as attractive as the US incentives available for investment in qualified small business stock (see Cohen, “Reward the Risk Takers Who Build Canada,” *Build Canada*, July 17, 2025). Instead, we seem content to rely largely on the tax costs of emigration to keep our startups in Canada. This is not a viable strategy. Our timid tax policy reflects our minimal appetite for economic risk.

Think Very Hard About Joining OECD Crusades

Prioritizing Canada means not automatically adopting every international tax initiative being peddled by countries far less dependent on trade with (and far less geographically proximate to) the United States than Canada is. The fact the United States tends to opt out of these initiatives only increases the competitive disadvantage that Canadian participation can create.

Canada’s DST “own goal” is a prime example of a self-inflicted policy mistake. Its uniquely harmful impact on us was both entirely foreseeable and completely avoidable. The clearest evidence of this is that, while Canada rescinded its DST in response to threatened US retaliation, other countries have kept theirs in place. It was clear from the outset that the United States—the one country whose taxpayers were directly affected by the DST, and the country to which Canada is most economically exposed—would never allow the Canadian DST to proceed without serious bipartisan blowback.

The recent OECD-inspired Canadian legislative amendments listed above do not address Canada’s most important economic issues, and in some cases they may be counter-productive. Base erosion through interest deductibility either is not a problem for Canada—because other rules already address it—or ranks far below the more urgent priorities of a country facing long-term underinvestment, declining productivity, and the need for major investments in strategic, capital-intensive industries. The need for broad industry exemptions under the EIFEL regime suggests that these rules are too blunt an instrument for the limited benefits they bring. Canadian lending to Canadian businesses should be fully exempt from EIFEL.

When Canada considers adopting OECD-led initiatives, the key question to ask is: Does this initiative support Canada’s broader economic strategy? We need to pursue policies that work for Canada in its unique situation: the tail must stop wagging the dog.

A Buck Is Not a Buck

We must also move past the Carter commission slogan that “a buck is a buck,” in favour of real-world pragmatism. Not all forms of commercial activity are equal. Consider the following points:

- Some activities (for example, digital services) are more mobile than others and therefore harder to tax effectively.
- Canada has inherent non-tax advantages in certain sectors (such as natural resources and energy).
- Some activities, such as venture capital investment, generate greater spillover benefits in the form of jobs and taxable income than other activities do.

A tax system that ignores economic realities in favour of antiquated slogans does neither the country nor its tax base any favours. People and businesses today have choices about where to live, work, and invest, and other countries are actively competing to attract them. Whether we like it or not, and despite multilateral efforts to mitigate tax competition, Canada operates in a world where it needs to compete for the people and businesses that contribute most to growth and productivity. If that requires taxing some activities more lightly than others, so be it.

Cost-Benefit Choices

A reformed tax system must abandon ideological purity and make pragmatic cost-benefit choices that accept something less than perfection. Measures that inflict cost and complexity on the many in pursuit of a small number of potentially non-compliant taxpayers—and minimal additional revenue—should be reconsidered through a more pragmatic lens. A tax system focused on eliminating every possible leak regardless of compliance costs can suppress business investment and be a cure that is worse than the disease.

Canada’s foreign affiliate system raises very little revenue from the non-active business income of foreign affiliates, yet it imposes costly and burdensome surplus account tracking requirements on Canadian corporations with foreign operations. If Canada moved to a full exemption regime, as recommended in the 2008 report of the advisory panel on Canada’s system of international taxation, the only losers would be tax advisers. The EIFEL rules are similarly overbroad and complex and should be dramatically simplified so as not to target every possible time-value-of-money equivalent (a frustration familiar to anyone who has applied these rules to a lease portfolio). The hybrid mismatch rules present similar concerns. Leaving aside debacles such as the last-minute cancellation of bare trust reporting, the willingness of taxpayers to expend ever-increasing amounts on compliance—under a system whose administration consumes ever more public sector resources—has been exhausted.

Conclusion

Although Canada faces many challenges, it also has many natural advantages. We can change course if we are willing to use

tax policy to get our economy back on track and, ultimately, grow our tax base. Canada needs to align its tax policy squarely with its larger strategic economic objectives: our country now has economic priorities that far outweigh ensuring that large multinationals with Canadian group members pay at least 15 percent on all income earned worldwide. Let's concentrate on Canada's most pressing economic problems and take a broader view of what our tax system could achieve. ■

Is Canada's Tax Policy Fit for Purpose in the Ruptured World Order?

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In January of this year, Canada's prime minister asserted in Davos, to widespread acclaim, that there has been a rupture in the rules-based world order. Canada's diplomatic relationships and its trade, defence, and economic policies are being significantly reoriented in response to an assertive and aggressive United States.

But have Canada's tax policies adapted to this new world order? I contend that disappointingly little has so far been accomplished in the tax policy domain under Prime Minister Carney's leadership. The competitiveness of Canada's tax system has yet to be treated with the same urgency as our trade, security, and non-tax economic policies.

What Is Canada's Tax Policy Under Prime Minister Carney?

Readers of this newsletter may have shared my optimism that serious tax reform would finally begin when Mark Carney became prime minister on March 14, 2025. His Liberal Party's 2025 election platform pledged to conduct an expert review of the corporate tax system, and his immediate cancellation of both the consumer carbon tax and the ill-advised increase in the capital gains inclusion rate hinted at a shift toward improving Canada's tax competitiveness.

However, after more than a year of Prime Minister Carney in power, one full budget cycle, and the 2026 spring economic update, significant tax reform has not materialized. Tax measures announced by Mr. Carney's government have helpfully repealed some of the most egregious tax policy blunders of his predecessor, but otherwise they have, so far, failed to meet this moment of immense economic threat to Canada's prosperity.

A review of the Carney government's major tax policy initiatives to date reveals a surprising lack of ambition, given the crisis at hand. Most of these initiatives have focused on affordability and redistribution rather than Canada's long-term competitiveness and economic performance. These measures include fulfilling the campaign promise to reduce the lowest tax bracket rate to 14 percent—at an eye-catching estimated fiscal cost of about \$28.2 billion over five years, according to

the parliamentary budget officer (PBO). The government also introduced GST relief for first-time buyers of new homes up to \$1.5 million. In addition, the GST tax credit was increased (at a projected cost of \$11.8 billion over six years, according to recent PBO estimates) and disingenuously rebranded as the "groceries and essentials benefit." Groceries are already exempt from GST, so a natural question posed by the rebranding is whether the GST tax credit is now being inappropriately untethered from its longstanding purpose of offsetting GST regressivity. Federal fuel excise taxes were suspended until September 2026, effectively giving Canadians a summer gas tax holiday—a measure reminiscent of the gimmicky two-month suspension of GST, in Christmas 2024, on items such as restaurant meals, wine, beer, and children's toys. The PBO recently estimated that the temporary fuel tax suspension will cost the government approximately \$2.1 billion.

Although these tax measures may provide some relief to Canadians who are struggling with affordability pressures, they impose a huge fiscal burden that will effectively be financed through additional federal borrowing that shifts the costs to future taxpayers. This is a regrettable policy choice, because none of these initiatives is likely to improve Canada's long-term competitiveness and economic performance.

Tax measures aimed at improving competitiveness and reducing unwarranted compliance burdens have been largely confined to the repeal of several notorious Trudeau-era policies. These measures include—in addition to the cancellations mentioned above (of the carbon tax and capital gains inclusion rate increase)—the repeal of the underused housing tax, the elimination of the luxury tax on boats and aircraft (although this tax is retained for automobiles), and the cancellation of the digital services tax (DST).

The current government's tax policy emphasis on equity and fairness, and its continued neglect of Canada's tax-competitiveness problem, was also evident in the recent economic update. The limited tax measures included enhancements to the disability tax credit, tweaks to accelerated CCA for LNG facilities and to the investment tax credit for carbon capture and storage, and several other minor measures. These included making permanent the capital gains exemption for transfers to employee ownership trusts and relaxing the rules for the home buyers' plan. On the compliance front, some lower-income Canadians will have their tax returns automatically prepopulated so that they can more easily access benefits delivered through the tax system. However, a recent C.D. Howe Institute article suggests that the impact of this measure will be modest.

Absent from this underwhelming record is any meaningful use of tax policy to attract the business investment that Canada so desperately requires in order to improve its lagging productivity—a problem described as an "emergency" by a senior Bank of Canada official in a 2024 speech. There is no indication that the government is moving forward with its promised

corporate tax review. At this point, Prime Minister Carney's tax policy appears very similar to the hyperprogressive policies of his predecessor, focused primarily on costly affordability measures designed to benefit lower-income Canadians.

What Should Canada's Tax Policy Be Instead?

There are three widely accepted, long-established goals of principled tax policy: equity, neutrality, and simplicity. Sound tax policy requires balanced tradeoffs among these competing objectives.

Equity refers to the fairness of tax measures and how the tax burden is distributed. One dimension of equity is whether taxpayers in similar circumstances pay similar amounts of tax (horizontal equity). Another is whether taxpayers with a greater ability to pay bear a proportionately larger share of the tax burden (vertical equity). The level of progressivity deemed appropriate reflects political value judgments, including how much inequality voters are willing to accept as the outcome of hard work and entrepreneurial risk taking. As noted above, equity and fairness objectives appear to have motivated the current government's focus on tax measures enhancing affordability.

Neutrality refers to the impact of tax measures on incentives and behaviour. An ideally neutral tax system would interfere as little as possible in commercial and family decisions. The taxation of income inevitably discourages the generation of income to some extent, and the goal of tax policy is to impose the smallest disincentive possible in this regard. The neutrality objective is also closely tied to efficiency and competitiveness. Tax measures that depart from neutrality distort economic decisions and may result in a less productive allocation of resources, and unduly high tax burdens can make an economy less desirable in the global competition for scarce labour and capital. In the [December 2023 issue](#) of this newsletter, I outlined a "back-to-basics" tax policy, arguing that Canada's tax policy under the Trudeau government had largely abandoned neutrality as a guiding principle, as exemplified by that government's heavy reliance on activist tax measures to influence and shape taxpayer behaviour.

Simplicity refers to the ease with which taxpayers comply with the tax system, and taxing authorities administer it. It is a measure of how understandable, predictable, and workable the tax system is in its practical, real-world applications, such as determining tax liability, enforcing the rules, and resolving disputes. Canada's overly complex tax system is widely regarded as failing this test of simplicity. Most taxpayers require professional assistance even for basic compliance, spending time and money that could be reduced under a simpler system. For years, Canadians have been clamouring for tax reform to declutter and simplify our tax system and make it easier for ordinary taxpayers to navigate.

In my opinion, Canada's current tax policy does not properly balance the competing objectives of equity, neutrality, and

simplicity. The system continues to overemphasize a particularly progressive version of vertical equity while underemphasizing neutrality and simplicity.

We must reorient Canada's tax policy to restore neutrality and simplicity as objectives equal in importance to equity. This will require bold tax reform that once again makes competitiveness a priority of our tax system and eliminates many of the distinctions and specific treatments that add unwarranted complexity and compliance burden.

For this reason, I strongly endorse the recommendations in the C.D. Howe Institute's [Big Bang Tax Reform](#), released in March 2026, and the general thrust of CPA Ontario's [Tax Reform for Growth in Canada](#), published in October 2025.

For business income taxes, I support a meaningful reduction in the combined federal-provincial corporate tax rate, along with greater rate harmonization that would eliminate the small business deduction (SBD) and other non-neutral features of the system such as (to take two recent examples) the preferential rates for zero-emission technology manufacturers and special punitive rates for large financial institutions.

As I argued in the [June 2020 issue](#) of this newsletter, the SBD is a poorly targeted and outdated tax expenditure that could be replaced with more efficient non-tax supports for small business startups. Having a single corporate tax rate (while maintaining the refundable tax mechanism for the investment income of CCPCs) would allow for significant simplification; the system could return to a single dividend gross-up and tax credit rate, eliminating the need for corporations to track their "general-rate income pool" (GRIP) or "low-rate income pool" (LRIP) balances, as well as the need to classify dividends as eligible or ineligible. A single rate would also enable the government to peel back complex rules governing eligibility for the SBD, including the association rules and other detailed anti-avoidance provisions (sometimes the source of costly tax disputes) used to restrict multiple claims to the \$500,000 annual business limit. Although such reforms would be controversial and likely to be opposed by small business lobby groups, they would bring the small business sector significant compliance savings. Business investment in Canada would surely be encouraged by a more competitive unified corporate tax rate.

For personal income taxes, I support a reduction in the number of income brackets, and a flattening of the progressive rate schedule so that the combined federal-provincial top marginal tax rate remains below 50 percent across Canada. To simplify the system, taxpayers could be permitted (as proposed by the [March 2026 C.D. Howe report](#)) to choose a single tax credit in place of the plethora of bespoke deductions and credits. Further measures could include income averaging and elective spousal unit taxation, for the reasons I outlined in the [June 2025 issue](#) of this newsletter.

These reforms could be paid for, and potentially made revenue-neutral, by raising the federal GST rate (while

increasing the GST tax credit to offset the potentially regressive effects of the higher rate on lower-income Canadians). This would help reduce Canada's overreliance on income taxes and shift more of the tax base toward consumption expenditure. The resulting improvement in incentives would raise aggregate incomes and generate additional tax revenues, and the simplified system would reduce compliance costs.

Should Canada's Tax Policy Be Used for Geopolitical Leverage?

Returning to this article's headline question, it might be tempting to view tax policy as one of the many tools Canada can use to advance its interests in the current geopolitical environment. After all, the US administration's hegemonic bullying has extended into tax policy. The US threat of retaliatory withholding taxes under section 899 of the Internal Revenue Code compelled Canada to withdraw the DST and coerced the G7 to accept the side-by-side exemption from pillar 2 for US-based multinationals.

But it does not follow that Canada should reshape its tax policy in the service of short-term geopolitical objectives. The fundamental role of tax policy has always been to raise the revenues that government needs, in the least costly manner possible, while balancing the competing objectives of equity, neutrality, and simplicity. Using tax measures as bargaining chips would compromise these longstanding tax policy principles, and we should resist that approach.

Instead, the current crisis should spur meaningful tax reform focused on making Canada more competitive. That is the critical role for tax policy in this new world order. ■

Why Models Matter in Attracting Capital

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Canada is competing for institutional capital at a moment of global economic upheaval. In this article, we discuss the important role that the modelling of expected after-tax cash flows plays in the investment process. Tax laws and administration that prioritize simplicity and stability tend to be easier to incorporate into investment models and can encourage capital investment. By contrast, complexity, unpredictability, and frequent change can make outcomes harder to model and may reduce Canada's competitiveness as a destination for long-term investment.

Competing for Capital in a Ruptured World Order

Earlier this year, Prime Minister Mark Carney announced that the federal government will host the Canada Investment Sum-

mit in Toronto this September. The summit will bring together global institutional investors, with the objective of unlocking up to \$1 trillion in private capital for nation-building projects.

Canada has made similar efforts before. In 2016, the federal government and BlackRock co-hosted a summit aimed at attracting institutional investment, but the results were underwhelming. A recent RBC report found that net investment outflows from Canada exceeded \$1 trillion between 2015 and 2024. This is a striking figure, given that global investors continue to seek long-term infrastructure and energy assets that offer stable returns—assets that Canada could deliver. The challenge is that investor interest does not necessarily translate into committed capital.

The largest driver for investment decisions is the underlying economic opportunity itself, and investment models give this primacy. Models translate project fundamentals into risk-adjusted returns that can be ranked in relation to other opportunities, and ultimately are used to determine where to allocate capital. At the same time, the valuation metrics produced by these models are sensitive to tax expenses. While Canadian corporate tax rates have remained relatively stable, the stability and certainty of the tax system overall could be improved. Uncertain tax outcomes introduce model risk, which can quietly increase hurdle rates, weaken the effectiveness of tax incentives, and negatively affect the investment environment. In today's environment of economic uncertainty and mobile capital, stability and predictability are competitive advantages. If the September summit is to produce durable change, a more stable and predictable Canadian tax policy should be part of the solution.

Models Drive Capital Allocation

Institutional investors make allocation decisions by using investment models built by deal teams. Although modelling practices vary by asset class, discounted cash flow (DCF) modelling—typically supported by downside scenarios and sensitivity analysis—is the dominant method used by private investors to analyze and approve investments. DCF models project future cash flows to compute valuation metrics such as internal rate of return (IRR) and multiple on invested capital, often over multi-decade time horizons for infrastructure investments.

Mechanically, models begin with operating assumptions, such as revenue and operating costs. Then they adjust for taxes, working capital, and capital expenditures, and layer in financing assumptions (debt levels and interest expense) to determine the cash available for distribution to investors. Taxes affect both the timing and amount of cash and therefore have a direct impact on free cash flow. When tax outcomes depend on layered regimes, discretionary administration, or evolving interpretations, these factors can introduce uncertainty into the model, limiting the defensibility of projected cash flows.

In practice, deal teams build high-level models for first-round bids in order to assess quickly whether a transaction clears baseline return thresholds. Tax advisers are typically engaged later, so early-stage models reflect tax by relying on statutory or blended rates, or on assumptions provided by the seller. Early tax uncertainty is therefore managed through conservative modelling.

As transactions progress, tax assumptions are refined, including those for tax rates, depreciation deductions, exit and withholding taxes, interest deductibility, and the availability of tax credits that affect distributions. Where uncertainty persists, it is managed by deal teams reducing assumed tax shields, embedding downside assumptions in the model, or reclassifying favourable outcomes as sensitivities. Shifts in tax assumptions between early and binding bids can materially affect IRRs. Repeated tax-driven swings between the early and later stages of modelling can shape how global investors view a jurisdiction. In particular, jurisdictions that become known for late-stage tax “surprises” can be discredited over time.

Stable Rules Support Stable Models

Deal teams consistently emphasize that, while effective tax rates matter, a key question is whether a modelled deal can be underwritten with confidence when presented to the investment committee. Policy stability is central to that assessment: without it, the reliability of projected tax expenses—and, in turn, projected cash flow—is called into question.

Canadian corporate income tax rates have been relatively stable since 2012. However, the broader tax framework has shifted considerably over this period, largely reflecting OECD-led reforms to protect the tax base, including expanded interest limitation and anti-avoidance rules. Key changes include the foreign affiliate dumping rules (announced in 2012 and extended in 2019); extensions to the thin capitalization rules (announced in 2012 and extended in 2013); the back-to-back rules (announced in 2014); the excess interest and financing expenses limitation (EIFEL) rules (announced in 2021); and the hybrid mismatch rules (first released in 2021, with further draft legislation released in 2026 to expand their application).

Canada’s transfer-pricing framework, which also affects interest deductibility, has evolved over this period as well. Most notably, amendments enacted through [Bill C-15](#) in March 2026 embedded OECD principles directly into the legislation, shifting the framework toward a substance- and conduct-based analysis and expanding the CRA’s adjustment powers. These changes added another layer of complexity to an already technically demanding set of rules. The cumulative effect has been to layer new regimes on top of existing ones. The introduction of the EIFEL rules, in particular, required deal teams to revisit and, in some cases, rework models for existing investments.

Despite these changes, Canada compares relatively well with other jurisdictions when it comes to the stability of its

tax policy. Last spring, a proposed US tax measure in the [One Big Beautiful Bill Act \(OBBBA\)](#) (proposed section 899 of the Internal Revenue Code) would have imposed a retaliatory tax on investors from countries deemed to have “unfair and discriminatory” tax systems. Although this measure was not enacted, its introduction profoundly unsettled investors. Other enacted measures in the bill—most notably, the effective roll-back of production and investment tax credits for wind and solar projects—also disrupted the deal environment. More recently, Australia released [draft legislation](#) that would materially expand the definition of taxable Australian property, with retroactive effect to 2006. For long-term investments such as infrastructure, these mid-stream rule changes can undermine modelling assumptions and erode the confidence of investors.

In today’s geopolitical environment, a commitment to long-term policy stability is a competitive advantage. Policy change is inevitable in a democracy, but there is a tradeoff between necessary reform and the costs of instability that needs to be carefully balanced, especially now, as governments face pressure to continually refine regimes and introduce incentives. As one investment professional we spoke to put it: “We can work with good policy and bad policy, but uncertainty kills deals.”

Uncertainty Creates Risk in the Model

Tax rules that cannot be reliably modelled increase the cost of capital. In practice, models—especially in the early stages—are typically built in-house by deal teams, not by tax lawyers or accountants. Uncertainty is priced as risk, raising the hurdle rate and weakening the deal environment.

Investors address tax uncertainty by requiring higher returns and applying wider downside ranges. At the same time, uncertainty also results in greater friction in the investment committee approval process. In some cases, tax uncertainty is managed through tax insurance, which can mitigate downside risk, but insurance comes at a cost, further reducing returns. Even if tax risks are insured, uncertainty is not removed from the investment decision; it is simply priced into it.

Uncertainty arises from several sources. It can result from frequent legislative change, where rules are continually evolving or subject to successive revisions; from vague or principles-based legislation, where outcomes cannot readily be determined at the modelling stage; and from inconsistent or unpredictable administration, including situations where guidance is withdrawn or applied unevenly. The examples below illustrate how uncertainty affects both the effectiveness of tax incentives and the modelling of core deductions.

Clean Economy Investment Tax Credits

Canada’s expanded [clean economy investment tax credits \(ITCs\)](#) were introduced alongside US incentives enacted under President Biden’s [Inflation Reduction Act](#) to promote renewable energy investment. While ambitious in headline terms,

the practical value of an ITC depends on factors that often remain unknown or unresolved early in the investment process.

For deal teams, two issues are central: whether the project is eligible for the full credit, and the timing of credit receipt. If either is uncertain, the credit is typically discounted in the base-case model. For example, a project that is expected to be eligible for a 30 percent headline ITC may be modelled with an assumed 20 to 22 percent ITC, with the remainder reflected only in sensitivity analyses. Several factors contribute to this discounting. Most headline ITC rates depend on meeting labour and apprenticeship requirements, with the credit reduced by 10 percentage points if those requirements are not met. Projects frequently rely on contractors, and although compliance with the credit requirements can be addressed contractually, claimants rarely have direct control over the contractors and the documentation that they keep, which creates perceived qualification risk.

Uncertainty also arises from detailed technical requirements and, for some credits, regulatory review. For example, the clean hydrogen and CCUS credits (summarized in this recent [BLG memo](#)) require detailed project submissions to Natural Resources Canada before claims can be filed with the CRA. As of December 2025, only one-third of ITC claims had been accepted as submitted (Renucci, Redekop, and Francoeur, “[Clean Economy Investment Tax Credits](#),” presented at the Seventy-Seventh Canadian Tax Foundation Annual Tax Conference, Calgary, November 30-December 2, 2025, at slide 16). Faced with these risks, deal teams often further discount the expected value of the credit or include downside cases in the materials they present to investment committees.

Timing uncertainty also matters. ITCs are typically claimed after construction milestones have been achieved and are subject to audit and administrative processing, which can delay payment. For example, we have seen a model assume an 18-month lag between submitting a claim and receiving the credit, which reduced both the present value of the credit and the project’s IRR. Where eligibility or timing cannot be resolved early in the process, credits are only partially reflected in base-case cash flows, with the full value recognized only in sensitivity analyses or upside cases. In this way, uncertainty can undercut the effectiveness of otherwise generous incentives by limiting how much of their value investors are prepared to underwrite.

Interest Deductibility

Another example of uncertainty is interest deductibility. In Canada, interest is generally considered a capital expenditure and is therefore deductible only by exception, where the specific requirements of paragraph 20(1)(c) are met. Over time, interest deductibility has been further constrained by a series of overlapping regimes, including expansions to longstanding rules (such as the thin capitalization rules), and newer

post-BEPS measures such as EIFEL. The context is important: because interest in Canada is not presumptively deductible as an ordinary business expense, each new rule limits an already conditional deduction. Historically, these limitations were well understood, relatively mechanical, and capable of being modelled with reasonable certainty. Today, however, because additional regimes have been layered on without broader structural redesign, deductibility often turns on the interaction of multiple regimes that operate alongside each other, each with its own scope, definitions, and assumptions.

The policy trajectory reflected in Canada’s interest expense limitation rules diverges from that of many other jurisdictions. In many OECD countries, interest is generally deductible to begin with and then subject to defined limits. Following the BEPS project, many jurisdictions responded by replacing or superseding earlier rules with earnings-based limitations (often EBITDA-style caps similar to the approach reflected in Canada’s EIFEL rules). While Canada’s EIFEL rules generally align with OECD recommendations, their cumulative effect in Canada is distinct.

In practice, interest deductibility can hinge on factors that are difficult to determine at the bid stage, including future earnings, group-wide information, and classification or structuring outcomes. This makes it difficult to integrate tax assumptions into models with confidence. This matters: for leveraged investments, interest is a long-term driver of cash flow, and even small differences in annual deductibility can compound significantly over time. We have seen deal teams respond to these limits and uncertainties by adopting conservative base-case assumptions. This can produce significant differences in the value of the tax shield between early-stage and later-stage bid models. Repeated adjustments of this kind can shape broader perceptions of Canada’s reliability as an investment jurisdiction.

Making the Product Match the Promise: Policy Implications

Tax uncertainty does not deter institutional capital outright, but it quietly changes the terms on which capital is willing to engage. Hurdle rates rise, and incentives may be discounted. At the same time, geopolitical uncertainty may strengthen Canada’s hand, and areas such as tax policy, which are firmly in our control, should be leveraged to the country’s advantage. Ultimately, the pitch Canada is making to investors in September will be evaluated by deal teams that are building models like those described above. If tax policy is to support Canada’s investment ambitions, it must be designed with an understanding of how investments are modelled and how uncertainty is priced. In that sense, tax policy is not only a revenue tool but also part of Canada’s investment proposition and economic brand.

The following suggestions are meant to start the discussion:

- 1) *Design rules that can be reliably modelled:*
 - Prioritize simplicity and limit layering new regimes onto existing ones where possible. Periodically consolidate the rules, if they have accumulated.
 - Commit, where possible, to long-term rule stability. At a minimum, the duration of tax incentives should align with investment time horizons.
 - Ensure that administrative practices deliver timely, predictable outcomes for all types of investors.
- 2) *Design tax rules with institutional capital in mind:*
 - Assess Canada's exit tax treatment against jurisdictions that provide clear, reliable treatment for pension funds and sovereign investors (for example, jurisdictions with codified exemptions or qualified institutional investor regimes, such as the United States and the United Kingdom).
 - Carefully consider whether and when the rules should differentiate between direct and portfolio investors (for example, based on ownership thresholds or control) and whether those distinctions remain appropriate or should be revisited in negotiations with key trading and investment partners.
- 3) *Implement global initiatives thoughtfully:*
 - Reassess OECD-derived rules that add complexity without commensurate benefit, or that are not appropriately tailored to the size and structure of Canada's capital markets.
 - Consider targeted bilateral actions (for example, lowering dividend withholding tax rates under treaties for key trading and investing partners) where such reductions could meaningfully increase Canada's competitiveness.

The upcoming September summit gives Canada an opportunity to narrow the gap between investor interest and committed capital. Tax rules that can be confidently underwritten and consistently applied are a tool Canada can use to ensure that our investment environment matches its promise. ■

Getting the Canadian Tax House in Order

Kim Maguire and Ilana Ludwin, Osler Hoskin & Harcourt LLP

Canadian tax practitioners may grumble as they wade through recent international tax rules enacted as part of the OECD/G20 BEPS project, not to mention the endless stream of OECD reports. But there is no question that the OECD and G20 provide effective forums that allow many countries—in particular, middle powers like Canada—to reach consensus on areas of international tax law that might otherwise trend toward a race

to the bottom or result in a web of complex unilateral measures. The United States' lack of enthusiasm for global consensus and multilateral measures is nothing new. However, the United States' approach to international relations has become more aggressive and unpredictable since President Trump returned to (and redecorated) the Oval Office.

The New World Order in International Tax

In his speech at Davos in January 2026, Prime Minister Carney described the new world order and acknowledged the fragility of the current system—more visible after the US-led rupture. At the same time, he emphasized the continuing importance and potential of middle powers working together. His words related to international relations generally, but they apply equally to the international tax system, including the work of the OECD/G20. Crucially, Prime Minister Carney stressed that middle powers need strong domestic economies in order to improve their position on the international stage. A functional, rational, and efficient tax system is a key part of a strong domestic economy.

Canada, like other OECD and G20 nations, has implemented significant tax reforms in recent years. While the push for reform is both understandable and potentially beneficial to the public—particularly when aligned with global consistency—Canada must critically assess its own tax system to ensure that it is simplified, fosters tax certainty for both taxpayers and the government, and supports rather than hinders economic productivity and growth. In other words, it is time to declutter, get our tax house in order, and ready ourselves for this new world order.

In this article, we set out some specific recommendations.

Canadian Policy Responses

To help achieve Mr. Carney's vision of a forward-looking, globally competitive Canada, it is crucial that we not only modernize our tax framework but also send a clear signal that Canada is open for business. This means moving beyond outdated approaches and embracing reforms that (1) position Canada as a destination for investment, innovation, and growth; and (2) counter Canada's reputation as a high-tax jurisdiction unfriendly to business. It means asking questions like the following: How is our current tax system sapping our productivity? What features of the current system have led Canadian tax and legal advisers to recommend that their international clients avoid or minimize their presence in Canada? What features inhibit Canadian businesses from growing outside the Canadian market? To what extent can and should we change those features while preserving key policy objectives and revenue levels? And how can we protect the Canadian tax base while enhancing tax certainty?

Some targeted fixes could be implemented quickly. Many were identified in an open [letter](#) sent by Osler Hoskin &

Harcourt LLP to Finance Minister Champagne in May 2025. We highlight three of these measures here.

Increase CASD Funding

The first change we recommend is to increase the funding and resources available to the Competent Authority Services Division (CASD) of the CRA to enhance tax certainty in cross-border tax matters. CASD plays a critical role in seeking to minimize double taxation of international businesses, as envisioned by tax treaties, through its administration of the mutual agreement procedure (MAP) and advance pricing arrangement (APA) programs. An effectively functioning CASD could strengthen Canada's global reputation as a jurisdiction that welcomes investment, and it would provide greater tax certainty for multinational businesses.

Unfortunately, the CASD has been significantly under-resourced in recent years. In our view, there is a need to increase the speed, quality, and range of its services, especially because several recent changes are likely to amplify demand for CASD support. These include (1) the recent transfer-pricing amendments (together with the ongoing lack of simplified contemporaneous documentation regulations); (2) uncertainty about corporate residence arising from the multilateral instrument (MLI), which has in recent years taken effect in Canada and many other countries; and (3) the multilateral disputes that will inevitably arise under the Global Minimum Tax Act (GMTA). Demand for CASD services is also affected by the absence of substantive safe harbours for low-value intragroup services and routine transactions. The government could consider charging taxpayers processing or user fees, if necessary, for access to CASD services (similar to the fees charged for advance tax rulings), in order to cushion the budgetary impact of increased staffing caused by CASD's increased workload.

Permit Cash Pooling

Cash-pooling arrangements are intragroup transfers commonly used by corporate groups to centralize cash resources so that the cash can be deployed in the group as needed. These transfers—which may involve actual cash movements or may be purely notional—minimize the group's borrowing costs. Cash pooling is a common, non-tax-driven feature of modern, multinational treasury operations. Many countries' tax systems accommodate cross-border cash pooling, but Canada's rules are remarkably hostile to such arrangements. As a result, Canadian members of global groups are often simply excluded from these arrangements, which results in higher group borrowing costs.

Numerous overlapping rules can make cash-pooling arrangements involving a Canadian group member complex or even unworkable. These rules include the shareholder loan, upstream loan, back-to-back loan, and thin capitalization rules (on top of the usual transfer-pricing and interest deductibility rules). The cash-pooling example provided by the CRA at the

2025 IFA Canada conference only highlights the unnecessary complexity and impracticality of Canada's approach to cash pooling. In addition, the CRA's position is that cash pooling may have to be reported as a notifiable transaction under section 237.4, specifically because of designated notifiable transaction NT-2023-05, "Back-to-Back Arrangements." In short, the current rules make cash pooling risky, costly, and impractical for Canadian group members to participate in.

We can appreciate that the tax regulation of cash-pooling arrangements has some sound tax policy basis (after all, reasons exist for all of the rules cited above), but there are compelling economic reasons to make cash pooling easier. Surely Canada can find a way to strike the right balance by adopting a prescribed cash-pooling regime that permits short-term cash movements (which cash pooling is largely intended to facilitate) while providing for a practical approach to classifying and addressing longer-term loans, which many of the existing provisions in the ITA are intended to address.

Canada has several options for reform. The most comprehensive is to provide a safe harbour for typical cash-pooling activities, exempting them from all tax consequences and reporting obligations. More targeted reforms could include simplifying the interest deductibility rules, eliminating the thin capitalization rules (as further discussed below), and amending the back-to-back rules to permit aggregated apportionment rather than requiring taxpayers to trace specific funds. A more comprehensive approach would be best, but even incremental improvements would strengthen Canada's ability to compete for inbound investment and would help counter its reputation for having an unfriendly tax system.

Repeat Thin Capitalization and FAD Rules

Finally, Canada should seriously consider repealing, or at least paring down, the thin capitalization and foreign affiliate dumping (FAD) rules. Both of these regimes were originally intended to limit the ability of Canadian companies with foreign owners to reduce their taxable income through deductions for interest or other financing expenses. However, more recent measures now adequately limit earnings stripping, making these earlier-generation rules largely unnecessary. In particular, Canada enacted broad-based earnings-stripping rules—the excessive interest and financing expenses limitation (EIFEL) rules—in response to OECD BEPS action 4. The EIFEL rules limit deductions for interest and other financing expenses to a specified proportion of adjusted EBITDA. They were enacted at the same time as the GMTA, which is designed to ensure that large multinational groups are subject to a tax rate of at least 15 percent, further reducing the tax benefits of shifting income across jurisdictions. These recent measures, especially the EIFEL rules, should prompt a reconsideration of the thin capitalization rules.

The FAD rules should also be reconsidered. In our view, they are inconsistent with international norms, operate beyond their

intended scope, and can produce counterintuitive results for the unwary—most notably, a deemed upstream distribution whenever an affected Canadian company invests in a foreign affiliate. The FAD rules were first introduced in 2012, purportedly to address two concerns: debt dumping (that is, using money borrowed in Canada to buy shares of related foreign companies) and a form of surplus stripping (namely, using non-borrowed funds to make foreign investments—funds that would otherwise have been distributed as dividends subject to withholding tax). In practice, however, the rules have always applied beyond those scenarios. With the introduction of the EIFEL rules, it is difficult to imagine that much incremental revenue is gained from retaining the FAD rules, and the drawback to retaining both regimes is apparent. The complexity of the FAD rules, and the various elections that need to be considered to escape punitive outcomes, is indefensible. Most insidiously from an economic perspective, the FAD rules encourage non-resident acquirors of Canadian companies to strip out the non-Canadian assets and eliminate Canadian head office functions. We have seen this happen in our practice. In the absence of a compelling policy reason to retain both regimes, it would make more sense for Canada to repeal the FAD regime entirely or at least pare down the rules to reduce the overlap with the EIFEL rules.

Conclusion

Despite the complexity of the tax reforms arising from the BEPS project over the past decade, and despite their significant cost to taxpayers, the underlying tax policy issues that they were intended to address are understandable. Missing from the calculation have been a practical evaluation of the cumulative impact of these rules on business operations; careful consideration of whether the additional revenues they raise justify their overall economic cost to taxpayers; and a rigorous assessment by individual countries of whether domestic rules might be simplified or improved to offset the international tax reforms. Canadian taxpayers, advisers, and governments should seize this moment of focused nation building and work together to simplify our tax system and increase tax certainty. The reforms suggested in this article would be a good place to start. ■

Barn Raising for a Fractured World: Canada's Tax Policy Opportunity

Laura Gheorghiu, Gowling WLG

In this article, I discuss the role that Canada could play in addressing some of the tax challenges of the new world order. Within this framework, I also review some tax initiatives that could benefit the Canadian economy.

Threats on Many Fronts

At the beginning of the year, one would have been forgiven for identifying US-imposed tariffs and Russian hegemony as the principal geoeconomic risks facing Canada. The attacks on Iran and the closing of the Strait of Hormuz have since transformed the landscape, triggering a polycrisis of energy disruption, food insecurity, and inflationary shocks that is only just beginning to reverberate through the world's economies. In retrospect, the tariff volatility of 2025—now joined by threats of energy and water scarcity, and the growing risk of AI-driven unemployment—has begun to look like a practice run for what lies ahead.

Prime Minister Carney has played a prominent role on the international stage since his speech at Davos in January 2026, where he called on “middle powers” to unite in defence of the rules-based international order. On May 4, 2026, in addressing European leaders at the 8th European Political Community Summit in Yerevan, Armenia, the prime minister said that “we don't think that we're destined to submit to a more transactional, insular and brutal world.”

The current crises have profound implications for tax and fiscal policy, raising questions about the adequacy of Canada's revenue base, the financing of defence and energy infrastructure, and the tax system's role in accelerating economic diversification and the pooling of resources among collaborative countries. These crises call for a fiscal response commensurate with their scale. Should that response aim at coercion and concessions, or at fostering a new level of trust-based international collaboration?

Creating a Barn-Raising Global Order

At the core of the dominant worldview today is a belief that the world is fundamentally transactional—that cooperation is justified only where it yields immediate returns. The “middle powers” approach proposed by Mr. Carney challenges this strategy, resting on the conviction that durable alliances can be built around principles that participants will not surrender. The emerging divide is not between left- and right-leaning ideologies, but between transactional and values-based approaches to international relations. One can negotiate with counterparts who hold genuine convictions, but the negotiation must account for the other side's values and respect their

red lines. By encouraging countries to unite around shared values, pooled resources, and common goals, the middle powers' call to action offers the promise of solutions to current global challenges.

This concept recalls the barn-raising traditions of early Europe and 19th-century North America. Barns were necessary for survival in inhospitable conditions: they provided food storage, protection against the elements, and a space for the community. Their construction was an essential but costly endeavour, requiring more resources, expertise, and labour than any single family could muster. Barn raising addressed mutually assured survival: community members helped build one another's barns, relying on shared resources and expertise to ensure each project's success. Because every participant could count on the others for help and stood to benefit directly and indirectly from each endeavour, reciprocity could reasonably be presumed. Mutual assistance was further reinforced through community censure and the recognition of a shared fate.

For Canada, then, to be a successful middle power means adopting a problem-solving orientation and building a reputation for advancing the collective good, rather than operating on a purely transactional, narrowly self-interested basis. (This approach is discussed in a recent article by Stewart Patrick, titled "The Middle Power Moment.") The barn-raising tradition's reliance on reciprocity, predictability, and accountability should now find its expression in modern fiscal architecture.

Structural Change: Canada as a "Value-Add" Economy

Across major trading relationships, Canada's economy is concentrated in the early, upstream stages of global supply chains—in particular, the extraction and production of raw materials and intermediate goods, especially in natural resource industries. At the same time, Canada imports many goods from the later stages of production, goods that are closer to finished products. The structural consequence of this reality is a dual vulnerability: Canadian consumption is exposed to supply shocks, while Canadian exports are exposed to demand shocks. (Additional discussion of Canada's supply chains may be found in a 2022 statement prepared by Global Affairs Canada.)

Given that Canada's vulnerability is systemic, not partner-specific, diversifying trading partners will not, on its own, move Canada's economy further downstream in global supply chains or increase its ability to capture the value added by commercializing innovation.

Similarly, Canada excels at fundamental research but struggles to capitalize on innovation, due to a persistent lack of financing at the growth-equity and project-finance stages. In the medium term, addressing this problem will require a realignment of investments, tax incentives, and tax regimes.

Short-term success, however, will require collaboration with middle-power nations that have already developed the commercialization capabilities that Canada lacks.

Canada is not without bargaining chips. The country has a highly skilled workforce, critical minerals, energy resources (including hydroelectricity, oil, and natural gas), and extensive freshwater supplies, all of which are urgently needed by middle-power countries. As outlined in a recent article by Josh Welsh, Canada also benefits from the investment capacity of its pension sector, with a significant group of Canadian pension plans managing approximately \$2.6 trillion in assets.

However, Canada's greatest strategic asset may be its reputation for trustworthiness—a quality that could be the backbone of a barn-raising world order.

If Canada can persuade other middle powers to pool resources and specialize collaboratively, it can develop downstream production capacity far more quickly. For example, Canada and Australia could process critical minerals into battery components together, rather than exporting raw lithium. To take another example, Canada could invest pension plan surpluses across middle-power countries rather than concentrating them in a single jurisdiction. The returns from such ventures could be shared among participating countries according to pre-established rules. This would represent a structural shift for all participants and, in an arrangement founded on trust, could begin without prolonged negotiations.

Canada as a Culture of Tax Collaboration

If the structural case for collaboration is clear, the next question is how Canada's tax system can support it. A barn raising works only when every participant trusts the others to show up, do their share, and not revise the arrangement midbuild. That trust, applied to a new international framework, would mean forging a compact—both within Canada and among partner nations—built on three principles: (1) predictability (we will not change the rules on one another); (2) reciprocity (we expect all parties to meet the same standards, and we have built enforcement mechanisms into the system); and (3) transparency (each participant can verify compliance because institutions operate openly).

Tax policy alone cannot drive this change, but it must help enable it. Targeted tax incentives and direct equity investments for projects that would otherwise not obtain financing are preferable to broad tax cuts subsidizing activities that would have occurred anyway. In some cases, temporary compromises on certain policy goals may be unavoidable where economic sustainability, national defence, and resilience prerogatives demand them. In practice, this could mean building infrastructure for exporting oil and natural gas to Europe in the short term while enhancing incentives for clean energy development at home. Such tradeoffs can themselves generate the goodwill

needed for deeper long-term collaboration and can help ensure the viability and resilience of like-minded partners.

Canada has made use of this kind of collaborative tax architecture before. For example, the flowthrough share regime, used since the 1950s to channel investment into resource exploration, has helped pool private capital for public purposes.

The following are some potential approaches to designing tax rules aimed at building Canada's supply chains and domestic capacities through a culture of trust and mutual aid.

Financial Participation in the Whole Supply Chain

If middle powers want to speed up the onshoring of their supply chains, they could pursue joint ventures in which upstream suppliers of raw materials, such as Canadian businesses, supply inputs at concessional royalty rates in exchange for a share of future revenues once the downstream product reaches commercial scale. (That return could take the form of a net-revenue share or an enhanced return once capital costs are recovered.) Such arrangements would ensure that Canadian businesses share in the value they help create, even if the downstream processing occurs in another middle-power country.

Assuming that tax treaties could not immediately be renegotiated, certainty could instead be achieved through pre-negotiated mutual agreement procedure (MAP) agreements developed under an accelerated and publicly disclosed timeline to which tax authorities commit. This approach would provide taxpayers with greater certainty about the withholding tax rates applicable in foreign jurisdictions.

Alternatively, participating jurisdictions could offer certain projects reduced or zero domestic withholding tax rates or corporate income tax rates, in all of the participating jurisdictions, for a defined period. These benefits could be tied to performance covenants and subject to automatic review at predetermined milestones.

Building the Infrastructure of the Future

Canada recently announced its intention to create a sovereign wealth fund, although few details have been announced. The proposal is to finance the fund through borrowing. Additional liquidity could come from a temporary levy on designated upstream exports and from windfall taxes generated by higher oil prices. To encourage reinvestment, resource developers could be offered a tax credit for reinvesting in approved downstream or defence-related projects.

The government also plans to launch a retail investment product, similar to a bond, that would allow ordinary Canadians to invest in the sovereign wealth fund. In an article in the June 2025 issue of *Perspectives*, Armine Yalnizyan discussed possible features of such a product, including tax-free returns. The same vehicle could be extended to pension plans on terms

that allow tax-exempt or tax-deferred treatment. This would reflect the reality that building key infrastructure may call for deploying a portion of Canadians' pension savings, along with their other savings, in the service of the country's nation-building efforts. Collectively, this pool of patient capital could reduce the weighted average cost of capital enough to make very large projects economically feasible.

Fostering Innovation and Value Capture

Middle powers could adopt multijurisdictional (as opposed to purely national) patent box regimes. Such a regime would apply a reduced corporate income tax rate to qualifying income from intellectual property developed and exploited within participating middle-power jurisdictions. The rate reduction could be conditional on maintaining a specified share of manufacturing or high-value processing within participating countries, with the benefit clawed back if those activities are offshored. Expanding national patent box regimes into a multijurisdictional regime would support collaborative research and development while keeping the resulting economic benefits within the participating countries. Consideration should also be given to MAP mechanisms that facilitate these arrangements from a transfer-pricing perspective, as well as to any necessary adjustments to SR & ED credits and foreign tax credit regimes.

Similarly, the government could revive its previously proposed extension of the flowthrough share regime to innovative Canadian companies. Under such a model, individual investors could finance innovation in exchange for deductions tied to qualifying expenditures, thereby reducing the cost of early-stage capital at precisely the point where Canadian enterprises have historically struggled to secure it. This concept is elaborated in a 2025 BLG article.

Modernizing Tax Administration

The success of these initiatives will depend in part on modernizing the administration of Canada's tax system. A focused effort on data digitization (such as e-invoicing and electronic reporting) and trusted-taxpayer programs could reduce the need for burdensome audits and unnecessarily complex compliance processes. This would free up resources for the administration of the new incentive architecture and reinforce the transparency and trust that underpin the entire middle-powers proposition.

Conclusion

The answer to an increasingly transactional international environment is not heightened competition and a race to concessions. Instead, the answer lies in pooling internal and external resources, coordinating efforts, drawing on the most skilled members of the group, and building on trust and reliability. It is not only possible but also necessary for Canada to "raise barns" in this new landscape. ■

Tax Governance After Trump: Rethinking Canada's International Tax Strategy

Raphaël Clément, HEC Montréal

In October 2021, after years of working on a multilateral solution to the tax challenges posed by the digital economy, the OECD issued a [statement](#) outlining an agreed-upon two-pillar approach. The [statement](#) was ultimately endorsed by some 139 countries participating in the so-called [Inclusive Framework](#). In 2021, few observers would have predicted the current outcome: a “[pillar 2](#)” that has generated a competitive advantage for the United States; a “[pillar 1](#)” that is effectively dead; and digital services taxes (DSTs), including [Canada's](#), that have been abandoned under bilateral coercion.

In retrospect, this outcome was predictable. President Trump's administration has simply made visible a decades-old reality: American hegemony has long shaped international tax governance. In this article, I argue that today's breakdown in international tax arrangements gives Canada a unique opportunity to lead a fundamental rethinking of how international tax decisions are made. This endeavour would require moving beyond the institutions of the Inclusive Framework and the United Nations (UN) as currently conceived.

In his January 2026 Davos speech, Prime Minister Carney said that the task of the middle powers is to “build something bigger, better, stronger, more just,” in response to a “rupture” in the world order. How should those aims be achieved, from an international tax perspective? In my view, Canadian policy makers should focus as much on the decision-making process as on the substantive rules. The key questions are who gets to make the rules, on what basis, and with what safeguards against capture by the most powerful actors.

Power Asymmetries in International Taxation

When I listened live to Prime Minister Carney's speech in Davos, I was surprised by the following line: “[I]f we're not at the table, we're on the menu.” I had heard it before. It was the slogan used by some critics of the OECD at the [Third International Conference on Financing for Development](#), held in Addis Ababa in 2015. At that conference, there was a push to discuss international tax reform in a UN-led forum. Instead, of course, the OECD consolidated its leadership by creating the Inclusive Framework, which was based on the principle that countries would participate on an equal footing. Most non-OECD countries joined the Inclusive Framework, effectively confirming the OECD's central role in international tax reform.

Canada has played a leading role in OECD tax initiatives. But recent developments have shown the limits of the current governance structure—a view that non-OECD countries have been expressing for some time. India, for example, in

its [response](#) to a 2014 UN questionnaire on BEPS, called for greater UN involvement.

What Prime Minister Carney called the “sign in the window”—the pretence of equal footing in international tax negotiations—was taken down last summer. Or, as Allison Christians asserted in a 2025 [article](#), “the ruse was revealed.” In June 2025, the G7 agreed to a so-called [side-by-side regime](#), effectively exempting US-based multinationals from key features of the global minimum tax (GMT) regime, despite the significant US role in the GMT's design. The side-by-side regime disadvantages Canadian and other non-US-based multinationals. The United States circumvented the decision-making process of both the OECD and the Inclusive Framework by coercing the other six G7 countries, including Canada, to exempt US-based multinationals on the basis that US domestic rules were similar enough to the GMT regime, even though they were clearly different. The G7 agreement was ultimately accepted and is being implemented, including through measures recently introduced in Canada's [Bill C-31](#).

US coercion was even more blatant when Canada gave up its last major tool for taxing the digital economy by rescinding its DST. It did so under the US threat of “revenge taxes” proposed under section 899 of the Internal Revenue Code (discussed by Robin Morgan in a recent [article](#) in this newsletter). After Canada announced this decision, White House press secretary Karoline Leavitt [declared](#) at a briefing: “It's very simple. Prime Minister Carney and Canada caved to President Trump and the United States of America.”

These recent events loudly demonstrate the reality of American hegemony, but this US influence has always been a feature (however quietly) of OECD policy development. Because the Inclusive Framework operates by consensus, the preferences of the most powerful player either paralyze the decision-making process or—as more often happens—control it. As some scholars have argued, consensus decision making produces a “minoritarian bias” (see Neil K. Komesar, *Imperfect Alternatives: Choosing Institutions in Law, Economics, and Public Policy* (Chicago: University of Chicago Press, 1994)). Pascal Saint-Amans, former head of the OECD's Centre for Tax Policy and Administration, says that without the United States, no progress can be made at the OECD. As he put it: “[translation] But unlike the others, their economic weight is such that a project without their explicit and active support is pointless” (Pascal Saint-Amans, *Paradis fiscaux : comment on a changé le cours de l'histoire* (Paris: Seuil, 2023), at 93).

OECD decision-making processes have always been structurally susceptible to domination by a hegemony. This vulnerability has allowed the world's most powerful actor to shape, delay, and ultimately opt out of agreed rules at will. The Trump administration has simply made these power dynamics—always present behind the scenes—impossible to ignore. The question is what the middle powers should do with that recognition.

Tax Cooperation Is Essential

Tax cooperation and coordination remain essential. It may be tempting to build a fortress of unilateral measures, but the progress of the last two decades has shown that cooperation is needed, and that it can work. Initiatives such as automatic exchange of information, country-by-country reporting, and the multilateral instrument show the value of cooperation and multilateralism, even if US participation in these efforts has been limited.

Experience shows that effective reform requires the broad engagement of both developed and developing countries. Both the Inclusive Framework and the United Nations risk producing limited results if developing countries lose interest in the Inclusive Framework while developed countries show little interest in UN-led initiatives.

Multilateral measures are still needed to address the taxation of the digital economy, and not much has changed on this front since the OECD BEPS action 1 final report in 2015. The solution may not be pillar 1, as currently conceived, but it is certainly not unilateral DSTs, which lead to political tensions between countries (see Jean-Pierre Vidal, “Imposition des géants du Web : défis au Canada” (2021) 154:2 *Revue française de finances publiques* 103-20).

Perhaps the path forward lies in revisiting ideas identified in the OECD BEPS action 1 report, particularly the concept of a nexus based on “significant economic presence.” This approach would allow source countries to tax digital businesses without requiring a physical presence (see Allison Christians and Kimia Towfigh, “CTF Digital Tax Log,” entry no. 4, August 21, 2020). The path forward could also involve new withholding taxes on cross-border digital payments. Either approach would require treaty-level changes that could take years to negotiate and implement. But that is precisely why the conversation should begin now.

The Way Forward

Canada cannot reform international tax governance on its own. No single country can. But the disruption of 2025 has created conditions for a coalition of middle powers—countries that are too large and well connected to be dismissed, too numerous and diverse to be managed individually through bilateral pressure, and credible enough with the developing-country blocs to act as genuine bridges between them.

The concept of negotiating through blocs rather than as individual states deserves serious attention. One of the structural vulnerabilities of the current Inclusive Framework is its reliance on country-by-country consensus. In practice, this allows the most powerful states to shape outcomes through the credible threat of bilateral consequences. A coalition of middle powers would be far more resistant to that kind of pressure. Such a coalition, organized around shared interests, would not need to take the form of a binding bloc. It could instead

function as a coordinating platform, enabling countries to negotiate together, present aligned positions in multilateral forums, and share technical expertise. The key question is whether Canada can help create conditions in which no country has to stand alone.

To secure broad support for such an alliance, developing countries must have a meaningful voice at the table. The power asymmetries that we see today should not be reproduced in a new system. Smaller countries fear being “on the menu” as much as middle powers do. Regional groupings offer one model. The African Tax Administration Forum (ATAF) is an example of regional coordination on tax matters. The ATAF helps its members build the expertise and the influence needed to present more unified positions in global tax negotiations.

But how can this new system be “bigger, better, stronger, more just”? The experience of the Inclusive Framework offers some guidance on a new governance structure. We can see an outline of ideal design features: universal or near-universal membership; voting structures that prevent domination by any single state; a formal dispute resolution mechanism with real enforcement capacity; and a secretariat with genuine technical independence, transparent governance, and a mandate that covers both the substantive rules of international taxation and the procedural conditions under which those rules are made and revised.

I do not know what the ideal forum for this reform would be. Developed countries have long been skeptical of returning tax negotiations to the United Nations. The United Nations still lacks the technical expertise and governance structure needed for such a role, and these concerns are not adequately addressed in the proposed UN framework convention on international tax cooperation. At the same time, the OECD’s role has been negatively affected by the US challenge to the organization’s relevance. Even so, the OECD remains the main locus of technical expertise and institutional leadership in international tax. Redesigning the governance structure of the Inclusive Framework may therefore be the most realistic path forward. In my view, one thing is certain: whatever form the new framework takes, policy makers should try to ensure that it does not perpetuate existing power asymmetries.

Conclusion

This is a moment of clarity that should be taken advantage of. For middle powers, the underlying dynamics of the current system are now impossible to ignore. Canada can lead international tax governance reform. It has the credibility to lead a genuine rethinking of how international tax decisions are made. The issue is not only what the technical rules should be but also who makes the rules and with what safeguards. That task will not be easy, but the problems are too obvious to defer, and the opportunity too important to miss. ■

Financing Canada's Hinge Moment: Setting the Stage for Tax Policy Reform

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Canada is at a turning point. This is a historical moment in which responses to domestic and international pressures for change could have generational consequences. Multiple structural transformations—economic, social, environmental, and geopolitical—are happening at the same time. Will tax policy play a role in shaping how Canada responds to this moment? Yes. Canada needs more tax revenue to ensure fiscal sustainability at manageable debt levels, but it also needs tax reform to promote productivity, competitiveness, and fairness.

Historical Hinge Moments

Canada has gone through several hinge moments in its relatively young history. As always, this time is different.

In the 1930s, Canada and other industrialized allies experienced the Great Depression. We responded by creating a modern welfare state. Canada's success with the Allied forces in the Second World War set the stage for a sustained period of industrialized growth and the global recognition of Canada as a middle power.

In the 1970s, Canada experienced oil shocks and high inflation. The alienation of the western provinces and the Quebec separatist movement highlighted serious social and political divides. Canada responded by introducing new economic policies, adopting the Charter of Rights and Freedoms, and rebalancing federal-provincial relations. Canada's decision to embrace continental free trade in the late 1980s and early 1990s reshaped our economy and our relations with the United States and Mexico. Canada's response to a near sovereign debt crisis in the mid-1990s changed the direction of public finances and set the stage for a period of fiscal stability.

The Current Hinge Moment

Today's turning point is different from previous ones because multiple transitions are happening simultaneously. Digitalization and emerging technologies such as artificial intelligence are changing workflows, labour markets, and tax bases. US policies on trade and security are driving geopolitical fragmentation and the realignment of global supply chains. Wars in Europe and the Middle East underscore the need for Canada to move quickly to meet the 2025 NATO Hague summit target of spending 3.5 percent of gross domestic product (GDP) on core military defence.

These major shifts are taking place while Canada faces the ongoing challenge of boosting living standards held back by sagging productivity. Progress in addressing a myriad of important policy issues (health care, income inequality, rela-

tions with Indigenous peoples, and climate) has been slow and expensive. At the same time, government coffers have been reduced by efforts to stabilize the economy after global financial and health shocks, and by more recent affordability challenges tied to food, housing, and energy prices.

Weak performance in both the public and private sectors has undermined trust and confidence in our leaders and institutions.

Prime Minister Carney has talked about a rupture in political and economic relations. Middle powers like Canada can no longer trust relationships with large hegemonic powers. This hinge moment encompasses not only future pressures but also policy shortcomings of the past.

Policy Response: Budget 2025

The government's initial policy response to the current hinge moment is set out in the so-called Canada Strong Plan, as outlined in the 2025 federal budget. This plan envisions a multi-year strategy aimed at making Canada more resilient and competitive during a period of global disruption and significant technological change.

The plan has four pillars:

- 1) Build physical capacity through new government spending on infrastructure and housing.
- 2) Improve productivity, innovation, and competitiveness through new and enhanced tax credits and funding. These measures are intended to spur business investment, support the development and implementation of AI and quantum technologies, and redirect trade corridors toward new markets.
- 3) Make major long-term investments in defence and security.
- 4) Introduce a new fiscal strategy that reallocates resources toward new priorities and brings greater policy focus and transparency to capital investment. This reallocation approach relies partly on reviews of spending efficiency. The fiscal plan will distinguish between operating and capital spending.

The 2025 federal budget sets out the government's fiscal strategy and plan and provides a large public-finance down-payment to support it. Projected budget deficits are expected to effectively double in 2025-26 and 2026-27, reaching about 2 percent of GDP. The debt-to-GDP ratio is projected to increase modestly and then stabilize over the next five years.

The increase in deficits and debt has set up an ongoing debate over whether the new strategy is fiscally responsible. The government argues that the higher deficits are modest relative to those in most other OECD countries and are needed to support capital investment, boost productivity, diversify trade, and meet commitments to boost defence spending. Critics of the strategy argue that the larger deficits will reduce fiscal buffers

against future economic shocks and are unfair to future generations, which will face higher debt interest costs and less fiscal room.

A deficit in the 2 percent range is not large in today's current weak economic environment and is providing some short-term support for macroeconomic stability. Over the medium term, it will be important to hold the government to account for how it executes its capital investment strategy and national defence buildup. Will these investments deliver good value for money?

The government also plans to implement a new fiscal-planning framework. The aim, under this approach, is for the operational budget (which includes current program spending and debt interest costs) to be balanced by 2028-29. After that, the government plans to run modest deficits in the range of 1 to 1.5 percent of GDP in the capital budget.

The split between operating and capital spending is generating a debate over the merits of a golden rule in public finance—specifically, the principle that budgetary deficits should be incurred only to finance capital spending. The government argues that this approach is rational given Canada's investment shortfall, which is hurting productivity. Critics argue that the definition of "capital investment" in the 2025 budget is too broad in scope because it includes tax expenditures and subsidies that support operating spending. In their view, this approach risks reinforcing a bias toward ongoing deficits.

There is legitimate scope for the government to strengthen its fiscal-planning framework by (1) adopting a tighter definition of "capital investment"; (2) building explicit fiscal reserves around the 2028-29 target of an operating balance; and (3) adding a medium- to long-term fiscal target for debt.

The 2026 spring economic update indicates that the government remains on track to balance the operating budget by 2028-29, despite the global impact of a new war in the Middle East. Additional revenues from higher oil prices have been used to fund a range of measures related to affordability, training, and the environment, which the government describes as a bridge to the future. The government has also announced plans to create a sovereign wealth fund to encourage domestic and international investment in Canada. This is an effort by the government to highlight its four-pillar strategy centred on capital investment to address the hinge moment.

Tax Policy and the Hinge Moment (Year 1)

The Carney government's early tax policy response to the turning point could be described, on balance, as targeted, investment-focused, and complex. With some notable exceptions aimed at addressing affordability challenges, the tax measures so far are largely designed to encourage private capital to respond to global economic and political change.

People looking for early signs of broad-based tax reform will be disappointed. Early tax policy directions have given priority

to targeted incentives over tax rate cuts, sector-specific credits over broad-based reforms, and only modest simplification measures. In its first year, the Carney government used tax policy as one tool among many to advance a broader economic repositioning. It has not viewed tax policy in isolation and has, to date, made no commitment to a broader tax review.

As part of its investment-first strategy, the Carney government is introducing a range of targeted tax measures, including investment tax credits (for strategic sectors such as clean electricity, critical minerals, manufacturing, and AI), accelerated depreciation, and modernization of the SR & ED program. These targeted incentives are designed to direct investment toward strategic sectors, rather than relying on broad corporate tax cuts to improve competitiveness.

Without question, these measures—sector-specific investment credits combined with layered eligibility rules—risk making an already-complex tax system even more complex. But complexity is the price of mission-driven policy tools.

A trio of announced measures—lowering the bottom personal income tax rate; increasing the GST credit; and temporarily pausing the federal fuel excise tax increase—were presented as policy responses to affordability challenges.

In its first year, the Carney government faced strong political pressures to address the high costs of food, energy, and housing. It prioritized fairness and relief over broader structural reforms aimed at enhancing efficiency and competitiveness.

Year 2 and Beyond

Canada is reviewing parts of its tax system, but it has not yet committed to a full-scale structured review. Will it do so? What will it take to make this happen?

The policy reviews now under way and planned for are narrowly focused. They include reviews of, for example, tax expenditures, modernization of the SR & ED program, clean energy tax credits, and international tax rules. On the administrative side, the government is committed to a broad review of the CRA. The policy pressure to broaden the review into a wider examination of the tax system may come from the need to fund Canada's higher NATO defence-spending commitment.

Canadians probably do not fully appreciate the political commitment and additional resources required for Canada to meet its NATO commitment of spending 3.5 percent of GDP on defence by 2035. In current dollars, this increase—from 2 percent to 3.5 percent of GDP—would require \$50 billion more in annual spending on defence. Because this increase is not fully accounted for in the government's projections (Canada is expected to hit 2.0 percent in 2025-26), there is a gap in the fiscal-planning framework. The additional spending would amount to about \$3,300 on average per household in 2026, or about 5 percent of average taxable income. The enormity of this challenge was not emphasized by Prime Minister Carney in his [speech on forward guidance](#).

With the global economy facing significant downside risks, as highlighted by the International Monetary Fund, Canada may struggle to hit its fiscal target of balancing the operating budget by 2028-29. Financial markets could also increase the pressure on Canada to make greater progress in lowering its debt-to-GDP ratio in order to create more fiscal space to address the next global shock. These pressures suggest that Canada needs more tax revenue.

As Canada opens markets at home and abroad for foreign direct investment and exports, it is likely that the competitiveness of our tax system will come under closer scrutiny. Some readers will recall that Canada's tax competitiveness has already been under scrutiny since 2018, when the United States reduced its federal headline corporate tax rate from 35 percent to 21 percent, and Canada's response was essentially limited to accelerated depreciation for certain investments. According to the *US Tax Foundation*, Canada ranked 22nd out of 38 countries in corporate tax competitiveness. That helps explain the Liberal Party's election promise to conduct an expert review of Canada's corporate tax system, a commitment that has not yet been met.

Recent studies by various research institutes, including the C.D. Howe Institute [paper on tax reform](#), have largely concluded that Canada's current tax system is impeding economic growth and requires significant reform. One problem is that Canada relies heavily on personal and corporate taxes, which, as policy experts contend, impose unnecessary economic costs. Tax policy experts make the case for shifting the tax mix toward less distortionary sources of revenue (such as consumption taxes), together with measures to simplify the tax system and strengthen incentives for innovation and capital investment.

This Year Is the Right Time for Tax Reform

The 2026 federal budget, expected this fall, could provide a timely opportunity to launch an independent review of Canada's tax policy. Experts from the private and public sectors and from Parliament could work together to suggest reforms for future implementation that would support the government's agenda in a fiscally responsible way. A system-wide review has been overdue for decades.

To expedite the process, the government could develop and announce the objectives, mandate, governance structure, and timelines for a review before the release of the 2026 budget. The objectives could include growth, competitiveness, fairness, efficiency, and fiscal sustainability. The scope of the mandate could be expanded to cover all tax statutes and could incorporate ongoing reviews of tax expenditures and administration. An independent advisory panel could draw on expertise from a broad range of perspectives—labour, business, social policy, Indigenous leaders, tax practitioners, and economists. Parliament should be involved in the setup of any such panel,

while the Department of Finance and the CRA should play a supporting role. Clear timelines should be established, with reports and recommendations delivered within two years. ■