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Did this company engineer the largest tax dodge in Canadian history?

By Bruce Livesey in News, Energy

Cameco President and Chief Executive Officer Tim Gitzel speaks with media following the company's annual general meeting in Saskatoon, Wednesday, May 28, 2014. Canadian Press photo

For Don Kossick it's been a lonely battle – a sort of one-man crusade, if you will.

The Saskatoon-based activist and community organizer runs Saskatchewan Citizens for Tax Fairness, which lobbies against corporate tax evasion. Two years ago, Kossick managed to raise enough moneyto pay for a billboard sign in downtown Saskatoon with the blaring headline "Pay Up Cameco".

Headquartered in Saskatoon, Cameco Corp. is the world's largest publicly-traded uranium company – producing as much as 15 to 20 percent of the global uranium supply. In fact, it provides most of the uranium used in Canada's nuclear reactors.


Don Kossick screenshot from Quint

But Cameco is now in hot water: the federal government is accusing the $2.8-billion company of operating a massive tax dodging scheme for years – and potentially depriving state coffers of as much $2.1-billion in cash. Cameco, which denies these allegations, goes on trial in Toronto this September. And If the company is found guilty, it would constitute the largest tax avoidance case in Canadian history. Meanwhile, the US Internal Revenue Service (IRS) is seeking (US) $32-million in back taxes from Cameco – and is investigating to see if the company owes more.

Yet, despite the vast sums involved, Kossick is finding it difficult to raise awareness in Saskatchewan about the Cameco case. “What (Cameco does) is give away money here and there so everybody thinks they’re fine,” he explains. “They are very effective at dodging public concern.”

Last year, Kossick arranged for Dennis Howlett, executive director of Canadians for Tax Fairness, an Ottawa-based NGO that lobbies against tax avoidance, to tour Saskatchewan and talk about the Cameco matter. Kossick says this stirred up some attention, but notes Cameco has been burnishing its image with a hospital fundraising campaign of its own called “Cameco Cares” – which involves sponsoring prominent musical acts to visit Saskatchewan, including the Barenaked Ladies in 2014, and Huey Lewis and the News last year. “They are having Sarah McLachlan coming to play this summer,” says Kossick.

Photo of campaign sign by Don Kossick

Overall, the Cameco tax dodging case has received scant attention in Canada. But this might change, especially with the Panama Papers thrusting tax evasion and offshore havens into the limelight once again.

While the Panama Papers highlights the controversy of mostly wealthy individuals hiding money offshore, multinational corporations are just as prone to this practice. Two weeks ago, Oxfam released a report that estimates America's top 50 multinationals dodge (US) $111-billion in taxes every year, while sapping an estimated (US) $100-billion from poor countries, and use at least 1,600 subsidiaries to horde (US) $1.4 trillion offshore. The result was that, on average, these corporations pay about a 26 percent tax rate – as compared to the 35 percent US tax law demands – with only 5 of them paying the full amount. "We are interested in the fact that these big multinational companies are playing by a different set of rules than either most individuals or ordinary taxpayers or small businesses," says Robbie Silverman, Oxfam's senior tax adviser.

The case of Cameco reveals how Canadian corporations are doing the very same thing. In fact, both Loblaws Cos. Ltd. and the silver mining company Silver Wheaton Corp. are being pursued by the Canada Revenue Agency (CRA) for avoiding taxes by using offshore havens, potentially owing hundreds of millions in back taxes (both companies deny the allegations). As Arthur Cockfield, one of Canada's leading tax scholars who teaches at Queen's University's law school explains: "TheIncome Tax Act is filled with provisions that encourage companies like Cameco to do what they are doing."

How Cameco set up its offshore scheme

Cameco is a big player in Saskatchewan's economy. It was created in 1988 as a result of a merger of two crown corporations which finally became fully privatized 14 years later.

Today, Cameco operates uranium mines around the world, but principally in northern Saskatchewan, where it owns the McArthur River and Cigar Lake mines – among the largest and richest uranium deposits on the planet. Cameco also runs a uranium refinery and conversion facilities in Ontario. The company was also recently in the news for laying off 500 workers at its Rabbit Lake mine due to a worldwide glut of uranium.

According to the government's lawsuit, Cameco's tax scheme originated in the late '90s. By then, the company was worried about low-priced Russian uranium flooding the world market due to the collapse of the Soviet Union and decommissioning of its nuclear weapons. The uranium in the warheads was now available to be used in nuclear reactors. "Which could have a devastating effect on (Cameco's) business and its survival," says the lawsuit. Meanwhile, uranium prices were low, stuck at about $10 a pound.

In 1999, Cameco decided to restructure its operations to deal with this market threat. Previously, the company sold its uranium directly to customers. Now Cameco was going to do things differently.

To begin with, they entered into purchase agreements with other uranium companies, notably Russia's Tenex, that controlled massive stocks of Russian uranium. By doing so, they were helping to stabilize and ultimately increase uranium prices.

But they also took steps to minimize their Canadian tax burden. To do so, the company established a marketing subsidiary in the low-tax haven of Switzerland, in the canton of Zug. Cameco then drafted a 17-year uranium supply agreement with this Swiss subsidiary at a fixed price of $10 a pound. The plan was to sell their uranium to their customers through this Swiss operation instead of directly from their Canadian offices.

Today, the federal government says this subsidiary really existed only on paper and had no real business activity: in fact, it had just one employee, who actually lived in Germany. The subsidiary rented an office within a law firm that did some legal work for the company. In the government's claim, it says Cameco's Swiss subsidiary "performed only nominal functions" and that "all substantive functions" were performed by its Canadian head office and staff.

So how did Cameco lower its tax bill? Before, when it sold uranium directly to customers, it did so for whatever world prices were going at the time. Which also meant, the higher the price, the more profits it made in Canada and the higher the tax paid to the CRA.

But by setting up a Swiss subsidiary, Cameco could now employ "transfer pricing" to lower its tax bill because most of the profits would be made in Switzerland, where taxes were much lower (around 10 percent compared to closer to 30 percent in Canada).

What few people realize is that about 60 percent of trade between countries is actually done between subsidiaries of individual corporations – such as Apple's head office in California selling iPhones to an Apple-owned subsidiary in Canada. A transfer price is the price of a good sold between two subsidiaries of the same company.

Transfer pricing becomes an issue for governments because it's a way for companies to shift their profits to countries where taxes are lower. As the UK-based Tax Justice Network has observed: "Transfer pricing is not, in itself, illegal or necessarily abusive. What is illegal or abusive is transfer mispricing, also known as transfer pricing manipulation or abusive transfer pricing."

By establishing a subsidiary in Switzerland, and entering into the 17-year contract that fixed the price of its uranium at $10 per pound, Cameco is now accused of mispricing its uranium, especially after uranium prices began to rise.

Indeed, starting in 2003, uranium prices started to ascend, hitting almost $140 by 2007. But Cameco was claiming artificially low profits in Canada because it was only getting $10 a pound from its Swiss subsidiary, thus paying much less tax than it should have to the Canadian government. Meanwhile, through its Swiss subsidiary it was selling both to itself and to other customers uranium at world-level prices – and recording the profits in Switzerland.

In fact, the Swiss subsidiary became the repository of all of Cameco's profits – where it was taxed at a much lower rate than in Canada – even though only 16 percent of its sales were in Europe (most of its sales were in Asia and the US). Thus, in 2012, the Bay Street equity research firm ***Veritas Investment Research*** estimates Cameco paid just $36-million in cash taxes on $680-million pre-tax cash flow from operations – or at a 5-per-cent rate. The difference between that and the statutory rate of 27 per cent meant a tax cut of more than 20 per cent, ***Veritas*** estimated.

By 2012, the Swiss subsidiary had earned $4.3-billion in profits during the previous six-year period. Meanwhile, Cameco was claiming its Canadian operation was losing money – a total of $1.3-billion during the same period.

But Cameco was not done: the company also established a subsidiary in the low-tax haven of Barbados, which has a tax treaty with Canada. Court documents show Cameco paid this subsidiary 50 percent of its Swiss subsidiary's pre-tax profits of (US) $78-million in 2005, although it was also entirely a paper front with no actual business operations. Whether it used the Barbados subsidiary to repatriate its offshore profits is not clear, but is highly likely.

According to the government, these paper subsidiaries had the sole purpose of dodging taxes because they performed no business activities: all of the activities were carried out by its Canadian head office. And therefore the CRA believes the Swiss subsidiary's profits must be taxed at Canadian rates. "Neither (its Swiss or Barbadian subsidiaries) performed any function in the series of transactions… for which an arm's length party would pay," the government alleges at one point. "The series of transactions directed by (Cameco) amounts to a sham designed to deceive the Minister into concluding that (its Swiss operation), not (Cameco), was undertaking a business and incurring real risks."

In short, the buying and selling of uranium through Cameco's foreign operations, the government is claiming, were designed to avoid paying taxes. And due to the abuse of transfer pricing and low taxes paid in places like Switzerland, the total sum avoided now totals $2.1-billion.

Cameco, on the other hand, won't discuss the case, but argues its foreign subsidiaries are legitimate and its transfer price for uranium was set at realistic levels. They also claim that their offshore structures were permitted by Canada's income tax laws and are confident of prevailing in court. In regards to the IRS allegations, the company said in its February conference call with analysts: "We disagree with the stance taken by the IRS and will dispute it."

Veritas feels otherwise. After examining the government's case, the research equity firm is convinced Cameco will lose. "We feel the CRA has a good case based on the facts we have been able to compile publicly," says ***Veritas'*** president, Anthony Scilipoti.

Meanwhile, according to a 2013 court order, the government discovered Cameco had not provided them with all of the documents they requested in discovery, some of which were also redacted. The company has put only $50-million aside to pay for a possible settlement with the CRA – a sum ***Veritas*** finds alarmingly small given the serious allegations involved. Grant Isaac, Cameco's chief financial officer, said in February that this sum was determined as a result of "additional contract information we acquired... We concluded that the pricing uncertainty in our inter-company arrangement was less than originally determined and reflect our confidence we will be successful in our case."

Saskatchewan government faces deficits, and is saying little

Despite the amounts the CRA alleges Cameco dodged in taxes, there's been little hue and cry about the matter in Saskatchewan – even though the provincial government would have received almost half the money owed.

Premier Brad Wall has expressed concern over the issue going back to 2013, but has avoided publicly condemning Cameco. The premier's office declined to respond to an interview request over the issue. "For the most part the Wall government has been supportive of Cameco," claims Don Kossick.


Canadian Press photo of Brad Wall

This might be surprising given that Wall admitted in February his government is facing "serious revenue shortfalls" and will run a deficit this fiscal year and next (the province had moved away from a projected surplus to a $262-million deficit when it presented a budget update last fall).

Meanwhile, as the Panama Papers continues to reveal the extent of how much money is being squirreled away offshore, it's apparent that Corporate Canada is knee deep in this practice. As Dennis Howlett of Canadians for Tax Fairness, who visited Regina, Moose Jaw and North Battleford last year to discuss the Cameco case, observes: "Cameco is not alone we suspect. It may be more bold… A lot of companies are using offshore subsidiaries to shift profits in various ways and some cross the line – as I think Cameco's case will end up finding… But a lot of them go unchallenged either because it's too difficult to convict… or because the rules are so loose."