FEI Canada Press Release – March 1, 2005

IPAC COMMENTS ON 2005 FEDERAL BUDGET

OVERVIEW

Finance Minister Ralph Goodale presented the first budget of a minority government since 1979 on February 23, 2005. As would be expected of a minority government soon to face an election, Budget 2005 is a carefully crafted political/fiscal document that sprinkles increased spending from A (aboriginal issues) to Z (Zambia - as part of increased aid to Africa). For the corporate sector, there are tax reductions and accelerated CCA on "green" investments. For individual Canadians, Budget 2005 contains modest personal tax relief, expansion of eligibility for the disability tax credit, inclusion of new expenditures (including "medically required marihuana") as eligible medical expenditures, a new adoption tax credit, and increased retirement savings contributions. Removal of the foreign investment cap will provide more flexibility and potentially higher returns for retirement savings plans.

This report examines the budget in the context of the FEIC's pre-budget submission dated January 5, 2005 (found on FEIC's website at http://www.fei.org/canada/position-papers/CommentLtr/IPAC_Letter_Min_of_Finance_0105.pdf).

COMPETITIVENESS

The Budget Documents contain numerous references to the need to maintain a competitive economic and tax environment in Canada. It is suggested, and we agree, that the corporate rate cuts, increases in deductible retirement contributions, and accelerated CCA rates will lead to a more competitive and business-friendly economy.

FINANCIAL MANAGEMENT

Using conservative fiscal forecasts, Budget 2005 projects a balanced fiscal position in 2004-05 and for the next five years. This position relies on projected cumulative savings of $11 billion as a result of Expenditure Review Committee deliberations. However, it does include annual debt reduction of $3 billion from the Contingency Reserve and "Economic Prudence" reserves of $1b. in 2005-06, $2b. in 2006-07, $3b. in 2007-08, $3.5b. in 2008-09, and $4b. in 2009-10. In essence, the Budget is projecting real surpluses of these amounts through to the 2009-10 fiscal year. Projected debt reduction is expected to attain the government's 25% debt/GDP ratio by 2014-15.

The above conforms to the general thrust of the FEIC submission. Projected savings have been channeled to new initiatives. However, there are no statements which indicate specific and aggressive debt and program spending reductions as called for in the FEIC brief. The government indicates that Dr. Tim O'Neill, chief economist at the Bank of Montreal, will be conducting a review of the government's forecasting procedures and the Expenditure Review process is scheduled to continue.

FEIC notes the extraordinary growth in federal fiscal spending plans and that this growth is made possible by the projected increase in revenues from taxation. FEIC would have preferred the government find the monies to fund its initiatives without increasing spending levels (through reductions in other programs), and to reduce taxes to a more appreciable extent. The future balanced budgets are at risk should the projected economic growth falter and taxation revenues fall below planned levels. FEIC urges the federal government to reduce its fiscal role in the Canadian economy by reassessing this spending plan and working towards both lower spending and lower taxes.

COMPARISON OF THE FEIC SUBMISSION WITH THE BUDGET TAX MEASURES

1. Loss Transfer System

Our submissions over the past several years have called for a Canadian loss transfer system. Although not included in this budget, the 2004 budget did extend the loss carry forward period to 10 years.

2. Centre for Continuing Workplace Training and Education

Although the budget contained new spending for the Workplace Skills Strategy introduced in the 2004 Budget, none of the new initiatives noted in the Budget specifically address the substance of our submission.

3. Increased CCA rates for environmentally friendly capital equipment

The Budget provides for accelerated CCA rates for certain "green" capital expenditures incurred after February 23, 2005, and the inclusion of other equipment in Class 43.1, the accelerated CCA class.

4. Elimination of the half-year rule for environmentally friendly investments

This proposal was not included in the Budget.

5. Increased personal income tax thresholds

While there was a small gradual increase in the basic personal amount to $10,000 by 2009 and in the spousal amount to $8,500 by 2009, FEIC's proposal to increase personal income tax thresholds was not addressed in the Budget by any meaningful extent.

6. An increased minimum tax threshold

This recommendation was not included in the budget.

7. Increased RRSP and registered pension plan contribution limits

The budget increases the annual deduction to these plans as follows:

	RPP	RRSP
2006	$19,000	$18,000
2007	$20,000	$19,000
2008	$21,000	$20,000
2009	$22,000	$21,000
2010	indexed	$22,000
2011		indexed

8. Eliminate the cap on foreign investments in registered plans by 2010

The Budget eliminated the cap in 2005.

9. Increase the Pension Adjustment Reversal threshold

This proposal was not included in the budget.

10. Reduce corporate tax rates

While the business community would have preferred immediate rate reductions, Budget 2005 reduces corporate rates on business income other than that eligible for the Small Business Deduction to 20.5% in 2008, 20% in 2009, and 19% in 2010. Combined average federal and provincial corporate rates remain lower than comparable U.S. federal and state rates.

11. Eliminate the corporate surtax from selected sectors

The corporate surtax is eliminated from all sectors on January 1, 2008.

12. Eliminate the Large Corporations Tax

Currently scheduled for elimination in 2005, the Budget did not accelerate the phase-out of this tax.

13. Harmonization of the GST and provincial sales taxes

There was no mention in the budget of discussions with the provinces towards further harmonization of sales taxes.

OTHER ISSUES

The Budget announced that the government is recalling its previously announced proposal related to the determination of deductible business losses due to adverse commentary from the tax community. This proposal was introduced in response to several Supreme Court decisions which expanded the scope of interest deductibility and rejected the "reasonable expectation of profit" test formerly used by the CRA to attack losses claimed primarily by individuals. A new less restrictive proposal will be released in the near future for consultation.

The government will continue to monitor developments in the financial markets related to income trusts. Consultations with stakeholders are planned, to be followed by a consultation paper on income trusts.

In a wide-ranging discussion of potential environmental initiatives in a supplementary Annex, Budget 2005 referred to both tax incentives and dis-incentives. Hopefully, the latter is not an early warning of a future carbon tax.

SUMMARY

FEIC applauds the Federal Government for adopting several changes that were part of our pre-budget submission. However, many other proposals have not been included in the measures set out in the government's budget:

- A loss transfer or similar group reporting system – This is a challenge due to strong provincial opposition. Nonetheless, similar programs exist in most industrialized countries and FEIC will continue to suggest its inclusion in Canadian taxation policy.

- A Continuing Education Centre within the Workplaces Strategy - FEIC will continue to seek the opportunity to consult government with regard to this.

- Income tax proposals - Issues such as elimination of the half-year rule, the minimum tax threshold, and the suggested changes to the Pension Adjustment Reversal threshold are essentially technical issues which FEIC will continue to discuss with the Department of Finance. It may well be that resolutions of these concerns must await a more favourable political/tax policy climate.

- Increase personal income tax thresholds - The major issue for FEIC to continue to work towards is a decrease in the personal tax burden carried by Canadians. We will maintain our position with the government that a much more meaningful increase in the personal tax threshold for all Canadians will result in increased disposable income for all Canadians, but in a most meaningful way for those in lower income ranges.

*Please note that these represent the views of the Tax Policy Task Force - Issues and Policy Advisory Committee and do not necessarily represent the views of the FEI Canada or its members.