SUBMISSION TO THE HOUSE OF COMMONS STANDING COMMITTEE ON FINANCE

PRE-BUDGET CONSULTATION 2011

AUGUST 13, 2010

fei

financial executives international
dirigeants financiers internationaux
canada

August 13, 2010

Mr. James Rajotte, M.P.
Chair, Standing Committee on Finance
House of Commons
Ottawa, Canada
K1A 0A6

Dear Mr. Rajotte,

INTRODUCTION

Financial Executives International Canada (FEI Canada), on behalf of the Tax Policy Sub-Committee of the Issues and Policy Advisory Committee, is pleased to respond to the invitation by the House of Commons Standing Committee on Finance (FINA) to present a submission to FINA's 2011 pre-budget consultation. FEI Canada is acutely aware of the need to create and maintain an environment that ensures Canada upholds its strong global economic leadership and enhances Canadian productivity and overall competitiveness. The country's taxation system should encourage savings and investment; foster innovation, productivity and initiative; and enhance the economic and social well-being of all Canadians by eliminating unnecessary barriers to economic growth.

FEI Canada believes the following principles should form the basis of Budget 2011:

1) The focus should be on deficit reduction and maintaining good fiscal management to ensure that the Canadian economy will withstand future downturns. Policies should allow free market forces to lead the recovery, allowing the government to concentrate on rebalancing the books.
2) Enhancing productivity is critical to ensure global competitiveness. Given the Canadian dollar is moving towards parity with the US dollar, this issue needs priority status.
3) Policies should encourage investment and facilitate access to credit and capital markets.
4) Budget proposals should reduce the complexity of the taxation system and its compliance requirements, not add to them.
5) Policy initiatives should be prudent and incremental in nature, appropriate to Canada's relatively stable economic and financial situation, and benefit all Canadian taxpayers, businesses and citizens.
6) To the extent possible, initiatives should be revenue neutral over the short to medium-term or the legislated period of the initiative.
7) The tax system should provide Canadians with more flexible retirement planning opportunities.

Pursuant to the above principles, FEI Canada recommends that Budget 2011 include the following outlined measures.

A. COMPETITIVENESS AND ECONOMIC RENEWAL

In today's global economy, competitiveness is critical to the prosperity of, and in certain cases, the survival of, Canadian businesses. Competitiveness implies the most efficient use of resources; consistent with the desired degree of product quality, access to the capital required to invest in modern machinery and equipment, increased rates of productivity, and enhanced training and education. Competitiveness requires access to current research and the ability to capitalize on innovative product development. Competitiveness requires the accumulation of critical masses of labour and investment capital, and dictates that corporations accumulate, and retain, sufficient cash flow to expand and modernize their physical manufacturing structures.

We urge the government to implement measures that support Canadian economic value creators, encourage their global development, and improve Canada's domestic business climate. FEI Canada urges the government to maintain its scheduled corporate tax reductions. A supportive tax system is critical. Tax incentives are most effective when targeted directly at the desired outcome.

1) Knowledge-based economy

Canada must support growth of a digital and knowledge-based economy by facilitating investments that will enhance productivity and global competitiveness in order to provide employment for generations to come.

FEI Canada recommends that the government maintain and enhance the measures introduced in Budget 2010 to stimulate the creation of a digital economy.

2) Building Strong Labour Markets

Governments have traditionally extolled the virtues of life-long learning and re-training. Canadian workplaces require highly skilled and trained individuals to increase Canadian productivity. Increased labour productivity is dependent on the development of a highly educated and trained workforce. Up-to-date in-house training is especially critical to the development of workplace technical and IT employees. Government is urged to encourage creation of Canadian corporate champions of continuing education and training and to more publicly support corporations recognized worldwide for their creative and innovative approaches to employee skills development.

FEI Canada recommends that government encourage Canadian businesses to enhance the skills and qualifications of Canadian employees by:

a) **broadening the definition of what is currently deductible as qualifying education and training expenses;**

b) **introducing a refundable tax credit for qualified education and training, which will spur businesses to increase spending in this vitally necessary area;**

c) **introducing a personal deduction or tax credit for individuals who personally incur the cost of job-related education or re-training. Alternatively, displaced employees could be provided with a subsidy to undertake retraining.**

These measures will assist displaced workers acquire new or upgraded employment skills. The latter two can be funded through the notional EI account. A three-year time frame is recommended for these initiatives, both of which should be re-evaluated at the end of this period.

3) Manufacturing and Processing Machinery and Equipment

Budget 2007 reintroduced enhanced CCA for machinery and equipment used in manufacturing and processing. The qualifying time period has since been extended to 2012. Whereas this time frame may be appropriate for stimulating new investment in small projects, it is inadequate for major projects which take years to develop and complete.

FEI Canada recommends that the enhanced write-off for manufacturing machinery and equipment be extended for at least an additional five years, and that the termination date be reviewed periodically.

B. RETIREMENT PLANNING

Many Canadians must consider working beyond their expected retirement date as the financial crisis significantly diminished the value of their pension plans or investment portfolios set aside for retirement. To add flexibility to the employment opportunities of older workers and greatly enhance their retirement planning, **FEI Canada recommends that provisions be introduced which extend to age 75 the mandatory date for:**

a) **concluding contributions to the Canada Pension Plan for those who are not yet eligible for maximum pension payments;**

b) **contributing to RRSPs;**

c) **converting RRSPs into RRIFs.**

To ensure that the latter proposal is revenue neutral, the number of years over which an individual is required to withdraw RRIF funds should be reduced.

FEI Canada also recommends individuals should be granted a 125% deduction for the first $5,000 contributed to their RRSPs.

C. THE NEED FOR SIMPLIFICATION

The tax system should be reviewed with the objective of simplifying tax reporting. As demonstrated in a recent research study by FEI Canada's Canadian Financial Executives Research Foundation (CFERF), senior Canadian financial executives identified expansion of the taxation system and immediate regulatory and compliance issues as major concerns that could prove costly for our economy.

As noted in FEI Canada's 2008 submission to this committee:

"Canada's tax system is overly complex. The current tax system is a patchwork quilt of overlapping tax measures, regulations and CRA administrative practices. All too frequently, tax practitioners and corporate tax managers resort to detailed technical notes to determine the meaning of many budget measures. Consequently, the costs of complying with the tax system are excessive. FEI Canada believes that Canada's economy will grow at a much faster rate if the talented individuals working on corporate and individual tax reduction strategies could turn their attention to business generation initiatives."

FEI Canada recommends that the Act be thoroughly reviewed with the objective of eliminating complexity, in particular, those aspects of the Act which (a) do not lead to economic efficiency, growth and/or increased competiveness, (b) create excessive compliance costs vis-à-vis their policy objectives, and/or (c) are inconsistent with the above noted characteristics of a simple tax system.

The following is an example of our inordinately complicated tax system:

Group Tax Reporting
Canada is the only country which does not permit group tax reporting, i.e. consolidated tax filing or a loss transfer system. Many Canadian corporations annually devote an inordinate amount of time and money devising tax strategies whose sole purpose is to achieve the result which could be provided more effectively by group reporting. Additional costs are incurred as these strategies attract intense scrutiny by the CRA and/or the tax courts before being accepted as legitimate tax planning strategies.

FEI Canada recommends implementation of a loss transfer system, as it is much simpler to implement than tax consolidation.

This proposal will increase the competitiveness of Canadian corporations, decrease compliance costs, and allow corporate tax managers to spend more time advancing corporate growth and profitability. We recognize this initiative may be criticized as an immediate tax revenue loss. However, the lost tax yield is a timing issue, not a permanent reduction in the corporate tax yield. If the provinces do not accept group reporting, it would still be worthwhile implementing this proposal on a federal basis only.

Other worthwhile simplification initiatives include a review of the CCA system with a view to reducing the proliferation of classes, consideration of a joint personal tax return, permitting private corporations eligible for the small business deduction to use accounting income as net income for tax purposes, and a review of the implications of IFRS on the determination of net income for tax purposes to eliminate unintended implementation anomalies.

D. ACCESS TO CREDIT AND CAPITAL MARKETS

Capital formation is critical to economic development and growth. Without significant infusions of new capital and the free flow of capital, economic development is hampered, vitally needed maintenance and renewal is delayed, productivity is impaired, and employment levels are reduced. Canadian capital pools are insufficient to satisfy the constant need for new investment capital. Consequently, Canada has historically relied on foreign investors to provide capital not available from Canadian sources.

1) Withholding

Withholding taxes constitute a barrier to the free flow of capital. Withholding taxes on dividends create a bias for debt financing in Canada, and generally add to the cost of raising equity versus debt. There is a strong link between elimination of withholding tax on interest and dividends, and increased foreign direct investment and the free flow of capital. The elimination of withholding taxes on dividends would greatly improve the ability of Canadian companies to attract foreign capital and compete effectively with other jurisdictions.

FEI Canada recommends that:

a) **Withholding on dividend payments to non-residents should be reduced to the 5%/15% model in most new treaty negotiations;**

b) **Department of Finance work with all non-U.S. treaty partners to reduce or eliminate the withholding tax on interest and dividend payments to non-Canadian entities, and on dividend payments to taxpayers subject to the Canada-U.S. treaty.**

2) Debt Forgiveness

As a consequence of the financial markets crisis and deteriorating economic performance, some leveraged corporations have been forced to renegotiate debt. In some cases, a portion of the debt has been forgiven in order to allow the corporation to continue operating. Debt forgiven must be allocated to certain loss accounts in stipulated order. In essence, losses which are available to the corporation are reduced following the debt renegotiation. Under normal circumstances, this tax treatment is both reasonable and fair. However, the current financial market situation is not normal.

To encourage financial restructuring of the economy and to assist corporations who may require debt renegotiation to maintain the cash flow necessary to ensure the survival of the corporation, **FEI Canada recommends Budget 2011 should include a measure which defers the allocation of forgiven debt for three years.**

CONCLUSION

As outlined in this submission, FEI Canada has listed principles of budget decision-making and suggested measures intended to address the objectives of simplifying the tax system, creating sustained economic renewal, providing flexibility in retirement planning, and easing the credit and capital burden of Canadian businesses. As Canada moves through the current recovery period, budget proposals should be short-term focused and developed based on the Canadian reality. We believe the tax measures proposed conform to these principles and objectives. We strongly urge the government to consider these measures and implement them in the 2011 budget. FEI Canada stands ready to assist the government in fulfilling our mutual objectives.

Sincerely,

Barry Gorman

Barry Gorman, PhD, CA, TEP
Chair, Tax Policy Sub-Committee
Issues and Policy Advisory Committee

Michael Conway

Michael Conway, CA, ICD.D
Chief Executive and National President
Financial Executives International Canada

About FEI Canada (www.feicanada.org)

Financial Executives International Canada (FEI Canada) is an all-industry professional association for senior financial executives. With eleven chapters across Canada and more than 2,000 members, FEI Canada provides professional development, thought leadership and advocacy services to its members.

The Issues and Policy Advisory Committee (IPAC) is one of two national advocacy committees of FEI Canada. IPAC is comprised of more than 40 senior financial executives representing a broad cross-section of the Canadian economy who have volunteered their time, experience and knowledge to consider and recommend action on a range of topics of interest to Canadian business and governmental agencies. The current composition of IPAC is formulated to address the following areas: corporate governance, capital markets, tax policy, pensions, internal controls and public sector accountability. In addition to advocacy, IPAC is devoted to improving the awareness and educational implications of the issues it addresses, and is focused on continually improving these areas.