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Ensuring Canada’s Competitiveness

PRE-BUDGET CONSULTATION IN ADVANCE OF THE 2019 BUDGET | AUGUST 2, 2018

RECOMMENDATION 1: ENHANCING TAX COMPETITIVENESS

That the government undertake a comprehensive reform of Canada’s corporate tax regime with the aim of creating a more internationally competitive system, including reducing the corporate income tax rate, introducing full expensing for new investments in machinery and equipment, and exploring other measures to reduce business tax burdens such as exempting reinvested profits.

RECOMMENDATION 2: IMPROVING THE REGULATORY ENVIRONMENT

That the government immediately begin working to reduce the regulatory burdens, instability, uncertainty, and government-induced delays that have been discouraging business growth and investment in Canada.

RECOMMENDATION 3: SUPPORTING SMALL BUSINESSES SCALE-UP TO BECOME BIG BUSINESSES

That the government improve small and medium-sized businesses’ access to capital, limit the additional costs and reduce internal trade barriers, and reduce the costs and complexity of complying with Canada’s tax laws.

RECOMMENDATION 4: IMPROVING CANADA’S WORKFORCE PRODUCTIVITY

That the government reform foreign credential recognition and streamline the process and expand worker eligibility for federal job and re-training grants – particularly the Canada-Alberta Jobs Grant.

The Calgary business community acknowledges and supports the government's efforts to put business competitiveness at the forefront of 2019 Budget. Thank you for consideration of our recommendations.

ENSURING CANADA'S COMPETITIVENESS

Through consultation with Calgary's business community, the Chamber has identified four ways the government can ensure Canada continues to experience positive economic growth and a flourishing business community, including:

1. Enhancing Tax Competitiveness
2. Improving the Regulatory Environment
3. Supporting Small Businesses Scale-Up to become Big business
4. Improving Canada's Workforce Productivity

While our specific recommendations focus on the four priorities outlined above, the Calgary business community encourages the government to continue its work to improve market access, both international and domestic. The government must continue to work to conclude a modernized NAFTA, remove tariffs, and ratify the Comprehensive and Progressive Agreement for Trans-Pacific Partnership.

ENHANCING TAX COMPETITIVENESS

Corporate taxes impose the highest economic burden compared to all other taxes in Canada. Making Canada's business tax system more competitive will encourage private sector investment, reward entrepreneurship, and increase government revenue by keeping corporate tax revenue in Canada.

Given the international nature of investment, it is important that Canada's tax regime attracts rather than discourages capital. Canada failed to attract businesses investment, ranking 16th out of 17 comparable OECD countries in terms of business investment to GDP between 2015 and 2017. One reason for lagging investment is that Canada does not have the most competitive corporate tax environment; 21 of 33 OECD countries have lower capital taxes than Canada.

Free market business-friendly tax reform taking place in other developed countries will put Canadian businesses at a continued disadvantage if we fail to undertake competitive reforms of our own.

In 2017, the United Kingdom (UK), Norway, Italy, Israel, and Luxemburg all reduced their corporate taxes, with many developed countries announcing plans to reduce their rates in upcoming years. It is important for Canada to respond to these international reforms to ensure

Canadian businesses maintain their ability to access capital, as even small corporate rate reductions are closely related to increases in capital investment. Estimates suggest that reducing the corporate income tax rate by only 1% results in an increase in foreign direct investment by 2.5%.

The biggest threat to Canada's competitiveness, however, may come from tax reforms made by our closest neighbour and ally, the United States. Due to the recently implemented *U.S. Tax Cuts and Jobs Act*, Canada no longer has a tax advantage over the U.S. When considering corporate income tax rates and deductions, sales taxes on capital purchases, and other capital-related taxes, the U.S. will see a significant drop in their marginal effective tax rate (METR) on new investment. The U.S. aggregate METR will drop from 34.6% to only 18.8% - compared to Canada's METR of 20.9%. A recent International Monetary Report estimates American companies will cut capital investment in Canada by 6% due to U.S. tax reform alone.

Businesses do not make investment decision on tax rates alone, but (as discussed later), considering Canada's smaller market, uncertainty around market access, and increasing regulatory burden, Canada's investment environment is at a disadvantage.

IMPROVING THE REGULATORY ENVIRONMENT

A regulatory environment that fosters a stable rules-based economy is essential for business growth and investment attraction. The government can fulfill its goals of encouraging business and economic growth by ensuring costs associated with regulatory compliance are not onerous, regulations are reliable and stable, timelines are clear, and by refraining from injecting political interference into the regulatory process.

While Canada's overall ranking in the World Economic Forum's 2015-16 Global Competitiveness Report is a respectable 13th of 140 countries, Canada has room for improvement in the sub-ranking of burden from government regulation, ranking 37th. Reports from the OECD show similar concerns, according to a survey of global business leaders the single most problematic factor for doing business in Canada is "inefficient government bureaucracy."

Increasing regulatory burdens has been a key factor deterring large capital investments, especially in Canada's energy sector. There are up to 50 policy and regulatory initiatives currently being considered by the federal and provincial governments that could undermine investor confidence in Canada's energy sector. In 2018, Canadian energy companies are dealing with the introduction of carbon pricing, the West Coast tanker ban, new up stream emission considerations for pipeline project approvals, methane and clean fuels standards, and delays and uncertain approval timelines for major projects and pipelines. The business community is extremely concerned with the potential impacts the expanded roles and processes within the National Energy Board and

Canadian Environmental Assessment Agency will have on the viability of future, large capital projects.

It is not just the energy sector, the time required to construct infrastructure, build new facilities, and expand production and grow sites has increased.

Regulatory uncertainty and instability, delays, increasing burden, and political interference has resulted in the outflow of investment from Canada in "real time." In 2017, total capital spending on Canadian oil and gas was down 19% from 2016, and 46% from 2014. In comparison, capital spending on oil and natural gas in the United States last year increased by 38% to $120 billion. Between 2008 and 2016 the U.S has increased oil production 77% and natural gas production 35% - taking 8 years to get to the same level of production, that took Canada 150 years.

When developing regulations, the government needs to consider the international environment and ensure we are not unduly impacting industry's ability to compete on an international stage. Our products are in global demand. Canada has some of the most ethically and environmentally produced and grown products in the world, but excessive regulations are holding us back from accessing international markets. Government needs to incorporate international regulatory alignment to make it easier for Canadians to trade and do business abroad and seek greater regulatory cooperation into free trade agreements.

While the continuation of the Trans Mountain expansion is positive for business, this circumstance illustrates the broader significance of Canada's inability to approve and build major projects. Investor confidence in Canada is at risk until the core regulatory issues that resulted in the project and production delays are addressed.

SUPPORTING SMALL BUSINESSES SCALE-UP TO BECOME BIG BUSINESSES

By supporting small businesses scale and grow into bigger firms, the government will help businesses reinvest more on R&D, training, equipment, and wage growth.

Canada was ranked 2nd out of 190 countries in terms of ease of starting a business. 20% of the labour productivity gap with the U.S. is due to Canada having more small businesses and less big business than the U.S. In Canada, a business with less than 100 employees generates roughly $500,000 in economic activity, while the average Canadian business with 100-499 employees generates roughly $15 million in GDP.

And the issue is getting worse. Only a tiny fraction, 0.1%, of all businesses grow past the 100-employee mark – this is 40% lower than in 2001. Less than 2% of medium-sized firms (100-499 employees) become big businesses, which are key drivers of workforce productivity, job growth, and business efficiency.

More is required to support growth including reducing the layering of costs that disproportionately harms small business, working with provinces to harmonize regulations across Canada, and helping small business access capital.

A lack of regulatory harmonization between provinces impedes internal trade, by requiring slightly different standards to sell across provincial borders and making it harder for small businesses to reach new customers. According to the OECD, costs tied with varying regulations in each province are relatively more burdensome for smaller business, equivalent to a 15% tariff for smaller firms, compared to less than 5% for larger firms.

Limited access to capital has reduced Canadian businesses ability to scale up. Evidence from the UK suggests that full capital expensing can help small and medium-sized businesses acquire the capital the need to grow. After the introduction of more generous capital allowances, investment increased by 11%. A policy environment must be established not only to help entrepreneurs start a business, but to support businesses looking to expand production and grow larger.

The government could improve small and medium-sized businesses' access to capital, potentially through a Canada-wide investor tax credit, or through working with the Business Development Canada to make more capital available for small business growth. We also support the Canadian Chamber recommendation to establish a 15% refundable tax credit on eligible start-ups for angel investors, provide a tax exemption on venture capital gains.

BUILDING A COMPETITIVE WORKFORCE

Canada is one of the strongest OECD countries with Canadian students' science, math, and reading scores consistently rank in the top five among OECD nations. While a highly educated Canadian population is a significant competitive advantage, there is still room for the federal government to support businesses in improving workforce productivity.

In 2019, Canada is forecasted to be ranked 16th out of all OECD countries in terms of labour productivity growth since 2010. Despite a broad and growing consensus that Canada's workforce productivity needs to be improved, the gap with other leading jurisdictions has widened in almost every province over the past two decades.

While there are many factors that influence productivity, a noteworthy concern for many Calgary businesses is the "skills gap" – a mismatch between the skills supplied by our workforce and the skills needed by business. In 2016, 60% of large Canadian employers surveyed by the Business

Council of Canada said Alberta is the province where the skills gap is most persistent. Alberta's job vacancy rate has increased over the past two years, reaching 2.6%. The higher vacancy rate can suggest that businesses are having a difficult time finding employees – or employees with the necessary skills.

To address the skills challenge faced by businesses and improve the integration of Canada's immigrant population, the government could advance the recognition of foreign qualifications. Canada's immigrant population is among the most highly educated in the OECD, however, immigrants are currently at high risk of working in jobs below their formal qualification level. Greater recognition of foreign qualification would improve business access to higher, and potentially missing, skills.

Barriers to finding and employing foreign talent may also be hindering the innovative capacity of the Canadian economy. 53% of technology companies report that finding and hiring experienced management and executive-level talent is their biggest obstacle to growth.

Along with the priorities outlined above, the business community also wants the government to outline a path to balance by being disciplined in future spending. A balance budget sends a signal that Canada is a stable place for investments; continued deficits add to uncertainty about future tax increases to service and repay government debt.

Thank you for the opportunity to submit our written recommendations on improving Canada's business productivity and competitiveness. References are available for all our data and recommendations.

Sincerely,

Dr. Sandip Lalli

President and CEO