CPQ
S'ALLIER POUR LA PROSPERITÉ

COMMENTS FROM THE CPQ FOR THE 2018–2019 FEDERAL BUDGET

AUGUST 2017

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The CPQ's mission is to ensure that businesses in Quebec enjoy the best possible conditions – particularly in terms of human capital – for sustainable prosperity in a context of global competition. The CPQ is the focal point for employer solidarity, and its leadership has helped it become the undisputed benchmark in its spheres of activity. It works constructively towards a more prosperous society in which entrepreneurship, productivity, wealth creation and sustainable development are the prerequisites for raising the standard of living for the entire population.

Conseil du patronat du Québec – August 2017

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Introduction

In its comments, the CPQ is essentially responding to the questions posed by the Finance Committee, i.e., what federal measures would help Canadians to be more productive, and what measures would help Canadian businesses to be more productive and competitive. The two questions are obviously closely related in that the productivity of businesses is conditional on that of their workers, while the productivity of workers largely depends on the investments made and processes established by their employers. It is therefore essential that the federal government create a favourable regulatory and fiscal environment.

Contextual elements for fiscal year 2018–2019

The digital revolution: a crucial issue for businesses, workers and the government

Across the globe, the economy is restructuring in response to the “4th industrial revolution”: the massive and rapid penetration of digital technologies into all stages of design, production, distribution and consumption of goods and services, in all sectors of activity and in all occupations and professions. A great many businesses and workers, however, do not have adequate strategies or skills to make the necessary changes to their processes or methods. In fact, two thirds of Canadian workers lack the required skills to work effectively in a digital environment.[1] This must therefore become a priority, in terms of both young Canadians who are still in school (future workforce) and the people who are already employed (current workforce).

The ongoing digital revolution affects the way the government can and should intervene in the economy with businesses and workers. It also has a significant impact on the growth of the government’s tax revenues and on the fairness of the tax system. A very large percentage of electronic transactions between Canadian consumers and foreign suppliers currently goes untaxed. This not only deprives the government of revenues, but also affects the competitiveness of the Canadian competitors of these foreign suppliers. These impacts are being particularly felt in sectors such as media and retail.

The American context

Access to the American market could become more difficult in the coming years as a result of the entry into force of various protectionist measures by the U.S. administration. Furthermore, the American government has indicated its intention to amend its tax rules in order to promote American-made

[1] Source: OECD, 2013, *OECD Skills Outlook 2013: First Results from the Survey of Adult Skills.*

products, which would undermine the North American value chains established in recent decades. The anticipated reform of American corporate and individual income tax will no doubt have significant consequences for the competitiveness of our tax system and our businesses.

The following approaches should be explored in view of these structural and environmental changes.

2018–2019 budgetary priorities

A - Foster investment and innovation

Private sector investments in Canada have been on the decline recently. This compromises the capacity of the Canadian and Quebec economies to renew themselves, confront new challenges and take advantage of new business opportunities created by the digital revolution and the emergence of new export markets. It also affects employee productivity. Indeed, in 2016, for every dollar per worker invested by an American business, the Canadian business only invested 59 cents.[2] This finding can be explained by a number of factors, including the overall fiscal and regulatory environment and global uncertainty.

Canada must maintain a very attractive fiscal and regulatory business environment for all corporations. Although Canada's corporate tax rate is relatively competitive among G-7 countries, the situation is less rosy when it comes to the marginal effective tax rate (METR). Despite remarkable efforts to reduce the tax burden on businesses since 2007, Canada ranks 13th among the 34 OECD countries in terms of METR.

Furthermore, the government should invest in programs that exert structural leverage on productivity, innovation, marketing and reducing companies' environmental footprint. The government appears to have adopted the right approach in the last budget; however, the CPQ is concerned that the measures are not sufficiently concrete in the short term to create adequate momentum.

The government could consider the following measures to further encourage private investment and R&D: provide refundable R&D tax credits to large corporations and expand the accelerated deduction of capital costs for required investments. Both would be helpful to companies that must adapt their business models, processes and procedures to digital technology. Another approach would be that of Quebec, which provides a tax advantage to revenue attributable to a patent in order to encourage the marketing and manufacturing of innovations in that province.[3]

[2] Benjamin Dachis, William B.P. Robson and Aaron Jacobs, *Equipment Failure: Feeble Business Investment Costs Canadians their Competitive Edge*, C. D. Howe Institute, March 2017.
[3] The *Québec Economic Plan* of March 2016 provided for the creation of a deduction for innovative companies. Since January 1, 2017, this measure gives manufacturing firms that market a product that includes a patent protecting an invention developed in Quebec a lower tax rate on the revenue attributable to that patent.

Furthermore, there should be a review of the impact of the reduction of scientific research and experimental development (SR&ED) tax credits given that a resulting downward trend in investments in this area has been observed.

In terms of ecofiscality and the carbon tax, the announcement of a benchmark for carbon pricing – with an exemption for provinces or territories that already have a similar program – represents an additional and invaluable tool for fighting carbon emissions, and is part of a harmonized approach that takes provincial initiatives into consideration. However, given that Quebec has already implemented SPEDE (cap-and-trade system for greenhouse gas emission allowances), it would be unacceptable for the federal government to create additional tax obligations. Ecofiscality should not be about finding new revenues, but rather reallocating the tax burden to promote certain behaviours and environmental objectives.

It should be noted that consideration must always be given to the overall tax burden. If some housekeeping of tax expenditures is required, and if tax credits or other forms of tax relief are reduced or eliminated following an assessment of their effectiveness, the general tax rate should be reduced correspondingly.

Finally, aside from tax incentives, the government can be the first buyer of the products and services of innovative businesses, therefore demonstrating the usefulness of these innovations.

B - Promote competitiveness by investing in infrastructure

Another effective approach for the government would be to restore and develop public transportation and communication infrastructure. Such infrastructure should have sufficient flexibility and capacity to respond to the changing needs of commerce and industry, as well as to global trade flows. In metropolitan areas, infrastructure contributes directly to business productivity and competitiveness by improving the mobility of people and merchandise. On that front, the CPQ urges the federal government to invest in infrastructure as strategically and effectively as possible, specifically by investing in Quebec's airports, ports and logistical hubs, as well as in high-benefit public transportation projects. The federal government has an essential role to play in promoting the diversification of intermodal services, provided that its investment is fully integrated with provincial and municipal strategies. The CPQ would also like the federal government to round out the funding needed to extend the Blue line, which is an important project for the Montréal region. Another investment that would help improve the vitality of the Canadian economy and increase mobility is a high-speed rail line linking Québec City, Montréal, Ottawa and Toronto.

In the second phase of reinvesting in strategic infrastructure, it would also be helpful to think in terms of future needs, new technological realities, digital infrastructure needs and environmental considerations, such as the contribution of logistics chains to the reduction of greenhouse gases.

Finally, the CPQ would like future investments to be made without any undue delay, and the federal program to be linked to the Quebec infrastructure program (PQI).

Financing through the Canada Infrastructure Bank is obviously an attractive and promising option for projects that would not otherwise be funded.

C – Workforce availability and training

The CPQ believes that an employment insurance contributions credit for training expenses, particularly for formal training associated with new investments, would be another way for the Employment Insurance program to help improve the productivity of businesses and workers. Furthermore, the CPQ believes that the Employment Insurance program should strive to strike a balance between compensation for people who lose their jobs and incentives to work.

The CPQ would also like to bring to the attention of the Government of Canada the importance of investing more in training programs led by the provinces and territories to help unemployed people who are not eligible for employment insurance to upgrade their skills and enhance their employability. Specifically, we call on the Government of Canada to enhance its efforts to help under-represented groups and to establish incentives for employers who recruit workers from these groups.

Moreover, the changes announced to the Temporary Foreign Worker Program have still not been implemented. Delays and unpredictability can represent major obstacles to the ability of businesses to win contracts and maintain Canadian jobs.

D – Healthy public finances

The above considerations notwithstanding, the CPQ would like to remind the government of the importance of avoiding structural deficits. Instead, it should focus on policies designed to leave future generations a prosperous country in good financial health. A clear financial plan to return to a balanced budget over the next few years is very important, as is the financial security of future generations. We must not burden them with additional taxes so we can have services now. That is also why the CPQ would like to see measures that focus on increased private investment.

In terms of health transfers, the CPQ invites the government to look closely at the *Canada Health Act*, in cooperation with the provinces. We believe that the plan to tie transfers to the growth of the GDP will be insufficient to meet the needs of the aging population in Canada and Quebec. Furthermore, the CPQ believes that all of society would benefit if the private sector were permitted an enhanced presence in certain specific areas, where justified by actual advantages.

As for revenue, as stated in the Introduction, we think it is essential to adapt to new trade-related technologies and to deal with the issue of online sales that deprive the federal and provincial governments of tax revenues and negatively affect the competitiveness of Canadian businesses.

In addition, in seeking new revenues, for example, as anticipated in the current consultations on tax planning using private corporations, attention must be given to the potentially harmful effects on some businesses, notably SMEs. The CPQ will take the time to analyze and comment on the proposals submitted by the government in the context of this consultation.

With regard to the legalization of marijuana, there must be a balance in terms of price – and therefore taxes – in that if the price is too high, consumers will continue to buy from illegal suppliers, while a price that is too low could trivialize consumption of this product, thereby increasing its use. Moreover, given that the provinces will likely be assuming the brunt of the costs associated with this new market (health, social services, information, policing, etc.), it bears asking whether this new tax base should not be left to them in its entirety. Sales will obviously be subject to the GST.

Along the same lines, the government must continue to vigorously combat tobacco smuggling. Here again, a balance must be struck; for example, tobacco regulations must not unfavourably compare with those for marijuana.

The situation of airports is another file that should be examined. According to a Senate report,[4] high costs and inefficiencies are deterring demand for air travel and discouraging competition in the industry. The federal government should stop charging airports ground rent and transfer them to the authorities that already operate them.

E – International opportunities

It is important that our businesses be well prepared, particularly in terms of training and information, to take advantage of new business opportunities, notably as a result of the Comprehensive Economic and Trade Agreement (CETA). Work has already begun in anticipation of the NAFTA renegotiations, both globally and on certain key files such as softwood lumber and aerospace. The CPQ also encourages the Government of Canada to continue its efforts to promote more free trade with other countries and to diversify its markets. We are thinking in particular of the other parties to the Trans-Pacific Partnership (TPP), bilateral agreements with Japan and Korea, and the development of a trade strategy for China.

[4] Senate of Canada, The Standing Senate Committee on Transport and Communications: "The Future of Canadian Air Travel: Toll Booth or Spark Plug?" June 2012. Link: https://sencanada.ca/content/sen/Committee/411/trcm/rep/rep05jun12-e.pdf.