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Mr. Rob Merrifield

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● (1535)

[*English*]

The Chair (Mr. Rob Merrifield (Yellowhead, CPC)): We'd like to call the meeting to order. We want to thank our witnesses for coming forward. This is pursuant to Standing Order 108(2), a continuation of a study on the structure of Canada's federal revenue-raising system.

We have with us, from Financial Executives International Canada, Barry Gorman, chair, as well as Michael Conway, chief executive and national president.

We want to thank you, and we're going to yield you the floor, but before we do that I'll introduce the others.

Neil Brooks is here from York University.

From the OECD, by video conference, we have Christopher Heady.

With that, we want to welcome you again to the committee.

We'll yield the floor to Mr. Conway first. We're very interested in what you have to present to the committee. The floor is yours, sir.

Mr. Michael Conway (Chief Executive and National President, Financial Executives International Canada): Thank you, and good afternoon, Mr. Chairman and committee members.

My name is Michael Conway, and I'm pleased to present, on behalf of Financial Executives International Canada, our views on your study of the structure of Canada's federal revenue-raising system.

FEI Canada is a voluntary professional membership association comprising more than 2,100 of Canada's senior-most financial executives, organized into 11 chapters across the country.

The recommendations presented to you are the result of the collective effort of our tax committee, which comprises senior financial executives representing a broad cross-section of the Canadian economy and is chaired by Barry Gorman, who is with me today.

Our submission focuses on three key components necessary for a sustainable economic environment: competitiveness, efficiency, and accountability of federal spending.

Competitiveness is critical to the long-term prosperity, and in certain cases the very survival, of Canadian business. Competitiveness implies production with the most efficient use of resources, notably capital and labour, consistent with the desired degree of product quality, access to capital required to invest in modern machinery and equipment, increased rates of productivity, and enhanced training and education.

As demographics change, Canada faces a severe labour shortage. We must attract and retain the best and brightest talent with the know-how required to increase productivity and competitiveness. Therefore, we urge the government to implement mechanisms that support Canadian economic value creators, that encourage global development, and improve Canada's business climate.

A supportive tax system is critical to enhancing Canadian economic competitiveness. With this in mind, we submit recommendations related to three topics: corporate taxes, human resources training and development, and free flow of capital.

Let me begin with corporate taxes. We have three specific recommendations in this area.

First, accelerate corporate income tax reductions. FEI Canada congratulates the government for introducing rate reductions, but it is worthy to note that Canada's effective tax rate is still too high. FEI Canada submits that Canadian corporate taxation must be internationally competitive to make domestic business more productive and to facilitate direct foreign investment. We need only to look to numerous foreign countries, such as Ireland, that have significantly reduced their corporate taxes since 1980 as a successful means of attracting increasingly mobile capital.

Second, reduce the proliferation of non-neutral tax preferences. Some corporations claim various tax incentives as a means of reducing their statutory tax burden, resulting in significant effective tax rate differentials across industries. This disparity is heightened by the different provincial corporate tax rates and credits.

Third, encourage provinces to normalize their corporate income tax rate structures and repeal remaining provincial capital taxes.

Next, let's look at human resources training and development. FEI Canada urges the government to actively aid Canadian businesses in supporting the enhancement of employee skills and qualifications in two specific ways: first, by broadening deductible qualifying education and training expenses; and second, by introducing a refundable tax credit for qualified education and training.

Business responds to incentives that benefit operations. An employee education and training credit will spur business to increase spending in this vitally necessary area.

FEI Canada further recommends that the government establish a centre for continuing workplace education and training to stimulate development of world-class champions of continuing education, further details of which are included in our brief. This kind of program would be particularly beneficial to small and medium-sized enterprises.

Our final recommendation in the competitiveness category is the need for a free flow of capital. We urge the government to continue reducing dividend withholding taxes for non-residents, at a minimum, to the 5% and 15% model found in most new treaty negotiations. This reduction would result in minimal revenue losses, as this primarily relates to emerging economies, such as India and China, that still have higher withholding rates.

On the other hand, complete elimination of withholding taxes would provide Canadian businesses better access to global capital markets at the lowest possible cost. Thus, we would like to expand our submission by suggesting government study the feasibility of eliminating all withholding taxes.

I would now like to move to our second category of recommendations, which concern efficiency. A tax measure is efficient when it achieves its goals in a cost-efficient manner. It is FEI Canada's position that several aspects of the Canadian tax system do not support efficiency, do not blend with overall fiscal policy, and do not minimize interference with system equity.

● (1540)

Canada's tax system is an overly complex patchwork quilt of overlapping tax measures, regulations, and administrative practices. Consequently, compliance costs are excessive. Non-resident investors have noted that Canada has a bewildering proliferation of tax rules and multiple tax jurisdictions. Taxpayers need more stability and consistency in the tax-policy-making process and in the administration of tax rules.

To facilitate a transition to a more streamlined tax system, FEI Canada would like to highlight two recommendations. First, we recommend that the government work with the provinces to adopt a national harmonized sales tax. Many Canadian corporations transact business in multiple provinces, and there are variances in both sales tax rates and between the GST and PST tax bases. Sales tax registrants must submit sales tax returns to multiple taxing authorities and dedicate resources to multiple tax reviews, queries, and audits. In harmonized provinces, businesses receive the provincial portion of the HST paid on purchases, which is currently 8%. In non-harmonized provinces, businesses are refunded only the GST they pay, not the PST they pay on their purchases. By moving to a harmonized sales tax, businesses in the now non-harmonized provinces would be refunded all the sales tax they pay.

Greater harmonization of provincial sales taxes with the GST would enhance competition and reduce compliance costs, as taxpayers and the government would only have to deal with one tax authority. A harmonized sales tax makes for an efficient tax system. Harmonization in the Atlantic provinces appears not to have led to a decline in provincial tax revenues or to an increase in consumer prices.

FEI Canada is advocating that the GST not be reduced below its current level. If these consumption taxes were cut further, alternative forms of revenue would have to be found, and spending would have to be reduced to cover the shortfall.

Our second efficiency recommendation is to call upon the government to implement either group tax consolidation or a loss transfer system. Canada is the only G7 country that does not permit group tax reporting, either in the form of tax consolidation or loss transfer. Our research reveals that some corporations devote more than 1,000 person hours, or over half a million dollars annually, in specialist costs, devising complicated tax strategies to effectively achieve the same end result as group reporting. Implementation of this proposal will reduce the compliance costs of corporate groups. This will be especially beneficial to small and medium-sized enterprises, as they can less afford elaborate tax planning.

Our third and final category of recommendations concerns accountability on federal spending. Spending by the federal government certainly affects the revenue system, since the government must raise revenues required to pay for its program expenses and national debt charges. While we commend the government on some recent spending restraint initiatives, we note that 2006-07 program spending has increased back to its 1997-98 level of 13% of GDP, and the 2006-07 budgetary expenses are at their highest level ever. These trends are not conducive to responsible management of federal fiscal resources. Aggressive debt reduction will result in lower interest charges in future years, resulting in more resources available for either tax reductions or necessary increases in program spending.

Consider one thing: one-third of our current program expenditures are for old age security and health care, two areas we know will continue to cost more as our population ages. To meet these growing obligations, we urge spending restraint and the maintenance of the current debt reduction structure.

We encourage the government to reallocate funds in areas that lead to economic growth, notably for infrastructure funding for research and development, transportation, and post-secondary education.

Finally, FEI Canada encourages the government to implement a regular review of the tax system, which is needed to be in keeping with the principle of transparency and which will provide the opportunity to modernize Canada's tax legislation at regular intervals so as to support and preserve Canada's competitiveness domestically and internationally.

● (1545)

Ladies and gentlemen, FEI Canada thanks you for your time and for the opportunity to present our ideas to you. Dr. Gorman and I would be pleased to answer any questions you might have.

The Chair: Thank you very much.

Before we get to the questions and answers, we'll let the other two presenters go, after which we'll start our round of questioning.

We'll now hear from York University. We have Neil Brooks, the director of the graduate program in taxation at Osgoode Hall Law School.

Thank you for coming, and we look forward to what you have to tell the committee.

Professor Neil Brooks (Director, Graduate Program in Taxation, Osgoode Hall Law School, York University): Thank you very much. It's a great pleasure to be here, and I thank the committee for inviting me. I wish you good luck in the important task you've undertaken of examining the federal tax system.

Let me begin by speaking very briefly about the purposes of the tax system. The tax system is, of course, simply a policy instrument that the government has at its disposal in achieving its broad social and economic objectives. Therefore, in any kind of review of the tax system, it seems to me to make sense to begin by thinking about what purposes the tax system can and should serve. So I'm quite prepared to make some specific comments, but these comments will be kind of general.

It's commonly said that the tax system has three purposes: to raise revenue for government expenditures; to assist in mitigating the unequal distribution of wealth and income in society; and third, it can be used to attempt to influence social and economic choices that individuals make in their private activities.

I suppose the broad point that I would try to impress upon the committee is that the tax system should be better designed to serve the first two purposes, namely, raising revenue and achieving more equitable distribution of income; and the tax system should be used very sparingly, certainly more sparingly than it has been, for the third purpose, namely, trying to engage in various forms of social or economic engineering.

The most important purpose of the tax system is, of course, to raise revenue to finance government expenditures. In modern societies, governments have many important and irreplaceable functions to perform. Therefore, it's absolutely vital that the government have a tax system that's capable of raising a good deal of revenue in ways that are equitable and efficient.

I might just make three subsidiary points about that. One, I might note that by international standards, as I'm sure you're all aware, Canada is and always has been a relatively low-tax country. For example, in 2005, the last year for which you have comparable statistics, taxes in the average OECD country were about 36.2% of GDP. In Canada, taxes were only 33.4% of GDP, almost three percentage points less than the average industrialized country and about five percentage points less than the average European country. Total taxes collected in Canada have always been substantially below the international average calculated as a percentage of GDP; that is, we've always been a relatively low-tax country. Therefore, it seems to me just incidentally that if someone were looking for a cause for any malaise in Canada's economy or society, there's certainly no international evidence to support a claim that it might be blamed on high taxes.

Also, I might note that if you look across countries with high and low taxes, what you discover is that those countries with high taxes tend to have much better social outcomes than those countries with low taxes—that is, much better quality of life for their typical citizen.

Just by way of illustration, in the United States, for example, which is a relatively low-tax country, 22% of children live in families below the poverty line, whereas in the Nordic countries, which have relatively high taxes, the percentage of children living below the poverty line is 3% or 4%—trivial. In Canada, of course, which is a relatively low-tax country, but closer to the average than the U.S., about 13% of children live in families that are below the poverty line. There is a very close correlation between, in effect, children living in poverty and the amount of taxes collected in a country. That is to say, one thing that our taxes buy, or that higher taxes buy, is lower levels of poverty.

But in fact the same could be said about almost any social indicator. It's hard to think of a social indicator, whether it relates to environmental sustainability, gender equity, or equitable distribution of income, in which there's not a fairly strong correlation between taxes and better social outcomes. Indeed, those countries with high taxes that achieve these relatively good social outcomes in fact are countries that are at the same time achieving relatively high levels of economic growth and material well-being for their citizens. That is to say, when you look around the world at the international evidence, there appears to be no trade-off between having an equitable society and having high rates of economic growth. Generally, the international evidence is that those policies that are financed with higher taxes not only contribute to better social outcomes and a more flourishing democracy, but they also appear to contribute to a highly educated, healthy, and productive workforce.

A second subsidiary point about this purpose of the tax system is that this means that in order to raise a sufficient amount of revenue to finance functions of modern government, it's important that the government be able to rely upon a broad mix of taxes. Consumption taxes, income taxes, wage taxes, corporate taxes—all of those are important sources of revenue, and each tax should be designed so that it's collecting revenue in the most equitable and efficient manner possible.

● (1550)

Thirdly, I would make the obvious point that the recent tax measures would seem to needlessly impair the revenue-raising abilities of the Canadian tax system—for example, the cuts to the GST, which took about $13 billion out of the federal tax system; the introduction of a plethora of additional income tax loopholes, including tax-prepaid savings plans, which in future years are going to cost the government billions in lost revenue.

Indeed, if you look for this last fiscal year, all of the taxes collected by the federal government were made up of about 13.7% of GDP, which was lower than the level of taxes collected by the federal government as a percentage of GDP back in 1960, in spite of the many additional needs that our society would appear to have.

So that's my first point. The most important objective of the tax system is to raise revenue, and the committee ought to be examining the system to ensure that it's capable and it will in the future achieve relatively high levels of revenue.

Secondly, in addition to raising revenue, most people agree that the tax system is a useful policy instrument for achieving a more socially and morally appropriate distribution of income than that which results solely from market forces.

Two things suggest that this committee, in reviewing the Canadian tax system, should in particular be concerned about this important function of the tax system.

First, income in this country is becoming much more unequally distributed. Every measure of the distribution of income and wealth shows the real income of the typical family has essentially stagnated over the last three decades, while the rich have been getting much richer. Just by way of example, in 1980 the top 1% of income earners received about 7.5% of national income; by 2000, they were receiving 13.5%. The increasing concentration of income and wealth is staggering, and it will have severe social and economic consequences for the country. It will eventually threaten our economic prosperity, erode social cohesion, increase economic insecurity, reduce public health, distort the allocation of resources and talents, lead to the withdrawal of the “haves” from public life, erode democratic values, and ultimately diminish the flourishing and richness of Canadian society.

At the same time as the distribution of income has become more unequal, the effective tax rates paid by high-income individuals have been going down. Again, let me just cite one figure. In 1990 the top 1% of Canadians paid a much larger percentage of their income than the bottom 10%, considering all taxes. By 2005 the top 1% were paying less in taxes as a percentage of their income than the bottom 10%. That, it seems to me, is just shocking, and I would urge this committee, in their deliberations, to consider ways to make the tax system more progressive.

Finally, the income tax now contains a bewildering variety of implicit spending programs, measures by which the government tries to influence the social and economic choices that individuals make. Indeed, there are over 150 of them in the income tax alone, by any reasonable count. Of course, over the past two years the government has added greatly to that number: enriched the registered educational savings plans, exempted scholarships and bursaries, provided a tax credit for public transportation, implemented the children's fitness tax credit, eliminated the capital gains on publicly traded shares donated to private foundations. Those measures—and as I say, there are over 150 in the Income Tax Act—have absolutely nothing to do with the tax system. They're spending measures, even though the government keeps calling them tax cuts. They're not tax cuts; they're spending measures.

For example, with respect to the tax credit for fees paid for children's fitness programs, what the government is essentially saying is, for families that, let's say, spend $500 in fees for sending their kid to hockey school, what we will do is pick up one-quarter of the cost. So you send us your receipts for $500 for sending your children to a fitness school, and we'll write you a cheque for $125. It's a spending program. But instead of writing the cheque, what the government says is, “Well, instead of our writing you a cheque, just offset it against your tax liability”, and that's what people do. It has nothing to do with the tax system, other than the fact that it's being offset against their tax liability as a way of delivering the subsidy. That doesn't make it a tax measure. It's a spending measure that happens to be delivered in the tax system by allowing it to be offset against people's tax liability.

Most of those implicit spending programs in the tax system, to the extent that they serve any legitimate government function, are inequitable. They lead to inefficiencies. They lead to abuses. They're not transparent. The government has no control over the spending. They complicate the tax system. They make it unfair.

● (1555)

The real pathway to efficient and equitable tax reform would be for this committee to review all of those tax expenditures in the act and repeal those that serve no useful government function, or the ones that are so badly designed that they're just a waste of government money.

The ones that remain, the ones you want to keep, if you still want to keep those spending programs and matching people's receipts or spending, take all those programs out of the tax system and put them in a separate act. In effect, say to individuals that if they qualify for one of these spending programs, if they want to continue to deliver them in this way, they can offset the amount that they qualify for against their tax liability. Put them in a separate act and embed them in the budgetary process, like every other government spending program, so that Canadians can see their true cost, and Canadians can see who is benefiting from them. I think if you did that, most Canadians would be appalled at the cost of those programs and at how much the benefits largely go to well-to-do families.

Thank you.

The Chair: Thank you.

I can see we're going to have an interesting debate when we get to questions and answers.

We'll now move on to Christopher Heady. He's from the Organisation for Economic Co-operation and Development. Christopher Heady is the head of the tax policy and statistics division, centre for tax policy and administration.

The floor is yours, sir.

Mr. Christopher Heady (Head of Division, Tax Policy and Statistics Division, Centre for Tax Policy and Administration, Organisation for Economic Co-operation and Development): Thank you, and thank you very much for inviting me to speak to you today.

I'm going to talk about how the Canadian tax system compares to tax systems across the OECD. In my presentation I will refer to some of the charts that I believe have been provided to you.

First of all, there is a chart that reports tax revenues as a percentage of GDP. As Professor Brooks just indicated, this shows that in Canada the tax revenue as a percentage of GDP is somewhat below the OECD average. And I should say that these are tax revenues for all levels of government: federal, provincial, and local taxes.

If I move on to the tax mix, Canada is a country that, compared to most OECD countries, raises a rather high proportion of revenue from personal income tax, a rather small proportion of revenue from social security contributions, and a slightly lower than average—but not much—share from taxes on goods and services.

I think the main interest you have is in the actual tax rates, and so I'll move on and talk about trends in the main or top corporate tax rate that there have been over the past 25 years or so.

What we can see is that there have been very dramatic reductions in corporate tax rates across the OECD over the last 25 years, and in fact I must say that these cuts are continuing. For example, this chart shows, as the latest figure, the corporate tax rates for 2007, but at the beginning of 2008 Germany reduced its corporate tax rate from about 38% or 39% to just below 30%. So in fact, if we take that change into account, Canada now has the third highest corporate tax rate within the OECD.

On the next page, there is a comparison of corporate tax rates in the form of a table. The point this table makes is that large-sized OECD countries seem to be able to sustain a higher corporate tax rate than small-sized OECD countries, and that not only do small-sized OECD countries have lower corporate tax rates, but they've been cutting them faster. We would regard Canada as a medium-sized OECD country, and you can see that in 2007 the average for those medium-sized OECD countries was around 30%, considerably lower than the current Canadian corporate tax rate.

Another issue that is of concern to most countries is the tax rate on dividend income. So the next chart shows, for the years 2000 and 2007, the overall tax rate on dividend income, taking account of both the tax paid at the corporate level in corporate tax and the personal income tax that's levied on dividends. You can see here that once again almost all countries, or all countries in the chart—almost all—have shown a considerable reduction in the taxation of dividend income. Canada has certainly taken part in that cut, but you can see that Canada is above the OECD average; it was in 2000 and it still was in 2007. Again, here, Canada has a comparatively high tax rate.

● (1600)

One other aspect of the corporate tax system is the incentives that are given to research and development, and the next chart shows how Canada compares to other OECD countries. What you can see from the solid black bars is that Canada offers fairly generous, but not extremely generous, incentives towards R and D for large firms. But the little diamond shape above that shows that Canada has an unusually high R and D tax incentive for small and medium-sized enterprises, about the third largest in the OECD.

Moving on to looking at the taxation of labour income, we see that Canada, like other OECD countries, has cut its top personal income tax rate quite significantly over the past 25 years or so. Canada lies more or less in the middle of OECD countries in its current top statutory personal income tax rate. However, a measure that we use more often to look at the taxation of labour income is something that we call the tax wedge. That's something that measures the difference between the cost to employers of employing a worker and the amount that the worker actually takes home to spend.

What you can see in the chart is that Canada is substantially below the OECD average. We've split this bar up into personal income tax, employee social security contributions, and employer social security contributions, and the chart shows that it is not because Canada has a particularly low rate of personal income tax that accounts for its low overall tax burden on labour, but because its social security contributions are substantially lower than average in the OECD.

This chart looks at the situation for a single worker who's earning the average wage. The next chart shows that for that same worker, almost all OECD countries have reduced the tax wedge between 2000 and 2006, and Canada has been part of that trend.

The next chart shows the tax wedge for lone parents. Typically, lone parents don't earn as much as the average worker, so we've looked a lone parent earning about two-thirds of the average wage. You can see that Canada applies a very low level of overall taxation to the wage income of lone parents, about the same amount as the United States, and significantly less than almost all other OECD countries. Only New Zealand and Ireland have substantially greater preferences for lone parents at that income level. They in fact have a negative tax.

The final chart on labour income shows a very simple measure of the progressivity of the tax burden on labour income. You can see that the Canadian tax system has somewhat below average progressivity, and that progressivity fell between 2000 and 2006. However, I should say that I believe the figures would show an increase in progressivity if we looked at 2007, because of the changes in your personal income tax system that were introduced in 2007.

● (1605)

Let me finally move to the comparison of taxes on consumption.

Canada, like all but one of the OECD countries, has a value-added tax that you call a general sales tax. The exception is the United States, of course. The black bar shows the standard rate of your general sales tax in 2007. I should clarify here that the federal rate is shown, not the federal-plus-provincial rate, but the revenue we show is both the federal and provincial revenues from value-added tax or general sales tax in Canada. You can see here that Canada raises a relatively small proportion of its income from GST.

The final chart shows a comparison of environmentally related taxes. In most countries these are primarily taxes on motor vehicles and motor fuels, but there are a number of other more minor taxes as well. You can see that Canada falls very much in the group of countries that do not use environmentally related taxes very much; it's much more on a North American model, with rates similar to those of Mexico, somewhat higher than those in the United States, and substantially lower than those of most European countries.

That's the end of my presentation. Thank you very much for your attention. I'll be very happy to answer questions.

The Chair: Thank you very much.

We'll now move to our question and answer period. Mr. McCallum will start us off with a seven-minute round.

Mr. McCallum, the floor is yours.

Hon. John McCallum (Markham—Unionville, Lib.): Thank you, Mr. Chair, and thank you to all the witnesses for being with us today.

I'd like to try to ask each of you a few questions. Since I don't have much time, I would appreciate it if you could try to be fairly concise in your answers.

Professor Brooks, you used the words “social engineering”, which would perhaps be a bit pejorative if I used it, although I have. I have said on a number of occasions that rather than government discriminating, shall we say, by providing tax credits for young hockey-playing Canadians but not for young violin-playing Canadians, we would prefer to see general income tax reductions rather than what one might call boutique tax cuts.

I will ask each of you whether you think that general income tax cuts would be preferable to narrowly directed tax credits as a matter of general tax policy.

Mr. Brooks, would you comment?

● (1610)

Prof. Neil Brooks: I certainly agree with that. There's a long list of problems that you create when you try to deliver these subsidies through the tax system. They're hidden subsidies; they're not transparent. Government's not accountable for them—

Hon. John McCallum: I've got your answer. I want to go through—

Prof. Neil Brooks: Exactly. I can't think of hardly one I would retain, frankly.

Hon. John McCallum: Mr. Conway, would you comment, please?

Mr. Michael Conway: In our brief we talked about simplicity and the reduction of the non-proliferation of credits. We would prefer to get back to basics, simplify it, and then direct the incentives more specifically. So the answer would be—

Hon. John McCallum: Thank you very much.

Mr. Heady, could you comment?

Mr. Christopher Heady: I also would very much agree. In the OECD we think it is better to have a simple tax system and a low general rate, rather than a high general rate with a large number of special exceptions.

Hon. John McCallum: Thank you.

On the question of consumption tax—which we call the GST—versus income tax, given the choice between reducing consumption tax in Canada versus reducing income tax in Canada, which would you prefer?

Maybe I'll start with Mr. Heady. I do note that Canada's already relatively high on income tax and relatively low on consumption tax, so which would you prefer as a matter of tax policy?

Mr. Christopher Heady: I think it depends on what your priorities are.

Hon. John McCallum: I'm trying to be non-political. It's a matter of sane tax policy.

The Chair: That's okay, John.

Hon. John McCallum: Sorry.

Mr. Christopher Heady: I think that if the purpose of the tax reduction was to promote economic growth, there is a considerable amount of evidence that a shift from personal income tax toward consumption tax would promote the rate of economic growth, keeping the overall tax burden constant. However, there is a concern that a move of that sort could increase income inequality.

So to a large extent, the answer to the question depends on the relative weight you put on reducing income inequality compared to increasing the rate of growth. I think that is a question for politicians to decide in the countries concerned, rather than the OECD.

Hon. John McCallum: Right. What if you focused the income tax cut on relatively low-income earners?

Mr. Christopher Heady: If you did that, you might well get the best of both worlds, yes.

Hon. John McCallum: Thank you.

Mr. Brooks.

Prof. Neil Brooks: I agree with Chris. It is a dilemma. Consumption taxes are important revenue-raising taxes and they tend to be quite efficient. On the other hand, the income taxes are more progressive, so there is a kind of conflict between these two objectives that I talked about. But it does seem to me it was a terrible mistake to reduce the GST in Canada, because it collects a substantial amount of revenue in a relatively efficient way, and if the government wanted to have tax cuts, it seems to me the place to cut taxes would be at the low end of the income scale, on the income tax.

Hon. John McCallum: Maybe I'll move on, because I'm running out of time. I have one last question about corporate tax cuts.

The Chair: It will have to be brief.

Hon. John McCallum: Well, a quick answer.

Mr. Michael Conway: Our brief indicated we did not advocate a drop in the GST. That is clear.

Hon. John McCallum: Thank you.

On corporate income tax, I might point out to Mr. Conway that we advocated lower corporate tax before the government did it, so that's one of the areas in which we do agree. But I might also point out to Professor Brooks that we've also committed to a very aggressive so-called 30-50 plan that will reduce poverty by 30% over five years and child poverty by 50% over five years.

I'll start with Mr. Heady. I've never been a supply sider or a Laffer curve type who thinks tax cuts pay for themselves, but on the corporate tax side, they might to some extent when you take account of location, not only of activity but of reported income. So my question to you is this: does the OECD have an answer on the question as to what extent corporate tax cuts will generate additional revenue so as to be partially self-financing?

● (1615)

Mr. Christopher Heady: We think that lower corporate taxes do increase investment and so would increase profits, and we also think that countries with lower corporate tax rates would be more attractive places for multinational groups to locate their profits. But we don't have any evidence to suggest that those changes would completely finance the tax cut. We would expect that a cut in the corporate tax rate would normally involve a reduction in revenue.

What has happened in a lot of OECD countries is that they have accompanied cuts in the rate by broadening the base, removing various sorts of special exceptions and perhaps reducing the generosity of depreciation allowances, and that's how they've managed to maintain revenues while cutting corporate rates.

Hon. John McCallum: Is there time for others to answer?

The Chair: Actually, there is not. The time is gone.

Monsieur Crête, you have seven minutes.

[*Translation*]

Mr. Paul Crête (Montmagny—L'Islet—Kamouraska—Rivière-du-Loup, BQ): Thank you, Mr. Chair.

My first question is for Mr. Heady.

I would like your opinion on something that does not appear in your charts: tax havens. We know that many countries have revenue collection issues. Some aspects of this are murky. For example, nobody knows how much tax revenue is being lost because of tax havens. These days, we are all wondering who the winners and losers really are.

Can you provide data, statistics or references for us to use?

[*English*]

Mr. Christopher Heady: I don't have any data. One of the problems with tax havens is that they're typically rather secretive and it's very difficult to get the data. There have been a number of estimates, but they vary widely as to the amount of tax that is avoided by the use of tax havens. But even that doesn't tell us who benefits and who loses from that. So while we do believe there are serious problems, I'm afraid I can't provide an answer to your question.

[*Translation*]

Mr. Paul Crête: All the same, states are desperately seeking tax sources. Mr. Heady, you said that you do not have any data on the subject. I believe an international group of seven countries is conducting analyses on these issues. I thought the OECD was participating in the discussion.

Right now in Canada, there is no way of knowing what portion of interest income—from businesses or individuals—comes from tax havens, because our tax returns do not distinguish between these two notions.

Messrs. Heady, Conway or Brooks, don't you find it a little risky to release a study on taxation without knowing the import of this phenomenon?

[*English*]

Mr. Michael Conway: We are calling for a reduction in corporate taxes. As Mr. Heady pointed out, we believe it stimulates direct foreign investment into the country, and it's good to stimulate the economy. We used the Ireland example, where they significantly reduced taxes and had very strong growth in the economy.

[*Translation*]

Mr. Paul Crête: Do you realize that the government can keep cutting taxes until other countries do the same thing?

However, if the government wants society to accept the taxation rate, then don't people need to feel that it's fair, that nobody is evading or avoiding taxation, two ideas that do not mean the same thing? Don't you think it's important for us to have the legal means to get this information ?

It can be very hard to make recommendations if the impact of those recommendations is not assessed. We're talking about billions and billions of dollars here.

● (1620)

[*English*]

Mr. Barry Gorman (Chair, Tax Committee, Financial Executives International Canada): I'd like to pick up on two points you made in that last presentation. You started off talking about tax havens. A tax haven, by definition, is a jurisdiction where taxes are lower than somewhere else. At the latter part of your presentation you equated tax haven with tax evasion. That is categorically incorrect.

[*Translation*]

Mr. Paul Crête: I said there were two ways—tax avoidance and tax evasion—which are two different phenomena. I did not say that tax havens were one or the other.

In terms of existing legal and official measures, isn't Canada missing out on very significant amounts of income, such as in Barbados, if it doesn't know the economic repercussions of that situation?

Mr. Michael Conway: From a corporate perspective, we want to stimulate investment in the country. The market is international, and it is competitive.

You are right in saying that many countries are cutting their rates, but if we do not cut ours in response, we will not be competitive, and there will be no investment in Canada.

Mr. Paul Crête: I understand that the U.S. model is quite different. Regardless of where on earth the interest income comes from, it is taxed the same way. I do not really know the details of this issue, and I was wondering if you have any additional information for us about this.

[*English*]

Mr. Barry Gorman: I don't have any additional information. However, if we're talking about tax havens generally—and by the way, a number of jurisdictions in Canada are classified as tax havens for international investors—the issue is not whether it's tax evasion, tax avoidance, or whatever. The issue is whether the corporation or individual is complying with the law of the land, as it's written today.

If the law of the land today says I can invest in some country, I would be prudent to do that. Therefore, to go back to your original question, if you're concerned about tax havens, by all means try to do a study on the impact of tax havens, but be careful of the terms you use for tax havens.

[*Translation*]

Mr. Paul Crête: The book on tax havens says that there are currently three reasons for multilateral action. It is important for countries to work together. A committee of seven countries is studying this issue.

I would just like you to tell me if you know the extent of this phenomenon. Do you know if Canada is currently losing a lot of income? Even the Canada Revenue Agency cannot provide those numbers.

[*English*]

Mr. Barry Gorman: Of course, the magnitude of the issue is something we can't discover.

[*Translation*]

Mr. Massimo Pacetti (Saint-Léonard—Saint-Michel, Lib.): Mr. Speaker, a point of order. I would like to know which book Mr. Crête is referring to.

Mr. Paul Crête: It is a book about tax havens by Christian Chavagneux and Ronen Palan. It explores the subject in detail and is part of a very well-known collection.

An hon. member: When was it published?

Mr. Paul Crête: The book was published in 2006 by Éditions La Découverte in Paris.

[*English*]

The Chair: Thank you very much. Our time has gone, but we'll have a very quick answer.

Prof. Neil Brooks: I'm not aware of any Canadian studies on how much income of Canadian multinational corporations is put in tax havens and lost through tax evasion or avoidance. But there are some American studies, and the numbers are absolutely huge. There isn't any reason to believe that the numbers wouldn't be comparable in Canada.

We should undertake a study. A number of years ago, in one of its reports, the Auditor General suggested there were billions of dollars of Canadian tax revenue lost through the manipulation of transfer pricing by Canadian corporations. So Canada ought to look at the rules in its international tax system that permit that.

Canada should also be supporting the OECD and other international organizations that are trying to prevent harmful tax competition, reduce bank secrecy laws in tax haven countries, and increase the use of exchange of information from countries we've traditionally regarded as tax havens.

So it's a crucially important area.

● (1625)

The Chair: Mr. Del Mastro.

Mr. Dean Del Mastro (Peterborough, CPC): Thank you, Mr. Chairman.

Mr. Heady, are there any examples of G7 or G8 countries that have higher corporate taxes, higher value-added taxes, higher personal income taxes—especially at upper-income levels—and higher productivity than Canada; where they have lower unemployment than Canada and are outpacing Canada in growth; where they have ongoing budget surpluses or decreasing national debt? Are there any examples of those countries right now, other than Canada?

Mr. Christopher Heady: I'm not completely sure about the unemployment rates in all of the OECD countries. Certainly there are countries with considerably higher taxes than Canada that have good economic performance and good productivity growth. Sweden is one example that has a tax-to-GDP ratio of about 50%—very much higher than Canada's. Finland is another country with good economic performance and high rates of tax.

As Professor Brooks said earlier, looking across countries it's very difficult to see any consistent relationship between tax and economic performance, because there are so many other things that influence economic performance.

Mr. Dean Del Mastro: I would personally argue—and I'm sure I could make a pretty strong tax case—that it's likely not in a country's interest to have very high taxes across the board, and consider that you could maintain growth, high employment, and so forth, and have no penalty on the broader economy.

I noticed in your presentation that some countries significantly increased their value-added taxes, comparing 2005 to 2007. One of them was Italy. When Norway and Sweden increased their value-added taxes, did that result in higher personal savings? Did it result in higher employment or anything like that?

Mr. Christopher Heady: First of all, I have to say that chart is not showing the VAT rate in two different years. It's showing the VAT revenue in 2005 and the VAT rate in 2007. It doesn't show, for example, that Italy has increased the VAT rate.

Mr. Dean Del Mastro: I see. So there are no examples of countries that have actually increased their value-added taxes over those two years?

Mr. Christopher Heady: A lot of countries have increased their VAT rates. The most recent example that comes to mind is Germany, which increased its VAT rate by three percentage points.

Mr. Dean Del Mastro: What did that do for its economic growth, or employment, or personal savings?

Mr. Christopher Heady: I don't know about its personal savings. I think its economic growth has improved, but I'm not sure it's necessarily due to the increase in VAT; there were other changes.

● (1630)

Mr. Dean Del Mastro: I'm sorry. I don't have a lot of time.

If there are zero savings in the economy, or you're approaching zero savings.... Is there any difference between reducing a personal income tax or reducing a VAT if people are spending virtually everything they're earning? Isn't is true that virtually everything becomes a consumption tax?

Mr. Christopher Heady: There is a difference, which is that the personal income tax is more progressive than the consumption tax.

Mr. Dean Del Mastro: I wouldn't argue that with you. But very broadly speaking, if you have zero savings it doesn't matter what form the taxes are; everything is being consumed anyway. Is that not correct?

Mr. Christopher Heady: That is correct.

Mr. Dean Del Mastro: Thank you.

Mr. Conway, I want to get to you on a couple of points you made.

First of all, this is in the spirit of non-partisanship. You mentioned that the federal government should maintain projected debt reduction in a schedule whereby the majority of annual surplus is directed at federal debt. The government has paid off $37 billion in debt in just over two years. Would it have been a good idea at the end of the year to create an additional $7 billion fund toward unspecified infrastructure programs? In your opinion, would that have been a good idea, or were we better to pay down debt, as the government did?

The Chair: Mr. Conway, go ahead.

Mr. Michael Conway: One-third of the program spending relates to old age security and health care, something we know is going to increase as the population ages. That should provide us with the incentive to find the money through various means, and one of the ways we were suggesting was to pay down the debt in order to reduce the interest so we have the money to meet the obligations that the elderly and the sick have.

Mr. Dean Del Mastro: Thank you.

Mr. Gorman, I appreciate that you mentioned the difference between tax evasion and tax avoidance. We'd love to help investment in Canada avoid what we see as a very regressive tax, the retail sales tax, by moving toward a harmonized GST across the country. Your report talks about it being the single most important action that these provinces can take to improve their overall provincial, and Canada's, tax competitiveness.

Could you elaborate on that a bit? Do you see examples of where that is in fact the case?

Mr. Barry Gorman: In my personal experience, at least in Nova Scotia, the major benefit of harmonization has been the elimination of red tape, the number of auditors, the number of sales tax returns, etc., virtually all of which gets translated back into the business, especially small businesses. Unfortunately, you really can't isolate the impact of a measure like that and say it created something or other. But as a general statement, I am quite convinced that there is no business person in Atlantic Canada who would go back to the old system.

Mr. Dean Del Mastro: Would it help foster better east-west trade, in your opinion, more domestic trade east-west?

The Chair: Mr. Del Mastro, no, that's it. I'm sorry.

Don't worry about answering that.

Mr. Turner, the floor is yours.

Hon. Garth Turner (Halton, Lib.): Thank you.

Mr. Conway, do you agree, yes or no, that spending money on infrastructure is a good idea?

Mr. Michael Conway: We have indicated it is appropriate to control spending, but that spending on infrastructure is the way to go. If we are going to look at what we're spending our money on, infrastructure spending is a good direction.

Hon. Garth Turner: All right, good enough.

Mr. Brooks, it's good to see you again. I haven't talked to you for a long time.

Mr. Brooks, when the Minister of Finance was introducing his most recent budget he said his tax-free savings plan was basically the jewel in the crown of this particular budget. You've just told us that this thing is going to cost billions, in your own words.

I think the minister only allocated $50 million in there as revenue that would be lost because of the tax-free savings plan. Can you tell us briefly why this thing is such a bad idea and will be so costly?

● (1635)

Prof. Neil Brooks: Well, Chair, I'm just using the government's own number. It doesn't cost anything in the first couple of years, or it costs very little, because you don't get an upfront deduction. In effect, you get to put your after-tax savings in and then any income from capital that you earn is tax free forever.

So when it's going to get costly is 20 years from now, or 10 years from now, and I think the government itself has estimated the cost 20 years from now is somewhere close to $3 billion.

Hon. Garth Turner: All right. Let me ask you this, based on your other comments. It seems to a lot of tax-planning professionals that the tax-free savings account will be of the greatest benefit to the higher-income earners—who've maxed out their RRSPs or have sizeable pension income—who will be able, for example, to be now sheltering $5,000 a year from, say, capital gains tax. Does that worry you?

Prof. Neil Brooks: It worries me greatly. Here are two fundamental things that are wrong with the plan. It stands tax equity, as we understand it in our income tax system, on its head, because the difference between these prepaid tax savings plans and registered retirement savings plans is that in these prepaid tax savings plans the income from capital is never taxed, which means that if I invest in one of these tax prepaid plans, and I get lucky, and over the course of 10 years make $2 million on my investments, that whole $2 million is free from tax. And as you probably read in the newspapers just a few days ago, there are Canadians who apparently have a quarter of a billion dollars in RRSPs, so we're not talking peanuts here.

If I put money into one of these plans and I make a million dollars, it's never taxed. On the other hand, if I put my money into savings in one of these plans and I lose money, it's never taxed. So here we have a person who's made a million dollars and a person who's lost money—both are taxed the same, namely, zero. That is inequitable.

Hon. Garth Turner: Yes, okay, thank you. Bad idea.

Now, Mr. Heady, it's a good idea for retirement, not a good idea for tax avoidance.

Mr. Heady, Britain has had a tax-free savings plan variety for a while. How does it differ from the one that has been proposed in Canada? I don't know if you're familiar with ours, but this is going to be a savings plan you can use. It's not related to retirement. It's not specific for any kind of goal. It just allows people to put aside money and not pay tax on it. How does that differ from the one that's in place in Britain?

Mr. Christopher Heady: Well, I'm not familiar with the Canadian scheme. The current scheme in the U.K. is tax free, yes. You put in money you've paid tax on and you don't pay any tax on the return, but there is quite a low limit on the amount you can put in.

Hon. Garth Turner: Is it open-ended or is it intended for retirement purposes?

Mr. Christopher Heady: No, it's open-ended. You can withdraw the money at any time.

Hon. Garth Turner: What's been the experience of revenue loss to the government?

Mr. Christopher Heady: I'm afraid I don't have the figures on the revenue loss to the government.

Hon. Garth Turner: All right, so we don't know the cost.

The Chair: Thank you very much.

Mr. Laforest, the floor is yours. You have five minutes.

[*Translation*]

Mr. Jean-Yves Laforest (Saint-Maurice—Champlain, BQ): My question is for Mr. Heady.

You submitted several charts and statistics that establish links between tax revenues, consumption taxes and income taxes. You talked about progressive taxation and you compared various countries.

Given the study undertaken by the Standing Committee on Finance, we should ask ourselves whether our taxation practices are the best way to make Canada competitive and to enable all citizens to live adequately.

Do you know if there is data showing which countries have the fewest citizens living below the poverty line? In other words, regardless of where those countries appear on the charts, are there countries where the incidence of poverty is low, but that nevertheless have satisfactory economic growth and good social measures?

● (1640)

[*English*]

The Chair: Mr. Heady, go ahead.

Mr. Christopher Heady: I think it's not possible to simply look at the tax ratios and talk only about, for example, the level of income or the instance of poverty, because there are so many other things that affect that. But what you can do is compare the progress different countries are making and try to relate that to the taxes that there are. When we study this, what we find is that countries that raise a lot of their money from corporate taxes do not do as well in terms of growth as do countries that raise more of their taxes from consumption taxes.

If you're looking to change the tax system in a way that would increase the rate of growth in Canada, the logic of that experience is that you should reduce corporate tax rates and replace the revenue with consumption taxes.

[*Translation*]

Mr. Jean-Yves Laforest: That's interesting, but I would like to go back to my question. Which countries have the most people living below the poverty line? Does the OECD have those statistics?

[*English*]

Mr. Christopher Heady: We do have statistics. I can't tell you exactly which countries were the very lowest, but I know they would include countries such as Denmark, Sweden, Finland, and probably Norway. These are countries with tax-to-GDP ratios that are considerably higher than Canada's.

[*Translation*]

Mr. Jean-Yves Laforest: That pretty well answers my question. It is fair to say that in countries with low levels of poverty, the tax system very likely reduces poverty. Those countries tax companies, individuals and consumption according to a model that reduces poverty.

I would also guess that countries with less poverty have good economic growth. That is very interesting. Thank you very much, Mr. Heady.

I have a question for Mr. Conway.

[*English*]

The Chair: Your time has gone, so you'll have to save it till the next round.

We'll now move on to Mr. Wallace. You have five minutes.

Mr. Mike Wallace (Burlington, CPC): Thank you, Mr. Chairman.

Thank you to our guests for being here today.

I'm going to start with the FEI for a moment. You represent financial executives from a corporate perspective, I'm assuming. Is that right? It's corporate issues.

Mr. Michael Conway: Yes.

Mr. Mike Wallace: If you look at one of your things under federal spending—I agree with the majority of what you say—you've got research and development in there as one of the items where you think we could be reallocating funds. Then I look at Mr. Heady's chart, and it shows Canada from the large firms, who are sort of middle of the pack, maybe a little ahead of the pack, and from the small and medium-sized firms, who are quite invested in tax incentives for R and D.

My question is this. Where would you like to see us? What more could we be doing? Are we not doing a pretty good job in that area already? What am I missing here, based on what I'm seeing, on a comparative basis—because we're talking about being competitive—from Mr. Heady's chart compared to what you're asking for in your report?

● (1645)

Mr. Michael Conway: In our brief, we urged the government to implement mechanisms that support Canadian economic value creators. Canada needs the champions that some of the SR and ED credits, the R and D credits, which is a good system, are promoting. We look at Research in Motion as a prime example of a Canadian corporation that came from nowhere, *x* number of years ago, and has become a global leader today. We need more RIMs in this country. So spending on infrastructure directed.... One of our points was that we need to control the spending, as we said, for the various reasons we discussed, but we said that when we're looking at spending we have to direct it, and the direction is towards infrastructure. And within the infrastructure we've talked about R and D because it promotes the Canadian economic value creators and the training.

Mr. Mike Wallace: Okay. I haven't had a chance to read your report, of course, so it's a general statement that this is an area that could use more funding. You're not saying exactly what percentage or an increase of any certain amount.

Mr. Michael Conway: We're saying, as we're looking at where we're spending money, spending on infrastructure that makes Canada more competitive is a good thing. Then when we start thinking about infrastructure, we think about R and D, we think about training, which is one of the reasons we've put forward the investment tax credit concept, to promote Canadian businesses, to do more training of our labour force.

Mr. Mike Wallace: You're segueing into my next question.

On the human resource training and development piece, you talked about broadening the definition of what's currently deductible, introducing a tax credit for qualified education. Can you give me some concrete examples of what is not included and what you'd like to see included? General things aren't helping much.

Mr. Michael Conway: I don't want to get too much into details, but there's actually an interpretation bulletin that specifies that certain types of training are deductible in the current year, and other types, interestingly enough, that are longer term are considered to be of a capital nature, and they need to be capitalized and the deduction spread over years. For us, that's counterintuitive. If you're promoting training and you're increasing the value of your workers, that should be something we promote, not defer over a long period of time.

Mr. Mike Wallace: Right. So if I give you my card, you'll be able to send me that note?

Mr. Michael Conway: Absolutely.

Mr. Mike Wallace: Okay.

To stimulate world-class champions of continuing education, is that a new program you want us to establish in this continuing workplace? Education and training, is that a program?

Mr. Barry Gorman: At the moment, we do not believe there is any such facility in Canada, at least as far as we've been able to discover. One of the real problems that corporations have is obviously finding in-house training, continuing education programs, things of that nature. We believe that if there were a university or a community college that would take on the task of literally being a clearing house for these kinds of programs and could get the Canadian business community to be made aware of its facility, it would be a tremendous service to the business community.

Mr. Mike Wallace: I have one more question for you, and hopefully I'll have some more time after that.

We've heard from other economists since we've been doing this study about the EI system that maybe we should have an experience rating system, in terms of the cost to businesses. Those who don't lay off too often and don't experience a lot of unemployment in their industry would have a different rating, in terms of their costs for EI, from those industries that do. Does your organization have any comment or any position on that?

Mr. Barry Gorman: We have never specifically taken a look at any EI issues of that nature.

Mr. Mike Wallace: That's it? Oh my gosh.

Thank you very much.

The Chair: Thank you very much. You're a little bit over already.

Mr. McKay, five minutes.

Hon. John McKay (Scarborough—Guildwood, Lib.): Thank you, Mr. Chair.

Thank you, witnesses.

It's pretty obvious to pretty well everyone outside this government that at some point or another carbon is going to have to be priced in some manner or another.

I'm looking at your chart, Mr. Heady, on page 19, where you talk about environmentally related taxes. If you flip that chart, you could pretty well chart Kyoto compliance, with Denmark and Norway and various other countries at the top end being fairly close to, if not Kyoto compliant, and the ones at the bottom end, being the U.S., Mexico, and us, not entirely Kyoto compliant. Probably the exception might be Japan.

Is that a fair observation?

● (1650)

Mr. Christopher Heady: I've never thought of it in that way. But certainly I think that environmentally related taxes, particularly ones that are closely related to carbon, are a very good way of trying to become compliant with the Kyoto Protocol.

Hon. John McKay: Is it your view that carbon-related taxes or environmentally related taxes change behaviour?

Mr. Christopher Heady: Yes, we do have evidence that they change behaviour.

Hon. John McKay: Professor Brooks, a little earlier you were a little bit concerned about, if you will, the third pillar of tax policy, namely the influencing and the changing of behaviour. Would you be of the view that excise tax or consumption tax, as it relates to an environmental issue, is a good thing, or is that not a good thing?

Prof. Neil Brooks: Not surprisingly, I like excise tax. I like all taxes.

Hon. John McKay: You might be in a minority on that point.

Prof. Neil Brooks: Sure. I love paying my taxes. I think they buy us the kind of society I like to live in.

I think taxes are useful in terms of getting prices right. If some activity is generating negative externalities, a market economy will only function efficiently if prices reflect the full cost and full benefit of the activity. Therefore, if we've got carbon and we know there's this enormous social cost, the market can't perform properly. So we've got to get that price right, and the way we do it is by imposing a tax on carbon to try to get the price right.

I'm not opposed to those.

Hon. John McKay: We have been living in a bit of a la-la land in terms of both water and air. We've never priced those as goods. So the product of the environmental degradation has never been priced into the ultimate product to the consumer.

I want to get both comments here, both on the business side and from your side. Is it your view that Canada is ready to deal with the issue of the pricing of environmental carbon, and the question really is, by what means?

I'd ask that of both Mr. Conway and Professor Brooks.

Prof. Neil Brooks: I think pricing carbon and activities that in effect cause social externalities is important. We've got to get the prices right, and therefore I'm not opposed to pricing any product that in effect generates negative externalities by imposing a tax on it. That's what excise taxes are all about. They're really not taxes; they're the government attempting to get the price of those products correct so the market can perform its allocated efficiency function.

You know the politics of it as well as I do, so I won't go into that. I just don't think there's a case for not doing it. I've never heard the case for not doing it, frankly.

Mr. Michael Conway: One of the themes running through our entire submission was simplification, which is why we called for the harmonized sales tax, the group tax reporting, and a review of the tax system. The tax act is huge now, and it's got to be looked at.

In terms of environment, I think a study should be undertaken in the same theme for harmonizing across the country. If everyone comes up with their own system, it's going to be like what we have with the GST right now and the non-harmonized provinces. Consequently, since the environment issue is in front of us, I would urge the government to consider a study bringing in a harmonized system, with all the provinces and the federal government looking at that, and carry it through to all the other themes, HST, and move toward a much more harmonized—

● (1655)

Hon. John McKay: B.C. goes one way, Alberta goes another, and there's no federal leadership on top. We agree.

The Chair: I think the point has been made and the time has gone, so we'll now move to Mr. Dykstra for five minutes.

Mr. Rick Dykstra (St. Catharines, CPC): Mr. Chair, I'm going to use 10 or 20 seconds of my time to point out that, with all due respect to all four of you gentlemen, the motion that Mr. Pacetti and I put on the floor was about tax policy and how we should tax versus how we should spend.

One of the reasons we've gotten into this is that we're trying as best we can...and I know this is Parliament Hill, and partisanship gets involved in it, but you can see how, once we start to talk about spending, we move directly into the partisanship of who can spend the taxpayers' money better.

Maybe this is just a general comment, Mr. Chair, that if we're going to expand the motion, we should do so formally, to say that we're also going to ask our tax policy experts to give us advice on how we should spend taxpayers' money. It makes it extremely difficult to work through this otherwise, and I think it's very difficult for our researchers and analysts to be able to give us a good indication of what is some top-notch advice that we're getting from you gentlemen.

That's not to say we aren't getting good advice from you; it's just that it gets itself mired in the muck.

Mr. Brooks, you did comment about the difficulty around current tax policy—whether it be from the last ten years, the last five years, or the last two years—with respect to finding a way to assist those at the lower end of the pay scale.

A question for all four of you concerns a couple of things we did and whether this is something we should continue. We've heightened the threshold for those who are in the lower income scale in terms of how much they have to pay in federal tax. For example, in 2006 about 625,000 people came off the federal tax rolls, and in 2008 an additional 300,000 came off the tax rolls.

This leads into the whole part of your comments about a consumption tax. We have to pay some political concern to the lowest-income folks, and not just tax policy concerns, so I want to get that perspective from all of you. Once we reach a point where we have the lower income scale of our wage-earners not paying federal tax, how do you propose we provide a way to benefit those individuals and families?

I know your opinion on what we have proposed, but I'm asking you, is there then a better way that you would propose, other than lowering the consumption tax, or maintaining a GST credit, or offering some form of credit to these folks? They aren't paying federal income tax anymore, which is a positive thing, while at the same time they're at the lowest income threshold in the country.

The Chair: That was a two-and-a-half-minute question, so we'll have two and a half minutes to answer. Carry on.

Mr. Brooks, you can start.

Prof. Neil Brooks: The only way to reach low-income people is through transfer programs. For example, it would have been much better policy not to reduce the GST but in fact use that revenue to increase the working income supplement, which I think is a very good program and can be substantially increased. In the United States, the comparable program is $4,000 a year, the earned income tax credit. I think the money could well have been used to do that in order to create some employment, and so on. I think it could have been used to increase the child tax benefit. That clearly benefits low-income people. I think it could have been used to provide more early childhood education for children, which clearly benefits low-income people.

I just think there would lots of ways. If what you're concerned about is low-income people, I don't think the GST credit did anything for them.

Mr. Rick Dykstra: I am concerned about them. Yes, it is in fact only part of it—

Prof. Neil Brooks: Food is exempt. Most of the necessities are exempt. That can't be the justification.

I'm sorry, I didn't mean to be partisan.

The Chair: Mr. Conway.

Mr. Michael Conway: It's interesting that Mr. Dykstra brought up the issue of the affordability of consumption taxes to lower-income earners.

Just as you indicated that possibly we shouldn't confuse one objective with another, we have proposed that the GST should not be reduced further. If there is a feeling that an incentive has to be given to lower-income earners, I wouldn't do it through consumption tax. You always have the ability to provide relief on the GST to the individuals earning less than a certain threshold through a credit mechanism. But I wouldn't do an across-the-board reduction of the GST just to benefit that selected constituency. There are other means. The consumption tax is a broad measure that applies across all of the constituencies.

If you want to target benefits to the low-income earners, there are other ways.

● (1700)

The Chair: Thank you very much.

Mr. Pacetti, you have five minutes.

Mr. Massimo Pacetti: Thank you to the witnesses for appearing. It's been very interesting.

I'm going to try to ask one question to the three of you and maybe frame it a little bit differently.

The government needs *x* amount of money to run the government and provide its services, and I think Mr. Brooks stated the two or three different criteria that it usually follows. If we were to look at just how the government raises revenues, there's always the other side of the equation, which is running programs.

Now, if I look at your brief, Mr. Conway, I'd say you want to simplify the system—and I don't mean to pick on your brief necessarily—but then in turn you say we need money for training, and we need to put money into commercialization and things like that.

What should we do, in your opinion? Should we be throwing all the tax revenue into a pot and then, as the government determines what its priorities are, invest in that fashion; or should there be dedicated funds, whether they be for CPP, QPP, unemployment programs, or any new initiatives? If we were to take, for example, training or commercialization, should there be separate revenue collected so that there is accountability to start one of these programs?

Mr. Michael Conway: We use the term “patchwork quilt of complex regulation”. The tax act has doubled, or tripled, or quadrupled in size since I took my CA. I'm glad I don't have to do it again.

Our first recommendation, which is actually the last recommendation in our study, is to move to a comprehensive review of the tax act to simplify it, because right now there have been so many initiatives one year after another—

Mr. Massimo Pacetti: I understand that part. I'm in total agreement.

Mr. Michael Conway: We have to bring it down to a base.

Mr. Massimo Pacetti: You say that in your first point, but then in the third point you say let's put money somewhere else. That complicates it even more, because this is just what you're asking for. Again, I don't mean to pick on you, but the next person will ask for something else, and the next person will probably ask for three or four additional things.

Mr. Michael Conway: I appreciate that. We did indicate we're trying to lessen the proliferation of imbalances across the system. We recognize there have to be some selective incentives in particular areas, but we're just pointing out that the tax act has become so thick, and year after year of budgets—

Mr. Massimo Pacetti: So do we use your criteria, or how simplify it? Where do we draw the line in the sand?

Mr. Michael Conway: I think it comes from doing a comprehensive review, and starting from almost ground zero, and then selectively identifying the areas that you want to incent.

If we take the CCA classes, for example, right now, embedded in the tax act there are something like 45 CCA classes. You can't find things anymore. We can start from scratch. Most OECD countries have around 10 classes. We can go down to 10 classes and just make it a lot simpler.

We use the example of high-priced consultants making lots of money, something that only the large corporations can afford in order to maximize their tax availabilities.

Mr. Massimo Pacetti: So the government should do the same thing and hire consultants, then.

We have limited time.

Mr. Brooks, maybe you can answer in the same vein. I may be picking on one particular aspect of your 10-minute presentation, but did you say that if the spending doesn't provide any services, if there is no purpose for the money, it shouldn't be provided?

Prof. Neil Brooks: Exactly. Go systematically through them, and if there's no legitimate government objective being served by these tax expenditures—as I say, there are over 150 of them in the act—they should just be taken out.

Mr. Massimo Pacetti: Again, on a non-partisan basis, if there is a legitimate purpose, should the government use its moneys from general revenue, or should it be a dedicated tax for that specific use?

● (1705)

Prof. Neil Brooks: No, I don't think it should be a dedicated tax. I think the government should design a tax system that is as equitable and as efficient as possible to collect the amount of revenue they need and then allocate that money to spending programs based upon their priorities. But I don't think you should try to link, in effect, the tax that's collected with something, because there's never a connection between them.

Mr. Massimo Pacetti: And the basket of collected revenue, should that be a combination of the consumption, corporate, and personal?

Prof. Neil Brooks: Exactly. And indeed, even on EI. I don't understand why we have EI premiums, because it's totally unrelated to the benefits. So you either go to a system where you experience rate, which some people are in favour of.... I'm not. What I would do is take those EI premiums and just turn them into a general payroll tax, because as these charts show, one area where Canada is below international standards is in social security contributions, essentially payroll taxes. I think what we should do is take those EI premiums, turn them into a federal payroll tax, collect the money through that payroll tax, and finance EI out of general revenues.

Mr. Massimo Pacetti: Mr. Heady, very quickly.

The Chair: I'll allow one for Mr. Heady.

Mr. Massimo Pacetti: In the same sort of vein but more toward the revenue side, on the corporate side, when is enough enough? When is it low enough, where it really won't impact whether you'll attract more additional foreign investment? I'm referring to corporate taxes. What's your experience?

The only country I could think of that is doing a good job is Ireland. Is there a point where the corporate taxes won't make a difference and a company will stay or make the investment whether the corporate taxes are at a certain rate or not?

Mr. Christopher Heady: I don't think you can say that there's any corporate tax rate where a further reduction wouldn't encourage additional investment. What I think is that there are some countries where changing the corporate tax rate doesn't make much difference, but those are countries with very weak tax administration and very poor general conditions for investment. But for a country like Canada, I couldn't see that there's some rate below which you shouldn't go.

Mr. Massimo Pacetti: The social security programs are what I'm looking at. Will a company or a corporation look at social security benefits, like Canada has?

The Chair: A quick answer, and then we'll move on. Go ahead, if you have an answer.

Mr. Christopher Heady: Sir, we know that when companies are investing they look at the social security contributions they have to pay. We don't know whether they look at the benefits. But I would assume that they do look at the benefits, yes.

The Chair: Thank you very much.

Mr. Menzies.

Mr. Ted Menzies (Macleod, CPC): Thank you, Mr. Chair.

Mr. Conway and Mr. Gorman, I know you've done a lot with assessing the provincial taxation systems, and we've also heard from you and many other prior witnesses about the need for harmonization. I think we all recognize that, especially our witnesses on asset-backed commercial paper last week also pushing for that.

Could you give us some assessment? We realize it's provincial jurisdiction and we can't interfere, but could you give us some assessment on how we might move forward with that, how we would encourage the provinces to listen to what you and others are saying?

Mr. Michael Conway: We'd be pleased, because we think HST is one of the things that would really move forward in terms of the simplification of the system.

One of the resistances you'll meet for the provinces taking it on is obviously a concern for loss of revenue. There are various ways to recover this perceived lost revenue. Number one, the increased efficiency that runs through the simplification theme of our brief will lower the cost of businesses. So those lower costs will result in either reporting higher profits, on which they'll pay taxes, or it will enable various companies to employ more workers, who will pay more income taxes. So it'll be back-filled by taxes from those two areas. It'll be not only less costly for the corporations to administer, but less costly for the provinces to administer, so they'll save money there.

Finally, though, we do underline that the federal government will probably have to provide incentive to the non-harmonized provinces to adopt HST, just as they did with Quebec and the Atlantic provinces when they went the harmonization route. But through the careful discussion of that, I think it's something that will benefit all.

● (1710)

Mr. Ted Menzies: We've heard from one particular association, a large group, the Canadian Restaurant and Foodservices Association, about the impact on them of a harmonized sales tax, and I can't help but agree that it is going to impact them. They're not the only ones, I'm sure, who see some problems with this. How do we deal with those situations? What type of tax do we put in place, or what type of tax do we remove, if that's the case, to allow them to compete with the homemade meals in the supermarket?

Mr. Barry Gorman: From a basic competitive position, if the tax in a particular jurisdiction on a particular good or service is all the same and the compliance costs of collecting that tax are quite reduced, competition should naturally take its own course. I'm not sure the federal government is looking to find specific industries that it would benefit; I think your objective is to benefit all industries equally. All industries in, say, Ontario or Saskatchewan would benefit equally from the simplification of the sales tax system.

Your problem is overcoming the perception that individual provinces will be worse off after harmonization. The only evidence available is, of course, the three eastern provinces, which harmonized eight or ten years ago. Looking at the revenue trend in those three provinces, they're certainly collecting more sales tax now than they were before harmonization. There are all kinds of variables over a period of six of seven years that would go into the consumption tax yield, but it's quite clear that those provinces are collecting more now than before, helped a lot by the federal government agreeing to a monetary stipend to shoulder the blow.

Mr. Ted Menzies: That's the sort of incentive that takes long-term planning, to make sure it does benefit the whole country.

The Chair: We'll now go to Monsieur Crête.

[*Translation*]

Mr. Paul Crête: My question is for Mr. Heady and the other witnesses here.

In Canada, we are unique in that our neighbours are the Americans. Even though it seemed impossible several years ago, the Canadian dollar is now almost at par with the U.S. dollar.

Based on your European experience or your expertise, do you think that a significant increase in the GST would prompt more people to go shopping in the United States? How can we curb that trend? It that even possible?

[*English*]

Mr. Christopher Heady: The experience in Europe is that there is a certain amount of cross-border shopping when there are countries that have very significantly different rates of tax. But it's usually a very limited phenomenon, because the difference in value-added tax rates between neighbouring countries in Europe is usually fairly small, and therefore you would need to be planning to purchase a great deal for it to finance any significant sort of trip. I think, in fact, the greatest incidence of cross-border shopping is not with respect to differences in value-added tax rates, but differences in excise duty rates.

On things such as alcohol and tobacco, there's considerable cross-border shopping between, for example, the United Kingdom and France that is driven by the differences in excise duty. The VAT difference would go the other way, but I don't think French people go to England because of the 2% difference in the VAT rate.

● (1715)

Mr. Michael Conway: Thank you.

I agree with Mr. Heady. A 2% variance in the consumption tax is not what's going to do it; it's the fact that the Canadian dollar has significantly surged from 67¢ up to par that has made the big difference. That really underlines the need for improved productivity in this country, which is one of the reasons we're calling to enhance skills training through the tax credit. If you want to get at the flight of people across the border to Buffalo and Plattsburg, it's not the 2%; it's the 30% differential in the currency, which now really makes it time to start focusing on productivity and competitiveness in Canada.

[*Translation*]

Mr. Paul Crête: The Canadian dollar is now at par with the American dollar. Please clarify your example; I may not have understood.

Where are we in terms of productivity with respect to the Americans? We have to keep in mind that most of our trade is with the U.S.

Mr. Michael Conway: Canadian corporations were less efficient before. That was not as obvious when the Canadian dollar was worth 67¢. Now that it's worth $1, things are much more expensive. Canadian companies are becoming far less competitive abroad. That's why it's very important to focus on Canadian competitiveness above all.

Mr. Paul Crête: I do not want to make value judgments, but I would like to understand why—what was the thinking when companies pocketed money during those years and did not put any aside to improve their productivity?

Mr. Michael Conway: That's a good question.

Mr. Paul Crête: Were they doing what the shareholders wanted or were they just going with the flow?

Mr. Michael Conway: That's a good question. There are many examples of companies taking drastic measures when they are in trouble, but those same companies don't tend to do anything when things are going well. When their products become less competitive internationally, they decide that it might be time to take measures similar to the ones suggested for employees.

[*English*]

The Chair: Your time is up.

Mr. McKay is next.

Hon. John McKay: Mr. Conway, in your presentation, you—as have many others—quote the Irish tax experience favourably, and certainly there's a lot to be said. It's quite a dramatic drop from 24% to 12%, and the growth in GDP and the foreign direct investment is pretty astronomical, particularly for a country of that size. Being of Irish descent, I'd like to think that's all because we're way smarter than everybody else. However, I have this sneaking suspicion that it may have as much to do with the subsidies from the EU as it has to do with smart tax policy.

So I'd be interested in comments from Mr. Conway, Professor Brooks, and Mr. Heady on the dramatic growth in the GDP of Ireland, and what's attributable to their tax policy and what's attributable to subsidies from the EU?

Mr. Michael Conway: Since I'm also of Irish descent, I like one of your suggestions.

Voices: Oh, oh!

Hon. John McKay: On that point, we're agreed.

Mr. Michael Conway: Other European countries receive subsidies as well, and the difference with Ireland is that they did the reduction of corporate taxes, and in our view, this drove a significantly higher growth than their counterparts.

● (1720)

Mr. Barry Gorman: I was just going to make a comment that a tremendous percentage of the EU subsidies to Ireland are in the agricultural field, so if you're talking corporate taxes and comparing them, or increased productivity, economic growth, and economic subsidies, or subsidies from the EU, I think you have to be careful that you don't take a broad brush and make the simple statement that there's one cause to some economic reaction. On the other hand, you don't mix everything into the pot, because as I said, economic activity in Ireland—and I'm sure Mr. Heady can support this—has clearly increased. Taxes have clearly gone down. But whether the economic increase is totally attributable to EU subsidies or tax rates, you could never say it's one or the other. It always has to be a combination.

The Chair: Professor Brooks.

Prof. Neil Brooks: I have two really quick comments.

One is that I don't think the tax had very much to do with it. A whole series of factors led to that growth of direct investment in Ireland. Among many others, they just got their timing right. It just happened to be at the time when these large high-tech U.S. firms were looking for a place to locate their firms in order to export in the EU. There was an English-speaking population, highly educated. Indeed, one of the cleverest things they did with those EU subsidies was to get rid of all tuitions for higher education. They had this very highly educated, low-wage workforce all ready for the big high-tech U.S. firms, so they located in Ireland in order to get into the EU. If it had happened at some other time, the effect would have been very different.

The second comment is that even if it did work, it only worked for one country. It's a beggar-thy-neighbour policy. What if every European country reduced their corporate taxes to 12%? What would be the effect? Zero. There's an enormous collective action problem with respect to corporate taxes. That's why the most you can advise a country is to keep its corporate taxes about in the middle of the pack and to try to negotiate with countries around the world not to try to beggar their neighbour in the way Ireland did. Why did Germany put up with it? In part they put up with it because Ireland was such a poor country at the time. There were just very unique circumstances that can never be duplicated.

The Chair: Mr. Heady.

Mr. Christopher Heady: I wouldn't think it was the EU subsidies; I would think it's partly the tax. The other big thing, as Professor Brooks said, was the fact that Ireland joined the European Union, and thus it was a location in which firms could establish themselves and have access to the whole of the EU market. That happened at very much the same time, so it's very difficult to disentangle the two.

The Chair: Thank you very much.

Mr. Del Mastro and, I believe, Mr. Wallace are going to share a quick segment, and then we'll call this meeting over.

Mr. Dean Del Mastro: Thank you, Mr. Chair.

Mr. Heady, very quickly, I wanted to go back to one of your graphs, which was entitled “Top statutory personal income tax rates”. These would be the taxes paid by the highest-income earners in the economy. I note, for example, that Canada is considerably higher than the United States. It is always—we talk a lot of politics here obviously—politically extremely unpopular to ever talk about reducing the top marginal tax rate, the top effective tax rate on high-income earners.

That being said, we do have 13,000 Canadian-trained medical doctors working in the United States. Most left at a time when our dollar was low and our taxes were high. There is a need to be somewhat competitive with jurisdictions, is there not? Is that not a broad-based theory that we should be trying to follow in Canada if we want to avoid brain drain?

Mr. Christopher Heady: I think it's difficult, because when people are deciding where they want to live, they're not only thinking about how much tax they get but also about what the cost of living is. One thing that can happen in countries where people pay somewhat more tax is that they also get somewhat more benefits. For example, European countries pay higher taxes, but they all have free medical care. They all have almost free higher education. So you have to look at both the taxes that are paid and also the state services that they receive in exchange.

● (1725)

Mr. Dean Del Mastro: Right. I don't disagree with you. We have those things in Canada as well. Obviously we have taxpayer-funded health care, and we have lower tuition fees on average. But we did lose an awful lot of our best minds to the United States at a period when we had a low dollar and a high tax rate. So it's a real danger.

Mr. Gorman, I wanted to give you a very quick second on east-west trade. I'm really concerned about the patchwork system of regulations and taxes we have in Canada. Would harmonized sales tax be of advantage to east-west domestic trade in Canada?

Mr. Barry Gorman: Harmonized sales tax definitely would, because you would eliminate the distortion that was referred to earlier in which one province has higher sales tax than another so that trade moves one way.

If every province had the exact same sales tax rate, if you could ever get to that point, you would have the most beautiful tax system in the world, because taxes would then be eliminated from the business person's decision, and that's the key issue.

Mr. Dean Del Mastro: Thank you. I appreciate that.

The Chair: Mr. Wallace, go ahead, please, very quickly.

Mr. Mike Wallace: Very quickly, Professor Brooks, I think there are four marginal rates and four income thresholds they apply. Based on your work and your opinion on how things should work, would you change any of that from a tax perspective, in terms of the number of personal marginal rates we have in the tax system and the thresholds at which they apply?

Prof. Neil Brooks: Well, we do apply, for example, our top threshold. Indeed, Chris would know this, but I think we're a little out of line with the OECD. I've heard people say that our tax threshold is quite low—and it is low compared with the Americans, but not low compared with the other industrialized countries.

Again, you can play with those rates, but I think there's a good case to be made that you should have a relatively high threshold, and then just have one rate that goes through most of those income ranges, and then a couple of rates at the top. I would certainly impose an additional rate on people earning over, say, $250,000—and that number is just arbitrary—and maybe have another rate for people earning over $1 million.

But I think there's something—

Mr. Mike Wallace: So you would add rates?

Prof. Neil Brooks: Yes, I would add a couple of rates at the very top end. Exactly.

Mr. Mike Wallace: Thank you.

Prof. Neil Brooks: There's lots of revenue to be made up there, and our rates—

Mr. Mike Wallace: You love revenues. You love taxes, don't you, sir? You love them.

Prof. Neil Brooks: I like the services they buy for us; we benefit enormously from them.

Mr. Mike Wallace: Okay, thank you.

The Chair: Thank you very much.

With that, we're going to call the best part of the meeting over.

I want to thank the witnesses for coming forward, particularly Mr. Heady. I understand that you're a little bit ahead of us, about six hours, so that would make it about 11:30 in Paris. You did such a great job at committee, why don't you just take the rest of the day off?

Some hon. members: Oh, oh!

The Chair: That would be really great.

We certainly appreciate your taking the time to be here.

Mr. Christopher Heady: You're very welcome.

The Chair: Thank you.

For the committee's information, we had a steering committee meeting prior to this. We will be starting on Bill C-50 on Wednesday, hearing from the minister again, and from another minister the following Monday. Mark Carney is going to be here on the April 30.

I don't want to presume anything, but Bill C-50 should take our attention for the foreseeable future on our calendar. So I'll just give you that information for now.

Thank you.

With that, the meeting is adjourned.