THE STANDING SENATE COMMITTEE ON NATIONAL FINANCE

EVIDENCE

SAINT JOHN, New Brunswick, Wednesday, November 22, 2017

The Standing Senate Committee on National Finance met this day at 1 p.m. to study the Minister of Finance's proposed changes to the Income Tax Act respecting the taxation of private corporations and the tax planning strategies involved.

Senator Percy Mockler (*Chair*) in the chair.

The Chair: Honourable senators, our committee is in Saint John to continue its special study on the proposed changes to the Income Tax Act. These changes were put forward by the Minister of Finance during the summer of 2017, and they pertain to the taxation of private corporation and tax planning strategies.

Our first panel of witnesses this afternoon is composed of Mr. Jeff Saunders, Tax Partner, Teed Saunders Doyle; Christopher Neal, Partner, Beers Neal LLP; and Andrew Costin, Corporate Lawyer and Partner, Gorman Nason. Thank you all for accepting our invitation.

I have been informed by the clerk that the first presenter will be Mr. Saunders, to be followed by Mr. Neal and Mr. Costin.

Mr. Saunders, the floor is yours.

Jeff Saunders, Tax Partner, Teed Saunders Doyle: Honourable senators, I would like to thank you for the opportunity to appear before this committee to discuss this important topic. Our firm, like many accounting firms across Canada, has spent hundreds of hours analyzing the proposals released by the Department of Finance on July 18, and the subsequent revisions announced the week of October 16. We feel that the modifications announced the week of October 16 are positive, and we applaud the Department for these improvements. However, we still feel that the proposals related to income splitting and passive income are overly complex and will have significant negative consequences for a large number of our small business clients. We also have serious concerns regarding the lack of details available for these proposals. Phrases such as "fair", "fairness" and "fair share" appear multiple times in the July 18 report. Unfortunately, these phrases are neither defined nor quantified in the report. I'd like to bring to your attention just a few scenarios where we feel the proposals do not result in outcomes that are fair.

Consider a small business owner who, based on the advice of her accountant, has been saving for the past 15 years to help provide for her daughter's education by accumulating some investments inside her corporation. Her plan has been to pay dividends, through a family trust, to her daughter to help with the cost of her education, and, under current tax rules, the daughter would pay very little tax on these dividends. Now that her daughter is almost ready to start university, the rules have been changed and the amount she has worked so hard to set aside has effectively been cut almost in half. This is because dividends flowing through a trust to her daughter will now be subject to a 46 percent tax rate. An instant tax increase of 46 percent on funds accumulated over 15 years of hard work does not seem fair.

Now, consider a small business owner who used the sale of his business as his retirement fund. He sold the assets of the business rather than selling the shares. This resulted in his retirement fund being held inside his corporation. He planned to draw the funds out of the corporation over time as dividends to himself and his wife. His wife would not meet CRA's definition of active in the business, but was very supportive during the lean years as a start-up, and she carried the majority of the workload at home raising their children. Now, in their retirement years, this couple is no longer able to split their income to reduce their tax bill, and it is too late for them to make alternate plans. Their neighbours, who have their retirement funds in RRSPs or company pension plans, are allowed to split up to 50 percent of their income. This does not seem fair.

Lastly, consider a small business owner that owns an apartment building. The operation is not big enough to have more than five full-time employees, so it does not qualify as an active business. Under these proposals, if he works hard and grows the business and earns more than $50,000.00, the excess income will be subject to a 73 percent tax rate. His larger competitors are subject to tax rates of 13 percent or 29 percent. This does not seem fair.

We believe there should be some sort of grandfathering or carve out of these rules to allow income splitting on funds that have already been accumulated. We also feel that spouses in general should be exempted from the income splitting proposals due to the nature of the spousal relationship and the impact running a small business has on a family. The type of contribution made by many spouses cannot be easily captured in a reasonableness test. We also believe that real estate businesses, which are currently considered to be passive, should be exempted from the $50,000 threshold.

One key additional problem with these proposals is the number of unknowns associated with them. We are close to the time these rules are to be implemented and our clients are asking us to help them to plan for these tax changes, and we still don't know the details of the changes or what the impacts will be. For example, will the $50,000 passive income threshold be indexed to inflation? Is the $50,000 threshold based on gross income, net income or taxable income? Does the $50,000 threshold create a barrier to growing from a small business to a medium or large business? How will the grandfathering of existing investments be done? And how will the government distinguish between some investments in passive assets by corporations and investments held by angel investors or venture capital inside corporations? We would like to be able to answer these questions for our clients but, with the information currently available, we simply cannot. All of these unknowns have put much of our tax planning for clients on hold. It has also put much of our clients investing in growth plans on hold. The uncertainty introduced in July by these proposals has left longstanding plans in limbo and made it almost impossible to do future planning. With all due respect to our Minister of Finance, hearing him on November 1 ask this Committee "to just suspend disbelief for a few months," does not engender confidence in the process. Small businesses need certainty in order to arrange their affairs.

We believe that these proposals should be shelved or, at the very least, delayed pending an economic impact assessment, royal commission or comprehensive tax reform. Thank you very much.

The Chair: Thank you, Mr. Saunders.

Mr. Neal, please make your presentation.

Christopher Neal, Partner, Beers Neal LLP: Honourable senators, thank you for undertaking this important study. I am a chartered public accountant, a chartered accountant. I'm a qualified expert in taxation at the Court of Queen's Bench, and I've been practising taxation for over two decades.

Small business owners, including professionals, bear signification monetary and professional risk. It is this risk-taking that drives the creation of small business which, in turn, drives business expansion, new technologies and employment, and, ultimately, turns small businesses into big ones. Modifications to the tax proposals were announced with very little in the way of detail, leaving small business owners and their families in very uncomfortable and stressful positions. The taxation proposals put forth as modified will result in serious negative consequences to small businesses. For example, our clients have already planned acquisitions and expansions that are now on hold, at least until the modifications are properly detailed. These plans may or may not come to fruition; it will depend upon those details. We have other clients that are considering selling their operations.

One local MP was quoted as saying that 97 percent of small businesses will now not be affected by the proposed changes to the passive investments being saved inside a corporation. We considered our clients. It appears the modified proposal on passive investments will affect roughly one third of our clients, either immediately or in the future. But, again, with scant and uncertain details, that number could be greater.

In terms of the proposal around income splitting, or income sprinkling, it is proposed that a reasonableness test will be applied that focuses on the level of effort and/or risk associated with that family member who is receiving income. I argue that spouses have the same, or nearly the same, overall risk as the business owner themselves. Lenders require security and personal guarantees. Regardless of whether that spouse directly provided a guarantee or a security, that spouse is at risk if this business fails. Moreover, I argue that in certain circumstances the entire family unit may be at risk. A family with dependents faces all the negative financial and social consequences if that business fails.

Concerning passive investments earned inside a corporation, under current legislation, that particular income inside a corporation is already taxed at in access of 52 percent, which is well above what would be considered a middle class tax rate, yet the government has proposed further taxation. Passive investment is used or often used by small businesses as a backstop for tough economic times, unexpected illnesses, maternity, lending security or buying out business partners. Again, amid the uncertainty, it appears these thresholds of $50,000 in passive investments income and total savings inside the corporation of $1 million will be nowhere near sufficient an amount such that small businesses are able to leverage their capital, thereby creating employment, all with the objective to grow their small business. It's effectively a tax on their capital. These thresholds should, but appear not, to take into account the size of the business. An entity employing 25 needs far more in the way of capital than one employing three.

The federal government has proposed a reduction in the small business tax rate of 1.5 percent. I submit that is nearly meaningless in the face of the passive investments proposal. This is because it is likely that the passive investment proposal will penalize businesses that do not invest a particular year's profit directly in the business, in the case where that business has already saved their $1-million. For example, a trucking company can add only so many trucks before those trucks are sitting around empty. Reducing the small business rate will not incent business investment in any way. The amount of dollars in question is simply not enough.

In closing, the process by which these proposals were introduced has exerted significant stress and pressure on our country's small businesses. That is unfair treatment. Would this government introduce such uncertainty for publicly traded companies? Would this government introduce such uncertainty for offshore arrangements? I suggest they would not. This government would be well-advised to cease this initiative, strike a commission, study the matter in full, and resolve to rewrite Canada's tax code such that it is fair for all. Thank you.

The Chair: Thank you, Mr. Neal.

Mr. Costin, please.

Andrew Costin, Corporate Lawyer, Gorman Nason: Good afternoon, Mr. Chair and fellow senators. I'd like to welcome each and every one of you to Saint John, and thanks for having me here today.

I'm a corporate commercial lawyer practising here in Saint John, New Brunswick, at the law firm of Gorman Nason. My primary area of practice is corporate and commercial law, and a significant part of that is commercial real estate. The bulk of what I do is I'm doing purchases, mergers, acquisitions, divestitures, and all of these things that I do in my practice involve the two gentleman, and their expertise that they have, right next to me, Mr. Neal and Mr. Saunders. And tax planning is such a significant part of what my clients are seeking whenever we are looking to purchase an apartment building, if they're looking to convert property, if they're looking to buy or sell business, if they're looking to create a family trust.

I have to say that this entire process from the federal government has created a cloud of uncertainty that has made it exceptionally difficult for my clients to make business decisions, and for me to advise my clients, and I know my friends here to advise their clients.

I come from a business family. I'm the third generation of a construction company based in Amherst, Nova Scotia. My dad is 65 years old, and his heart and soul is into a business that was started by my grandfather in 1947. His retirement is his business. So the stress that a 65 year old gets when our Minister of Finance comes out and essentially labels us all as tax cheats for being these Canadian-controlled private corporations. It has created significant uncertainty and stress amongst the business community.

I'm also involved as the President of Uptown Saint John, the local business improvement association, and I also, myself, practice to a professional corporation. So these potential changes affect my practice, affect my family, and my clients.

The main issue that I have here and that I want to communicate today is uncertainty. In my line of work, if I don't know exactly what the federal government is intending to do, if they're governing through sound bites, I can't do my job, I can't advise clients, and, more importantly, business despises and hates uncertainty. I can tell you that as a business person, I can tell you that as someone from a business family, and I can tell you that from speaking to my clients. And the damage, I would submit, has already been done in putting forward these purported amendments or these potential amendments.

I would want to hone in on this $50,000 allowance on the passive income side. I watched Pierre Poilievre ask our minister, for what I thought was the better part of half an hour, on whether that is $50,000 per corporation, per shareholder, are the related corporations, is there different treatment of trusts, is this tied to inflation? All of those things, and he had the same answer which was basically speaking to the points that the high-end, high-level points, sunny ways, that the government is looking to establish. And it is very stressful and frustrating, both from my own personal perspective where I'm looking to build up a nest egg in a professional corporation for my retirement, at 31, and for my clients who are constantly taking deferred earnings that are inside a corporation, to invest in private business.

If you all go walk up and down Canterbury Street, uptown Saint John has really seen quite a great renaissance, and I would take the position that a lot of that investment is triggered by investment from tax deferred earnings inside a small business corporation. That is passive income. You have an entrepreneur who has the sweat equity, and you have the angel investor who has money sitting in a corporation that they're willing to lend, and that is what Morneau extensively is referring to as "dead money", which I, personally and professionally, find to be offensive and untrue. I also make note of the fact that we have what's called tax integration in Canada, meaning that just because I don't draw the money out of my professional corporation, it's already getting taxed at a significantly high rate. The government's getting their fair share, I would say, already. And it seems asinine to suggest that this money is just being tucked away or hidden when the real issues, in my professional and personal opinion, are with these offshore treaties that I think should be looked at and opened and renegotiated.

I also want to point out, very briefly, to the point that CRA, there was an Auditor General's report that came out, I believe it was yesterday, and it was rather ironic to see the CRA get audited, but they said that CRA right now cannot handle the volume of questions and issues that are arising. So, now the federal government wants to add a further layer of uncertainty of auditing obligations on our Canada Revenue Agency, and I just think it's personally going to be an absolute nightmare.

I know there are going to be questions from the floor, but in closing, from where I'm sitting, the federal government has essentially attempted to overhaul what I believe to be 40 to 50 years' worth of respected tax and legal principles and vehicles over a 75-day period. Yet, as an aside, they had no problem taking some time on Energy East, years at a time. Seventy-five days, they were looking at overhauling our tax system as we know it without, quite frankly, doing their homework, from my personal opinion and my professional opinion. So the message I have is that the overhaul of our tax system cannot be reduced to misinformed tax bites and these sham consultations. Thank you.

The Chair: Thank you very much.

The first question will go to Senator Marshall, to be followed by Senator Eaton, Senator Pratte and Senator Neufeld.

Senator Marshall: Thank you for being here today. I think my questions are kind of technical. We usually ask general questions of the witnesses, but we've all got a tax background, so I figured I'd make the most of your testimony.

I did want to talk about passive income. I appreciate the comments that I got on the passive income when you did your opening remarks, because we touched briefly on this, this morning, with another witness who had indicated he had been on a conference call with officials from the Department of Finance. My question was whether they able to get a definition of passive income.

But before we get into that, you referenced the question to the minister about passive income and whether it was per company or per shareholder. That was at the House of Commons Finance Committee, and I saw that also. So you took one of my questions, that's okay, I've got another one here for you. So, the passive income, everybody talks about it and they talk about the $50,000 and whether it's adequate or not, but I went back into the Department of Finance website last weekend because I wanted to make sure that I understood exactly what was going to fall into passive income. And we've had other tax experts testify, and we had somebody in Calgary say that the way they're reading what's been released so far is that there's going to be five pots now for retained earnings, and passive income is going to be in there, there's going to be a grandfathering one and then one that's not grandfathered. So, I'd like to hear all of you address this, do you have a good understanding of what can be classified as passive income, or are you like me, I'm not quite sure anymore? I'm probably going to start with Mr. Saunders.

Mr. Saunders: Thank you. I guess, based on historically, we feel we have a pretty good understanding of what passive income has been in the past. Generally, it would be things, dividends, interest, rent, royalties, with certain conditions and exceptions, of course. But, under these proposals, we're somewhat assuming that definition will continue, but we don't know that for sure.

Senator Marshall: So where is that term, "passive income", defined? Is it in the Income Tax Act?

Mr. Saunders: I don't believe it is specifically defined in the Act, no. It has been more through case law and interpretations with CRA that, over the past 40 years, we've sort of come to an understanding of what that is.

Senator Marshall: So it's possible that when Budget 2018 comes out and puts through the details for these proposals, that there might be a new definition of passive income, is that possible?

Mr. Saunders: That's correct. One thing we've been somewhat nervous about or curious about is insurance policies held inside a corporation.

Senator Marshall: Yes.

Mr. Saunders: Some of those generate sort of an income component that has always been exempted from tax because it's considered an insurance product. We don't know if the definition of passive income could be broadened in the budget to suddenly catch that type of income. If it does, the estimates, similar to what Chris said, of maybe a third of our clients being affected, that number would easily double if insurance was to be, sort of, brought under the scope of passive income.

Senator Marshall: Mr. Neal, could you also talk about passive income so as to enlighten my understanding of what it is?

Mr. Neal: Yes, passive investment income has been defined over the years by application of the law and interpretation. I echo some of the things that Mr. Saunders said, the cash surrender value life insurance is not a taxable item, but I'm led to believe this passive investment is based on what is otherwise taxable. So, does that mean life insurance is excluded? If so, I might quit and simply go sell life insurance because that will be the best asset and the only asset a corporation would be able to have. Also, I don't know, and Mr. Saunders brought this up, if I sell my business assets inside of my corporation, so I don't sell my shares, I sell my business assets, I'm going to do so, hopefully, at a gain. Whether that's an eligible capital property gain or an actual capital gain, I'm going to sell it at a gain. Historically, a capital gain on anything is passive. So, does that mean the disposition of a business is now going to be considered a passive investment?

I also don't understand whether this $50,000 is $50,000 per shareholder? If I'm a partner in a company and there are three of us and I've got another company, is it split? If my spouse has a company and my spouse's company, does that get $50,000 and I get $50,000? We don't know. I also don't know if the $50,000 is a way to get to the $1 million, or if the $1 million is the way to get to the $50,000. Is the $1 million the max, or could I have $10 million, as long as I don't have more than $50,000 investment? Will there be a mechanism, if I go over the $50,000, to pull it out? If there is a mechanism to pull out passive income above $50,000, therefore, my investments can just continue to grow inside the corporation, but I can take that money out, I'm not sure what this thing does. Because I'm going to take the money out and pay $52,000-plus, but I'm paying $52,000-plus inside the corporation already.

Senator Marshall: Right. But our understanding is that if you take it out, you pay the $52,000 inside the corporation. You take it out, and then that's where you come up with the $73,000 because you're refundable, you no longer get your refundable tax back.

Mr. Neal: That's why I'm wondering if is there a mechanism. So if I have a company and I make $75,000 after these rules, is there a mechanism that says, "Okay, we won't penalize you on the $25,000, you have to take that out personally and pay your full shot tax"? Is that the mechanism? If so, I don't know what this achieves because I can continue to let my investments grow. If it is such that, no, it's a penalty, you cannot take it out, how do you manage your investments with that type of precision? It's impossible.

Senator Marshall: And this goes back to the pots, doesn't it?

Mr. Neal: The pots, yes it does. You know, lining my pockets with these proposals should not be the result, and that's what's going to happen. The complexities are going to be enormous for a small business that doesn't understand the rules in the first place, now they have to deal with different pots of income and transferring income around between pots and out of pots. If I sit down with one of my car dealers and talk about this, he's going to think I'm crazy, first of all. Second of all, the fees are going to be enormous. The complexity is gone to an entirely different level.

Senator Marshall: Mr. Costin, have you got anything to add about the passive income? I'm getting more comfortable with it.

Mr. Costin: I'd be the stereotypical lawyer and just answer no until I had something in front of me, because we don't know what they're going to be doing. But the concern, the one thing that was raised with me, and I kind of go back to the CRA comment I had, someone said, "Well, what if you just go borrow like half a million dollars through your professional corporation, then invest it right before whenever these proposals take place, how is that going to be treated?". So, I mean, the concept of passive income and how they're going to look at this, and how that $50,000 is going to get dealt with, I mean, I obviously echo my friends who deal with that issue more than I do. They're correct in that it's defined by case law but, again, I don't even know if CRA is clear right now on how they're going to be handling this. Until the government comes out with something more substantive and concrete, it's anyone's guess, that's from my end of it.

Senator Marshall: Yesterday, we had a lawyer testify before us who does quite a few incorporations, and that's your field.

Mr. Costin: Yes, I do incorporations, shareholders' agreements.

Senator Marshall: She was telling us that, since July, since these proposals came out, she said that her work has kind of, you know, dried up somewhat because she's noticing a decrease in her line of work. Are you noticing the same thing?

Mr. Costin: To be honest, it all depends on any existing deals that I have. What I would say is the person that is looking to buy a multi-unit that has some money in a corporation set aside, is press play. For larger scale items, I don't think that has necessarily made changes, to be honest. But my re-orgs, I can tell you right now, and I would say across the board, it's safe to say that any tax-driven reorganization is, for the most part, on hold. I mean, I have family trusts lined up that didn't go.

Senator Marshall: People are uncertain.

Mr. Costin: All of my re-orgs right now are equity-driven, certainly not tax-driven. So, it would be safe to say, but my one particular practice is not —

Senator Marshall: Not impacted.

Mr. Costin: But I would say, across the board, this is absolutely poured some cold water on anyone looking for the family trusts, for estate freezes, all that stuff. I mean, I think people are waiting until the federal government gets its House in order, quite frankly.

Senator Marshall: Mr. Chair, do I have time to ask Mr. Saunders one technical question on an example?

The Chair: Yes.

Senator Marshall: Mr. Saunders, this is the one about the apartment building. You were saying if he works hard and grows the business and earns more than $50,000, the excess income will be subject to a 73 percent tax rate. If it's less than $50,000 and he leaves it in a company, when it comes out, isn't it still at 73 percent? The refundable tax, is that gone now? Do you know?

Mr. Saunders: We don't know for sure. We believe that, from what we've read from Finance, that the under $50,000 will still be subject to the current rules, so the refundable would be there.

Senator Marshall: Okay, and the refundable tax will come back but, above that, it won't?

Mr. Saunders: That's our understanding, but I couldn't say that for certain.

Senator Marshall: All right, that's great. Thank you.

The Chair: Senator Eaton, please, to be followed by Senator Pratte.

Senator Eaton: ...and put aside $50,000 every year, $45,000, $35,000, and it goes up to $1 million, then I'm taxed at the 52 percent when I withdraw it, right? But if I go over $1 million, say I've got that apartment building for 30 years and I start accumulating over $1 million of passive income, then I start getting taxed at 72 percent or 74 percent?

Mr. Saunders: Actually, Senator, I would say that the apartment building itself, unless you have more than five full-time employees, the income on the rental is passive income. So, you don't get the $40,000, $50,000 a year to get to $1 million, you could already be at $1 million or $2 million by owning the apartment building.

Senator Eaton: That's right. But say I owned the apartment building. I'm not selling it, it remains an asset but I accumulate more than $1 million, then I start getting charged 74 percent?

Mr. Saunders: I believe so, yes, under the proposal — now that 73 is taking into account, sort of, the corporate and the personal level of tax.

Senator Eaton: I'm not like my former Auditor General of Newfoundland here; I'm a bit more simplistic. We've heard from a great number of doctors. So you pay off your medical debt and set up your practice. You pay for that and you start saving for your old age at, say, 50, 45. What kind of pension would you get if you accumulated $1 million?

Mr. Saunders: I haven't run those numbers but I have read some reports from others, it would not be a huge pension. I don't have specific numbers for that.

Senator Eaton: So what we're saying to most people who work very hard — small business owners, doctors, professionals — your pension is really capped at $1 million, because after that you're going to be charged 74 percent tax rate?

Mr. Saunders: Essentially, yes.

Senator Eaton: Thank you.

Senator Pratte: I'm trying to get a hold, on passive income, of how many or what proportion of CCPCs would be affected by this. And you're familiar with the numbers that have been put out by the Department of Finance that only a small number of CCPCs actually hold passive investment, and actually a very small proportion actually receive a significant amount of passive investment income. But I hear you say, and I think, Mr. Neal, you mentioned that discussing with your clients, your impression is something like one third of your clients would be affected, even with the $50,000 threshold. I'm just wondering, is it because the Department of Finance, is it because their numbers are defective in some way? Or is it because there's a misunderstanding of what passive income is? Help me out here. Whose numbers are wrong?

Mr. Neal: I'd like to think the accountants' numbers are right. I don't know where Finance is getting their numbers. I can tell you where I'm getting mine: from private tax returns, private financial statements.

We have 36 people that work at our firm, three offices, so we're not a small enterprise for this part of the world. So, our cross-section of clients is quite large. We have some very successful clients who are large, and we have smaller ones who are just starting. I'm seeing the actual financial statements and the tax returns which produce those figures. So, unless there was an analysis done of people's tax filings, CCPCs, and, keep in mind, there can be multiple companies, one person can have multiple companies with passive investments throughout, I don't know how they get the numbers. So, what we did is we sat down, the partners at my firm, with our senior team, and we had the list of clients and we went down and we said, "Who is going to be affected now or in the future?", and we highlighted them. And it was in excess of a third.

Senator Pratte: That means that those businesses would have capital invested or would soon have, or eventually have, according to your estimations, capital invested of $1 million or more?

Mr. Neal: Correct.

Senator Pratte: And, therefore, derive yearly passive income of $50,000 or more?

Mr. Neal: They will hit that based on how their performance was in the past. They will hit that either in the very near future, we have some clients who will be hit immediately, year one. We have some clients that bonuses will be paid out in the millions of dollars in 2018. Millions of dollars in bonuses because it would make no sense to leave the money behind in the corporation. So we have a number of clients who will get millions of dollars — and I've already spoken to them about this — in bonuses. They're hit right away. Other clients, by virtue of how they've done in the past, will hit the $1 million or the $50,000, depending on which one you look at, in the future over a period of time.

Senator Pratte: Mr. Saunders, Mr. Costin, you can certainly also have a word on this. Give us an idea of what sort of companies we're talking about here, because for most people, $1 million is a lot of money, and companies that would have $1 million in capital to invest passively. I don't like this word "passive." What sort of companies are we talking about? Are these big, private companies? How big do you have to be to have $1 million to invest, not in your company for the moment, but invest passively on the stock market or in start-ups or whatever?

Mr. Saunders: Well, we would have a range of clients in almost every industry that could be affected now, or would some day hope to get to the level where they would be affected. Real estate is the first one that comes to mind, because they're not necessarily having to save $1 million in cash or investments, just buying a $1 million apartment building gets you to that level. As soon as you buy that first building, in some cases. In that case, you have a $1 million building and a mortgage or almost $1 million probably, and you're still subject to these rules potentially, if that rental property is profitable. In other cases, it would be sort of older businesses that are nearing retirement that have been, sort of, accumulating funds over time. Other cases, it would be, as I alluded to earlier, when you sell the business, if you sold the assets rather than selling the shares. You sell the assets and get a cheque that goes into your company, and suddenly you go from having an active business to a pot of investable cash. Those would be the main areas we would see it.

Mr. Costin: To that point, I guess I'd come back to my comment on the questions raised to Pierre Poilievre, because I echo that. I have a lot of clients that, to buy a $1 million building, and my understanding of this is in line with my friends here, that they would fall under that $1 million. But if you have a company with 10 shareholders and you have $1 million, that's kind of the issue that I'm at, and that was the question that Poilievre was putting to Morneau, which I thought was a very fair one.

They were also not talking about interrelated companies. But the problem I'm having, just generally because I think you've got the technical answers there, the problem I generally have, when someone says, "This is only going to affect X-percent of businesses, only the most wealthy of businesses," they say, who gets into business to be subpar? Who gets into business? Who goes to law school to make no money? Who becomes an accountant to make no money? It's the noble pursuit of capitalism that creates jobs in this country, and it's the backbone and driver of this economy. So that's my general response to this whole dialogue around, "Well, only this small percentage, only the elites, only the most successful are going to be hit by this", because, to me, that is unfair and that is, quite frankly, against the spirit of capitalism that built this country.

Mr. Neal: Senator Pratte, if I could just quickly give you an example, if you looked at this in a vacuum and said, "Well, there's a business and they have assets and it produces profit and that's going into passive investments, and, hey, it's $1 million, that's a lot of money," if it worked like that, then I think the debate would be easy. But it doesn't. As an example, we have a car dealer and we wanted to move buildings, we wanted to upgrade, and so we said, okay, well, we're in a building now, what do we do, I don't know, who wants to buy a used car dealership building, single purpose, around here? Nobody. So we rented it out. It's got a couple of million dollars into it, now it's passive. He goes out and borrows $5 million to build the new facility. He's got passive investment of $1 million in excess, it's $2 million is what he's got into that, and then it's a passive investment now. Yet, he put $5 million into a new building, created jobs, brought a new car dealership to town, construction, plumbers, everything. It's about balancing it off. No one in business who's active is going to take all their cash and put it in their operation, they're going to tuck some away, leave it there, and then leverage, borrow money from a lender, and put that into the business. Meanwhile, the passive investment is sitting there. We could take that passive investment and pay off the debt, but why would you do that? Interest is deductible, last time I checked, as long as it is used for business purposes. So, your balance sheet is such that you have passive investments built up, but you could have significant debt that you're carrying as well. So I think you've got to look at the balance sheet from both sides.

Senator Pratte: I have one last, very short question for Mr. Neal.

You mentioned in your presentation that one of the problems you had with the threshold, if I understood you correctly, was that it was the same for any kind of business, whether it was a small or large business, that's something that we've heard. One question that I had in my mind is that, if the government was going to move forward with this idea of taxing passive investment, passive income, whether, at least, it would not envisage a threshold that would vary according to the size of the business, which would certainly be better than having a fixed threshold. However, of course, the trick would be what the threshold would be relative to what? I wonder if you would have ideas to suggest? Would it be total revenue? I wonder if you would have ideas to suggest on that point?

Mr. Neal: You could come up with many different measurements, but I think revenue would not be. If you consider a general contractor who builds buildings but really has no real amount of employees and subs it all out, they might have $100 million or $200 million in revenue and $50,000 in profit. So revenue wouldn't be a measure. Assets couldn't be a measure.

Look at a business like mine. We don't have a lot of assets because we're people-based, but if you look at car dealers, for instance, a significant amount of assets. I think that to say they'll have different levels that apply to different sizes of business, look, that is adding so much ridiculous complexity to small businesses who struggle to get capital, who struggle to get employees, who struggle to find avenues to help them export, who struggle with their working capital. They're profitable, they have inventories, they have receivables, and they're exporting, and they can't get working capital because banks won't lend to them. To add this type of complexity and cost, to me, is absolutely asinine in the circumstances. I'm not convinced you could come up with a reasonable measure that moves people up the ladder based on the size of the business for these passive investments, I just don't see it.

Senator Neufeld: Thank you very much, gentlemen.

The issue about retirement, and the clients that you folks have, I just want to read to you what the Minister of Finance said in one of your committee meetings. And the Minister of Finance told the committee that "government recognizes the need to retain funds within the corporation for business purposes", actually, that's pretty normal, but it wants to discourage using private corporations to save for retirement. What would drive a finance minister to say that about small business? Look, I've had a small business, a number of them in my lifetime, and I hoped that at some time I'd be able to put some money away in that company, and when I sold it, I'd pay whatever taxes I had to, but it wasn't about a cap, it wasn't about government saying, "By the way, you're bad if you're over this cap, you're okay if you're under". Why would that even begin to make sense, to not plan for your retirement? I mean, you hear government officials say not enough Canadians are planning for their retirement. Then we have a finance minister who gets up and says, “By the way, you shouldn’t plan for retirement”. Maybe you’d have a little bit of insight to add to that?

Mr. Saunders: Well, I would respectively disagree with the finance minister on that. If I was advising clients, I would not advise them to pull all the excess cash out of their company, put it into an RRSP, because when the economic downturn, the rainy day comes, to get those funds back into the company, they would have to pay a high tax rate, they will have lost their RRSP contribution room, so they can’t get it back into the RRSP after the fact, it would be a very inefficient and expensive way to save within that business. And I’ve seen clients that had saved, one in particular, in a small town, had saved a little over $1 million over 20, 25 years. Factors outside of their control decimated their industry, and they used that $1 million pot, they spent every dime of it, to keep the doors open and keep people employed, rather than, you know, they could have easily just said, “All right, well, we’ve got our pot, we’re going to walk away and this is our retirement.” But they didn’t do that. They kept the business going and eventually were able to turn it around and get it back and start saving again for their retirement. So I don’t fully understand what the minister’s perspective would be on that.

Mr. Neal: I believe that Finance has this idea that there are some, a few, or many, whatever number they want to put on it, are incorporating, Canadian control private corporation, for the sole purpose of getting access to the small business deduction tax rate, and there is no other reason for the incorporation. I feel that is what has been said. So with that in mind, I ask why you would take down 90 percent of the rest of us, is my first question.

My second question is, why wouldn’t you define then what a small business is? We do know, or I do know, that there are people who incorporate who probably should not be incorporating. That is, they’re likely employees. If you looked at the application of their duties, they’re more likely an employee than they are a business. They’re not independent. There are existing laws, current legislation, that already deal with that; it’s called a personal services corporation. However, the world is changing. Employers now don’t want the burdens associated with a lot of these employees that are there on a short-term basis, whether it’s eight months or a year and a half. They don’t want the workers’ compensation, they don’t want their share of the EI, they don’t want to deal with the pension, they don’t want their share of the Canada Pension, they don’t want the cost associated with termination. So, the encouragement is, and they encourage this, the large public corporations encourage them to incorporate effectively, by using parties that are in the middle, that go out and find these workers, match them up with these large corporations, and say, “Hey, I’ll get you a contract, you’re independent”. These people are then talking to somebody like me and saying, “Hey, can this work? Can I incorporate?”, and you look at it and say, yeah, you probably can, I think, by virtue of this middle person between you that’s gone and recruited you and stayed in the middle in order to get you this job, or this contract. That is happening. But that is the nature of what’s happening, and it is not being driven by the little people on the street. It’s being driven by large corporations, and I think it’s wholly unfair to take the position that there are people incorporating just to get the small business deduction and point their fingers at them. I think people need to look a little further than that.

Mr. Costin: With respect to your question, Senator Neufeld, when our current finance minister says that he wants to take away the ability of Canadians to save for retirement through a private corporation, two words come to mind; one is Morneau, and the other one is Shepell. They do happen to be in the business of, and I do not mean anything partisan by this, but that is just a fact. I mean, there is currently a conflict of interest investigation. And I hear you. My dad is a small business owner. I mean, his retirement is his business. He keeps the business healthy. And what I'm faced with, and I'm speaking to my accountant on it, and my clients are speaking to their accountants on it and me on it, is if I leave money inside a professional corporation, and they keep saying that we have no problem with them using it for an active reason, how is someone going to be able to effectively audit that? Because what comes to mind, with me, if I say I'm leaving $20,000 in there in the event that there's a cash cull by virtue of our partnership agreement. Or, I'm leaving $15,000 in there because we anticipate in ten years, there's going to be an expenditure to purchase a building in Fredericton where we'll be opening an office. I mean, all of these things, how can someone come in and audit that?

Further to your point, I believe there was dialogue around, well, the small business owner can take money out of their corporation and stick it into RRSPs and, essentially, you can only buy publicly-traded companies, I can't invest in small business through my RRSP as it currently stands. I think that's something that is severely overlooked.

Another issue that comes to mind is a lot of entrepreneurs that I act for and, look, I tend to deal with the minute book, my friends here deal with the financial statements, but a lot of them, they aren't paying themselves, especially the guy starting out. They're not paying themselves big salaries or any salary at all, so their RRSP room is minimal, if anything. Not to mention, if you ever had to liquidate your RRSPs and stick them back into your business through a shareholder loan, it's extremely inefficient.

Senator Neufeld: The other thing I believe we've heard, and we've heard a lot of stuff, I can tell you, that the tax system in Canada is viewed around the G8, let's say, as relatively a sound system. I mean, it does need updating, obviously, I think we can all agree to that, because of the last time it was updated, but is that correct? Other countries, do they look at Canada and say, "That tax system they've got there is not certain", or do they say, "You know, for what they're dealing with, it's generally pretty good"?

Mr. Neal: From what I see, just like us looking at other countries' tax systems, they probably don't quite understand it. It is a complex set of rules filled in with jurisprudence for interpretive purposes, an application of the particular laws. I don't quite know the answer to that question other than I will say that the incentives that are put in that Income Tax Act were done by government, not by us. And the Income Tax Act, in 1971, was an inch and a half, and now it's four and a half, and that's public policy being jammed in, in every budget. Everyone gathers around the TV and waits for the goodies, and you're going to get this credit if you buy this, and that credit if you have this kid, and if this kid does this, then you get that and you get this, and all these things get jammed into this Act, and they're all interlinked, and it makes it bigger and bigger and bigger. So, the one criticism I have heard for anything that I've dealt with anybody outside the country is, they do comment that there's a lot of public policy that Canada puts through their Act.

Senator Neufeld: Would you gentlemen agree with that?

Mr. Costin: I believe that's fair. I went to high school in Boca Raton, Florida, and did my undergrad at the University of Rhode Island and studied business, and it's interesting how there's this conception that, you know, we have way higher taxes in the States or that we have a more public policy-driven system, but I would say both our systems are, from my experience and limited experience in cross-border stuff, they're both extremely complex, overly complex. I tell the story of I used to work with a lawyer who had a copy of the Income Tax Act in 1973 and it was about probably one tenth the size of the annual amendments that come out. But I really couldn't say that Canada is any better or worse than any other country. I would say both the United States and Canada should be simplifying their tax code and not making it more complex. And I understand that's what your American counterparts are at least looking to do.

Mr. Saunders: Yes, I would agree with all of those comments. I think, in general, we have a good tax system, it's just the nature of 100 years of history has gotten increasingly complex and difficult. I expect, even the three of us, there's probably parts in that book we've never read. And I know, earlier this year, when I received my new version of the Income Tax Act in the mail, they actually had an insert, it was the one hundredth anniversary, so there was a reproduced copy of the original Income Tax Act, all ten pages of it.

Senator Neufeld: Are you aware of any other country, we'll stay within the G8, that actually says we're going to have passive income, whatever that is, and there's going to be a cap, one cap, for everybody? Is there any other place that you can think of that a finance minister has said, "I'm going to actually control how much money corporations can keep in their bank account for whatever purpose they want", whether they need to buy a $1 million-and-a-half tractor to keep farming, or whether they need to buy a $100,000 tractor to keep farming? And this comes from a person who stands up and says wealthy people are taking advantage of the tax system, and we've heard from a lot of people about this issue, they're not wealthy. But you hear from a finance minister that gets up and says, when he got caught not claiming to the right officials, how much money he held in companies and actually had a $5 million interest on that money over that period of time, the two years that he was finance minister, and he just said, "Well, I'll just give that $5 million to charity". Now, that's nice of him to give $5 million to charity, I don't take that away from him. That's what I call wealthy, someone who can just say, "That $5 million, it can go because I'm still right and I'm perfect, but I want to put a cap on those hard-working people out there, that they can only put away $1 million for their retirement, and they shouldn't even put money away for their retirement". How would you feel about that if you were that small businessperson that listened to that, from what's supposed to be about second-in-command to the Prime Minister of the country?

Mr. Saunders: I would say to the first part of your question, I'm not aware of any other country that would have a similar type of rule. Regarding the wealthy and fairness in general, I've always told people that I'm not a billionaire, I'm never going to be a billionaire, but even if you are, in my mind, no matter how wealthy you are, I, personally, don't think a tax rate above 50 percent is fair.

Senator Neufeld: Exactly.

Mr. Saunders: And in regards to how myself and other small businesses received comments like that, I would say it was not received well.

Mr. Neal: For the record, senator, my firm has no clients that fit that profile that you described, and we are not a small firm. So, when you're thinking about wealthy, perhaps that's the definition. I am one of those small business people who has heard this. I am. I am somebody who has put my capital on the line. My firm just acquired a firm in June. We went into the Bank of Montreal and we asked them for the money, and they couldn't wait to give us the money. As soon as I signed my company over to them with its passive investments, they were more than happy to give me a cheque. So, to me, hearing that kind of talk, is insulting for the years that you put into a business, and, in my case and my colleagues' case, here, the years of university, I'm the first one to go in my family, and to come out on the other side, and put yourself out there, and hang your own shingle, and take a risk, and listen to that, it's insulting.

Mr. Costin: It would maybe be a somewhat self-serving answer because I'm not knowledgeable on the tax codes of other countries, but I'm not aware of any other country in the G8 that has this purported cap that they're looking to reinstitute. I am friends with lawyers in the States that I've gone to school with. I do, from time to time, keep them apprised of this, and they think it's nuts, and that's even in context to what's currently happening there. I'm not sworn this afternoon, but I can advise the Senate committee that if I wrote a cheque for $5 million to any charity, they better not cash it. So, I would not fall under that.

I would echo my friend's comment. Gorman Nason traces back to really the late 1960s. It has been Gorman Nason since 1983, and I don't believe we would have a client that would fit that description. And I'm not the guy that does the taxes, but I would also think don't you get a massive tax deduction for donating that much money, so it basically means he pays, yet again, less tax? And I want to make it clear that, you know, I don't have any issue with public sector, big business, small business. I think, quite frankly, to my friend's point, 50 percent is way too much for anybody making any amount of money, and, especially, when the bulk of our taxes are paid by the highest earners. And yet they're being vilified, and yet we have money that appears to be, and I'm not an expert on this and very few would be in this market for lawyers, but on this cross border offshore stuff, we've got a lot of money sitting out there. And, for some reason, that's not being addressed. So, I agree with you, and it's, to me, it's just categorically offensive as someone that just incorporated my professional corporation last year.

Senator Neufeld: One thing I would just like to add, the tax changes that have been proposed, will have no effect on that person that can just kick $5 million out. Zero.

Senator Oh: Thank you, gentlemen.

Mr. Neal, you are a very sharp tax accountant. I always advise investors and newcomers, new immigrants that come to Canada for investment, I say you need a good tax lawyer and a good accountant. Now, looks like we need three.

The findings of the Auditor General in relation to the CRA were mentioned earlier. Are you all in agreement that the agency is simply not ready to carry out such expensive changes to our tax system if it already has difficulty not only answering but responding accurately to Canadians?

Mr. Saunders: I would certainly agree with that. I'm not aware of what steps CRA has been taking to get prepared for these changes; I assume they have been doing whatever they can. But, based on past history, and as you mentioned, the Auditor General's report, the ability to just get through on the phone and talk to a person is incredibly difficult. And then the Auditor General's findings, I believe it was 30 percent of the people asking questions are getting incorrect answers. Anything that makes the tax law more complex, more difficult, is only going to increase the volume of questions they're getting, and the greater risk of getting incorrect answers.

Mr. Neal: The current operation of CRA has been a slow, steady slope. The ability to get the Canada Revenue Agency, not only to answer the phone or answer your question, which, if they do answer the question, I submit to you be very cautious. When I'm involved, the answer is generally incorrect. The CRA has been going for years in this direction. To get them to answer the phone is difficult, to get them to answer a question is difficult but, even deeper than that, they conduct audits, of course, of our clients. It takes months and months, if not years, and if you have to go to an objection stage, you might want to object and then put everything away for further months. We have objections that have taken up to two years to resolve, and we're not talking millions of dollars in tax, we're talking $100,000 or $80,000 or $50,000 in tax. If you want a ruling out of CRA, good luck. There's a year to get a ruling. We had an audit where they applied their interpretation of HST law, the same auditor to the same industry, clients of ours that operate across the street from one another, and they applied the law differently to the two clients. One, they assessed based on their interpretation which I disagree with. The other one said, "Well, you better start doing it, but I'm not going to assess you". The same auditor within a year. There is something wrong with the Canada Revenue Agency.

Mr. Costin: I echo my friends' comments; they're correct. Quite frankly, when there's more uncertainty, as I've previously stated, as my friends have previously stated here, it leads to the need for, to your point, more accountants and more lawyers. And that may keep lawyers and accountants busy, but that is not what's best for the Canadian economy.

To your point of immigration, I have done select situations where I've acted for businesses where the business owners are immigrating here, and it's not just Immigration Canada, CIC, you can't speak to a human being on the phone anymore, CRA is the same way. What I have basically taken out of this is, if these measures pass, whatever money they think they're going to get in extra revenue is going to have to be kicked, probably twofold, to CRA for them to properly audit this and to enforce this, because that's the concern we have. My friends have hit it on the head. It takes so long, there's no certainty, and while there are great people that work there, it's very hard to get things moving along. A lot of times, what I see happening here is widespread litigation on this because, what Chris just said is absolutely correct, you will have a situation where the same auditor can assess two very different findings on something there might already be an ITA bulletin out there and it's already deemed to be settled, but yet it turns into litigation. So, I, based on the most recent Auditor General's report, I don't think CRA is prepared to take on this additional burden that they're going to be placing on them.

Senator Oh: So if the reform is not carried out or gone through, would you agree that your clientele would drop but your fees would go up?

Mr. Costin: To be blunt, probably, yes. You're probably right. Anyone that can afford to, because in order to get things moving the way you want them to, or if you have so much skin in the game that you can't just walk away, it's going to cost more. The more complex it gets, the more it's going to cost in lawyers, the more it's going to cost in accountants. And that's the comment that you hear in the States, you need significant resources to fight the CRA on rulings, you need significant resources to set things up the way they are. And I do want to point out that, in New Brunswick, it came out that they've raised revenue, they've raised tax on the 1 percent, that's the rhetoric that's being used, and they've lost money on it. So, I see a situation where they're going to raise taxes, there's going to be someone there with a Masters in science and MIT on Bay Street that finds a new way, a new work-around, and then, basically, the people that have the capability to, they reorganize, and the government loses out on that revenue.

Mr. Saunders: I certainly agree. I think one of the reasons our firm, and Mr. Neal's firm, have been out sort of trying to educate the public and push back against these proposals is because, even though it will increase our fees to our clients, we know that, in general, it is bad for the economy and for small business in general. So, I think that overrides that self-interest that, in the short-term, we might get a little bit more money from them but, if they go out of business, it doesn't help anyone.

Senator Oh: Thank you.

The Chair: Senator Cools, do you have a question or comments?

Senator Cools: A little bit of both maybe. It's an issue with me but, years ago, CRA used to be Department of Government and some years back, for a whole host of reasons and nothing to do with the National Revenue, they made it an agency. And it had to do with government reorganizing itself to make it harder for unions to get members within the departments, that sort of thing. But this bothered me when it happened, and it stuck in my head for many, many years. And one of the recommendations that was already suggested for this committee is that we recommend that the CRA be reconstituted as a department of government with a minister that [inaudible] minister directly responsible. I just want to let you know that these stories that I hear of the hardships and the harshness of which they deal with people and I hear endless stories on a daily basis and it's really a terrible, terrible thing. I heard about a particular case where a man was a used car salesman and, somehow, one of those cars that he had sold to somebody turned up in a robbery or a crime somewhere, and they moved in and locked all of his money for weeks and weeks, and just had the man in a terrible, terrible state, the small businessman. I just put that out to you. But my real question to you is, one, I wanted to thank you for sharing your experience and your knowledge with us, in the very generous way that you did, but my real question to you is that we are expected to write and produce a report, and part of that report is always a good itemization and summary of our observations, our findings and our recommendations. So, if I were to say to you, what do you think our best for recommendations should be, what would you tell us to do?

Mr. Saunders: Well, the first recommendation I would make would be to slow down. A massive revision to the Income Tax Act is too important, it affects too many lives and people and businesses to do it in a haphazard or rushed way and get it wrong. We know every year there's a budget coming, there's going to be changes, rates go up or down, brackets move around, we can deal with that. These are fundamental changes that upend 40 years of tax planning that people have been doing, and it's dramatic and it has a huge impact, and I don't fully understand why it's being done in such a rush.

Mr. Neal: There are a number of very juicy parts of the Income Tax Act, retirement compensation arrangements, individual pension plans and rules around stock options. They're remaining. Those are generally designed for the wealthy, the big, big companies. They are remaining after these proposals. So, what is going to be taken away is what we discussed today for small business, but those stay. Also, I understand, what's going to stay is when you donate shares out of company at a capital gain, you don't pay tax on that capital gain, but you also create a capital dividend account, and you can take that money out of your corporation, tax-free. Which is what I'm sure Minister Morneau did, if those shares were held in a corporation, he would have donated the shares, by the way, not the cash. That would've created a capital gain that's not taxable inside the corporation, but it also would have created a $5 million tax-free payment that he could take out. So, I'm confused why this government has said that they're going to close tax loopholes for the wealthy when, in fact, those tax loopholes are going to stay. So, my advice would be, look at this income tax as a whole. Slow it down, as Mr. Saunders did. It has got to be fair for everybody. Stop trying to pick out who's wealthy and who isn't, because it's the wealthy ones who are pointing the fingers at the ones who are not.

Mr. Costin: Well said by both my friends. The main thing that I guess I would communicate to you that I guess I would like to see in a report would be that this has to be done properly. I, professionally and personally, am not opposed to taking a look at our Income Tax Act, holistically, but key word, holistically. Not engaging in what some could argue to be a form of class warfare and vilifying one specific group. And the thought process that I had there is, I mean, this is something that would require a Royal Commission, would require, from my perspective, significant input from tax professionals such as the two sitting next to me, and basically getting a look at the whole picture. I agree that, I mean, if we're going to look, if we're going to be consistent, and I think everyone's taxes are too high, but if we want to take the position of we're going to tax everybody more, why aren't you looking at the stock options? Why aren't we looking at offshore? And, really, that's the take I have on this. And from your question as to why it was done the way it was or how it's done, I honestly think this was political. I think they ran on, big surprise, they ran on essentially raising income taxes on people that were incorporating, especially the professionals. And I'm aware of one change they made to the two corporation rule that lawyers took advantage of the previous year, and that was done in the usual form. There's an ITA bulletin, it's an interpretation bulletin, here's what we're going to do. There wasn't this splashy we're all about fairness and equality, and everyone has got their pitchforks in hand, it was just done very quietly and it was affected.

My take on it is, quite frankly, not enough people noticed and, come election time, Morneau and Trudeau want to say that they did what they said they would do. That is my take on this, that's the only way I can read into this because if they were going to make these changes, why wouldn't they do it right? Why wouldn't they sit down with lawyers, why wouldn't they sit down with accountants and actually point us to something substantive? So, I would be telling them, the damage has been done, from the interim uncertainty, but you guys need to go back to the drawing board and get this right.

The Chair: Thank you.

Senator Cools: And then, chair, finally, my comment. This is another pet issue of mine. I've spent a lot of years working on the national finance, and I was always taught and always believed that government has very strong, powerful constitutional powers to raise taxes. But the taxing power remains a sacred trust. And it has always been thought by the great constitutionalist that it is a trust between government and citizens, and it's never, a government is never, ever to violate that trust. And it's unfortunate that we don't speak in these terms anymore, but that is what it is. It's a trust between the governed and the government. Thank you so much.

The Chair: Thank you.

Senator Cools: Good recommendations, though.

The Chair: Before we close, I have a question for the witnesses. In light of the Paradise Papers and the Panama Papers, and given your expertise and what I've heard from you, do you believe that this reform we're looking at, if passed, could decrease tax compliance and thus reduce the tax revenues collected by the federal government?

Mr. Saunders: I think it's certainly a risk. As I believe Mr. Costin mentioned, the recent newspaper article on tax rates going above 50 percent in New Brunswick, and the revenue went down. I believe there have been studies as well that show when taxation reaches a level that the people being taxed don't feel it is fair, they pursue methods, mostly legal, some less than legal, to avoid that tax. You know, we see it sort of in the small business arena, you see some clients working for cash under the table. We certainly don't advise our clients to do that, it's illegal, we don't want to be associated with that, but we know it does happen. And I would expect that these proposals would lead to people trying to find methods to reduce their taxes. If their tax bill is going up by $20,000 next year, they're going to look to ways to find that.

Mr. Neal: These small businesses, they're smart people. They have built businesses from nothing, a lot of them to big businesses. We have clients and 150, 250 employees, and they've worked through tougher things than this. They will deal with this in a fashion in which their income tax will be managed. We are already, in a number of discussions concerning, "Hey, how can we do offshore things? We're big enough". Nike has a swoosh offshore that charges a royalty every time a shirt or a pair of sneakers are sold, perhaps we can do something different. From a restaurant owner saying, "Why don't I put my recipes offshore," to Nike putting their swoosh offshore, there's a lot of options available. The underground economy has now been encouraged. The underground economy now will have a full tank of gas, I've already heard it, it's already been noted to me on multiple occasions, and this will spur an underground economy.

Mr. Costin: Absolutely, I agree with my friends again. People generally act rationally, and there is typically a cost benefit analysis that is taken into consideration. If you're going to get, basically, beaten up black and blue for going to work every day, you're going to start looking at alternate options. I've had a client that has come to me and said, "Andrew, what would it take to move my business to Maine?", and I'm hearing that quite a bit. And I make a point of saying that this is happening in the midst of the Americans saying they want to lower their tax rates. We have Paul LePage in Maine fighting for every job he can get right now. And so, it's like with NAFTA, that big sucking sound, if it is not sustainable or too expensive to do business up here, I have clients that are going to do it, my friends have clients that are going to do it, and even the smaller people, I mean, from my experience, and, look, I'm on the younger end of the spectrum, but I'm still certain, if you raise rates, if you do something, someone, somewhere with a PhD that's a genius that went to MIT is going to come up with a way to pay less taxes somehow, and it will be legal. That's just what it is. So, in short, I think this is not going to be a positive thing for business, the economy. I can't say that it would even lead to any more revenue for the federal government.

The Chair: Mr. Saunders, Mr. Neal and Mr. Costin, on behalf of the Senate Finance Committee, thank you very much for sharing your views, your comments and your recommendations. You have certainly been informative.

Senators, our next witness is Mr. Mike Holden, Chief Economist with the Canadian Manufacturers and Exporters.

Mr. Holden, thank you very much for accepting our invitation. We will ask you to proceed to make your presentation, followed by questions from the senators.

Mike Holden, Chief Economist, Canadian Manufacturers and Exporters: Thank you very much and thanks for the opportunity to appear here before you today.

I'm here to speak on behalf of Canada's 90,000 manufacturers and exporters and our association's 2,500 direct members about the taxation of Canadian controlled private corporations and about Canadian tax competitiveness generally.

Before I go any further into my opening remarks, I would like to extend regrets on behalf of our New Brunswick Vice President, Joel Richardson, who was invited to appear in front of this committee. Joel is a member of the New Brunswick government's task force on worker's compensation and he unfortunately had a scheduling conflict with some public hearings that they're holding in Moncton today and he was unable to attend.

For those of you who don't know CME, we are Canada's largest industry and trade association with offices across the country, including here in New Brunswick. More than 85 per cent of our members are small and medium sized enterprises and our objective as an organization is to see those businesses prosper and grow, creating economic growth and good jobs for Canadians.

As outlined in our formal submission to the Department of Finance, CME had a number of concerns with the initial CCCP tax reform proposals that were released in July. To name just a few — they did not account for key differences between small business income and salary income; they deterred entrepreneurship and innovation; they discriminated against family succession; and they increased the complexity and compliance burden of an already challenging tax system.

We're pleased to say that the changes announced in October address many of these specific concerns. However, they do not address the broader issue of tax competitiveness which we believe to be far more important than a selective pursuit of tax fairness.

There's a growing gap between Canada's apparent tax competitiveness and the outcomes we are seeing. We fare well compared to U.S. headline tax rates and against countries like France, Germany and Australia. But we are in the middle of the pack against other OECD countries and we are not seeing the results that we believe we should.

Business capital investment in Canada has fallen by 11.6 per cent over the last three years and manufacturing has fallen by 15.3 per cent. Canadian businesses invest less as a percentage of GDP than any other country in the OECD except for Greece. New Greenfield foreign direct investment in Canada has fallen by 40 per cent since the pre-financial crisis. In the United States by contrast, it has increased by 41 per cent. In 2005, Canada attracted 4.6 per cent of all new global Greenfield FDI. By last year, that 4.6 per cent had fallen to 1.6 per cent.

So Canada has a relatively competitive business tax system and yet we are losing ground on pretty much any results based measure that you would care to consider.

So either our tax system is not as competitive as it appears to be or our tax advantage is not large enough to compensate for other, more significant, cost disadvantages.

There is no denying that our headline corporate tax rates are more attractive than those in the U.S. The reality however, is the U.S. governments offer manufacturers a huge array of tax credits, holidays, subsidy programs and other incentives to attract businesses south of the border. Some of these are explicit, others are negotiated. In the end however, the value of those tax breaks and subsidies completely eclipses Canada's apparent tax advantage.

Our tax rates and business costs were obviously not enough to attract significant new investment to this country and now we're chipping away at that advantage. Depending on where you live, minimum wages, electricity costs, carbon pricing, CPP and workers' compensation premiums and provincial corporate tax rates are all increasing.

Through these actions and proposals like the CCCP tax reform, the proposal to tax employee benefits and expanding property taxes to include machinery and equipment here in New Brunswick, governments are sending the message to the business community that they will leave no stone unturned to satisfy their rapacity. Recently announced cuts to the small business tax rate do not compensate for this trend. In fact, we're concerned that the widening gap between small business and general corporate tax rates is creating a disincentive for businesses to grow beyond a certain size because of the punitive increase in marginal taxation that would result.

Meanwhile, recent proposed tax reforms have U.S. tax competitiveness moving in the opposite direction. The result will be an even wider cost gap between the two countries, less investment in Canada and more companies moving to the U.S. or making their next big investment in that country.

Uncertainty around NAFTA will only magnify this problem. Canada is not a large market. Our chief selling point as an investment destination is access to the North American economic space. The issue is not even about what happens if NAFTA is terminated or if a new deal is worse than the one we have now. The real issue is the business uncertainty that has already been created. Why would a business invest in Canada and expose itself to that uncertainty when it could just invest in the U.S. and avoid it altogether? We need to have a very good answer to that question, and at present we have no answer at all.

To sum up, issues like CCCP tax reform and tax fairness are a distraction from a far more important problem. Canada is not attracting new investment. Uncertainty around NAFTA is driving that investment south of the border and U.S. tax reform will only accelerate that process, unless we take decisive action.

In short, we need to abandon piecemeal efforts to address tax fairness and instead focus on strategic objectives, attracting investment and creating jobs. CME believes that Canada needs comprehensive business tax reform. We need a tax system that is simple and fair, that encourages our business to grow, that fosters innovation and above all, makes Canada an attractive place in which to invest. We need to get this right and CME is willing to work closely with the federal and provincial governments to make it happen.

Thank you all for your time and I look forward to your questions.

The Chair: Thank you, Mr. Holden.

The first question will go to Senator Marshall, to be followed by Senator Eaton and then Senator Pratte.

Senator Marshall: Thank you very much for your presentation. It was conveyed to us that you really do [inaudible]. The issue with the tax reform in the private corporations. We've been hearing from a lot of people about the tax reforms, but the tax reforms as they stand. But what you've done now is you've presented it on a bigger stage and it's only a small thing.

So what are you hearing? You represent a lot of manufacturers and exporters. What are you hearing from them? You're painting a very negative picture. We're certainly not at the top of the pack. I'd certainly want for us to keep what we have and I would want us to deteriorate any further. But the impression that I'm getting from reading your speaking notes is that we're probably going down as opposed to going up or staying where we are. What are your members saying?

Mr. Holden: Well, I think they're very concerned. As I said before, I think this issue of CCPC tax fairness touches on a significant share of our membership, if not the entirety of our membership. We have businesses that range from the very small to large multinational corporations within our membership base. And so for the businesses that are affected they're very concerned. They feel that their contribution to the Canadian economy is not being appreciated, that they're being taken for granted, and from their perspective they see themselves as the engines of growth of the Canadian economy. They're the ones who create jobs. They're the ones who contribute revenue, who put their own lives and their livelihoods on the line for the work they're doing, and they feel under appreciated. It is slightly inaccurate to suggest that they are being branded as tax cheats, but in some cases they feel that way.

I think the concern that our businesses are expressing to us, and this is not just the small ones anymore, but it is this decrease in cost competitiveness that we have in Canada of which the tax system is part of the problem because we have a large number of small increases in a wide range of areas. So for the last three or four years there's been increases in the Canadian Pension Plan premiums, minimum wage increases in some provinces, like I said electricity costs in Ontario and Manitoba, carbon pricing and provincial corporate tax rates. Most of those are not in the purview of the federal government. Some are and some are not. But from the business perspective and per business perspective they're all part of a single series of events that's eroding their competitiveness.

Senator Marshall: So when we've been talking to other witnesses from other areas we ask them what is the current situation now. With these tax changes on the horizon where do you think your business is and how are they going to cope with them? Some of the businesses and some of the individuals are saying that they'll move to other jurisdictions, like to other provinces, and others are looking at other countries, either south of the border or even further abroad. What would your members be saying to you as to where they are now and what they plan to do with these proposed tax changes?

Mr. Holden: I think it's fair to say that some of them have expressed exactly what you said. They are looking more and more at what the prospects are for moving their operations to the United States or to other countries. In the case of CCPC tax reform moving to other provinces doesn't matter quite as much. If you look at the larger group of tax changes there might be some encouragement to move from one province to another, but if we look at it only from an international point of view, yes, some are concerned. Some have expressed that desire at least to investigate the possibilities.

I think the larger issue is there is a risk of some businesses just up and moving their operations into the U.S. or someplace else. The more likely risk is that the United States is where they will make their next investment because it's expensive and costly to move and to sell your business in Canada and relocated to the United States. I'm not an expert on the procedure that's involved, but I think that it's the next investment that we're worried about.

Senator Marshall: So this would be, following your first point, business capital investment in Canada we're saying has fallen by 11 per cent over the last three years and manufacturing has fallen by 15 per cent. So you would see that continuing to fall? That's what you would think based on your background?

Mr. Holden: Yes, and there are two things there, just to be clear. The business capital investment falling by 15.3 per cent refers to businesses investing in their own operations, buying new machinery and equipment, buying new facilities in Canada. I also mentioned that new foreign investment in Canada or the creation of new Greenfield investments, like a brand new factory or brand new plant of some kind, those investments are also going down at the same time. So we have two situations. One where Canadian businesses are not investing in their own plants and/or expansions. And we're not getting new businesses coming in.

Senator Marshall: Thank you very much.

Senator Eaton: Thank you, Mr. Holden. You're bringing up a very good point about our lack of tax competitiveness, and you compare us to the U.S. where perhaps we look great right now in headlines, but in the end when you get down to calculating the tax credits, the holidays, the subsidy programs and other incentives. They do a better job. They become more competitive. If you had to recommend to our government what kind of tax credits or subsidy programs should we put in place to become more tax competitive in the future?

Mr. Holden: There are a number of possibilities. I think that the objective of whatever is pursued has to be encouraging businesses to invest more in capital machinery, equipment, technology and new advanced manufacturing technology.

Senator Eaton: So how would you do that?

Mr. Holden: Well there are a few options. One is in our pre-budget submission we recommended that the Government of Canada ... we have an accelerated capital cost allowance program. We recommended that one be created specifically for investment in advanced manufacturing, machinery, equipment, technologies and software. A permanent program that would allow businesses to write off these expenses within one year which would be a major change from the current ACCA, and that's something that I believe we see reflected in the U.S. tax proposals. So that would help, but at the same time you would also be only ensuring that we don't lose further ground against the U.S. with that particular step. But I think that that would be a solid step in the right direction.

Senator Eaton: Are there other recommendations you would make?

Mr. Holden: In our pre-budget submission we also recommended the extension of the Atlantic Investment Tax Credit to other provinces.

Senator Eaton: Could you explain that?

Mr. Holden: I'm not an expert on the program or I don't have the information off the top of my head, but it was a tax credit for companies that invested in their own operations here in Atlantic Canada. It was a regional development incentive program. It's a good program here, but we have an issue with the fact that businesses have access to certain federal government programs because they happen to be located in one part of the country and not another. We would like to see a program like that expanded and extended across the country.

Senator Eaton: So they won't favour one region of the country over the other.

Mr. Holden: Yes.

Senator Eaton: Anything else?

Mr. Holden: I think that the main issue which your previous panel touched on which I think is very important is the growing complexity of the tax code. I mentioned in my opening remarks we need a tax system that's simple and fair and where the compliance burden is relatively low. We heard before about how thick the tax code is getting. We need a system that is much simpler and more direct than what we have now and make sure that Canada is in fact an attractive place in which to invest.

Another possibility that we are considering but we would need to do more research on it ourselves, is we are looking at the possibility of what would happen if you provided a significant tax break on retained income within a company so that income that businesses invest in their own future is not subject to the same rate of tax as income that is distributed to shareholders for example. That's another possibility.

And the last one I might add is the issue of carbon pricing, which I don't want to get into too much detail on right now, but it's an important issue for manufacturers. Our membership is mixed on their views on this. We believe, as an organization, that the most important part is if you're taking carbon tax revenue out of companies you're removing their ability to invest in mitigating technology and mitigating machinery and equipment. We would like to see all money that is removed from those manufacturing businesses be given back on a dollar for dollar basis through either other tax cuts or investment incentives in new machinery and technology or even potentially if there's a list of preapproved —

Senator Eaton: In other words, they would invest in cleaning up their own company instead of paying the carbon tax?

Mr. Holden: Absolutely. When you take the money away from them you remove their ability to invest in making improvements. And something that redirects that money towards actually making improvements would not only make them more productive, it would also reduce their environmental footprint at the same time.

Senator Eaton: Thank you.

Senator Pratte: Mr. Holden, about the changes that were changes to the reform package that were announced mid-October, you did say in your presentation that your organization was pleased that those changes addressed many of the specific concerns that you had.

Many of the witnesses that we heard here in the Atlantic provinces and out West and in Ottawa told us that although they welcome those changes, they felt in many cases that the changes were insufficient or in many cases were very insufficient and that they still wanted that the whole package be shelved. So would you please elaborate on what your organization's views are on the whole reform package, especially on income sprinkling and on passive income after the changes that were brought in in mid-October? Do you feel that now that those changes have been made that this package is acceptable?

Mr. Holden: I would say that we are less concerned about them than we were previously. I wouldn't say that they're necessarily acceptable. The issue of passive income, our main concern when that issue first came out was about what effect that would have on businesses growing. We're still concerned about that. We haven't seen what the proposed changes are going to look like beyond the broad statements of allowing businesses to retain $50,000 or something that's going to target only the top 3 per cent. We don’t really know what that looks like so we can’t comment on it as it stands right now.

On the issue of income sprinkling, our main concern with that was with the complexity of how you would determine what would be a fair wage or under what conditions a person would be eligible for income sprinkling. We still have some of those concerns but they’re not quite as outstanding as before.

I think the main point I’d like to make though is that these particular changes I don’t think are that important. I think that the finance department’s direction is misguided in this area. This is not a high priority. As your previous panel mentioned, these are not the super wealthy who are dodging taxes.

Sorry, I lost my train of thought there which happens to me a fair bit.

The fact that this is a low priority and I think that it would do more harm than good as it stands now. So we’re not in favour of the proposals as they stand now, but I think that given the importance of investment and growth in this country we think that they should be dropped and focus on more comprehensive and holistic reforms.

Senator Pratte: Thank you. So you’re an economist and you do paint quite a negative picture of the investment situation in Canada, and those numbers are what they are, and yet there have been, in recent months, relatively positive news in Canada, the GDP growth, well not necessarily the last two months, but in general in 2017. GDP growth has been strong. The unemployment rate is quite low. So there seems to be sort of a contradiction between those big statistics that we usually use as an indicator in unemployment and GDP growth and those investment numbers that you mentioned. How would you explain this apparent paradox?

Mr. Holden: I would explain it by Canada has had solid economic growth so far in 2017. That’s absolutely true. If you look at when that growth took place, however, most of it was pretty much from a year ago, last November through to about May. Canada was travelling along at around 2 per cent growth or less than 2 per cent growth for about three years in a row, and we had about a six month blip of solid growth in about the 4.5 per cent range. Since about June there has been right back down to the 2 per cent growth. A lot of this has to do with the fact that with poor economic growth it doesn’t take much for the next year to look a lot better.

I live in Alberta and Alberta is supposed to be leading the country in GDP growth this year and next year, but most of that is just because it had done so badly the previous year that anything looked like an improvement. And in Canada it’s not as direct as that, by any stretch, but it’s a short term blip. I don’t think looking ahead we’re going to be seeing much more than going back to the 2 per cent growth.

The investment stuff that I highlighted points to a slightly more subtle issue though and I think that is what your long term overall growth trend is going to be. If we’re not investing in our companies and businesses are not moving to Canada and local companies aren’t expanding, it may not necessarily see the economy drop off a cliff, but it will result in lower long term growth. So just to make up some numbers, if the economy were to grow at a steady state of 2.5, 2.6 per cent and that was sort of the status quo give or take, if that dropped to 2.2 per cent on a year to year basis we wouldn't really notice that much but it would add up over time. And it is that growing wedge in growth rates that we're concerned about in future.

The Chair: Thank you.

Senator Neufeld, please.

Senator Neufeld: I'm sorry I had to step out for a minute, so maybe this has been asked.

Further to Senator Pratte's questions, when you talk about business capital investment has fallen by 11.6 per cent and manufacturing 15.3 per cent, and you talk about GDP growth, how does the federal government investment in infrastructure affect those numbers? So the federal government has borrowed billions of dollars in the last couple of years and invested in infrastructure, at least that's what I understand. So would that make a difference in Canada's GDP growth at all in those numbers but business investment has fallen?

Mr. Holden: Yes, it would make a small difference but it would just be a small difference. I think the important benefit that comes out of infrastructure investment is, first of all, we believe it would have to be actual economic infrastructure — roads, bridges, ports, intermodal linkages, anything along those lines, things that would improve Canada's productive capacity. Investments in those areas will yield a short-term benefit, a small short-term benefit in terms of an uptake in GDP, but it's their longer term benefit that's of more value.

Senator Neufeld: Those numbers really bother me and it should bother all Canadians. What do we have to do to change that? What does Canada have to do to actually turn that around?

Mr. Holden: I think what we need to do is work to make Canada an attractive place for businesses to want to be, and how we do that is making sure that we have solid access to the U.S. and to other markets, solid access to domestic markets, a highly skilled and productive work force, and a competitive tax structure and low business cost scenarios like utilities, electricity costs and the reasonably low regulatory burden, not in a way that compromises people's health and safety, but one that focuses on outcomes rather than on prescriptions.

So there isn't any one answer to your question. I think there's a large series of things that need to be done. But you know if we're here talking about tax reform today I think that we need tax policies that encourage businesses to grow, not just rewarding small businesses for being small, but encouraging them to take the next step. As an important corollary, we also shouldn't abandon those kinds of policies the moment the businesses grow up and reach a certain size. At the end of the day we want people to start up small businesses. We want them to grow into medium size businesses. We want medium to grow into large. We want large to grow into multi-national. Those should all be positives. Those should all be objectives of ours not just kind of cut things off at a certain point in terms of the investment supports that are being offered.

Senator Neufeld: One thing you mentioned was electricity prices. That's interesting because I think we compete well, other than maybe Ontario right now, with our neighbours south of us. In fact, I think we compete very well. I know the electricity rates relatively well and I think we do compete there on a level playing field.

Mr. Holden: I think that's fair and I think that one of the challenges with these kinds of tax and competitiveness issues is that there's a larger overarching problem but the specific elements of that problem vary depending on where you happen to be. It is an issue in Ontario. It's an issue in Manitoba, I believe, but elsewhere not as much.

Senator Neufeld: Thank you.

The Chair: Senator Oh, please, to be followed by Senator Cools.

Senator Oh: Thank you, chair.

I want to bring the question down south. With the U.S. tax reform coming up, the NAFTA talks are in trouble and our economy is so tied up with the U.S. Do you think we should have a complete review of our tax reform or tax policy, a comprehensive study? I think now we're at a crossroad with the U.S. tax. They have a businessman as President and he knows what he is doing. He's lowering taxes to attract investment. Look at his recent trip to China. He brought home the biggest contract ever for the past four presidents. So small business owners are the engines of our economies. Do you think that we should completely take an overhaul look at the long term? What are we going to do now? The U.S. is moving in a direction. Should we tap into it or whatever? Can you comment on that?

Mr. Holden: Thank you for the question.

Yes, I would have said we needed a comprehensive tax review anyway, and I think that the factors that you mentioned just underscore the urgency with which we need to do that. I mean whether or not Canada's headline tax rates are competitive with the U.S. right now they're still failing to attract investment and NAFTA is going to accelerate that process or NAFTA uncertainty is going to cause more businesses to pause before they decide to locate here because if any part of their business is tied up in trying to export into the United States then it's a safer bet just to locate into the U.S. to begin with and avoid the headaches. That's something that we're concerned about. Tax reform in the U.S. will only make that more attractive. So I absolutely do think it's necessary for us to have a good long hard look at our tax system and make sure that we are creating a system that is competitive, that encourages growth, but still gives governments the revenue they need to provide important services.

Senator Oh: So if the U.S. lowered their taxes we are going ahead with the reform. So do you think there would be a capital flight going, brain drain going south of the border?

Mr. Holden: It's hard to say right now without specific changes being explicitly set out and compare to what things are like in Canada. I think that that is a very real risk and it may not be a dramatic capital flight and a dramatic brain drain, but it certainly will give businesses a reason to consider it more closely than they would have in the past. If it's not a one-time catastrophic capital flight, it certainly will provide a slow flow of capital out of Canada into the U.S.

Senator Oh: Thank you.

Mr. Chair: Senator Cools, do you have a question?

Senator Cools: Not so much a question. Today we were hearing from doctors and the whole notion of physician recruitment and the impact that so many things are having on the healthcare system. Somebody put this magazine, which is from the Fredericton Chamber of Commerce. Lo and behold, I'm not a magazine reader, I just opened it up and here on one of the pages the headline is "Physician Recruitment Supported by Committed Community Members" which supports all the things that the doctors were saying earlier today. I find that very interesting. So I just wanted to note it for the sake of the committee. I think we're going to have to grapple with this because the real issue before us is going to be at the end of the day, the tax changes but also shortage of doctors and healthcare.

Thanks.

The Chair: Thank you.

Senator Marshall, please, to conclude.

Senator Marshall: Just listening to you talk and thinking about the U.S., I'm not holding them up now to be a model of perfection, but if you look at what's happening down there, what's dominating all the discussion there? Tax reform, renegotiation of NAFTA. It seems like whatever we hear coming out of the States is aimed towards promoting business. That's my opinion anyway. So they're real go-getters for business. Then you look at us and our government, I'm not just saying this government, you can go back years, we seem to be focused on public sector spending, imposing new taxes, complicating our tax code. It just seems like the total overall environment is completely different. Do you think that makes a difference?

Mr. Holden: I think it makes a huge difference. As you said before, nobody, and I don't want to suggest that I'm holding the United States up as a model country in all respects by any stretch of the imagination. I don't think that necessarily gutting environment regulations in the name of business growth is a good long-term move by any stretch of the imagination. But in the sense that the policies that you mentioned are creating the impression that it is a business oriented and growth oriented move, whether it's NAFTA or tax reform, I think that is absolutely true. In that sense alone we need to be mindful about what the United States is doing because our two economies are very closely integrated. The U.S. accounts for about three-quarters of our trade and most of that trade is not in finished goods, it's in parts moving back and forth across the border dozens of times. If a large competitiveness gap emerges over time between the two countries we're going to see less and less of that kind of movement and more of it just heading straight down to the United States and us buying finished goods from them.

Senator Marshall: They're looking at businesses to drive their economy and we're up here looking at government to drive ours. We're looking at the Canada Child Credit and infrastructure spending to drive our economy. It just seems like they're down there and we're over there and I don't know which is going to yield the better result. But when I look at what you have in your opening remarks...

Mr. Holden: I think the most important thing to remember out of all this is where does the money come from for those things? There's nothing wrong with expanding Child Tax Credits or addressing infrastructure. If those are social goals that we have as a country then that's great. But the issue is that we need to pay for them somehow. You pay for them by having a strong private sector. And it's been mentioned before and I'm sure you heard already, once you increase taxes beyond a certain point you start to lose money as a government because people will find a way, businesses and individuals will find a way to avoid paying as much tax. I think in some cases we've reached our limit on the personal income tax side in terms of how much revenue you can squeeze out of people before they take evasive action.

So it's the private sector growth we want to generate, and the healthier economy we have the more easily we are able to afford all of these things. I think that should be the overarching objective.

Senator Marshall: Well based on the witnesses we've heard during these hearings these proposed changes are going to damage small businesses to a great extent. So in the long term it's not going to bode well for the bigger stage that you're talking about in your remarks. Thank you.

The Chair: Before we adjourn, I have a question in view of your opening remarks, Mr. Holden. You mentioned that Canadian business invests less than any other country in the OECD except Greece. That's the statement you made. Then when we're looking at tax reform and modernization of what Canadians are somewhat concerned with, do you think, with your experience, that the passive income threshold of $50,000 is a solution to this problem?

Mr. Holden: No, I don't. I think that that passive income threshold of $50,000 is designed to allow individuals who own small businesses to be able to use their business as a vehicle for retirement savings that are other ways of generating income for themselves individually or for smoothing out flows in income from one year to the next.

As I understand the proposed changes, as long as the money is retained within the corporation, within a CCPC, most of these changes wouldn't have any material effect. And I think that it's pretty much for the individual who owns the business in the amount of income they extract from it as a dividend paying to themselves or their shareholders that that's where the main benefit or the main impact of that change would come in allowing them greater latitude for retirement savings, personal reward for entrepreneurship and risk taking and things like that.

The Chair: Mr. Holden, thank you very much for sharing your opinions and comments. If in the event you want to add to the study and our mandate from the Senate, you can do it through the clerk.

Do you have any closing remarks?

Mr. Holden: I have one closing remark, and that is to say that we as an organization are going to be undertaking a study on comprehensive tax reform ourselves as a way to contribute to this public policy discussion here in the country. We are in the initial stages of that. However, we're doing some work right now within the organization on the shred program, specifically, and on research and innovation tax credits, and once that is done we're going to be moving on to a broader comprehensive tax reform. We're in the middle of drafting a survey to our members on specific tax issues and once that report is finished we'll be happy to share a copy with this committee.

The Chair: Thank you very much.

Honourable senators, after we adjourn, we will meet in the lobby of the hotel so that we can have a visit of the industrial sites here in Saint John.

(The committee adjourned.)