

**Saskatchewan Party Caucus  
Summary of Proposed Recommendations  
Independent Business Tax Review, 2005**

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**A. General Corporate Income Tax (CIT):**

**Background:**

For 2005, the Saskatchewan CIT on general corporations is 17% -- the highest CIT in Canada.

Saskatchewan has established a special CIT rate of 5% on the first \$300,000 of net income earned by Canadian Controlled Private Companies (CCPC) incorporated in Saskatchewan -- often referred to as the Small Business Tax. The Calvert government has committed to increase the income threshold to \$400,000 by 2007.

Saskatchewan's CIT on profits from manufacturing and processing activities greater than \$300,000 is 10%.

**Recommendations:**

1. Reduce the Small Business Tax to 0% on the first \$400,000 of net income over four years;
2. Reduce the General CIT rate from 17% down to 11.5% over four years;<sup>1</sup> and
3. Expand the Manufacturing & Processing Profits Tax Reduction to include resource companies following the successful negotiation of a new Energy Accord with the federal government that removes resource revenues from the calculation of equalization entitlements.

**Impact:**

Eliminating the Small Business Tax (SBT) would make Saskatchewan the first Small Business Tax Free Zone in Canada.

Other Provinces with Competitive SBT Rates<sup>2</sup>:

Province	Rate	Threshold
Alberta	3.0%	\$400,000
B.C.	4.5%	\$400,000
N.B.	2.5%	\$425,000 <sup>3</sup>

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<sup>1</sup> For 2005, Alberta has the lowest General CIT rate at 11.5%. Quebec's CIT is 8.9% but there is no small business tax reduction.

<sup>2</sup> See attached Appendix I for a Schedule of 2005 tax rates for all provinces.

<sup>3</sup> New Brunswick has the lowest SBT rate and the highest income threshold in Canada and has committed to reduce its SBT rate and increase its threshold over the next three years as follows: July 1/05 -- 2.0% up to \$450,000; July. 1/06 -- 1.5% up to \$475,000; July 1/07 -- 1.0% up to \$500,000.

Reducing the General CIT from 17% to 11.5% would take Saskatchewan from having the highest General CIT rate in Canada to having the lowest rate (tied with Alberta as of May 2005).

Expanding the M&P Profits Tax Reduction to include resource industries would give Saskatchewan's mining, oil and gas and Manufacturing and processing industries the lowest CIT rate west of Quebec.

**Cost:**

Reducing the general CIT rate from 17% to 11.5%, increase the small business income threshold and reduce the Small Business Tax rate to zero over four years will cost approximately \$189.9 million per year when fully implemented (see attached spreadsheet).

*Note: No information is available to estimate the cost of expanding the M&P Profit Tax Reduction to resource companies. However, the significant increase in annual provincial government revenue as a result of a new Energy Accord will allow the province to reduce taxes on the resource companies that provided approximately 1 in every 7 dollars of provincial government revenue in 2004.*

**Balanced Budget Commitment:** All three tax reduction recommendations would be phased in over four years within a balanced budget (expansion of M&P Profits Tax Reduction to Resources is contingent on New Energy Accord). If provincial revenues are insufficient to cover expenditures in any given year, the implementation timetable would be delayed.

## **B. Corporate Capital Tax (CCT):<sup>4</sup>**

**Background:**

Saskatchewan's Corporate Capital Tax rates are the highest in Canada:

General and Resource Corps.:	0.6% on taxable capital of \$10 million/\$20 million <sup>5</sup>
Small Financial Corps:	0.7% on institutions with < \$400 million in taxable capital
Large Financial Corps:	3.25% on institutions with > \$400 million taxable capital
Resource Surcharge:	2.0%/3.6% of sales minus basic CCT payable <sup>6</sup>

<sup>4</sup> While a coordinated program of CCT reductions will certainly increase economic growth and tax revenue in Saskatchewan, no assumption with regard to increased government revenues is built into the costing estimates except those projected by Saskatchewan Finance in the 2005-06 Budget and performance Plan Summary.

<sup>5</sup> The exemption increases to \$20 million for corporations that pay all of their salaries and wages to employees of a permanent establishment in the province.

<sup>6</sup> Resource corporations pay a resource surcharge of 3.6% of sales minus CCT payable on sales from wells drilled before October 1, 2002. The resource surcharge on wells drilled after October 1, 2002 is 2.0% of sales minus CCT payable.

## **Recommendations:**

4. Eliminate CCT on new investment for four years
5. Reverse Decision to Impose the Resource Surcharge on Income Trusts
6. Phase out the CCT on General Corporations and Resource Corporations over four years.

## **Impact:**

Saskatchewan's corporate capital tax structure is the most aggressive in North America. Alberta and B.C. have no CCT and no resource surcharge. Manitoba's CCT is 0.3% on capital over \$5 million. Corporations with more than \$10 million pay a surcharge of 0.2% thereby increasing the rate to 0.5%.

Most tax experts and virtually the entire investment community identifies CCT as the most significant deterrent to new capital investment in Saskatchewan.

The federal government has already committed to phase out the federal Corporate Capital Tax gradually over the next number of years although no specific dates have been set.

Implementing the CCT reductions proposed above will send a critical signal to the North American investment community that Saskatchewan is ready to grow.

The Saskatchewan Party Proposal will create an investment environment that competes well with Alberta, B.C. and most American states.

## **Cost:**

The elimination of CCT on new investment for four years carries no cost as it is a "new growth tax cut" on investment that does not yet exist and is therefore not yet taxable to the province.

The reversal of the Calvert government decision to impose the resource surcharge on income trusts as of April 1/05 will result in forgone government revenues by \$20 million in 2005-06 and \$40 million in 2006-07 according to Department of Finance estimates.

The elimination of the CCT on General and Resource Corporations will cost approximately \$154.7 million when fully implemented.

**Balanced Budget Commitment:** The Corporate Capital Tax reductions proposed above would be phased in over four years within a balanced budget. If provincial revenues are insufficient to cover expenditures in any given year, the implementation timetable would be delayed.

## C. Manufacturing and Processing Investment Tax Credit (ITC):

### Background:

Manufacturing and processing companies get a non-refundable tax credit equal to 7% on the acquisition of qualifying manufacturing and processing equipment and facilities. Since the M&P ITC is non-refundable, it is only available to companies with positive net income. As a result, the ITC is not bankable for many smaller businesses and most start-ups. It also increases the overall cost of capital and creates a barrier to new business start-ups or existing business expansions.

### Recommendation:

7. Make the Manufacturing and Processing ITC a refundable tax credit through interim application every quarter.

### Impact:

By making the ITC a refundable credit, it does not have to be claimed against net income and is therefore bankable even when the corporation is not profitable. (Quarterly claims could be paid at a rate of 80% with the outstanding balance paid after year end to ensure compliance)

The ability to apply for the M&P ITC on a quarterly basis strengthens business cash flows, reduces the cost of capital and removes a significant barrier to growth especially for smaller and/or start-up businesses.

Since Alberta does not have a PST, companies in that province are not exposed to the additional capital costs.

### Cost:

In 2005, the M&P ITC is estimated to cost \$17.5 million. While it is difficult to accurately project how much an expanded M&P ITC would cost if it was made refundable and payable quarterly, we estimate the cost would at least double in the first year and then grow at about the rate of economic growth in each year thereafter. This estimate would make the cost of the proposal \$18.3 million when fully implemented.

	2005-06	2006-07	2007-08	2008-09
<b>Sask. Party Proposal</b>	\$17.5 million	\$35.0 million	\$35.9 million	\$36.9 million
<b>Calvert Government</b>	\$17.5 million	\$18.0 million	\$18.4 million	\$18.6 million
<b>Incremental Cost</b>	\$0	\$17.0 million	\$17.5 million	\$18.3 million

**Balanced Budget Commitment:** Changes to the M&P ITC would be implemented over four years within a balanced budget.

## D. Research and Development Tax Credit:

### Background:

Most provinces in Canada offer some kind of refundable R&D tax credit on qualifying purchases.

In 2005, Quebec offers a refundable 35% R&D tax credit. Ontario offers a 20% refundable credit. Three provinces offer a refundable 15% credit. Manitoba and Saskatchewan offer a non-refundable 15% tax credit.

### Recommendation:

8. Increase the R&D Tax Credit to 20% and make it a refundable credit through interim application every quarter.

### Impact:

One of the important themes in Saskatchewan Party leader Brad Wall's 2004 economic paper, *The Promise of Saskatchewan: A New Vision for Saskatchewan's Economy*, is a commitment to support innovation in Saskatchewan. Research and development is a fundamental component of innovation whether it occurs at the University or in the development facilities of private companies.

Increasing the R&D tax credit and making it refundable on a quarterly basis supports private sector innovation while reducing the cost of capital and removing a barrier to growth. (Quarterly claims would be paid at a rate of 80% with the outstanding balance paid after year end to ensure compliance)

### Cost:

As with the expansion of the M&P ITC, it is difficult to estimate how much a refundable 20% R&D tax credit would cost. In 2005, the provincial government estimates the current 15% non-refundable credit will cost \$10 million. We estimate the cost of our proposed changes would increase the annual cost of the R&D tax credit to approximately \$16.6 million (33% increase due to the increase in the credit and another 25% as a result of the refundable nature of the credit) in the first year and then increase by a rate equal to economic growth in Saskatchewan thereafter:

	2005-06	2006-07	2007-08	2008-09
<b>Sask. Party Proposal</b>	\$10.0 million	\$16.6 million	\$17.0 million	\$17.5 million
<b>Calvert Government</b>	\$10.0 million	\$10.3 million	\$10.5 million	\$10.8 million
<b>Incremental Cost</b>	\$0	\$6.30 million	\$6.50 million	\$6.70 million

## **E. Incentives for Investment in the Livestock Processing Industry:**

### **Background:**

As the 2005 SARM Annual Convention, Saskatchewan Party Leader Brad Wall called for an incentive to promote investment in livestock processing capacity similar to the incentives related to Saskatchewan-based Labour Sponsored Venture Capital Fund (LSVCF).

### **Recommendation:**

9. Establish a 20% tax credit (similar to current LSVCF provisions) on investments in Saskatchewan-based livestock processing capacity.

### **Impact:**

Saskatchewan's livestock industry has been devastated by the BSE crisis and the closure of the American border to most Canadian cattle. Development of new markets and adding local processing capacity are two key actions that must be taken to address the challenges facing the livestock industry.

The provision of an incentive to drive investment in value-added processing in Saskatchewan will assist the livestock industry and contribute to the growth and sustainability of the provincial economy.

### **Cost:**

This Proposal is a new growth tax cut because it proposes to forgo tax on investment that does not currently exist and therefore is not currently taxed by the province. Since no existing government revenue would be given up, the incremental cost of the Livestock incentive is zero relative to current year government revenues.

## **F. Other Issues That Impact Business Competitiveness in Saskatchewan**

Two other important factors that directly influence new business investment and private sector economic growth are property taxes and labour laws. Also, resource royalties are an important consideration because of the prevalence of oil and gas industry in Saskatchewan. Unfortunately, neither of these factors was included in the mandate of the Business Tax Review Committee.

### **Property Taxes**

Property taxes are the largest tax on capital in Saskatchewan. The high rates at which business taxes are applied in Saskatchewan create a significant barrier to private sector investment growth, job creation and new capital investment. Any attempt by the province to evaluate and recommend

changes to the mix of taxes and fees assessed against Saskatchewan businesses must include property taxes if it is to be effective.

## **Labour Laws**

Saskatchewan's labour laws are recognized across the continent as lacking balance and therefore have contributed to Saskatchewan's reputation as an anti business jurisdiction. Saskatchewan must review provincial labour legislation to ensure a legislative environment and a Labour Relations Board that respects the principles of transparency and accountability; provides high quality, safe and healthy workplaces; and balances the interests of employees and employers while promoting the continued growth of Saskatchewan communities and the economy.

## **G. Equalization Reform**

The unfair manner in which Saskatchewan is treated with regard to calculation of federal equalization entitlements has been well documented. The Saskatchewan Party has joined with the Calvert Government in calling for a number of changes to the equalization formula that will address the unfairness of the current program and also result in a large increase in provincial equalization entitlements in the short term.

The Saskatchewan Party has also joined with the Calvert government in calling for the negotiation of a Saskatchewan Energy Accord similar to the Accord recently signed between the federal government and the provinces of Newfoundland and Nova Scotia. The Atlantic Accord effectively excludes off-shore oil and gas revenue from the calculation of provincial equalization payments and will therefore generate more than \$3.5 billion in new revenue for Newfoundland and Nova Scotia by 2012.

A Saskatchewan energy Accord structured in a similar manner to the Atlantic Accord would generate between \$400 million and \$1 billion per year for Saskatchewan because it would end the federal government's practice of clawing back up to 108% of Saskatchewan's annual oil and gas revenues. The new revenue could be used, in part, to create the most competitive climate in Canada for new investment, job creation and economic growth while investing in important government services including health care, education, social services, infrastructure, environmental protection and community safety.

While the proposals presented above do not depend on a new equalization agreement with Ottawa, the increased revenues from changes to the equalization program and the establishment of a Saskatchewan Energy Accord will ensure the business tax reductions could be achieved on the proposed timetable. In the event the Calvert government fails to negotiate a new equalization deal, the proposed tax reduction plan may require a longer implementation period to ensure the provincial budget remains balanced.

## **H. Conclusion:**

Saskatchewan is at a crossroad. There is a choice to be made.

We can choose to continue to grow the size of government and increase government presence in the economy. This is the choice of the current provincial government and it has been the choice of successive government of three different political stripes over the past 6 decades.

It is an approach that has failed Saskatchewan.

Fortunately, Saskatchewan has another choice.

We can choose to break out of six decades of our children and grandchildren leaving to find opportunities somewhere else; six decades of big government and high taxes and declining quality of life.

We can choose to compete and win creating an economic climate that welcomes private sector business growth, new investment and the entrepreneurial spirit.

The Saskatchewan Party believes the proposals we make today will establish a solid foundation upon which to finally deliver on the 100 year old Promise of Saskatchewan.