

June 4, 2008

Mr. Rob Merrifield, Chair
House of Commons Standing Committee on Finance
304 Justice Building
House of Commons
Ottawa, ON K1A 0A6

Dear Mr. Merrifield:

The Certified General Accountants Association of Canada (CGA-Canada) understands that the House of Commons Standing Committee on Finance is currently undertaking a study and hearing from witnesses on the structure of Canada's federal revenue-raising system. CGA-Canada welcomes the opportunity to participate in this consultative process by providing its views on this important subject.

CGA-Canada is a national professional accounting organization that represents 68,000 CGAs and students. The association sets standards, develops education programs, publishes professional materials, advocates on public policy issues, and represents CGAs nationally and internationally. CGA is the fastest-growing accounting designation in Canada. The CGA designation focuses on integrity, ethics and the highest education requirements. Recognized as the country's accounting financial leaders, CGAs provide strategic counsel, leadership and direction to all sectors of the Canadian economy. This year marks the 100th anniversary of the founding of the CGA designation in 1908.

In terms of the structure of Canada's federal revenue-raising system, there are two specific issues that CGA-Canada wishes to address – tax simplification and tax harmonization.

- **Tax simplification**

Canada's *Income Tax Act* has grown from 11 pages in 1917 to 2,860 pages today (index excluded). What was promoted as a "temporary" measure to underwrite the war effort has become an entrenched feature of the Canadian economy, built on a patchwork of unnecessarily

complex and cumbersome rules that often require the services of professionals such as accountants and lawyers.

According to a new study undertaken by PricewaterhouseCoopers (PwC), companies in Canada are subject to 49 different taxes and 18 other payments to governments at the federal, provincial and municipal level. In addition to this complexity, companies are also subject to more than 200 possible "taxing points" – that is, the number of tax obligations a business would be required to fulfill if it were subject to all taxes in all jurisdictions. The PwC survey found that these companies spent \$2.1 million a year to comply with these taxes, and the average time spent on compliance was the equivalent of 11 full-time employees dealing solely with tax compliance.

When CGA-Canada consulted with stakeholders, practitioners and publicly listed Small and Medium-sized Entities (SMEs) (see CGA-Canada's 2006 report entitled *Tackling Compliance: Small Business and Regulation in Canada*), it was reported that almost 86 per cent of SMEs rely on an external accountant to assist with taxation filing requirements. In turn, tax practitioners feel strongly that filing requirements are complex, and that decisions and interpretations are difficult to obtain on a timely basis. Moreover, for government, the system is costly administer. A recent publication by the Fraser Institute shows that Canadians spend a significant amount of time, energy and money complying with Canada's tax system – at an estimated cost of up to \$30 billion annually.

The subject of taxation has always been of importance to CGA-Canada, and our association has put forward many tax-related recommendations to the House of Commons Standing Committee on Finance through our written submissions and annual appearances. CGA-Canada has called for redefining fair and competitive taxation, presented suggestions on how to ensure the consistent application of tax legislation, and supported major structural reforms to the tax system to improve Canada's productivity relative to its trading partners.

CGA-Canada believes the federal government ought to appoint a panel of experts to undertake a fundamental review of the tax system. Furthermore, the panel should be given a specific mandate to overhaul and simplify the *Income Tax Act* by consulting widely in the context of a public forum and bringing forward third party recommendations to the Government of Canada, to be tabled in Parliament.

Perhaps one of the most significant challenges with simplifying taxation is identifying a starting point. Canada's tax system is massive, the legislation is excessively comprehensive and the volume of interpretive materials is overwhelming. Below are a few guiding principles and suggestions to approaching the exercise of tax simplification:

A. Remove outdated and irrelevant sections of *Income Tax Act*

Capital Cost Allowance (CCA). There are at least 52 classes for the CCA, most of which are not relevant to the average business or taxpayer. For example, many of the CCA classes refer to dates of acquisition, and many of these dates are twenty or thirty years in the past. If any of these assets were to still exist, their value would likely have depreciated to zero, rendering the CCA irrelevant. In addition, the practice of using the CCA system as an incentive for businesses to invest in certain sectors of the economy should be reviewed. This is one of the main reasons why the CCA system has become so complicated. CCA classes and rates should be realistic and reflect economic conditions as well as accounting criteria. Incentives to industry ought to be provided through other means – such as tax credits, subsidies or other non-CCA based provisions.

Alternative Minimum Tax (AMT). Numerous pages of legislation are devoted to this tax which does not appear to increase government revenues on a long term basis or in any measurable way. In most cases, if a taxpayer is assessed and pays AMT, he or she is entitled to a future refund equal to the amount of AMT paid. This begs the question: what is the relevance of such a tax?

Capital Gains Exemptions. These provisions are not only complex but frustrating in that they appear to emphasize why a taxpayer is *not* entitled to the exemption or why the amount of the exemption *should* be reduced. For instance, if a taxpayer has claimed more rental losses than investment income in the past, or has written off an allowable business investment loss, the taxpayer's exemption is reduced or eliminated. There are numerous other rules that limit one's ability to claim the exemption.

Other provisions. There are a number of provisions that specify a dollar amount that is not realistic according to today's standards. For example, there is a provision under the *principal residence rules* relating to farmers which allows a farmer to claim up to \$1,000 per year of ownership as his or her claim for a principal residence exemption. If one is to consider a farm house purchased 30 years ago, that has likely increased to \$300,000 or \$400,000 in value, this dollar figure is not practical. Similarly, the threshold for *capitalization of small equipment* – which took years to be increased from \$200 to \$500 – is still far too low and out of touch with present day reality. In fact, the *Income Tax Act* is cluttered with issues such as these that are, for the most part, no longer relevant. Updating the dollar amounts would make it easier for one to calculate and would not require valuations and allocations, which can subsequently be questioned by CRA. In short, provisions within the *Income Tax Act* ought to demonstrate currency and relevancy.

B. Codify the *Income Tax Act*

The number of paragraphs, subparagraphs, sections, subsections, etc. is mind-boggling and the way in which they are ordered or arranged is difficult to follow. Consideration ought to

be provided to re-arranging the *Income Tax Act* so that it is easier for the average taxpayer to understand. Every taxpayer must abide by the rules, but not every taxpayer can afford a specialist like a tax lawyer to decipher the Act.

C. Re-write the *Income Tax Act* in plain English and French

Principle C builds on Principle B: make it easier for the Canadian taxpayer to understand; lessen the need for interpretation; this equates to greater compliance.

According to tax specialists, one of the most complex areas of income tax legislation involves corporate transactions, such as re-organizations, stop loss rules, anti-avoidance and related provisions. Moreover, one of the main reasons why these sections of the *Income Tax Act* have become so complicated is that they have been constantly expanded and amended since their initial introduction. Some tax practitioners say various sections of the Act have reached a point where they need to be repealed and re-written.

In addition, the complexity of the GST legislation and regulations as well as the phenomenal growth in same since its introduction in 1991 warrants attention. This too affects every business in Canada – large, medium, small and micro. It also speaks to the benefits associated with sales tax harmonization, an issue further discussed below.

D. Manage the taxation burden

Today's *Income Tax Act* is 260 times the size it was when it was first introduced in 1917. That's because a plethora of additions along with regulations have been made to the Act, while next to nothing has been removed since its inception.

The provincial government in British Columbia, through its Regulatory Reform Initiative, has set a zero-net increase target – that means for every new regulatory requirement introduced, requirements in other areas must be streamlined and simplified.

It would be worthwhile to consider applying the same logic to the *Income Tax Act* – every addition ought to be accompanied by a subtraction of some form, by removing or streamlining one rule, provision or section that is outdated or irrelevant.

The bottom line: Canada needs a fairer, more efficient tax system that has a simple tax base. Tax simplicity makes use of fewer resources – such as time, energy and money - and makes it easier for taxpayers to comply, resulting in a more secure tax base with predictable revenue.

As aptly stated by Sheila Fraser, Auditor General of Canada:

"For the Canada Revenue Agency, increasing taxpayer compliance is a measure of success comparable to increasing net profit in a private-sector business...both are bottom-line indicators of an organization's effectiveness."

CGA-Canada believes that one way to move toward a simpler, fairer, more efficient and basic form of taxation is through a Harmonized Sales Tax (HST).

- **Tax harmonization**

There has been a great deal of discussion on the topic of harmonizing federal and provincial sales taxes – that is, replacing provincial retail sales taxes (RST) with the federal Goods and Services Tax (GST).

Think-tanks such as the C.D. Howe Institute have studied the effects of the HST reform in the Atlantic provinces when Newfoundland and Labrador, Nova Scotia and New Brunswick moved to the HST in 1997, and concluded it would be in the best interests of the other provinces to follow suit. In its April 2008 publication *"Slicing the Pie: Federal Assistance for Provincial Sales Tax reform,"* the C.D. Howe Institute states at the very outset that *"few tax changes offer as much economic promise as replacing provincial retail sales taxes (RST) with a value added tax like the federal Goods and Services Tax (GST)."* The Fraser Institute has also been an advocate of the HST, turning its attention to the province of Ontario and noting the *"enormous economic benefits available to Ontarians through harmonization"* in one of its December 2007 articles and commentaries. CGA-Canada adds its voice to these and other prominent national organizations like the Canadian Chamber of Commerce, the Canadian Council of Chief Executives and the Canadian Federation of Independent Business - all of which recognize the value of a harmonized sales tax.

So, what are the benefits of a Harmonized Sales Tax (HST)?

- Simplifies Canada's tax structure
- Increases compliance rates and lowers compliance costs for taxpayers
- Lowers administrative costs for government
- Reduces red tape for businesses
- Strengthens Canada's tax system

Basically, harmonization simplifies the tax system. Instead of dealing with two different tax rates and tax bases as well as two separate tax administrations, consumers and businesses deal with only one tax rate and tax base, one set of rules and a single administration. The differing tax bases of the PST (provincial sales tax) and GST leads to a situation whereby businesses, for example, are forced to operate with two sets of sales records and, as a consequence, additional compliance and reporting costs. It stands to reason that businesses – and consumers – would

be more apt to comply with the rates and rules under a single sales tax system which is simple in its nature.

At present, there are five provinces (British Columbia, Saskatchewan, Manitoba, Ontario and Prince Edward Island) that still levy an independent RST. CGA-Canada is pleased to note the federal government's willingness to work with these five remaining provinces to help facilitate the transition to provincial value-added sales taxes harmonized with the GST, as indicated in *The Budget Plan 2008*.

Sales tax harmonization on a national scale would give Canada the strong tax advantage it seeks in all provinces – it would improve business tax competitiveness and attract new investment as well and increase Canada's productivity and competitiveness.

- **Recommendations**

That the federal government:

1. Undertake the immediate and necessary steps to simplify Canada's tax code; and
2. Work with the remaining provinces that levy retail sales taxes to move to a value-added tax (VAT) with the same base as the federal GST.

We thank you for the opportunity to comment, and remain available for further discussion on any matter pertaining to Canada's tax structure.

On a final note and in the spirit of contributing to this discussion, please find enclosed a copy of a recent brief completed by CGA-Canada (*Is Cutting the GST the Best Approach?*) which draws on the familiar debate of consumption vs. income and capital taxes as a means to providing the most appropriate form of tax relief to Canadians. I trust that Finance Committee members will find this of interest and assistance to their deliberations.

Sincerely yours,

Original Signed by:

Carole Presseault, Vice-President
Government and Regulatory Affairs

Encl: *CGA-Canada Issue in Focus: Is Cutting the GST the Best Approach*