

The Chamber

Building the Best Business Climate in Canada

SUBMISSION TO THE PERSONAL INCOME TAX REVIEW COMMITTEE

Part I - Efficient Resource Management

The Saskatoon and District Chamber of Commerce has led the campaign over the last several years that would have this province assume its rightful position as a leader in Western Canada and as a true player in the global economy. This is a resource rich province with inherent beauty, rich diversity of culture, and significant potential for growth. Yet over time, we have seen other jurisdictions that arguably have less potential than Saskatchewan, take advantage of the benefits of economic growth, jobs for youth, and a positive climate for investment. Significant volumes of research direct attention towards issues related to competitiveness of the market and the level of inputs that impact upon return on investment and the ability to retain and attract further investment.

One of the least sophisticated representations of the conundrum we face in Saskatchewan is the one that leads us to the following argument: *“Is the glass is half full or half empty!”*

Public administrators directed within the reality of limited resources must recommend for choices from among competing social and economic policy imperatives. Ultimately, for every winner there is a corresponding loser in the competition for the allocation of financial resources. In the absence of wealth creation this situation actually becomes exacerbated in that pressure on employment, education, health, and social services increase without the necessary resources to offer sustainable remedies to growing social needs.

Tax cuts, on the other hand, as a measure of pure stimulus and one of the often ignored policy instruments available to public administrators have a distinct advantage in terms of impact on the economy. Studies which examine the costs of delivery social programs indicate that spending one tax dollar may in fact bear a cost of between 15% and 50%. This deadweight cost of taxes is illustrated in two policy papers titled: (i.) “Some Neglected Costs of Government Spending in Farm Programs,” (Alston, Julian M. and Hurd, Brian H.); (ii.) “On the Use of Distributional Weights in Social Cost-Benefit Analysis,” (Harberger, A.C.). In other words, the frictional loss impact due to the distortions caused by the collecting of taxes implies that for each dollar spent, less than a dollar actually benefits the targeted stakeholder.

Alternatively, tax cuts offer greater disposable income, increased opportunities for investment, and ultimately new wealth creation. As the new wealth circulates through the economy, existing businesses

increase investment and remain in the market place, new businesses are attracted, and more jobs are created. Thus, an economic development policy that would appear on the surface to give up sources of tax revenue, instead causes a broadening of the corporate, property, payroll, and personal income tax bases. Quite deliberately and in a manner that has inherent long term sustainability, more resources become available through tax cuts to fund social policy initiatives than would be the case under the policy that advocates for tax collection and government spending. Taxation and government expenditure are inherently inefficient. When choosing from among alternatives and establishing priorities, there is better return from a tax cut policy which, itself is inherently more efficient. This will fuel the economy and generate more wealth.

It is further the position of the Saskatoon & District Chamber of Commerce that in the absence of choices, if the Minister can opt for only one significant and stimulation measure, then a cut in small business corporate income tax offers the greatest potential for return (see Part III). Retaining and entrenching the financial stability of existing businesses while simultaneously attracting new business investment to a lower cost and more competitive business climate will enhance job creation, improve quality of life and grow the financial resource pool necessary to support social programs and community amenities. A cut in Small Business Income Tax is:

- ab Affordable for Saskatchewan
- ab Marketable (A Niche for Saskatchewan)
- ab Stimulative and Unchallengeable

The result is a **win-win-win situation** for **government, business, labour**, and the **community**.

Part II- Relocation: We Are Losing Saskatchewan Residents

1.) Saskatchewan Tax Payers Are Concerned about Relocation

The Saskatoon and District Chamber of Commerce believes that “Saskatchewan Tax Payers” are very concerned about the tax consequences of living in this province. This concern is shared by both individuals, small businesses, and corporations. But how many people are interested in possibly relocating to another province or country as a result of our currently uncompetitive tax system?

In an attempt to answer this question the Saskatoon and District Chamber of Commerce sent surveys to 88 accounting firms in Saskatchewan. The survey asked the following question: (submitted to CGA and CA firms)

- ab For your firm, approximately how many clients (expressed as a number or as a percentage) inquire about the tax consequences of relocation, both personally and at a corporate level?

You will find the results of this study in the appendix to the submission. The data definitely supports our

theory with respect to the concern surrounding our current tax legislation. The study gives us an idea of the number of Saskatchewan tax payers that are interested in the benefits of leaving our beautiful province. Unfortunately, our high marginal tax rates are slowing an economy that needs fuel! We as a province must convince our residents that we will be competitive with respect to taxation. We must convince others that Saskatchewan is the place to live!

Another study conducted in the fall of 1998, by Anderson/Fast & Associates and the Saskatoon & District Chamber of Commerce also illustrates this relocation problem (see appendix). The primary objective of this survey (of more than 500 business-decision makers) was to gain a better understanding of the perceptions and opinions of business people within Saskatoon and surrounding regions. These perceptions are important because a business community's strength and energy relate back to perceptions that it has of the business climate, the business community itself, and its future. This in turn, eventually has important implications on a community's development.

The Saskatoon & District Chamber is quite disturbed when they hear that business is considering relocation. This is disturbing because before we attract new businesses, we have to quite losing the businesses we have.

Unfortunately, when business considers relocating, our economic environment suffers. The results of this, on the surface are two-fold. First of all, the number of businesses established in the province of Saskatchewan decreases. Secondly, potential entrepreneurs perceive this relocation consideration as an indication that the business climate in other provinces is superior to that of Saskatchewan.

Should Saskatchewan be concerned when a Saskatchewan business person says: "I'm thinking of relocating my business." Or are these businesses really serious when they talk of relocation? If you are perhaps someone who does not believe that people are in fact leaving, we caution that the information included in the appendix to this submission may be hard to stomach.

2.) *Brain Drain in Saskatchewan*

Yes. This "brain-drain" effect that is often talked about is real in Saskatchewan. Today more than ever, our educated youth and most skilled workers are leaving our province because they feel that employment opportunities are seriously lacking in Saskatchewan. But this "brain-drain" argument has been heavily debated and it is an argument that requires quantitative support. This quantitative support can be found in a report titled: "Survey Research & Analysis of Post-Secondary Students in the City of Saskatoon," (A.T. Galt & Associates. December 1997).

This study was conducted for the Saskatoon & District Chamber of Commerce to determine exactly

how many graduate students are actually leaving for greener pastures. This survey offers considerable insight and hard facts with respect to the prevailing impressions shared by Saskatchewan's Youth. Included in the appendix to this submission is a copy of the executive summary, the major findings of the report, recommendations, and conclusions.

The results will clearly illustrate that people in general think that Saskatoon, Saskatchewan is a great place to live! It is a beautiful city that is attractive in many ways. The same can be said about many cities in Saskatchewan. Saskatchewan has been referred to as the "land of the living skies," where at times you can see for hundreds of miles. This province was built by hard working people that saw the "land of the living skies," as a land of opportunity. Now today, many cannot see this opportunity as it is hidden behind a big black cloud called "*High Taxation.*" And it is this high taxation that is keeping our province from realizing its true potential.

So if one stares across our province, you can see that Saskatchewan has the greenest pastures. Therefore, people aren't leaving for greener pastures. People are leaving because they are making an economically intelligent decisions. It's time to stop forcing people out of Saskatchewan; It's time for Saskatchewan to lower taxes!

Part III - Saskatchewan: We Can be Competitive in the Next Millennium

1.) Unless there is a fundamental change to provincial tax policy, such as a single rate approach like Alberta, or new recognitions of household expenditures such as a provincial tax credit for property taxes and mortgage interest, do not move to a tax on income approach.

A new tax on income that maintains a slightly different personal exemption with a provincially tiered tax structure will unnecessarily complicate an already complicated tax system.

Such a non-parallel system will be less transparent, potentially more inequitable as a tax system, and will aggravate an already difficult competitive position for Saskatchewan.

2.) Whatever approach the Provincial Government ultimately chooses, tax competitiveness must be addressed.

a) The Tax Review Committee should investigate potential strategic responses to competing tax jurisdictions.

Both Manitoba and British Columbia have reduced small business income tax rates to 5% over the next few years.

Saskatchewan could eliminate small business corporate taxes completely at a cost of \$55,000,000, or less than 1% of the provincial budget, but Alberta has become much more dependent on total corporate income tax revenue of \$1,711,000,000 or approximately 9.6% of the provincial budget, versus \$193,200,000 or approximately 3.5% for Saskatchewan.

This change in policy speaks largely to individual or family owned businesses that see small business corporation tax rates as part of their personal tax loads. Such an approach is unlikely to be duplicated by our more tax cut aggressive competitor because of that province's corporate income tax dependence. This approach would offer an incentive and mechanism to fuel incremental growth by small business in Saskatchewan and differentiate Saskatchewan from our competition. Elimination of small business corporate income tax will offer:

- i)* A clear policy signal to foster growth in Saskatchewan business.

- ii)* Augment equity for small business enabling additional debt leverage to accelerate growth. Because of the limited equity resources of a small family owned business, this benefit should not be underestimated.

- iii)* Personal income tax will ultimately be paid on any small business corporate earnings, so there is no real long term tax cost to this approach.

This approach would offer a hard to copy comparative advantage, strongly signal government support for small business growth, and have no long term tax cost to the provincial treasury. The medium term potential of an elimination of small business corporate taxes is to increase investment and job creation in Saskatchewan.

- b)** Provincial personal income tax cuts should be implemented quickly regardless of the tax approach.
 - i)* Tax cuts are stimulative and will offer quick growth payback in government revenues in the face of low consumer interest costs and during this low inflationary period.

 - ii)* Such stimulation is drastically needed if we expect to create jobs at a rate sufficient to employ our

young people, including aboriginal youth who desperately require additional job opportunities in Saskatchewan. The youth exodus from the province can be stemmed by encouraging investment (no small business income taxes) and increased disposable income expenditures (personal tax cuts).

iii) Reasonably large provincial income tax cuts are needed just to offset the negative impact of pending dramatic Canadian Pension Plan increases which are predicted to cost Canada 2.5% in lost Gross Domestic Product growth, and more than 250,000 jobs. Saskatchewan can neither afford its share of lost GDP growth or the lost job opportunities.

c) Personal income tax cuts are affordable and sound policy because:

i) Currently tax revenues are growing faster than the Saskatchewan economy. By limiting further government expenditure increases to inflation and population growth, revenues will be sufficient to fund sizeable cuts (\$100,000,000 or more per year based on previous budgets).

ii) Tax cuts should be prioritized over program expenditures. They are more stimulative and they will strengthen the province's future financial capacity to a greater extent than program expenditures. Growth will occur more dramatically through tax cuts. Tax cuts are more stimulative than program expenditure increases because the frictional loss of government flow-through inefficiencies are eliminated. Various economic studies indicate that Government frictional loss inefficiencies are estimated to cost between 10% and 40% of any government flow-through expenditure. (See appendix; Frictional Loss and the Deadweight Cost of Taxes)

iii) Tax cuts offer incentives for young people and financially independent retirees to stay in Saskatchewan thus strengthening the income makeup and age distribution of the future Saskatchewan population making future social policy expenditures more affordable and secure.

3.) Tax cuts could occur more quickly if more provincial debt was retired through the disposal of assets and corporations that have a greater present value than their cash dividends to the Provincial Government.

4.) There are several psychological benefits to entering into a competitive tax position. Alberta demonstrated the psychological benefit of announcing but not yet implementing tax cuts. A statement of lowering Saskatchewan taxes to meet or beat the competition in certain areas over time would stem the exodus of people, increase investments from existing businesses and strengthen the case for new businesses locating or starting up in Saskatchewan.

Part IV - The Cost of Doing Nothing or “Rearranging the Deck Chairs”

Should the Saskatchewan government choose to not meet or beat the tax competition, the path for Saskatchewan will be progressively more difficult. Funding capacity for government services will erode. Job creation and investment will stagnate. The consequences of not cutting taxes for the future of Saskatchewan will be disastrous. The Provincial Government cannot stand still while other jurisdictions in Canada and elsewhere heat up their tax competition.

To suggest that Saskatchewan people do not care about their current and future tax load is to suggest that Saskatchewan people are ignorant to options and further promotes a myth that our citizens do not care about their lifestyle choices and their interest or ability to support themselves or their family members into the future.

In today’s wired world, the sword of “location doesn’t matter” cuts both ways.

Saskatchewan residents can and have left our province. Those most likely to move now and in the future include:

1. Well educated and trained young people in pursuit of building a career, a family and a home.
2. Financially independent retirees whose children have largely left Saskatchewan.
3. Business owners who can expand operations elsewhere or who are seeking to sell Saskatchewan operations to pursue other interests.

In each case the Saskatoon and District Chamber of Commerce has developed practical examples:

Example 1. **A young information technology operator making \$125,000 per year with a spouse at home raising two infant children.** The difference between Saskatoon and Edmonton for income tax will be enough to fund a \$125,000 mortgage or make the loan payments on two new cars. The difference for the same worker paid in the equivalent of \$125,000 Cdn in Mesa, Arizona is a \$125,000 mortgage and a loan payment on one car (ignoring the higher salaries paid to such a worker in the United States).

Example 2. **A retired couple with \$60,000 in pension / RRSP income.** The difference between Saskatchewan and Edmonton after tax income is approximately \$4,000

per year after Alberta implements its single rate system. \$4,000 per year is sufficient to pay for:

- the RESP contributions for two grand children
- an annual winter vacation or cruise
- the payments on a used motorhome.

If the \$60,000 is derived from RRSP savings (estimated at \$1,200,000 in value) the tax difference at death would pay for a quality family owned lakefront cottage for the surviving children.

Example 3. A business being sold by a principal owner intending to flow \$8,000,000 in capital gain sale proceeds to themselves and their spouse would be exposed to over \$400,000 in additional taxes in Saskatchewan versus Alberta which would pay for a high quality home in any city in Alberta.

All of these examples ignore the negative economic impact of personal expenditures lost to Saskatchewan over the life of forced relocation and the impact on investment decisions in Saskatchewan with corporate decision makers and job creators leaving Saskatchewan.

Just one large accounting firm in our province deals with approximately two requests weekly for corporate and personal relocation tax impact analyses annually.

With just one million people, an aging population, and huge job creation needs for our aboriginal youth, can Saskatchewan afford to lose even one young, talented individual who will pay more than \$500,000 in provincial income taxes in their working lifetime (not counting the jobs that individual will create along the way)?

Can Saskatchewan afford to lose the \$75,000 in provincial income taxes the retiree will pay during their retired lifetime, or the \$132,000 in provincial income tax at death from even one portable retiring couple?

Can Saskatchewan afford to lose the \$660,000 in taxes paid from the sale of a business relocating to Alberta prior to the business sale?

Does the Saskatchewan Government want businesses to relocate head office operations, for corporate investment decisions to be made elsewhere? Does the Government want Saskatchewan based businesses to pay salaries and the related taxes elsewhere?

A 1999 Canadian Federation of Independent Business (CFIB) survey of business showed that more than 80% of the businesses find that Saskatchewan's personal income tax system negatively impacts their business, with reasons including:

- ab Lowered customer's disposable income.
- ab Reduced retained earnings.
- ab Negatively affected overall provincial competitiveness.
- ab Hindered ability to attract and keep qualified labour.
- ab Increased complexity in completing tax returns.
- ab Reduced company's competitiveness.

(Source: Canadian Federation of Independent Business, 1999 Saskatchewan Pre-Budget Submission)

It is the view of the Saskatoon and District Chamber of Commerce that Saskatchewan income taxes and small business corporate taxes must be reduced to meet or beat the competition regardless of the approach to taxes adopted by the Province. To do otherwise dismisses the possibility to grow our economy at an accelerated pace, and will encourage more talented young people and financially independent people to leave our province.

Alberta changed its tax system in response to tax competitive pressure from the United States in an effort to retain workforce talent and investment. The United States has eliminated its deficit and will, at least to some extent, cut taxes further. Our tax competitors will continue to move their taxes lower. Failure to respond to these competitive pressures is unacceptable to our Chamber members. These investors in Saskatchewan await the Government's response as they plan their future investment decisions.