



THE CANADIAN  
CHAMBER  
OF COMMERCE

LA CHAMBRE  
DE COMMERCE  
DU CANADA

## ***2008 Federal Budget***

Today, Minister of Finance Jim Flaherty tabled the Conservative government's third budget. The theme of this year's budget is "responsible leadership for uncertain times." The aim is to strengthen Canada's economy amidst global economic uncertainty.

**Section A**, outlines the key measures announced today,  
**Section B** provides the Chamber's analysis of the budget and  
**Section C** concludes the analysis of the budget.

### **The Federal Government's Fiscal Outlook**

Budget Plan 2008 estimates the size of the underlying surplus at \$12.9 billion for 2007-08, \$3.8 billion for 2008-09, and \$3.0 billion for 2009-10. Proposed measures (i.e. program spending and tax reduction) absorb \$2.7 billion in 2007-08, \$1.5 billion in 2008-09, and \$1.7 billion in 2009-10. \$10.2 billion is allocated for debt reduction in 2007-08, \$2.3 billion in 2008-09 and \$1.3 billion in 2009-10 leaving the government's books balanced over the planning horizon.

### ***A. The Budget Plan: Highlights of Measures Announced***

#### ***Spending Initiatives. Budget 2008:***

- **Invests in people by:** introducing a consolidated Canada Student Grant Program to replace the former Millennium Scholarship program; streamlining and modernizing the Canada Student Loans Program; enhancing the flexibility of Registered Education Savings Plans (RESPs); and modernizing the immigration system to speed up the processing of permanent resident applications.
- **Invests in knowledge, science and innovation by:** providing additional funding to Canada's three university granting councils and to the Indirect Costs of Research program; and allocating funds for Genome Canada to support strategic large-scale R&D in the automotive sector to develop greener and more fuel-efficient vehicles.
- **Supports communities and traditional industries by:** helping older workers stay in the workforce; promoting Canada's forestry sector in international markets; and allocating funds to farm programs and to improve access in potential cash advances to Canadian farmers.
- **Invests in infrastructure by:** making the Gas Tax Fund a permanent measure to allow municipalities to better plan and finance their long-term infrastructure needs; setting aside funds in support of capital investments to improve public transit; and announcing the establishment of a Crown corporation to support public-private partnerships.
- **Ensures a Cleaner, Healthier Environment by:** strengthening and ensuring the effective implementation of Canada's ecoACTION plan; setting up the regulatory framework for industrial air emissions; providing funds for full-scale commercial demonstration of carbon capture and storage in the coal-fired electricity sector; increasing CCA rates for carbon dioxide pipelines; expanding the CCA for clean-energy generation equipment; and investing to support nuclear energy.
- **Invests in leadership abroad by:** committing funds to the Canada Border Services Agency so it has additional resources to manage the border; introducing a higher-security electronic passport by 2011 and doubles the validity period of this passport to 10 years; expanding the joint Canada-US NEXUS program; allocating funds to introduce the use of biometric data into visas issued to foreign nationals

entering Canada; to meet the priorities under the Security and Prosperity Partnership of North America; and investing to improve services for Canadians traveling, living and investing abroad including new embassies and missions in emerging markets.

### ***Tax-Related Measures***

- Introduces a new Tax-Free Saving Account (TFSA) that allows Canadians to contribute up to \$5,000 a year with the ability to carry forward unused room. Investment income earned within the account will not be taxed and withdrawals will be tax free. Canadians can withdraw from the account at any time without restrictions.
- Provides assistance to the manufacturing and processing sector by extending the accelerated capital cost allowance treatment for investment in machinery and equipment for three years. The 50% straight-line accelerated CCA treatment will apply for one additional year. Accelerated treatment will then be provided on a declining basis over a two-year period.
- Increases the CCA rate for railway locomotives to 30% from 15% on purchases made on or after February 26, 2008 and for reconditioning and refurbishing costs.
- Improves the SR&ED tax incentive program and eases the tax compliance burden by reducing the record-keeping requirements for automotive expense deductions and taxable benefits. The enhanced SR&ED ITC now available to small Canadian-controlled private corporations on the first \$2 million of qualified expenditures will be available for the first \$3 million. The upper limit for the taxable capital phase-out will increase from \$15 million to \$50 million. The upper limit of the taxable income phase-out range will also be increased from \$600,000 to \$700,000. Budget 2008 proposed to extend the SR&ED ITC to certain activities carried out outside Canada. Eligibility will be limited to a maximum of 10% of the Canadian SR&ED labour expenditures.
- Removes disincentives to work for seniors by raising the current Guaranteed Income Supplement from \$500 to \$3,500.
- Streamlines the cross-border business and investment environment by streamlining cross-border tax-withholding and return-filing rules.
- Extends eligibility for the mineral exploration tax credit to flow-through share agreements entered into on or after March 31, 2009.
- Creates the Canada Employment Insurance Financing Board to enhance the independence of premium rate setting and ensure that Employment Insurance (EI) premiums are used exclusively for the EI program. The Board will implement a new EI premium rate-setting mechanism and maintain a cash reserve of \$2 billion (provided by the government) to ensure that premium rates do not increase more than the 15-cent limit in the event of a downturn.

## ***B. Canadian Chamber's Analysis of Budget 2008***

### ***Program Spending***

The Canadian Chamber was pleased to see a number of our key tax policy recommendations adopted in the fall *Economic Statement*. In sharp contrast, Budget 2008 was relatively light on tax measures and heavy on spending. The budget proposes a total of \$5.9 billion in new measures from 2007-08 to 2009-10 of which, only \$285 million is directed to tax relief.

The Canadian Chamber is also discouraged that program spending continues to rise at a rapid pace and stands in the way of further debt reduction and tax relief. Program spending increased at an average annual rate of 8% between fiscal 2000-01 and 2006-07 and is projected to rise by almost 7% in 2007-08. Annual increases of 3.4% in 2008-09 and 4.9% in 2009-10 are expected. Nominal GDP growth is forecast to average 3.5% in 2008 and 4.3% in 2009.

The Canadian Chamber urges the federal government to maintain growth in program spending in line with growth in nominal GDP. Preferably, the government should cap growth in program spending to approximately 3% per annum based on anticipated growth in population plus inflation. This strict discipline would enable us to drive down the debt faster and have room for additional tax relief.

In 2007, 17 government organizations undertook strategic reviews of their programs and spending. Ministers examined departmental spending amounting to \$13.6 billion (or 15% of total direct program spending). As a result of these reviews, savings of \$199.3 million in 2008-09, \$310.6 million in 2009-10 and \$386.2 million in 2010-11 were identified. The resulting savings are being redirected to fund new initiatives. We strongly urge the federal government to review all programs on annual basis and allocate spending to productivity enhancing areas like education, infrastructure (including the border) and innovative solutions that facilitate travel, trade and commerce. In this regard, the Canadian Chamber applauds the proposed measures in Budget 2008 pertaining to these areas including over \$150 million investment to address six of the recommendations made last week in the Chamber-led coalition "Finding the Balance: Reducing Border Costs While Strengthening Security" report.

### ***Debt Reduction***

Fiscal 2007-08 will mark the eleventh consecutive year the government of Canada recorded a surplus. Canada's federal debt (accumulated deficit) has been reduced from its peak of \$562.9 billion in fiscal 1996-97 to an estimated \$457.1 billion as of March 31, 2008. The federal debt-to-GDP ratio has dropped from a peak of 68.4% in fiscal 1995-96 to under 30% in fiscal 2007-08.

Interest savings resulting from debt reduction will be returned to Canadians as part of the government's Tax Back Guarantee, something the Canadian Chamber fully supports. This means that by 2009-10, \$2.0 billion annually will not be going to interest payments, but returned to Canadian taxpayers.

In the October 2007 *Economic Statement*, the government committed to pay down debt by \$10 billion in 2007-08 and \$3 billion per year the following two years. Budget 2008 commits to reducing debt by \$10.2 billion in 2007-08; however, in the following two years debt reduction appears to be less of a priority. In fact, the government is balancing its books by sacrificing on debt reduction. Should the economy slow more than predicted, the government's books can tilt into a deficit position.

### ***Developments on the Tax Front***

Budget 2008 contains a number of positive developments on the tax front to bolster the competitiveness of Canadian businesses. The enhancement of CCA rates with respect to certain asset classes will encourage new investment. Improvements made to Canada's SR&ED program, including administrative improvements, will facilitate access to the program, improve its consistency and predictability and enhance the claims process.

The introduction of the Tax-Free Savings Accounts (TFSA) was welcome surprise. It makes it easier and more attractive for individuals to save given that investment income earned within the account will not be taxed and withdrawals will be tax free. Moreover, Canadians can withdraw from their TFSA at any time without restrictions making it possible to deal with an emergency situation or to use the money as they wish (for example, to start a small business or purchase a home). The TFSA will also provide seniors with an additional vehicle to meet their ongoing savings needs, particularly after the age of 71 when they are required to begin drawing down their retirement savings. Overall, it will enable the country to better deal with the aging baby-boomer generation and enhance Canada's ability to attract and retain the best and brightest people.

Budget 2008 also increases the flexibility of the Registered Education Savings Plans (RESP) program by increasing the number of contribution years after the plan is entered to from 21 to 31 and the contribution age limit for a family plan by an additional ten years. This will provide students with additional savings to help finance their post-secondary education.

Despite these positive changes, much more needs to be done. Quoting the finance minister...“Canadians still pay too much tax”. High marginal tax rates on individuals remain a barrier to growth by reducing the incentive to work and stay in Canada. The government must reduce personal income tax rates across all income tax brackets, but particularly for low- and modest-income families because they face the highest marginal rates of all as a result of clawbacks of multiple benefits. It must also increase the thresholds at which the marginal tax rates kick in. In Budget 2008, the government stated that it intends to implement further broad-based tax relief with a particular emphasis on personal income tax as fiscal resources permit.

Another unfinished area of business is the harmonization of provincial retail sales with the GST. The government must continue to work with the five provinces that have retail sales taxes to facilitate the transition to a harmonized tax. This will lower marginal effective taxes rates by a sizeable magnitude and would have a significant impact on the competitiveness of Canadian businesses.

### ***C. Conclusion***

Economic uncertainties highlight the importance of putting in place policies that promote and enhance flexibility so that our economy and businesses can adjust and adapt to changing circumstances and economic shocks now and in the future. In many respects, the measures contained in today's budget are welcome and bode well for increasing productivity and competitiveness.

At the same time, there is unfinished business. Canadian businesses require on operating environment that lets them fully realize their capabilities. Governments must lighten the burden of regulation, cut interprovincial trade barriers, better utilize immigrants through recognition of foreign credentials and improved labour market integration, adopt a single securities regulator; ensure that our tax system is simple, efficient and fair; and our corporate and personal income tax rates are internationally competitive.