

# Submission to the Select Standing Committee on Finance and Government Services

Prepared by the Canadian Bankers Association

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# Introduction

The Canadian Bankers Association (CBA) welcomes this opportunity to provide its input to the Select Standing Committee on Finance and Government Services, as the Committee prepares its recommendations for the 2012 British Columbia Budget.

The Canadian Bankers Association works on behalf of 52 domestic banks, foreign bank subsidiaries and foreign bank branches operating in Canada and their 267,000 employees. The CBA advocates for effective public policies that contribute to a sound, successful banking system that benefits Canadians and Canada's economy. The Association also promotes financial literacy to help Canadians make informed financial decisions and works with banks and law enforcement to help protect customers against financial crime and promote fraud awareness.

Our submission offers the banking industry's views and recommendations in a number of areas that are of interest to the Standing Committee such as: supporting private sector job creation; maintaining British Columbia as a preferred destination for investment; and helping families.

As the Budget Consultation document states, under the stewardship of the provincial government, 335,000 jobs have been added in the province since 2001. This is occurring with a government that committed to a competitive tax system – British Columbia has the lowest provincial personal income tax rates in Canada and among the lowest corporate income tax rates in North America. It also has diversified its export markets with shipments to Asia outstripping those to the U.S.

There are also some headwinds. In addition to a slow economic recovery in the U.S., and economic challenges in other parts of the world, the provincial government must manage a projected \$3 billion shortfall. In order to navigate this uncertainty, a strong and healthy banking system is an essential cornerstone to help families buy homes and save for retirement, help small businesses grow and thrive and to promote Canada's and British Columbia's brand internationally.

The banking system has a unique perspective on, and an important stake in, British Columbia's economic future. For instance, in 2010:

- Banks and other deposit-taking institutions contributed close to \$5.2 billion (3.35%) to the province's GDP;
- Banks directly employed 28,450 people in British Columbia (if indirect employment is included – technology, accounting, actuarial, legal – this number is much higher);
- Banks paid \$270.5 million in provincial and municipal taxes; and
- Banks authorized \$71.3 billion in credit to British Columbia's businesses, of which \$11.7 billion was provided to over 161,600 small and medium-sized enterprises (SMEs).

We are pleased to offer our views on ways to support private sector job creation; promote investment and on ways to help families in British Columbia.

# Supporting Private Sector Job Creation

## A Competitive Tax Regime

The CBA commends the government on its decisions in recent years to eliminate capital taxes and to reduce corporate and personal income tax rates in order to become a more attractive jurisdiction in which to work, invest and set up businesses. We also believe that the replacement of the provincial sales tax with a harmonized value added tax would have promoted additional economic growth in B.C. While the implementation of HST in BC and Ontario last year led to a significant increase in taxes paid by banks, we are supportive of the tax because, aggregated across all economic sectors, it reduces the marginal effective tax rate on new capital investments which create jobs and growth. We recognize and accept the decision made by British Columbians; however we hope that provincial sales tax policy can be revisited at some point in the future.

In contrast, we are concerned by some recent proposals to raise corporate income taxes and to re-institute the capital tax on large banks and credit unions: taxes which hinder economic growth. We urge the B.C. government to maintain its commitment to a corporate income tax rate of 10 per cent which, in combination with a projected federal rate of 15 per cent, will provide an internationally competitive rate, which is vital to encouraging new investment that would improve business productivity and create jobs. Similarly, taxes on capital have been widely recognized as a barrier to attracting new capital investment. That is why B.C. and other provinces eliminated these taxes over the course of the last decade. Well capitalized banks are critical to the financial health of the province. To the extent that their capital is depleted by taxes, it is not available to provide a base for the expansion of credit to other sectors of the economy. Capital taxes on banks and credit unions are particularly perverse as these financial institutions are required by law to hold large amounts of capital to withstand risks, especially during periods of financial market turbulence.

## Taxation of Corporate Groups

We would also like to focus on another area that affects tax competitiveness, namely efficient tax administration and, in particular, the taxation of corporate groups. The CBA welcomed the November 2010 federal consultation paper on the taxation of corporate groups. Corporations, including financial institutions, carry on business through a variety of organizational structures. Frequently these structures involve the use of separate legal entities which are nonetheless economically integrated into the corporate group<sup>1</sup>. However, in Canada, corporations are required to report and pay tax on their income on an unconsolidated or legal entity basis. As a result, losses incurred by some affiliates within a corporate group cannot be offset against profits earned by other affiliates in a timely manner. In the absence of loss transfer provisions within the *Income Tax Act*, the Canada Revenue Agency (CRA) has developed administrative practices to permit losses to be utilized through indirect means, but they are *ad hoc*, costly and unpredictable for both corporations and governments. A formal system for the taxation of corporate groups would address these shortcomings.

The CBA believes that a loss transfer system similar to that in place in the United Kingdom is the preferred starting point as it would be relatively simple to implement and administer. It would significantly reduce the

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<sup>1</sup> In fact, the Bank Act and governing legislation for other types of financial institutions require them to set up separate legal entities for certain lines of business.

costs and uncertainties associated with the current Canadian system while achieving the main objective sought by taxpayers: the ability to use tax losses and credits currently if there is capacity in the corporate group<sup>2</sup>. The CBA looks forward to working with the federal and provincial governments and other members of the business community to develop an improved approach to the taxation of corporate groups and an equitable manner of allocating the income and losses of corporate groups among the provinces.

**Recommendation: Continue to work with the federal and other provincial governments to design and implement a formal loss transfer system for corporate group taxation.**

## **Interprovincial allocation of corporate income taxes**

While the advantages of consolidated tax reporting have been identified for decades, the impact on tax revenues of individual jurisdictions in a federal state have not been as easily resolved. For example, provincial tax revenues from a profitable B.C. corporation could be reduced or eliminated by an offsetting claim for the losses of an affiliate operating in another province (to the detriment of B.C.), or the reverse could happen (to the benefit of B.C.). These interprovincial transfers increase uncertainty regarding the tax revenues available to a province in any single budget period as revenues may be impacted by economic circumstances in other jurisdictions. The recent consultation process prompted discussions surrounding a number of potential solutions. For example, explicit disclosure of loss utilization transactions could become the basis for a provincial loss recapture system. Alternatively the current interprovincial allocation formula could be adapted to use attributes of the corporate group on an aggregate basis.

There are additional longstanding issues surrounding the allocation of corporate income taxes paid by banks and other deposit-taking institutions. Changes in the manner in which financial products and services are produced and delivered as well as the increasing complexity in financial instruments have raised provincial concerns that the special allocation formulae for these institutions no longer produce an equitable result. There are frequent provincial challenges to the results of the allocation formula in which individual provinces may unilaterally reassess an institution to increase their share of the total pie. Resulting appeals can take as long as 10 to 15 years to resolve. These disputes create uncertainty for all provincial governments with respect to their tax revenues for a particular year since all must ultimately agree to a revised allocation. They also create uncertainty for the financial institutions involved with respect to their tax liabilities since they may end up paying tax twice on the same dollar of income and are charged interest on “late payments” when the allocation between provinces is changed. Both sides also incur greater administrative costs.

**Recommendation: Continue to explore measures to update interprovincial allocation methods as they apply to corporate groups in general and to the financial sector in particular in collaboration with the federal government and other provincial governments.**

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<sup>2</sup> The CBA's complete submission can be found at [http://www.cba.ca/contents/files/submissions/sub\\_20110411\\_taxation\\_corporategroups\\_en.pdf](http://www.cba.ca/contents/files/submissions/sub_20110411_taxation_corporategroups_en.pdf)

# Maintaining B.C. as a preferred destination for investment

## Single Securities Regulator

For many years, the CBA has advocated for efficient securities regulation, with a strong belief that a national securities regulator will benefit all Canadians. This advocacy is rooted in our experience of being a federally regulated industry. We are convinced that a single securities regulator will attract investment, improve investor protection and promote confidence in Canada's capital markets to the benefit of all Canadians. Canada's consolidated federal regulation and supervision of banking is one of the reasons why Canada's banking system performed so well during the financial crisis. The financial crisis revealed the importance of having a unified regulatory structure with clear accountability. While Canada has this on both the prudential and the consumer protection side, we do not have it with securities. This must change. This is why the CBA continues to support the federal government in its efforts to create the Canadian Securities Regulatory Authority (CSRA), led by the Chair of the Canadian Securities Transition Office (CSTO), former head of the British Columbia Securities Commission Mr. Douglas Hyndman. More specifically, the CBA has demonstrated this support by intervening in the federal government's reference to the Supreme Court of Canada on the constitutionality of the proposed *Canadian Securities Act*.

A unified regulatory structure with clear accountability is integral to well-regulated capital and financial markets. As the financial crisis demonstrated, capital markets, their products and their institutions are closely linked to the financial markets more broadly. Risk moved quickly from unregulated financial institutions through to the capital markets and then to regulated financial institutions, ultimately affecting the economy. The CSRA, with its responsibility for monitoring Canada's capital markets, will contribute to the integrity and stability of the financial system in cooperation with a number of other federal organizations.

The CBA believes it is important to be able to transition from a provincial to a national system of capital markets regulation while being responsive to local and regional needs. This is why we are supportive of the CSTO initiative to obtain meaningful provincial and territorial input. It is in this regard that the CSTO has relied on the advice of the Advisory Committee of Participating Provinces and Territories as well as the Participating Regulators Committee (including representatives from British Columbia).

While respecting the process before the Supreme Court of Canada, it is with the help of participating provinces and territories that tremendous progress has been made implementing the Transition Plan for the CSRA. Work has begun on the drafting of initial regulations; designing the processes, rules and organizational details related to the Canadian Securities Tribunal; outlining a fee structure; designing a compensation plan; planning for information management and developing an organizational plan and role descriptions.

**Recommendation: We encourage the government of British Columbia to support the federal government in its efforts to create a national securities regulator.**

# Helping Families

## Pooled Registered Pension Plans (PRPPs)

While Canada has a strong retirement income system, some Canadians are concerned about their own retirement security. Banks and other financial institutions have the necessary expertise and infrastructure to help Canadians save for their retirement. The CBA believes that a private sector pension option can build on that expertise and infrastructure while helping the government achieve its public policy goals. This is why the CBA supports the proposal for Pooled Registered Pension Plans (PRPPs) announced last year, and is working very closely with the federal and provincial governments as they design and implement the plan over the coming year.

The PRPP balances the needs of working Canadians who are not saving enough with those of the vast majority of Canadians who have adequate retirement income. We believe that PRPPs, by providing Canadians with a simple and cost-efficient opportunity to participate in a structured pension plan and the flexibility to tailor their retirement saving strategy to fit their financial goals, are an effective way to help Canadians achieve their retirement goals. They also address the concerns of small businesses that recognize the value of pension plans and would like to offer them to employees but find that the administrative burden, potential legal liability and financial costs as administrators render them not worthwhile.

We are supportive of the overall objective to provide an accessible, straightforward, low-cost and easy-to-use pension plan that takes advantage of the benefits from the pooling of resources and professionally-managed funds for the benefits of Canadians. The public policy objective of the PRPP is to expand the retirement coverage of individuals who currently do not participate in a pension plan, particularly the self-employed and employees of small businesses. Consequently, PRPPs should address the participation and enrolment of individuals to ensure that a maximum number of Canadians participate in PRPPs. This will also ensure that the scale of the plans is sufficient to enable the cost savings envisioned by the government. In addition, rules should be harmonized between provinces in order to ensure that Canadians benefit from the highest possible cost savings. Other features, such as locking-in of funds to ensure that they are used for retirement savings purposes and provisions for a predictable income stream in retirement, also require careful consideration to ensure that the government's objectives will be achieved and that Canadians benefit from the lowest possible fees. Lastly, strong consideration should be given to simplifying the supervision of PRPPs by assigning regulatory and supervisory responsibilities to the jurisdiction under which the administrator falls. In the case of federally regulated financial institutions such as the banks, this would be the Office of the Superintendent of Financial Institutions (OSFI).

**Recommendation:** In designing the PRPP, governments should focus on expanding pension plan coverage by making PRPPs appealing to employers, employees, and the institutions that would act as administrators. In accomplishing this there are a number of considerations and actions that should be taken:

- All participants in a PRPP should have the same opportunities to accumulate savings and make withdrawals in retirement.
- The regulatory regime should be efficient and not impose undue obligations and costs on employers and administrators.
- The regulatory regime should be harmonized across the country.

- **Regulatory and supervisory responsibilities should be assigned to the jurisdiction under which the administrator falls. In the case of federally regulated financial institutions such as banks, OSFI would be the prudential regulator and supervisor for PRPPs.**

## Conclusion

The recent recession and global financial crisis highlight the benefits to the British Columbian economy of a stable and sound banking sector. The sector contributed to a stable employment and economic base for British Columbia, paid hundreds of millions of dollars in provincial and municipal taxes and financed thousands of businesses, from SMEs to corporations. We believe public policy should build on that stability and soundness, for the benefit of all British Columbians and Canadians.

We commend the government on its measures to create jobs, diversify exports and lower personal and corporate taxes. We have made recommendations that will promote business investment and job creation and, ultimately, contribute to the economy of British Columbia. These recommendations involve the enhancement of British Columbia's taxation system, including measures to improve effectiveness and efficiency; supporting capital markets regulation through support for a national securities regulator; and implementation of Pooled Registered Pension Plans (PRPPs).