A Strong Banking System for a Strong Quebec

02/02/2024

ASSOCIATION DES BANQUIERS CANADIENS
CANADIAN BANKERS ASSOCIATION

Submission to the Ministère des Finances

Recommendations

The Canadian Bankers Association's (CBA) welcome this opportunity to participate in the pre-budget consultation for the Ministère des Finances (Ministère). Our submission identifies opportunities and recommendations for consideration by the Ministère in the development of its next budget.

The CBA's key recommendations, as summarized, are for the Government of Quebec to:

- Remove the Compensation Taxes for Financial Institutions to promote job creation in Quebec.
- Encourage the federal government to undertake a comprehensive review of the national tax system to ensure it aligns with the needs and goals of Québécois, improves productivity, and attracts international capital investments. One step is the removal of sector specific taxes such as the Financial Institutions (FI) Tax and the Canada Recovery Dividend (CRD).
- Support the establishment of a permanent multi-stakeholder housing roundtable to coordinate housing policy across all levels of government. The objective of the body would be to remove barriers to the supply and increase construction of social housing to protect the province's most vulnerable households.
- Broaden its financial literacy initiatives in secondary schools to encompass targeted programing for priority groups, including lower-income individuals, Indigenous Peoples, and newcomers to Quebec.
- Collaborate with the CBA and government agencies to increase cyber security awareness and strengthen Québec's cyber resilience.
- Adopt a financial consumer protection regime targeted at payment service providers and extend these standards to under and unregulated activities.
- Collaborate with industry and the Government of Canada to design targeted investments and tax incentives that create pathways to net-zero, while taking a balanced and flexible approach to new regulation.

Introduction

The CBA is grateful for the opportunity to contribute to Quebec's next budget through its 2024-2025 pre-budget consultations.

The CBA works on behalf of more than 60 domestic and foreign banks operating in Canada and their employees. The CBA advocates for public policies that contribute to a sound and thriving banking system that ensures Canadians, including the Québécois, can succeed in their financial goals. We also promote financial literacy to help residents of Québec make informed financial decisions and work with banks and law enforcement to help protect customers against financial crime and promote fraud awareness.

A strong and healthy banking system is an essential cornerstone to help households manage their finances, help small businesses grow, and promote Québec's economy in attracting capital investments. Our submission offers the banking industry's views and recommendations for Québec's upcoming budget.

Banking Industry and the Québec Economy

Canada's banking sector has a longstanding history of supporting the economy in Québec. In 2022, the banking industry contributed approximately $10.6 billion (or 2.7 per cent) to Québec's GDP and paid over $1 billion in provincial and municipal taxes. Furthermore, banks in Canada provided $22.6 billion in dividend income in 2021 and a further $26.0 billion in 2022 that went to seniors, families, pension plans, charities, and endowments across Canada, including in Québec.[1]

The banking industry invests heavily in new technology to meet the needs of Canadians. In the last decade, Canadian banks invested approximately $115 billion in technology across Canada. With a network of over 950 branches and 3,550 bank-owned ABMs across Québec, Canada's competitive banking system provides ready access, good value, and wide choice of banking services to consumers and businesses. Additionally, financial advisors and planners employed by banks help Québécois plan for times of heightened economic uncertainties and financial pressures.

The banking industry's workforce in Québec is inclusive and talent driven. Of the more than 46,000 employees at the six largest banks in Québec, approximately 54 per cent of the workforce is represented by women and visible minorities constituted 26 per cent, with significant representation in all management

[1] CBA data.

levels.[2] Additionally, banks are making special efforts to increase representation of Indigenous people within their workforces and support. Banks in Canada are progressive employers that proactively support and foster diversity, inclusion, and equality in their workforces.

Canada's banks have been ranked as safest in the world through the 2008 global financial crisis and the recent and rapid interest rate increase.[3] Banks' reliability and stability help families buy a home and save for retirement, help small businesses grow, and support Québec's growing communities. For instance, as of the end of 2022, banks in Canada have $182.6 billion in residential mortgages outstanding and authorized $254.5 billion in business credit in Québec.[4] Of the authorized credit, $53.6 billion went to small- and medium-enterprises (SMEs). Further, businesses in Québec, including SMEs, are well-served by the financial sector owing to a tremendous amount of competition. According to the Innovation, Science and Economic Development (ISED) *Credit Conditions Survey*, 91 per cent of debt financing requests for small businesses were approved in 2022 in Québec[5], with the debt approval rate in the province averaging 88 per cent annually since 2010.[6]

Compensation taxes, Canada's productivity problem, and the need for tax reform

We believe eliminating Québec's Compensation Tax for Financial Institutions will encourage job creation and economic growth in the province. Despite sector specific taxes such as Québec's Compensation Tax (as well as the federal government's Financial Institutions (FI) Tax and the Canada Recovery Dividend (CRD)) widely recognized as counterproductive public policy that will impact Québeckers, the Compensation Tax was extended twice beyond its original 2019 expiry date.

Bank customers, suppliers, employees, and shareholders – many of whom are based in Québec - ultimately bear the impact of any disproportionate level of taxation on the banking sector. Customers could see raised prices and reduced availability for goods and services while Québec-based employees could see downward pressure on job creation and wage growth.

The negative impact of discriminatory taxes on the financial sector is compounded by Canada's

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[2] Ibid

[3] World Economic Forum's annual Executive Opinion Surveys ranked Canada's banks as the healthiest with soundest balance sheets, compared to over 130 jurisdictions, from 2008-2018. Additionally, Global Finance magazine ranked all of Canada's big six banks in the top 29 in the list of World's Safest Banks 2022 – sorted by asset size, Canada's big six banks rank as the safest.

[4] CBA data.

[5] ISED, Credit Conditions Survey – 2022, August 2023.

[6] Based on ISED Credit Conditions Surveys and Statistics Canada's Survey on Financing of Small and Medium Enterprises.

internationally lagging labour productivity, which is among the lowest in the G7. Taxes negatively impact investment in productivity enhancing areas of intellectual property,[7] information technology, and machinery and equipment at a time when Canada's investment rate is half the rate of the United States.[8] Owing to the sluggish growth in labour productivity, Canada is projected to be one of the worst performers among advanced economies in the next 40 years.[9]

We believe Canada's productivity outlook can be improved through a redesign of Canada's inefficient tax system that distorts capital decisions.[10] An efficient tax system incorporates relatively lower rates on a broader base to maintain government revenues and encourage growth and innovation. The Organisation for Economic Co-operation and Development (OECD) has stated that creating tax advantages for specific activities typically draws resources away from sectors that can make the greatest contribution to productivity gains and economic growth.[11] Thus, provincial and national tax systems should align in encouraging growth and innovation by letting Canadians and businesses make choices driven by economic decisions rather than by tax considerations.

Recommendation: We strongly encourage the Government of Québec to eliminate the Compensation Tax for Financial Institutions in order to promote job creation and economic growth in the province. Additionally, we ask the Government of Québec to advocate to the federal government for a comprehensive review of Canada's tax system to increase productivity and ensure Canada can compete internationally for capital investments. One such step is the removal of sector specific taxes such as the FI Tax and the CRD.

Supporting housing affordability

We recognize that each city and province in Canada has unique needs and challenges with respect to housing affordability. That said, Québec has not been immune to this recent challenge. RBC Economics estimates the share of household income needed to cover home ownership costs at 51.9% and 34.4% in Montréal and Québec City, respectively. While Québec City remains affordable, unaffordability in Montréal is near an all-time high.[12]

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[7] OECD, "GDP per hour worked" (indicator) (accessed on 30 May 2023).
[8] OECD, OECD Compendium of Productivity Indicators 2023
[9] BCBC, OECD predicts Canada will be the worst performing advanced economy over the next decade…and the three decades after that, December 2021
[10] International Monetary Fund, Fiscal Monitor: Achieving More with Less, April 2017
[11] OECD, Tax Policy Reform and Economic Growth, OECD Tax Policy Studies (2010)
[12] RBC, Housing trends and affordability, December 2023

As the population continues to grow in the province, we believe that an imbalance between home supply and demand will contribute to affordability challenges. The Canada Mortgage and Housing Corporation (CMHC) estimates that Québec needs to build an *additional* 620,000 units above current construction trends to restore housing affordability by 2030.[13] Québec's housing affordability challenges have important social and equity implications that could reverberate across generations, as many young Québecers have been effectively priced out of homeownership and the crisis most affects those with the lowest incomes.

The challenges are especially dire for those who require social housing. According to Scotiabank Economics, Canada's stock of social housing represents just 3.5 per cent of its total housing stock, among the lowest in the OECD. In the near-term, we encourage the Government of Québec to accelerate the construction of social housing to meet the growing needs of Québec's most vulnerable. A study by the Mental Health Commission of Canada estimated that for every $10 invested in supportive housing, there is an average savings of almost $22 across health care, social services, and justice - in addition to social returns.[14]

Over the long-term, the only sustainable option for improving affordability is to expand the supply of housing, including rental units. Project approvals should be expedited and measures to increase housing density should be implemented.

To correct supply-demand imbalances, greater coordination between various levels of government is necessary. The CBA supports the establishment of a permanent housing roundtable, bringing together representatives of federal, provincial and municipal government authorities, along with bankers, builders, boards of trade, real estate professionals, market rental housing providers, non-market housing organizations, and civil society organizations. Often these stakeholders are not part of the consultation process but have substantive sectoral policy expertise and are on the frontlines of the housing crisis. A permanent roundtable would provide a valuable forum for sharing perspectives on obstacles to housing affordability, and for generating solutions.

Recommendation: We encourage the Government of Québec to contribute to efforts across all levels of government to remove barriers to housing supply. We support the establishment of a permanent housing roundtable, as we believe leveraging stakeholders' collective knowledge will create sustainable, vibrant, and healthy communities in the province. We also encourage the Government to increase social housing construction to protect the province's most vulnerable households.

[13] CMHC, Canada's Housing Supply Shortage: Restoring affordability by 2030, June 2022
[14] Canadian Mental Health Association Ontario, Housing First: The Path to Recovery

Strengthening financial literacy

Financial literacy is an essential life skill. Developing an understanding of money at a young age will help people better manage their money in the future, but people of all ages need to have the necessary tools to make informed financial decisions and the knowledge to avoid financial fraud and scams. The banking sector has long recognized that it has a role to play in supporting and strengthening financial literacy, and banks support many such programs to help Canadians.

The CBA applauds the leadership demonstrated by the Government of Québec through the introduction of a mandatory Secondary 5 course focused on financial literacy in 2017, which covers consumer rights, debt, savings, purchasing power, and taxes. This is a laudable policy, providing students with a well-rounded understanding of managing their financial well-being and building economic resiliency.

We encourage the Government of Québec to broaden its financial literacy initiatives to encompass targeted programming for priority groups, including lower-income individuals, older adults, Indigenous Peoples, and newcomers to Québec. By doing so, we can ensure that financial literacy in Québec is both inclusive and accessible.

Further, while banks have advanced security and layered fraud detection, the realities of a connected world mean that cyber threats are not limited to bank systems and technology. The Canadian Anti-Fraud Centre has noted a 40 per cent year-over-year surge in cybercrime losses, with many incidents going unreported. Globally, about three billion phishing emails are sent daily. In the digital era, cyber security is a shared responsibility, with banks collaborating with each other, the government, and law enforcement to safeguard Canada's critical infrastructure. It's also crucial for individual Québecers and the province's businesses to adopt basic cyber security practices and to be aware of common frauds and scams. Provincial government collaboration with the CBA and organizations such as the Canadian Centre for Cyber Security to disseminate important cyber security resources would support efforts to help residents of Quebec avoid cyber security threats.

Additionally, for many years now, the CBA has collaborated with the Autorité des marchés financiers (AMF) on financial literacy by sharing relevant information and best practices. The CBA now looks forward to further partner with the AMF on the upcoming Québec Financial Education Strategy, set to be published in the spring of 2024.

Recommendation: We encourage the Government of Québec to expand its financial literacy

initiatives to priority groups. Additionally, we encourage the Ministry to collaborate with the CBA and federal government agencies to increase cyber security awareness and strengthen the cyber resilience of Québecers.

Consumer protection for users of payment service providers (PSP)

The payments ecosystem continues to rapidly evolve with the surge of non-traditional PSPs. PSPs are entities, including Big Tech companies, that perform payment functions as a service or business activity and currently offer financial services and products to consumers.[15] At present, these PSPs are largely un or under-regulated and pose various risks, including the risk of loss of consumer funds (financial risks); the risk of operational and security failures; and market conduct risk. Market conduct risk refers to the behaviour of PSPs that may harm consumers.

While the Bank of Canada and the federal Department of Finance have developed a federal supervisory framework for PSPs under the *Retail Payment Activities Act* to address certain risks, the federal framework is silent on market conduct. With over 2,500 PSPs currently operating in Canada[16], and the expectations of increased use and trust that consumers will place in PSPs once they are supervised by the Bank of Canada, the absence of market conduct regulation is a significant gap in consumer protection.

Globally, the G20 and OECD have recognized that financial consumer protection requires a more targeted set of rules than general consumer protection.[17] The key risks that these principles seek to mitigate include (but are not limited to):

- Consumers incurring fees that have not been properly disclosed by a provider;
- Consumers having reliable access to their funds held by a provider, consistent with that offered by banks;
- Consumers being held responsible for fraudulent transactions; and
- Consumers not having a line of recourse in the absence of a clear complaints-handling process.

[15] Payment functions include provision/maintenance of accounts held, the holding of funds, the initiation and authorization of electronic funds transfers or clearing and settlement services on behalf of end-users.
[16] Canada Gazette, Part 1, Volume 157, Number 6: Retail Payment Activities Regulations.
[17] Market conduct and subsequent consumer protections associated with financial product principles are outlined in the G20/OECD High-Level Principles of Financial Consumer Protection.

Failure to address these risks, among others, can decrease consumer trust in the financial system. Financial services and products have the potential to disproportionately impact the well-being of consumers and must be addressed specifically rather than through overarching consumer rights across industries.

Recommendation: As part of Quebec's consumer protection framework, we encourage the Ministère des Finances to support the adoption of a financial consumer protection regime targeted at PSPs. Enhancing standards for financial consumer protection should also extend to entities that embed payments processing for merchants, as they introduce the same risks as PSPs.

Transition to net-zero

The financial sector is central to securing an orderly transition to a low-carbon economy. By financing the climate transition, banks are helping Canada meet its net-zero ambitions while ensuring we reliably meet energy demands in a volatile global context. Though banks are helping to finance greener forms of energy, the full transition to net-zero will not happen overnight.

The CBA acknowledges Québec's plans for substantial investments to support the climate transition over the next decade, outlined in the province's first framework policy on electrification and the fight against climate change, the 2030 Plan for a Green Economy. We agree that the implementation of the 2030 Plan for Green Economy will rely on many sources of funding, including public and private'. Businesses, governments, and individuals working together on the fundamental reshaping of our economies and societies is critical. Banks look forward to opportunities to support the generation of more clean energy, grow our economy, and cut emissions across the province.

Additionally, the transition to a net-zero economy provides further reason to review Canada's tax system, consistent with our second recommendation. Some estimates suggest that Canada will need approximately $2 trillion in over the next three decades to transition to a net zero economy.[18]

Recommendation: We encourage the Government of Québec to collaborate with industry and the Government of Canada to design targeted investments and tax incentives that create pathways to net-zero, while taking a balanced and flexible approach to new regulation.

[18] RBC, The $2 trillion transition: Canada's road to net zero, October 2021

Conclusion

Upcoming challenges to Québec, whether influenced by global or domestic factors, highlight the need for a strong and stable banking sector that will benefit the province's economy. Directly and indirectly, the banking sector plays a vital role in the province's economy. A strong banking sector supports Québec's business ecosystem, particularly as it relates to lending to SMEs.

Thank you again for the opportunity to contribute to the Government of Quebec's 2024-2025 pre-budget consultations. Our recommendations aim to ensure the banking system continues to support Quebec families and businesses through the uncertainty of today, while continuing to build a strong foundation for tomorrow.

Please do not hesitate to contact the CBA, and especially our Director, Québec Region, Eric Prud'homme, at eprudhomme@cba.ca or 514-840-8747, to discuss our pre-budget submission further.