POLICY PERSPECTIVES

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IT'S BECOMING MORE COSTLY AND COMPLEX TO DO BUSINESS IN B.C.

HIGHLIGHTS

- The aggregate tax burden on B.C. businesses has increased significantly in recent years. Since 2013, the implementation of new provincial taxes and some tax increases amount to nearly $5 billion in additional taxes paid annually beyond what businesses would have paid if the changes had not been implemented.
- The single biggest tax increase is linked to the elimination of the HST and return of the provincial sales tax. Under the PST system, businesses will pay an estimated $3 billion in sales tax on inputs used in their operations.
- The next biggest tax increase is B.C.'s new Employer Health Tax. Once MSP premiums are fully eliminated next fiscal year, we estimate the net tax impact on business is approximately $800 million.
- The third biggest tax increase is attributable to the two-percentage point increase in the corporate income tax rate in the province since 2013.
- Recently, electricity used by businesses was exempted from the PST, which provided a small tax break for businesses. The small business tax rate was also trimmed.
- Numerous changes to provincial labour laws and regulations are also adding to business operating costs.
- Since 2016, B.C. has seen a host of environmental reviews and legislative or regulatory changes which are completed or still underway. This is a policy domain where the cumulative impact of new laws and regulations makes it increasingly costly for businesses to operate and is discouraging new investment in some sectors.
- Taken holistically, the cumulative impact of higher taxes and mounting regulatory costs is weighing on investment and business sentiment in B.C. Adding to these competitiveness concerns is the fact that corporate taxes have been reduced significantly in neighbouring jurisdictions.

In most sectors of our economy, the cost of running a business in B.C. has risen significantly over the past few years, due in part to government decisions and changes in various areas of public policy. The impact has been greatest on medium-sized and large firms and companies operating in "traded-goods industries."[1] However, in truth, government-determined costs have been trending higher for most businesses in the province.

For a typical B.C. business, the most visible government-driven cost increases have come in the form of higher and – in certain cases -- new taxes and fees. But apart from taxes, a myriad of other policy and regulatory measures have also been adding to the economic burden on business.

It is important to note that, taken individually, many of the tax and other policy measures discussed in this paper may be well-justified. In some cases, the costs attached to specific policy changes can be absorbed by businesses with little negative impact. What matters more is the layering-on of additional taxes and regulatory costs, together with the emergence over time of ever-

[1] Defined as industries that produce goods that can be exported. In B.C., they include energy, forestry, mining, agri-food, and all segments of manufacturing.

more complicated and delay-prone administrative processes.

Evaluating and quantifying the effects of tax and regulatory measures is challenging. Taxes, for example, may not be applied uniformly. Preferential small business tax rates and the structure of the new Employer Health Tax – which depends on the number of employees in an organization – are examples. The amount of tax paid by a business is affected by its industry sector, its energy intensity, whether it must ship its goods beyond the local market, and its use of capital versus labour inputs, among other factors. Regulatory requirements also differ across sectors and firms: pulp mills, mining companies and agricultural producers, for example, face government-determined regulatory and compliance issues that a software company or professional services firm in Metro Vancouver probably does not. For this reason, this report focuses on business tax changes at the aggregate level and other significant regulatory and policy developments that have broad cross-industry implications. We do not seek to delineate which industry sectors have been most affected by any specific government measure.

Most of the tax and regulatory changes considered in this report fall primarily in the provincial domain. However, to present a more complete picture, a handful of recent federal policy measures that have affected business in B.C. are also discussed. We also touch very briefly on the topic of property taxation at the local government level.

The period of interest starts in 2013. This timeframe was chosen to capture policy and regulatory developments during the tenure of the previous B.C. government as well as that of the current government.

A RISING AGGREGATE PROVINCIAL TAX BURDEN ON BUSINESS

The tax burden on B.C. businesses has increased significantly in recent years. As documented below, this fiscal year companies in B.C. are paying nearly $5 billion in "extra" or additional taxes, compared to the situation they faced back in 2013.[2]

The single largest tax hike for businesses in B.C. came in April 2013, when the Harmonized Sales Tax (HST) was eliminated and the province reverted to the antiquated **Provincial Sales Tax (PST)**. With the HST, a value-added consumption tax, businesses received offsetting credits for taxes paid on inputs purchased as part of the production process (such as equipment, software, legal services, construction materials, and vehicles). In contrast, with few exceptions, under the PST system businesses pay the 7% sales tax on most purchased inputs and receive no offsetting credits. Most British Columbians probably experience the PST as a sales tax that applies when consumers buy goods (and some services) at the retail level – e.g., clothing, electronic products, building materials, etc. But the reality is that businesses are responsible for approximately 40% of all PST revenue collected by the province.

The single largest tax hike for businesses in B.C. came in April 2013, when the Harmonized Sales Tax (HST) was eliminated and the province reverted to the antiquated Provincial Sales Tax (PST).

In the first fiscal year following the reinstitution of the PST, the province collected $5.3 billion in sales tax revenue. This year (2019-20) the government expects to raise $7.6 billion from the PST. Assuming businesses account for ~40% of all PST revenues, collectively they will pay over $3 billion in sales tax this year, on inputs used in the production and delivery of a wide variety of goods and services. Under the HST system this sales tax would have been fully credited. Apart from the direct tax burden imposed by the PST, there are significant additional business compliance costs[3] from having to deal with the PST and the separate federal GST system.

The return to the PST eliminated two key reasons for switching to the HST in the first place – i) reducing the tax burden on capital investment, and ii) making B.C.'s export-oriented and import-competing industries more internationally competitive. Reducing the tax burden on capital investment (buildings, machinery,

[2] This calculation ignores the impact of the temporary measures announced by the federal government in November 2018 which will allow quicker write-offs on certain categories of business investment. In its 2019 budget, the B.C. government accepted the pass-through impact of these federal measures (B.C.'s corporate income tax system is integrated with that of the federal government). For B.C., the estimated cost of this is $800 million over the next three years, which can be considered as a form of temporary tax relief for B.C. companies undertaking investments that qualify for immediate or faster write-offs under the federal tax changes.

[3] We estimate these added compliance and reporting costs at $200 million per year – costs that B.C. firms did not face under the former HST.

equipment, technology platforms and so on) is beneficial because it strengthens the case for deploying capital in B.C. And that matters to workers and citizens, not just to business owners, because new investments make B.C. firms more productive and allow them to pay higher wages/salaries and to expand their operations.

Compared to the PST, the HST system was also a way to reduce costs and improve competitiveness for B.C. exporters and for other businesses that compete with imported goods in the domestic market. For most B.C. exporters, prices are set in international markets, meaning they must absorb the additional costs flowing from the application of the PST. For exporters with some flexibility in pricing, higher government-imposed costs from the PST may lead them to hike the prices of their products, but this may cause them to become less competitive and lose both market share and export sales. Since the restoration of the PST, the government has done very little to mitigate the additional economic burden on B.C. businesses, including the incremental burden on capital investment, compared to the situation that prevailed under the former HST regime.

Two one percentage point increases in **B.C.'s corporate income tax rate** since the start of 2013 have also added to the business tax burden. A one-point increase (from 10% to 11%) was legislated in 2013, followed by a second increase in 2017. Based on budget forecasts, the two-point jump in the CIT rate translates into an additional $700 million in provincial government revenue in the current fiscal year, compared to the revenue that would have been collected had the rate remained at 10%.

It is important to recognize that all other jurisdictions in North American that have implemented carbon pricing schemes have taken steps to shield their trade-exposed industries from all or part of the tax to ensure they remain competitive. B.C. now stands alone in having done essentially nothing along these lines.

The ***B.C. carbon tax*** was frozen at $30/ton of emissions between 2012 and 2017, but the freeze was then lifted and the tax was increased to $35/ton in 2018 and then to $40/ton on April 1st of this year. These increases translate into an additional $428 million in revenue in 2019/20 and $656 million the next fiscal year (when the tax rises to $45/tonne). We estimate that business are responsible for 40-50% of the carbon tax revenue, so the rising carbon tax will add ~$170-$215 million in aggregate operating/production costs this year beyond what companies would have paid if the tax had remained frozen at $30/tonne.

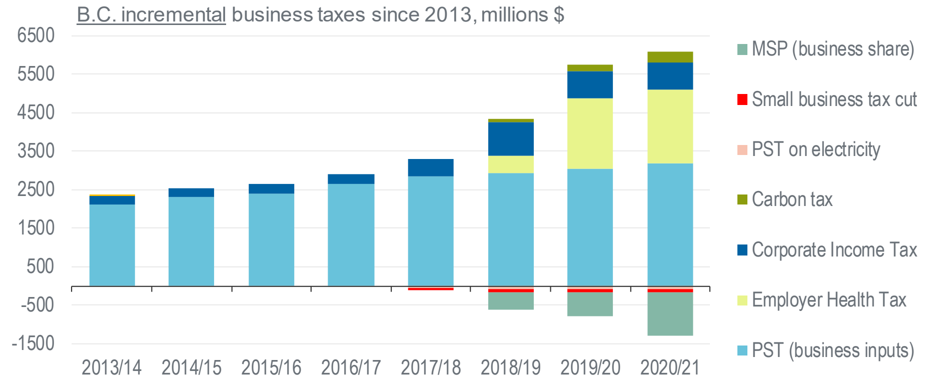
It should be recalled that under B.C.'s carbon tax policy as unveiled in 2007-08, the government promised to use part of the revenue from the new tax to finance a two-point reduction in the corporate income tax rate over four years, phased in as the carbon tax increased from $10/ton to $30/ton. The government of the day followed through on this pledge until 2012. However, as noted above it reversed course in 2013, hiking the CIT rate from 10% to 11%, with a further one-point increase announced in the NDP's first budget. Today, large and mid-sized B.C. businesses face a provincial CIT rate of 12%, the same rate as in 2008 when the carbon tax was adopted. For most companies, the net result of the province's "carbon tax shift" regime is that they are paying exactly the same corporate tax rate as in 2007, but collectively businesses now have to stump up several hundred million dollars more every year to cover the extra cost of fossil fuel energy and energy inputs.

With revenue neutrality jettisoned and the carbon tax on track to climb to $50 per ton of emissions by 2021, the competitive position of some of B.C.'s biggest export industries – including forestry, mining, natural gas, manufacturing and transportation – continues to erode. It is important to recognize that all other jurisdictions in North American that have implemented carbon pricing schemes have taken steps to shield their trade-exposed industries from all or part of the tax to ensure they remain competitive. B.C. now stands alone in having done essentially nothing along these lines.

The province's recently implemented ***Employer Health Tax (EHT)*** represents the second largest tax increase for B.C. businesses since 2013. In its first full year, the EHT is projected to raise $1.8 billion, with all of the revenue coming from the subset of employer organizations with annual payrolls over $500,000. Large employers shoulder a disproportionate portion of the EHT tax burden. Eliminating Medical Services Plan (MSP) premiums provides some offset, but the net effect is a substantial payroll tax increase for businesses because employers have only paid approximately one-half of aggregate MSP premium revenue (roughly $1.1 billion). The overall result is that employers in B.C. will be paying $700-$800 million more in payroll tax each year under the EHT, even after MSP premiums are fully eliminated in 2020-21.[4]

Provincial Business Taxes — Summary: In aggregate, B.C. businesses will pay $4.8-$5.0 billion more in taxes every year than they would have if the tax changes discussed above had not been introduced. This is a rough estimate, but clearly represents a sizable incremental tax load on B.C. businesses, especially considering the burden of new/higher B.C. business taxes is heavily tilted towards medium- and larger-sized enterprises. We should note the above summary estimate includes the fact there have been a couple of small tax reductions for B.C. business in the last two years: elimination of the PST on electricity consumed by businesses, saving businesses about $80 million annually; and a minor reduction in the B.C. small business tax rate from 2.5% to 2%, yielding tax savings of around $70 million annually for very small firms. In addition, as noted in footnote 2, in its 2019 budget the B.C. government accepted the pass-through effect of the temporary business tax measures announced by the federal government last fall, which allow for quicker write-offs on new investment in certain capital assets. This provincial decision will generate a time-limited overall tax saving of $800 million, for companies undertaking qualified investments over the next three fiscal years.

FIGURE 1: **BUSINESSES WILL PAY AN ADDITIONAL $5 BILLION TO THE PROVINCE THIS FISCAL YEAR DUE TO TAX INCREASES**



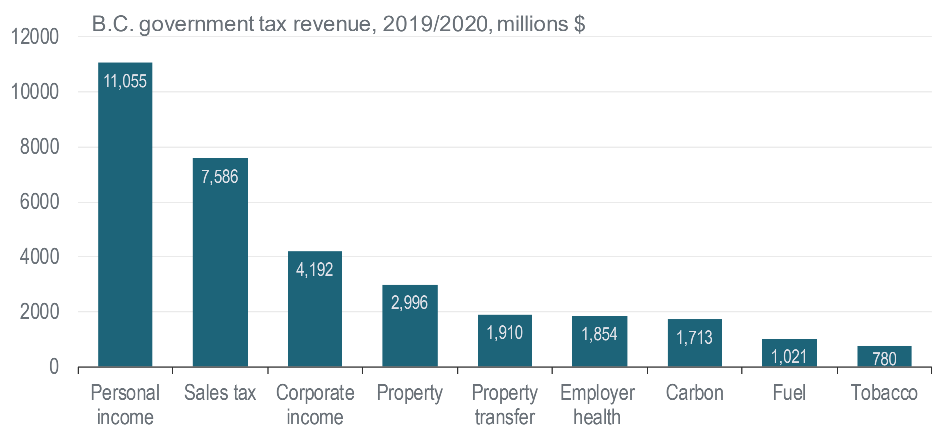
Source: B.C. Budgets and BCBC for some estimates of share of taxes paid by businesses.

SOME OTHER TAXES ARE ALSO RISING

Municipal property tax rates change annually, depending on assessed values. As a result, property tax rates can rise or fall, but the amount of property tax paid by businesses and collected by municipalities generally rises steadily. Historically, municipal property tax revenue has increased at a pace well above inflation plus population growth. In 2018, municipal property taxes paid by B.C. businesses amounted to $1.76 billion, an increase of 22% over what was paid in 2013. Over the same period, the province's population expanded by 7.8% and cumulative inflation was 9.1%. Thus, in 2018 the total municipal property tax bill facing business was about 5% higher, or almost $76 million more, than it would have been had municipalities kept spending increases in line with population growth and inflation. Across all businesses in the province, $76 million is not a huge sum. The difficulty, however, is that the additional tax – and the overall municipal property tax burden on business generally – tends to be unevenly distributed. Many businesses pay taxes dramatically out of alignment with their consumption of locally-provided services. Many municipalities have taken advantage of their wide authority to set tax rates for different classes of property to levy high rates on industrial and commercial classes and low rates on residential property. And in recent years some B.C. businesses have been hit with dramatic property tax hikes, while others have experienced more moderate increases depending on their location and industry sector.

[4] In 2019, the government will collect the MSP (at half the rate it was originally charged at) as well as the new EHT. This "double-dipping" only applies for this fiscal year as MSP premiums are fully eliminated next year.

FIGURE 2: **SALES TAX AND CORPORATE INCOME TAX ARE SIGNIFICANT SOURCES OF REVENUE FOR THE PROVINCE**



Source: B.C. 2019 Budget.

The federal government has also adapted measures which impact the business tax burden, apart from the temporary investment tax incentives unveiled last fall and referenced in footnote 2 above.

Changes to the tax rules governing Canadian-controlled private corporations (CCPC) introduced in 2018 have increased the tax burden (and tax-related compliance costs) for some smaller private businesses. More restrictive rules on "income sprinkling" and provisions that make it less attractive to earn investment income in a CCPC have reduced some of the previous tax advantages of operating a small business. We have not attempted to quantify the effects of these changes, but they have increased the tax burden on many smaller firms in B.C.

Rising CPP premiums are the most significant business tax increase the federal government has overseen in several years. Beginning in 2018, employers are required to pay an additional 0.15% in CPP premiums on their payrolls (up to a maximum threshold level of income). The premiums continue to climb annually thereafter, adding 0.5% to the 2018 rate by 2021 and a full percentage point by 2023. This translates into hundreds of millions of dollars of extra payroll costs for B.C. employers.

The federal government has also enriched EI benefits for maternity and compassionate leave. (The B.C. government followed suit, recently introducing amendments to the *Employment Standards Act* to expand maternity leave and extended and enhanced compassionate leave.) These are minor changes. The federal government implemented a slight reduction in EI premiums for 2019, which will save employers relative to the amounts remitted in 2018.

A NOTE ON TAX TRENDS IN OTHER JURISDICTIONS

Even as the business tax burden has grown in B.C., trends in tax policy in other jurisdictions have also undermined the province's relative competitive position.

Corporate and personal income taxes have been slashed in the United States. Of greatest concern, the business tax advantages that B.C. (and Canada) once enjoyed vis-à-vis the U.S. have largely disappeared. At the same time, Alberta has committed to lowering its provincial corporate income tax rate from 12% to 8% in stages, with the first one-point reduction coming into effect on July 1, 2019. These developments are adding to the competitive pressures on British Columbia. In addition, the relatively high personal income tax rates that B.C. levies on skilled workers, experienced managers and entrepreneurs are increasingly problematic at a time when many other jurisdictions are stepping up efforts to attract and retain top talent.

OTHER B.C. GOVERNMENT POLICY CHANGES AFFECTING BUSINESS

In the area of ***provincial employment law and policy*** there have been a number of recent developments that are of interest to the province's business community.

- Changes to the *B.C. Labour Code* and to the *Employment Standards Act*. While some updates to existing laws and regulations are justified, some of the changes enacted in 2018-19 will result in additional costs and greater legal complexity for B.C. businesses.
- British Columbia's minimum wage was increased to $12.65/hr on June 1, 2018. In June 2019, it rose another $1.20/hr. Thus, within the span of a year, the minimum wage jumped by more than 20%. The impact is mainly on smaller firms and service businesses that rely

disproportionately on entry-level workers.[5]

- The provincial Ministry of Labour recently established a temporary foreign worker registry.
- WorkSafeBC's operations and policies are being reviewed as part of the government's pledge to make the system more "worker-centered." The average WorksafeBC assessment rate held steady in 2019, but there is concern in the employer community that rates will be under significant upward pressure going forward given the government's inclination to enrich and broaden compensation for injured workers.
- Last year, the NDP government imposed a "Community Benefits Agreement" model for certain public sector construction projects. Over time, this will push up costs for both taxpayers and the users of the infrastructure assets developed under CBAs.

Since 2016, B.C. has seen a host of ***environmental reviews and legislative or regulatory changes*** that are either completed or still underway. This is a policy domain where the cumulative impact of new laws and regulations makes it increasingly costly for businesses to operate and discourages new investment in some sectors. Because it is difficult to quantify regulatory costs in aggregate, the main environmental policy and regulatory changes of interest to business are simply listed below:

- New provincial environmental assessment legislation has been passed. While the final regulations are still being developed, our judgement is that B.C.'s natural resource, infrastructure and manufacturing sectors will all be adversely affected by the changes to EA processes and new requirements imposed on project proponents.

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- Updated greenhouse gas reduction targets have been introduced as part of the province's refreshed climate plan. In addition to a higher carbon tax, the province is committed to more ambitious targets for reducing GHG emissions overall as well as for the major emitting sectors – industry, the built environment, transportation and agriculture.
- B.C. intends to legislate revised and more stringent low-carbon fuel standards and zero-emission standards for new vehicles. Both of these actions will lead to higher costs for businesses (and consumers) over time.
- The government is working on new and more stringent rules to limit methane emissions in the upstream oil and gas industry.
- B.C. is adopting higher energy efficiency requirements under the B.C. Building Code and intends to develop a new Energy Step Code for buildings.
- The government recently legislated a new "professional reliance" regime for regulating B.C.'s natural resource industries. For companies in natural resource sectors, the updated PR regime will translate into higher compliance and operating costs.
- The government has committed to developing provincial species at risk legislation, although at this stage few details on what this may entail are available.
- B.C. has increased water rental rates over the last few years.
- The province has implemented new rules for land-based spills management and responses.
- The province is advancing updated Cariboo habitat protection plans that, once in place, will further restrict access to land and resources and impose additional costs on affected industries.
- In the case of forestry, the government has adopted Bill 22 (governing transfers of tenure in the forest industry) and made changes to the *Forest and Range Practices Act*; in both cases, the result is higher costs and/or added legal complexity for logging firms and lumber producers.
- Last year, B.C. unveiled a new regulatory regime for salmon farming that will reduce industrial activity in the sector over time.
- In common with Ottawa, B.C, is adopting the United Nations

[5] It should be noted that the Business Council supports the gradual move to a higher minimum wage.

Declaration on the Rights of Indigenous Peoples (UNDRIP). However, this is being done without a clear indication of how it will apply to or influence the work of individual government Ministries, regulatory agencies, and statutory decision-makers. In practice, we believe the net result will be higher costs and increased complexity for companies doing business on the land base, but also for First Nations pursing land-based economic development.

SUMMARY THOUGHTS

Businesses in B.C. today are paying billions of dollars in additional/ higher provincial taxes beyond what they faced five or six years ago. In addition, the regulatory and broader legal environment for many B.C. industries, including many of our key export sectors, has become costlier and more complex. At the same time, competing jurisdictions have cut or are cutting taxes, are streamlining regulatory processes, and taking determined steps to become more competitive. B.C. is following a path that moves in the opposite direction: increasing the tax burden on firms and making it harder and more expensive to do (and grow) business.

Taken holistically, the cumulative impact of higher taxes and mounting regulatory costs is weighing on investment and business sentiment in B.C. The risk is that the province will chase new capital away and deter some companies from expanding their B.C. operations. Policy makers need to be more sensitive to the impact of provincial tax and regulatory policies on business. They should understand that without new investment and a desire by companies to expand, fewer jobs will be created, some existing jobs will be in jeopardy, and overall economic growth in the province will suffer.

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