

Budget Recommendations

Presented to the Select Standing Committee on Finance and Government Services

by the Chartered Professional Accountants
of British Columbia

BUDGET 2019-2020



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INTRODUCTION

The Chartered Professional Accountants of British Columbia (CPABC) is the training, governing, and regulatory body for more than 35,000 CPA members and 5,000 CPA candidates and students.

CPABC carries out its primary mission to protect the public by enforcing the highest professional and ethical standards and contributing to the advancement of public policy. CPAs are recognized internationally for bringing superior financial expertise, strategic thinking, business insight, and leadership to organizations.

CPAs are on the front lines of business in British Columbia, and they see firsthand what issues are affecting investment and the economy. Based on results from the annual CPABC Business Outlook Survey, 65% of CPA respondents perceive the current state of BC's economy to be 'excellent' or 'good,' and almost half (49%) think BC's economy will stay the same over the next two years.

This is positive news, as the province has had impressive economic growth in the past few years. According to CPABC's BC Check-Up, 2017 marked the fourth consecutive year of solid economic expansion in BC and the province had a GDP growth rate of 3.9% in 2017.¹

BC's population grew by almost 1.3% to 4.8 million in 2017. Of the 49,502 new residents, over 60% came from outside Canada, while just over one quarter came from other provinces. Population growth was largest in our province's most urban regions— Southwest BC, Thompson-Okanagan, and Vancouver Island/Coast.

Corresponding with this population growth is continued demand for real estate. Despite efforts to cool the real estate market in 2016 and 2017, housing prices continued to soar. As such, economic activity related to the housing market continued to expand, leading to significant job gains in industries like construction and finance, real estate, insurance and leasing.

Strong economic growth pushed employment to 2.47 million in 2017. With 87,300 new jobs, it was our province's largest job gain in the past decade. Not surprisingly, most of this job creation occurred in Southwest BC (56%), Vancouver Island/Coast (22%), and Thompson-Okanagan (13%).

In terms of BC's exports, which account for 38% of the province's real gross domestic product (GDP), British Columbians saw an increase of 12.7% in the value of exports to international destinations in 2017, despite ongoing trade issues with the United States.²

This was largely due to a dramatic increase in the value of BC's energy exports, driven by greater demand for natural gas from the US and for coal from Asian markets. Not surprisingly, exports of pulp and paper products to the US declined, but this was offset by greater demand from China, resulting in a 12.4% increase in the overall export value of this commodity.

Looking forward, predictions call for moderated economic growth, with TD Bank Economics projecting a real GDP growth rate of 2.4% in 2018.³

¹ TD Economics, Provincial Economic Forecast, Growth "Normalization" Underway After Banner 2017, June 19, 2018.

² BC Stats, Annual BC Origin Exports, data released May 3, 2018. International trade in commodities calculated on a customs basis.

³ TD Economics, Provincial Economic Forecast, Resilience in the Face of Uncertainty, March 15, 2018.

BC's economy can expect some moderation for the rest of 2018 and into 2019. The province is starting to see a cooling in the housing market, likely due to the new speculation tax and other policy measures, which may have slowed demand for single-family homes. The ongoing uncertainty over trade relationships with the US is starting to affect on BC exporters.

Given the current environment, it's critical that BC remains competitive and attracts investment, especially given our province's lagging business productivity. Low productivity undermines the long-term health of the economy and impacts the province's ability to fund education, health, and social services.

Moving back to the provincial sales tax (PST) made it more expensive to do business in our province, resulting in less available investment for equipment, new technology, and employee training.

The new employer health tax (EHT) will also add additional costs to doing business in BC. The province already struggles with lower wages; at \$55,096, BC's average labour compensation per worker is almost \$4,000 less than the national average.

With lower wages and high housing costs in the province, many employers are finding it a challenge to recruit and retain talent, especially skilled labour in key sectors such as tech and resources. While the educational attainment level of BC's labour force has improved over the past five years, it still lags behind the national average of 73%, again reflecting low business productivity.

It is important that the provincial government support a competitive, productive economy that allows businesses to grow sustainably.

As such, CPABC recommends that the BC government focus on the following policy areas to help BC businesses succeed:

- **Ensure BC's business tax competitiveness;**
- **Minimize the labour skills gap; and**
- **Maximize BC's export potential.**

Consultations aren't easy but they are necessary. We all have to do it in our own businesses, with employees, with stakeholders — it is not an easy thing. Especially when politics are becoming more polarized, and there's not so much a middle ground anymore. Still, let's engage and talk about solutions to create sound policies that work.

Ted Schisler, CPA, CMA
Senior Vice-President & COO, Interior Savings Credit Union, Kelowna, BC

ENSURE BC'S BUSINESS TAX COMPETITIVENESS

Maintaining business competitiveness is vital to long-term economic sustainability. Any negative tax changes could affect our province's ability to attract new businesses and investment. Over half of CPABC's members indicate that an increase in the provincial corporate tax rate would impact their company's or their clients' business investment plans.

CPABC continues to reiterate the need for a competitive tax regime in the province. According to the latest CPABC Business Outlook Survey, only one-third of CPA respondents think BC's tax rates and incentives are competitive, compared to 47% a year ago. A modern, efficient, and competitive tax system is critical to the productivity and overall economic success of BC.

This is reinforced by recent warnings from both the Organisation for Economic Cooperation and Development (OECD) and the International Monetary Fund (IMF) that Canada needs to reassess its tax system to remain competitive and keep up with shifting global tax changes, particularly in the wake of corporate tax cuts in the US.⁴

Our national body, CPA Canada, has also urged for a comprehensive tax reform at the federal level.

For the purposes of this submission, CPABC will focus on the employer health tax and the provincial sales tax on business inputs.

Employer Health Tax (EHT)

In the latest Business Outlook Survey, we asked CPAs how the implementation of the EHT will have an impact on businesses. Almost two-thirds state the EHT would 'increase [the] costs of doing business.' This is in line with findings from a recent survey by the Canadian Federation of Independent Business, which indicated that almost two-thirds of business owners say the payroll tax would have a negative impact on their businesses.⁵

While CPABC understands that the intention of the EHT is to shift health care costs from individuals to businesses, the cost burden will ultimately be placed on workers, as businesses could shift the additional cost back to employees in forms of reduced benefits, contract employment, and/or less frequent wage increases. The costs will not simply be borne by the employers, and will ultimately be passed along to their employees.

For those businesses that did not previously pay for MSP premiums, the additional costs of the EHT could further reduce financial capacity to pay wages. This would have an impact on the ability of many small and medium-sized employers to recruit and retain talent in an already tight labour market. Given this sector makes up the bulk of BC's economy, this is a serious concern.

Businesses, like employees and like investors, are transient in that they have the ability to decide where they actually want to conduct their business, where they source raw material, and where they employ people, which ultimately determines where tax revenues are generated.

J.P. Fowler, CPA, CA
CFO , Stewart Family Estates, Kelowna, BC

⁴ Sophie Nicholls Jones, "Canadian competitive edge at risk under current tax system, say experts," CPA Canada, August 10, 2018.

⁵ Richard Truscott & Mackenzie Cumberland, "Opinion: Disappointed business owners give B.C. gov't a 'D' grade," Vancouver Sun, July 2018.

⁶ CPABC, BC Check-Up 2018, www.bccheckup.com.

At \$55,096, BC already has a lower average compensation per worker amongst competitive jurisdictions like Ontario and Alberta.⁶ With high housing and living costs, BC may become a less desirable place for mobile workers, especially young professionals who can take their skill set anywhere.

This is especially concerning given the job vacancy rate is at record levels across Canada, making it easier for workers to find well-paid work in other parts of the country. This is a significant concern for BC CPAs, as they have consistently ranked the ability to recruit and retain skilled talent as the top challenge for business success in BC, which we discuss in the next section of this report.

Provincial Sales Tax (PST)

Only one-third of CPA respondents in the Business Outlook Survey think that BC's tax rates and incentives are competitive. And when asked what the government can do to improve our tax competitiveness, just over half (52%) identified 'ensure tax rates are globally competitive' as a policy option.

The current tax regime is a hindrance on investment and productivity, negatively affecting job creation and economic growth.

One way to ensure our tax rates are globally competitive is to simplify our tax regime. CPABC has consistently advocated for a modernized sales tax, and we are disappointed that the government has yet to act on the recommendations from the Commission on Tax Competitiveness.

In the most recent survey, almost half of our members indicate that the lack of input tax credits increased the cost to conduct business, while 21% indicate it has discouraged capital investment and 13% said it has delayed expansion plans.

By introducing an input tax credit mechanism, the government would remove a major hurdle for businesses to invest in capital, such as equipment, to improve productivity and, ultimately, competitiveness.

CPABC Recommendations

#1 CPABC recognizes that the government has committed to implementing the EHT in January 2019 and that this has serious implications for the provincial budget. However, CPABC is aligned with other business organizations in the recommendation to delay the implementation of the EHT until 2020 to coincide with the elimination of MSP premiums. This will give the government an opportunity to consult with BC businesses and fully assess what impact the EHT will have on business productivity.

#2 CPABC continues to advocate for the implementation of full PST exemption on business expenditure to encourage investment, maintain our province's business competitiveness, and drive productivity that is crucial for economic growth.

MINIMIZE THE LABOUR SKILLS GAP

CPABC's members have consistently ranked the ability to attract and retain skilled labour as the most substantial challenge to business success in BC today. Almost three-quarters (73%) say their business is experiencing recruitment challenges in finding employees with the right skills.

In 2017, BC gained a record 87,300 new jobs, to reach 2.47 million positions in total.⁷ Most of these jobs were created in BC's three most diversified regional economies—Mainland/Southwest, Vancouver Island/Coast, and Thompson-Okanagan. These development regions have the most educated workforces, which are largely employed in highly skilled service industries.

Other regions are also beginning to see increased demand for skilled employees, and the BC government has projected that between 2017 and 2027, over three-quarters of the expected 917,000 job openings will require some post-secondary education and training.⁸

Given this increased need for skilled labour there is growing concern about a labour skills mismatch, which occurs when a worker has either more or fewer skills than are needed for their job.⁹ Such a discrepancy can produce societal challenges; and according to the Conference Board of Canada, skills mismatches and shortfalls cost the province of BC billions in foregone GDP and millions in foregone tax revenues.¹⁰

Acquiring higher or specialized education is important for gaining and maintaining employment. However, new graduates often do not have the necessary skills and experience required to be work-ready.

Historically, post-secondary institutions, particularly universities, have focused on producing critical and creative thinkers, not grooming students for the job market. In addition, the skills employers require today may not be relevant in a year's time, making it extremely challenging for universities to tailor their curricula accordingly.¹¹

According to respondents from the CPABC Business Outlook Survey, the greatest challenge to business success in BC today continues to be the 'ability to attract and retain high caliber employees/skilled labour.' For the past five years, CPAs have consistently ranked this as the biggest challenge to business success in BC.

CPABC Business Outlook Survey 2018
Base: All Respondents, n=2,121

⁷ CPABC, BC Check-Up 2018, www.bccheckup.com.

⁸ WorkBC, British Columbia 2027 Labour Market Outlook.

⁹ OECD, Getting Skills Right: Skills for Jobs Indicators, July 10, 2017.

¹⁰ Conference Board of Canada, Skills for Success. Developing Skills for a Prosperous BC, February 2015.

¹¹ Source: SFU faculty spokesperson.

¹² Business Council of Canada, News, Every university and college student should have access to work-integrated learning, business and post-secondary leaders say, June 2, 2016.

In order to match individuals to the right jobs, and to allow businesses to stay competitive and productive, school-to-work transitions need to be improved through initiatives between post-secondary institutions and employers.

The Canadian Business/Higher Education Roundtable has committed to making work-integrated learning an essential part of undergraduate education.¹² One of the most commonly known work-integrated learning models is the co-operative (co-op) program, which has been widely accepted in Canada and the US.

Many BC universities and colleges already offer co-op programs to undergraduates. The programs alternate periods of academic learning with workplace experience for terms of four to eight months. This produces graduates who are better equipped with work-ready skills. Several high technology companies, such as Hootsuite, prefer to hire junior workers who have completed a co-op program.¹³

BC's post-secondary educators and industries need to expand their efforts to work together to change and improve their curricula and provide applicable job training, ensuring a supply of qualified graduates who are work-ready.

CPABC Recommendation:

#3 CPABC continues to recommend that the BC government make work-integrated learning a mandatory component of post-secondary education and work with post-secondary institutions and industry to explore innovative approaches that would create a broader-range of opportunities for students beyond the conventional co-op positions that are in place.

Our company is starting to get big enough to recruit and retain staff through the co-op program with the University of Victoria. It has been a good experience so far. It's also nice to be able to get local talent this way instead of having to recruit from elsewhere, which was something we've had to do for certain roles in the past.

Eric Erikson, CPA, CA
CFO, Redlen Technologies, Victoria, BC

¹³ Source: Hootsuite representative.

MAXIMIZE BC'S EXPORT POTENTIAL

The export of goods and services is the foundation of BC's economy. In 2017, the exports of goods and services to other provinces and international destinations constituted 38% of BC's real GDP. This sector generates not only thousands of direct jobs and income, but many more indirectly.

However, BC still lags behind the country as a whole with respect to foreign exports. In 2016, exports of goods and services to other countries accounted for 22.8% of BC's GDP, compared with the national average of 31%.

In 2017, BC earned \$43.7 billion from the export of goods, with over three-quarters of this from the natural resource sector. Based on total value, BC's top five export products in 2017 were as follows:

- Energy products — \$11.1 billion, or 25.3%;
- Wood products — \$9.73 billion, or 22.3% of total exports;
- Metallic minerals — \$5.34 billion, or 12.2%;
- Machinery and equipment — \$4.9 billion, or 11.2%; and,
- Pulp and paper — \$4.4 billion, or 10.1%.¹⁴

Just over half of all BC's exported goods were destined for the US market. However, BC's exports make up only 5.4% of all Canadian exports of goods to US in 2017.

Despite BC's dominance in Canada's softwood lumber industry, our province is a comparatively small player in trade with the US.

Disruptions in international trade relations have been affecting BC exporters. The expiration of the North American Softwood Lumber Trade Agreement in 2015, the new US-Mexico-Canada Agreement (USMCA), as well as Brexit in Europe could all have an impact on the volume and revenue of our exports.

Fortunately, over the past decade and more, BC's exporters and government have worked to enter new markets and diversify their products to reduce dependency on the US and open up new opportunities with other countries.

But entering new markets is not simply a matter of finding new customers in other countries. Exporters looking outside their traditional markets are required to understand different cultures, competitors, and technical or government requirements.

Given the trade dynamics with the United States, it is not surprising that CPA members ranked 'barriers to trade' and the 'current value of CAD vs. USD' as the second and third most challenging economic issues for business success in our province today. 'Housing prices' was the top challenge.

CPABC Business Outlook Survey 2018
Base: All Respondents, n=2,121

¹⁴ CPABC, BC Check-Up, www.bccheckup.com.

BC enjoys preferential trade relations with markets throughout the Americas, Asia and Western Europe. The recently signed Comprehensive Economic and Trade Agreement and the Comprehensive and Progressive Agreement for Trans-Pacific Partnership should benefit BC exporters, who enjoy a locational advantage, particularly with the US and Asia, with efficient and modern water, rail, road, and air connections to these markets. In addition, a low Canadian currency relative to the US dollar, should increase the attractiveness of our products.

BC's brand in its traditional exports is recognized worldwide. And it is important to continue to grow our province's share of international trade, by focusing on traditional products and by diversifying the product mix for both goods and services, adding value to products where possible, and entering new markets.

CPABC Recommendation:

#4 CPABC encourages the provincial government to explore ways to diversify markets and products (including services) by collaborating with other governments, exporters, and industry associations to establish new trade relations and maintain existing ones, and to devote resources to further research on what support BC exporters will need to grow their market influence.

HIGHLIGHTS FROM CPABC BUSINESS OUTLOOK SURVEY

Government Rating

Overall, opinions of the governments' performance in creating a good climate for business and investment in BC are not high. The federal government has the highest ratings with 29% positive (either 'good' or 'excellent'), followed by the municipal government with 26% positive and the provincial government (19%).

When asked to rank their top three priorities for the provincial government to improve BC's economy, CPABC members picked in order of importance: 'invest in infrastructure,' 'improve regional economic development,' and 'reduce government red tape.'

	Federal	Provincial	Municipal
Excellent	2%	1%	3%
Good	27%	18%	24%
Fair	43%	43%	44%
Poor	23%	33%	20%
Unsure	5%	5%	9%

Base: All Respondents, n=2,121

Top Economic Issues

Consistent with 2016 and 2017, the top economic issue that challenges business success in the province is 'housing prices.' Not surprisingly, those in the Lower Mainland and on Vancouver Island are more likely to indicate it as a challenge (87% and 84% respectively) compared to respondents in other parts of BC (74%). 'Barriers to trade' and the 'current value of CAD vs. USD' round out the top three most challenging economic issues.

	Housing Prices	Barriers to Trade	Current Value of CAD vs. USD
Major Challenge	57%	29%	26%
Moderate Challenge	27%	39%	42%
Minor Challenge	10%	19%	20%
Not a Challenge	4%	7%	9%
Not Applicable	3%	6%	3%

Base: All Respondents, n=2,121

Overall State of the Economy

BC's CPAs are fairly optimistic about the current state of BC's economy compared to their impression of the rest of Canada. 65% of our members consider BC's economic performance to be 'good' or 'excellent.' But this is down from 72% in the previous year.

	British Columbia	Rest of Canada	United States
Excellent	9%	2%	9%
Good	56%	48%	46%
Fair	29%	41%	29%
Poor	4%	3%	6%
No Opinion	3%	5%	11%

Base: All Respondents, n=2,121

Two-Year Economic Outlook

Looking at the economy over the next two years, fewer than one-in-five survey respondents feel the BC economy will improve in the next two years, while almost twice as many feel the local economy will worsen. Half think BC's economy will stay the same over the next two years. This result is consistent for Canada's economy, while a higher proportion feel the US economy will worsen over the next two years.

	British Columbia	Rest of Canada	United States
Improve	17%	17%	18%
Stay the Same	49%	46%	32%
Worsen	30%	30%	37%
No Opinion	4%	7%	12%

Base: All Respondents, n=2,121

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For more information, please contact:

Vivian Tse
Public Affairs Manager
Chartered Professional Accountants of British Columbia
(604) 488-2647
vtse@bccpa.ca
www.bccpa.ca

APPENDIX 1: ASSESSMENT OF RESPONSE TO 2018-19 RECOMMENDATIONS

2018-19 CPABC Recommendation	Third Party Endorsement
<p>Recommendation #1:</p> <p>Implement full PST exemption or input tax credit mechanism for business expenditure to encourage investment and to maintain our province's business competitiveness and drive productivity that is crucial for economic growth</p>	<p>In its November 2017 report, the Select Standing Committee on Finance and Government Services recommended the government conduct a review of the administrative burdens of the Provincial Sales Tax on businesses, and consider broadening the existing suite of exemptions to stimulate capital investment, maintain competitiveness, and drive productivity for economic growth.</p>
<p>Recommendation #2:</p> <p>Encourage active partnerships between post-secondary institutions, industry, and government departments.</p>	<p>N/A</p>
<p>Recommendation #3:</p> <p>Make work-integrated learning a mandatory component of post-secondary education.</p>	<p>In its November 2017 report, the Select Standing Committee on Finance and Government Services recommended the government expand opportunities for co-ops, internships, and apprenticeships to provide post-secondary students with work-integrated learning.</p>