Recommendations

As a result of investigating the consultation on community mental health services legislation we created four recommendations for the Graham legislative sub-committee. These were presented to the committee by David Reville from his perspective as a psychiatric survivor and in his present role as Official Opposition Health Critic for the Ontario Legislature.

1. Consultations which include consumers/survivors should be developed with the following considerations in mind:

- the issues under discussion should be generated by consumers/survivors;
- the consultation environment should be known to consumers/survivors;
- the consultation process should be consumer/survivor friendly.

2. Planning authorities charged with the responsibility of implementing the recommendations of the Graham Report must allow for significant consumer/survivor input both as members of the planning authority and as active participants in the consultations such as planning authorities undertake.

3. Support for consumer/survivor organizing should be provided so that consumers/survivors can be represented on planning authorities and/or participate in planning authority consultations.

4. The staff and non-consumer/survivor members of planning authorities should receive consumer/survivor sensitization and training; particular emphasis must be placed on the techniques that foster, rather than discourage, participation by consumers/survivors.

These recommendations were made to the Graham sub-committee on legislation in the hope of improving future consultations. They have implications for health and social planning authorities as they seek to enable consumers/survivors to participate as members of planning authorities and as they develop empowering processes so that consumers/survivors may assist in the development of a better community mental health environment.

References

Canada, Mental Health Division
1988 *Mental Health for Canadians: Striking a Balance.* Ottawa: National Health and Welfare.

Capponi, P.
1989a *Board sensitization package.* Toronto: The Gerstein Centre.

Church, K.
1986 *From consumer to citizen.* Toronto: Canadian Mental Health Association (National).

Church, K. and Reville, D.
1989 "User involvement in mental heath field in Canada," *Canada's Mental Health*, 37(2):22-25.

Church, K. and Reville, D.
1988 "User involvement in mental health services in Canada: A work in progress." A paper developed for distribution to an international conference on user involvement, University of Sussex, England.

Hutchison, P.; Lord, J.; Savage, H.; and Schnarr, A.
1985 *Listening to people who have directly experienced the mental heath system.* Toronto: Canadian Mental Health Association (National)

Hutchison, P.; Lord, J.; and Osborne-Way, L.
1986 *Participating with people who have directly experienced the mental health system.* Toronto: Canadian Mental Health Association (National).

Ontario, The Provincial Community Mental Health Committee
1988 *Building community support for people: A plan for mental health in Ontario.* Toronto: Ministry of Health.

Pape, B.
1988a *Consumer participation: From concept to reality.* Toronto: Canadian Mental Health Association (National).

Pape, B.
1988b *Shaping mental health policy: An action agenda for Canada - Conference Report.* Toronto: Canadian Mental Health Association (National).

Pape, B. and Church, K.
1987 *Community reinvestment: Balancing the use of resources to support people with mental disabilities.* Toronto: Canadian Mental Health Association (National).

Trainer, J. and Church, K.
1989 *User involvement in mental health planning.* Toronto: The Alliance Development Committee.

Trainor, J. and Church, K.
1984 *A framework for support for people with severe mental disabilities.* Toronto: Canadian Mental Health Association (National).

Warner, M.
1981 "The rise of community participation: Its impact on health professionals and the health bureaucracy." In D. Coburn, C. D'Arcy, P. New and G. Torrance (eds.), *Health and Canadian Society.* Don Mills: Fitzhenry and Whiteside.

World Health Association
1989 *Consumer involvement in mental health and rehabilitation services.* Geneva: WHO.

Corporate Taxation in Canada: A Background Paper

Kirk Falconer
Economics Researcher for an Ottawa-based Non-Governmental Organization

The author wishes to gratefully acknowledge the advice of Professor Neil Brooks, Osgoode Law School, York University, in this and other writings by the author in the area of Canadian tax policy

Introduction

The purpose of Canada's corporate tax system is to apply an annual levy on the business or property income or profits, from other sources, of firms resident in Canada. This sounds like a straightforward enough proposition but, of course, there is more to

corporate taxation than just that. When the federal government (or some provincial governments that have their own, sovereign corporate tax systems) determine policy that affects the taxation of corporations, it takes a number of issues into consideration.

For example, policymakers are extremely interested in what motivates foreign and domestic companies to invest in the Canadian economy. This leads to concerns about the size of the corporate tax burden (say, relative to our competitors, in particular, the United States) and what incentives the government may offer through the tax system to encourage, or retain, spending here. Government may also consider ways to offer special allowances to corporations experiencing volatile business cycles or problems securing investment capital and how best to influence firm spending on certain national priorities, such as more research and regional development.

However, at this time of on-going federal tax reform and a restrictive fiscal strategy, many Canadians also raise concerns about the level of contribution corporations make to the public revenue that supports desired social and economic programs. "Are corporations paying their fair share in taxes?" is a familiar enough question raised in many corners of the nation.

The function of this background paper is to briefly sketch how Canada's corporate income tax system operates, what the system's general impact is on the annual tax payments of corporations, what we know—and don't know—about the tax position of companies and what alternatives exist to the approach the federal government currently takes with respect to collecting a "fair share" from the corporate sector.

Corporate Taxation in Canada

In calculating the amount of tax it must pay every year to the federal government, an individual company is entitled to certain deductions reflecting costs associated with generating income over time. The history of corporate taxation includes extensive legal entanglements over what exactly constitutes a legitimate business expense in this regard. As part of this complex process, most corporations have access to key tax preferences - tax rate reductions, exemptions deferrals, deductions, credits, etc.—provided by government statute that serve to reduce tax payable even further on specific investments. At the end of this process, it is possible to figure out what the effective tax rates—taxes paid by corporations expressed as a percentage of profit—are for individual firms and sectors.

A tax preference deliberately distorts corporate spending to achieve a basic objective. For example, the federal government offers investment tax credits to corporations that directly reduce income tax payable for activity in the Atlantic, Cape Breton and other underdeveloped regions of Canada. The obvious objectives here is to make these areas of high unemployment and slow economic growth more attractive places for investment.

Another example is the manufacturing and processing deduction available to Canadian manufacturing firms. This incentive was introduced, in part, as a means of reducing the tax burden on this sector relative to its counterpart in the United States which was receiving heavy export subsidies from its government. Similar tax preferences have been introduced for other industrial sectors, such as agriculture, mining, oil and gas, and banking.

Every time a tax preference is introduced, the government can expect a moderate to large decrease in annual revenue as corporations find a new vehicle for lowering effective tax rates. In fact, this is how they are illustrated in budget documents. Commensurately, when a preference is restricted or terminated, the government projects an increase in revenue. This is why preferences are often referred to as tax expenditures—in real terms, they are nothing more than government spending programs conducted through the tax system.

The tax expenditure approach has been roundly criticized by many observers and analysts, including Canada's Auditor General for representing "hidden" spending that is not accountable to taxpayers because of the irregularity of government estimates as to their cost. This approach has also been criticized in some research as being more expensive than direct expenditure, for failing to delivery in real economic returns to Canadians and for being biased towards large, capital-intensive firms in wealthier regions of the nation. Canadian business spokespeople, on the other hand, have always maintained that the tax system is their favoured vehicle for government assistance for reasons of efficiency and minimal bureaucratic intervention.

An individual corporation may take advantage of as few or as many tax deductions, rate reductions, exemptions, deferrals and credits as are legally available to it. When tax preferences proliferated in the period 1972 to 1987, the result was that tens of thousands of profitable corporations had managed to build one tax preference on top of another and eventually reduce their year-to-year tax payable to zero. Still more paid only a modest amount of income tax. This, in turn, led to swift erosion of the corporate contribution to total government revenue.

Tables 1, 2, 3 and 4 highlight this experience from 1980 to 1987. The statistics reveal that the number of non-taxpaying, but profitable firms has grown by about one-half since 1980 to a total of 93,405 in 1987. In addition, by 1987, about one in every three dollars in corporate earnings, less other forms of income, went untaxed. Total untaxed profits for that year was $27 billion.

Over half of the total untaxed income in 1987 derives from the top 145 corporations which managed profits that year of about $106 million, on average. Over 80 percent of total untaxed profits were reported by those approximately 2,000 corporations with annual profits exceeding $1 million. The most favoured sector appeared to be banks, financial institutions and related enterprises which, overall, were responsible for about 60 percent of total untaxed profits and about one-third of all non-taxpaying, but profitable corporations.

A 1988 study published by the Canadian Tax Foundation notes that it was the precipitous drop in tax revenue caused by corporate tax preferences that was a major cause of growth in the annual federal deficit and net debt. The incumbent government understood this and in 1985, 1986 and 1987 took significant steps to stop the erosion of the tax base, culminating in the tax reform effort of the latter year. One of the prescribed goals of tax reform was to arrest tax avoidance on the part of profitable corporations. This was supposed to be achieved by a substantial broadening of the corporate tax base through the removal or restriction of a number of tax preferences,

Table 1
Growth of Taxable Corporations with Positive Profits and Zero or Negative Taxable Income Since 1980

Year	# of Non-Taxpaying Profitable Corporations	$ Million Total Untaxed Profits
1980	62,619	$9,966
1981	70,710	12,113
1982	83,076	10,504
1983	79,196	13,275
1984	85,430	15,264
1985	90,502	16,292
1986	95,386	21,981
1987	93,405	27,061

Source: Statistics Canada

Table 3
Share of Total Untaxed Profits of Non-Taxpaying Corporations by Size of Profits in 1987

Profit Size	Share of Total Untax Profits
$1,000-$24,999	1.7%
$25,000-$99,999	3.5%
$100,000-$999,000	10.7%
$1 million-$24.9 million	27.1%
$25 million and up	57.0%

Source: Statistics Canada

Table 2
Profitable Non-Taxpaying Corporations by Sector, 1987

	Number	$Million
Finance	33,595	$17,738
Manufacturing	5,753	3,026
Mining	1,232	2,716
Services	17,857	909
Transportation, Communication and Other Utilities	3,930	815
Wholesale Trade	6,472	790
Retail Trade	11,637	458
Construction	8,663	384
Agriculture, Forestry Fishing	4,266	224
	93,405	27,061

Source: Statistics Canada

Table 4
Average Number and Profit Size of Untaxed Corporations in 1987

Profit Size	Number of Companies	Average Size of Untaxed Profit
$1,000-$24,999	62,028	$7,300
$25,000-$99,999	19,056	$49,900
$100,000-$999,000	10,475	$277,600
$1 million-$24.9 million	1,701	$4.3 million
$25 million and up	145	$106.4 million

Source: Statistics Canada

such as capital cost allowances, investment tax credits, resource industry incentives, certain deductible business expenses and provisions affecting financial institutions.

Despite the concurrent cut in rates (from 36 percent to 28 percent), the government hoped to collect close to $5 billion more in revenue from the corporate sector over the five years of tax reform's implementation. In this way, the government intended to raise the corporate share of total federal revenue from a recent low of 11.2 percent in 1988 to 13.4 percent by 1994.

Of course, the jury is still out on whether the government's reform measure will have the desired impact (the Department of Finance has acknowledged that once tax changes are fully implemented, approximately 60,000 profitable corporations will continue to escape taxation). Since 1987, the government has introduced more corporate taxation—such as capital taxes for banks and the large corporations tax—out of concern for the deficit and on-going evidence that some of Canada's biggest business entities continue to pay little or nothing in annual income tax.

Disclosure of Corporate Tax Information

The statistics cited earlier were compiled by the Corporation Taxation Statistics branch of Statistics Canada. Reading them, one is left with the impression that Statistics Canada publishes reams of names of profitable corporations that avoid taxation. This is not, in fact, true, as Statistics Canada is forbidden by law to reveal any of the confidential information contained in the corporate tax returns on which it bases its' aggregate numbers.

It is no easy task to acquire a more current and focussed picture of the tax position of individual or groups of firms, except from what is gleaned, from time to time, by researchers from shareholder reports and other financial documents released by corporate officers. These are not particularly helpful in many cases as the data presented are either too general or too ambiguous as a reflection of tax accounting procedure.

For example, in a recent report of a top Canadian bank to its shareholders, an income tax provision for $302 million in, federal and provincial, incomes taxes is shown. This would suggest to the layperson that the actual remittance to government in taxes is, indeed, $302 million. But a provision of this variety is merely a reporting device. In fact, the transfer of a deductible amount to bank reserves to cover a percentage of its international debt exposure meant that the bank would be paying nothing by way of income tax that year. Actual remittance consisted almost exclusively of $113 million in capital taxes (federal and provincial taxes applied to shareholders' equity), of which $48 million was a federal liability. This is by no means clear, however, in the report.

Obtaining more precise information on the tax profile of Canadian corporations requires more resources on the part of independent researchers and better disclosure requirements on the part of government.

For example, in the United States, all publicly-traded firms are required to file an annual report or consolidated financial statement with the federal Securities and Exchange Commission (SEC). This is called "Form 10-K" and all information contained is available to the American public. This makes access to these documents relatively easy. In addition, "Form 10-K" ensures that each firm provides a formal "listing" of the tax preferences it puts to use.

A United States organization called the "Citizens for Tax Justice," supported by American labour, filters through this information and applies their own methodology for calculating the recent tax positions of top United States companies. Because of their attention to auditing and accounting rules, the data results of the Citizens' efforts are quite accurate, up-to-date and go virtually unchallenged by the business community. This work has led to more than a little embarrassment for some American corporate citizens and, on more than one occasion, has spurred major reforms of the tax system.

Canada has no national securities commission. However, information comparable to what is solicited from firms in the United States by the SEC (comparable, but apparently less detailed than United States corporate financial data which emerges from more stringent public disclosure specifications there) is also obtained by securities commissions in provincial jurisdictions.

Consumer and Corporate Affairs Canada also collects some corporate information, though this usually consists of financial statements and not shareholders' reports. In addition, this information is required only from firms with either $5 million in assets and above or over $10 million in gross annual revenue. Any corporation may easily obtain an exemption from this requirement for competitive reasons. All data are made publicly available for a fee.

Perhaps one of the best sources for corporate data exists in Canada's private sector, through the information services of the *Financial Post*. This journal collects data from companies directly, compiles it in a comprehensive, but accessible format known as financial "postcards" and makes it available to its readership including libraries.

Another way of assessing the tax position of corporations is to look at the annual cost of federal tax expenditures themselves. As noted earlier, this is impossible in Canada because the information is not published on a systematic basis. In recent history, two tax accounts have appeared, the last—*Account of the Cost of Selective Tax Measures*—being published by the Department of Finance in 1985. However, the information contained in this account is somewhat limited in value. For example, the most recent estimates of the cost of certain tax expenditures were generally two to three years old at the time of publication.

The absence of federal—and for that matter, provincial—tax expenditure accounts poses enormous difficulties for a serious examination of corporate taxation in Canada. This point has been made several times with regard to the federal jurisdiction by the Auditor General, who has argued in favour of the rights and responsibilities of Parliament in reviewing and approving such measures as they would any other budgetary item.

Since 1974, United States law has required a detailed listing and analysis of all federal tax expenditures as part of the President's annual budget submission to the Congress. This disclosure includes both historical and anticipated fiscal year tax expenditure estimates. The United States tax expenditure account permits elected representatives to examine incentives as a component of global government spending and to address questions as to their effectiveness and cost from year-to-year. The visibility of tax expenditures also prevents their being shielded from across-the-board, deficit-related cutbacks. Most states now have tax expenditure accounts as well.

The government of the United Kingdom also publishes a tax expenditure account on a regular basis.

Corporate Tax Policy Alternatives

Securing more federal revenues through the corporate income tax system is becoming a bigger challenge to policymakers. There are several reasons for this, one of the most important of which is our increasingly integrated global economy and the ease with which capital now travels. These developments portend important consequences for all domestic tax systems and the relative economic impact of assorted tax changes in individual jurisdictions today, and in the future.

There are steps the federal government can take, however. These include implementation of a version of the corporate minimum tax and termination or reduction of some tax preferences now available to Canadian firms. Policymakers can also turn their attention to tax issues in an international context.

The Minimum Tax Option

Proposals from several sources in Canada have emerged in recent years concerning a corporate minimum tax identical in design to the 20 percent tax in the United States. There, a minimum tax ensures some annual tax payment on the part of all medium-sized and large, profitable corporations. This is accomplished by preventing tax preference "stacking" on the part of firms to achieve zero taxation. Firms can continue to take advantage of various tax preferences but, in effect, a fixed percentage of these preferences experience a "clawback" by the minimum tax. Only those corporations experiencing real economic losses or utilizing "priority" incentives elude the full weight of the tax.

In practice, the individual corporation with annual earnings compares its standard tax liability with the alternative minimum tax calculation. The entity is then responsible for paying to the government the higher of the two amounts. A Canadian version of the corporate minimum tax is capable of collecting an estimated $1 to 2 million in new revenue, annually.

Another variant of the minimum tax which is worth consideration is known as the advance corporation tax. Used in the United Kingdom and Australia, this tax is applied to all dividends to ensure that the corporate surplus from which dividends are distributed to shareholders has been subject to a tax. This "prepayment" of tax is later offset against a corporation's mainstream liability, if it has one.

The federal government has argued that it already employs its own minimum tax in the form of capital or asset taxes on banks and large corporations. This is true, however, these taxes have nothing whatever to do with the profitability of the corporate taxpayer in a given year and are not especially famous for generating revenue. Neither do these taxes preclude the existence of tens of thousands of profitable corporations that are non-taxpaying—the large corporations tax, introduced in 1989, applies to only 3,600 firms.

Restriction or Elimination of Specific Corporate Tax Preferences

Clearly, one of the most efficacious way of increasing the revenue share of corporate taxes is to tackle tax preferences directly. This may, in some cases, be trickier than it sounds since one person's loophole may be another's sectorial or regional subsidy. A full accounting of the nature and scope of tax expenditures in Canada would bring more clarity to the available policy options. In addition, research has found that conversion of some tax preferences to direct spending programs might result in greater efficiencies and less cost to the federal treasury in meeting national goals.

One controversial tax preference that many have argued should be abolished is the special tax treatment of corporate capital gains. As a result of 1987 tax changes the proportion of capital gains to be included in a corporation's income will be increased to three-quarters this year (up from one-half).

In the past, non-taxation of a proportion of capital gains income has been represented in about one in five dollars of untaxed corporate profits. Full taxation of such income at the regular rate would certainly go some distance towards cutting the number of non-taxpaying corporations.

In 1986, the tax reform effort sponsored by former President Ronald Reagan eliminated this tax preference in the United States. As the Royal Commission on Taxation, the Carter Commission, proposed for Canada in the late 1960s, United States tax law now treats capital gains income as ordinary income. A similar initiative in Canada today would probably yield between $500 million and $1 billion from the corporate sector.

Another tax preference that has produced controversy has been the deduction for business meals and entertainment expenses. This measure allows individuals and corporations to deduct as a business-related outlay, and thereby used to generate income; the cost of meals, food and beverages; and entertainment, such as recreational events, resort accommodation, tickets for a theatre, concert, athletic event, etc., from their annual tax payable.

In 1987, the government decided to limit this deduction to 80 percent of total expenses for each claimant to recognize the "personal enjoyment" factor of business-related consumption. If the entire deduction was cancelled, the revenue yield would be about $1 billion, 70 percent of which would be attributable to corporate taxfilers.

The Canadian tax system has for a long time had a propensity for encouraging corporate concentation. This was demonstrated in a 1987 Statistics Canada study which showed that mergers, takeovers and buyouts and the fast growth of large conglomerates are strongly supported by such provisions as interest deductibility, the tax-free flow of intercorporate dividends, capital gains rollovers used in reorganizations, the treatment of tax losses and other incentives.

In particular, there have been calls for revisions to the rules governing the use of interest deductibility for share purchases. Achieving this end might be an immensely complicated, and possibly arbitrary, process as new rules would have to define what constitutes "paper entrepreneurship," as opposed to productive corporate activity.

Canadian policy makers might be well-advised, however, to look into those proposals that have been developed in the United States Congress in recent years. Measures such as specific dollar limits on deductions of interest incurred for financing mergers and acquisitions, an "acquirer's tax" in the case of hostile takeovers and an excise tax on profits arising from "buyoffs" when such takeovers threaten, are among the potential solutions that have been discussed there.

There are many other possibilities. Suggestions have been forwarded as to limiting depreciation allowances and other incentives available to real estate developers, one of the lowest taxpaying sectors in Canada, or the levying of a federal speculation tax. Eric Kierans and the late David Lewis, among others, advocated measures which aimed at slowing the annual growth of almost $40 billion in corporate deferred taxes. For example, an interest charge that would, in effect, act to limit deferral opportunities inherent in depreciation allowances. And as of late, there has been more discussion of how to clamp down on corporate tax evaders, through an increase in the number of Revenue Canada audits which have declined precipitously since the early 1970s, despite their revenue-generating capacity, and the enaction of stiff penalties for failure to declare income and misuse of tax preferences.

The Global Dimension to Corporate Taxation

When Canada enters into tax treaties with other nations, it does so as an autonomous tax jurisdiction interacting with other such jurisdictions. This approach is embodied in treaty terms outlined by the Organization for Economic Cooperation and Development (OECD).

There exist alternatives to this approach. One example is the unitary tax which has been developed and put into place in some American states, such as California. Unlike the OECD model tax treaty, the unitary tax recognizes that the proliferation of transnational enterprises which have increasingly complex financial interests in a wide variety of jurisdictions poses heady problems for local tax authorities.

The unitary tax operates through application of a formula that expresses the corporate taxfiler's liability in terms of the entity's worldwide activities and hence, worldwide profits. In large part, this is done to prevent transnationals from avoiding tax in a given jurisdiction through transfer pricing and cost-allocation maneuvering. For this reason, the unitary tax approach would appear to have considerable relevance to Canada and our history of foreign ownership.

In practice, the unitary tax is viewed by some, particularly in the business community, as being arbitrary and distortionary. On the other hand, many tax experts argue that, in the long run, it may make sense to move in the direction of unitary tax principles, or some comparable multilateral approach, in light of unceasing economic change and the unresolved dilemma of taxing transnationals.

Conclusion

The foregoing has been a survey of corporate taxation in Canada and some related policy options. It is apparent that a number of information gaps need to be closed for the purposes of more and better independent research in this area. An important contribution to this effort would be for interested parties in Canada to emulate the work of the United States "Citizens for Tax Justice" in identifying current, preeminent examples of tax avoidance through the collection of corporate financial data, chiefly in the form of shareholders' reports, and applying a rigorous methodology for calculating records of tax payment.

The above initiative in combinations with improved corporate disclosure requirements and federal government introduction of an annual tax expenditure account, with past and projected cost estimates, would greatly assist our understanding of Canada's corporate income tax system and provide some crucial guidance as to how to go about reforming it.