

Powering Entrepreneurship

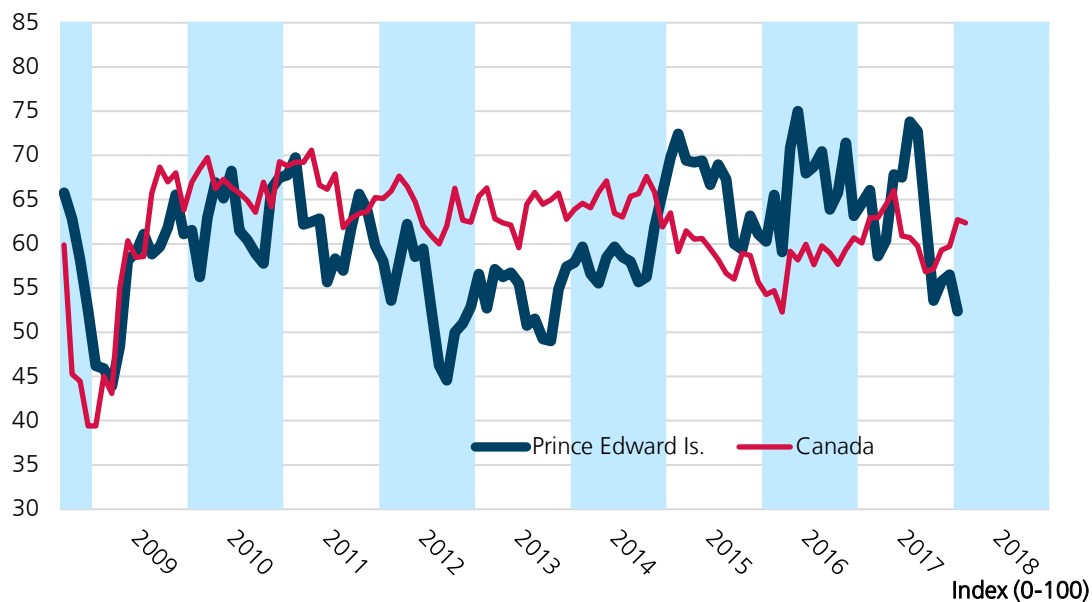
Erin McGrath-Gaudet, Director, PEI and Intergovernmental Policy

Entrepreneurs represent the best of the Island spirit – they’re innovators, job creators, and an integral part of our communities. The small business owners who help to drive Prince Edward Island’s economy are deeply invested in their communities and in the future of the Island. They want to see the Island thrive and provide opportunities for future generations.

State of Small Business on PEI

For much of 2017, small business owners on the Island showed considerable optimism about their performance relative to their counterparts nationally. Much of this relates directly to a low Canadian dollar, which provided a boost to many of our key industries. CFIB’s Business Barometer showed that optimism did take a drop in the Fall of 2017, much of which can be attributed to concerns around federal tax proposals and it has been slow to rebound (see Figure 1).

Figure 1:
Business Barometer®, January 2018



Source: CFIB’s Business Barometer Index, January 2018

Our Business Barometer also shows trends emerging which will serve as limitations to economic growth. While insufficient domestic demand remains a concern, labour shortages are now the foremost concern for Island businesses (see Figure 2). Given the aging population, it is likely that labour shortages will continue to be a constraint on growth.

Figure 2:

Limitations on growth



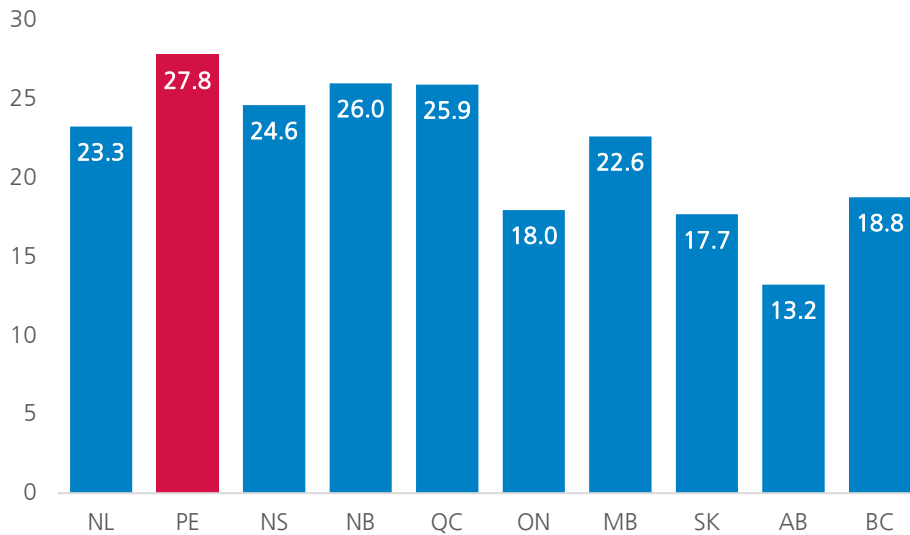
Source: Business Barometer, PEI data, 12-month moving average, January 2018

To achieve the prosperous future Island entrepreneurs want to see for the province, it is important government work closely with the small business community to ensure their realities are reflected in government policy and are full partners in a path forward.

The big picture

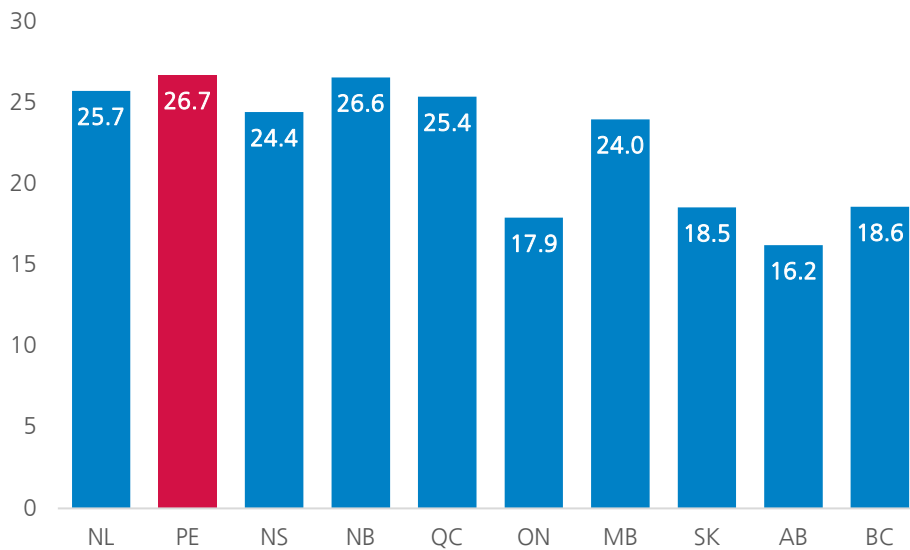
There are certainly many positive trends developing in PEI whether it be stronger-than-average economic growth or impressive immigration numbers. That being said, entrepreneurs remain concerned about the future of the Island. Even with recent immigration improvements, our population is aging and this means challenges for our labour force and succession planning as well as increased pressure on public services like health care. While PEI achieved a balanced budget in 2017-2018 and has an improving debt-to-GDP ratio, our net debt has grown considerably over the past decade and we are now beginning to see interest rates climb. Additionally, as a province, we already have a high-tax and high-government spending reality, topping all the other provinces for both revenues as a percentage of GDP (see Figure 3) and expenditures as a percentage of GDP (see Figure 4)

Figure 3:

Total Revenues (% of GDP)

Source: Provincial public accounts

Figure 4:

Total Expenditures (% of GDP)

Source: Provincial public accounts

CFIB recently published a report, *Winter is coming: Why Atlantic Canada's aging population should scare governments (and the people who pay for them)*, which explores sustainability challenges facing PEI and the rest of the Atlantic region. Among the recommendations in the report, governments should:

1. Age-test programs to make sure the long-term spending implications are understood and publicly report findings so that taxpayers are aware of the extent of challenges;

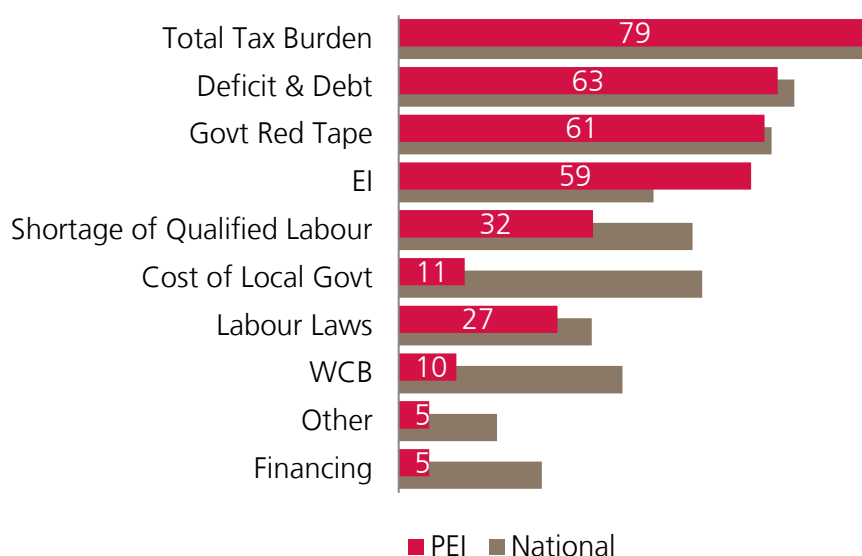
2. Continue to focus on spending restraint to ensure that debt is contained and that overall spending is sustainable over the long-term;
3. Look to increased regional cooperation as a means of finding spending efficiencies as is currently seen in areas of health care and joint procurement initiatives;
4. Focus on labour force and economic growth to help offset the impacts of an aging population. This should include productivity improvements and better matching of training and immigration programs to the labour needs of small businesses.

Taxation

While having a balanced budget is a substantial accomplishment, it is important to recognize that significant “pain” went into achieving a balanced position whether it be the hike to the small business corporate tax rate, the increased HST rate, or erosion of the value of personal income tax deductions and brackets. In addition, it is important to note that there are already plans to increase Canada Pension Plan (CPP) premiums as well as introduce a carbon pricing. These increases are always a challenge for small businesses to absorb. Given this environment, small business owners cite the total tax burden as their top concern for governments (see Figure 5).

Figure 5:

Which of the following are serious concerns to your business? (% response)



Source: CFIB, *Our Members' Opinions Survey, January-June 2017, PEI n=137*

With that in mind, and given the need for economic growth, it is time for PEI to invest in tax relief for Islanders and local businesses. Two notable areas in need of relief are the small business corporate income tax rate and personal income taxes. In addition, caution should be used when contemplating new taxes such as a carbon tax, and such changes should be revenue neutral for government.

Corporate Income Tax

Prince Edward Island ranked well relative to other Canadian provinces in the area of corporate income tax for small business until the significant increase to the small business corporate tax rate in 2013. PEI now has the highest rate in the region and second highest rate nationally. Small businesses do not have the same access to capital as larger businesses nor do they have access to the same level of grants, subsidies, government programs and tax credits. For small businesses, their profits represent their primary source of funds for growth, increasing wages, and investing in more productive equipment and innovation (see Figure 6) - all are behaviours in government's interest to encourage rather than discourage through higher taxes. **We recommend reducing this rate to at least the Atlantic Canadian average of 3 per cent over the next two years.**

Figure 6:

If the provincial government were to reduce taxes, how would your business use the savings? (select as many as apply)



Source: CFIB, PEI Pre-Budget Survey, November 2016, n=51

Personal Income Tax

The personal income tax system affects businesses in a number of ways. High personal income taxes affect the labour pool by making it difficult to compete for workers with other jurisdictions and/or attract entrants into the work force. High personal income taxes also lower disposable income for individuals and families, leaving them with less to spend on daily necessities or to save for longer-term needs, including retirement.

CFIB was pleased to see an increase in the basic personal exemption in last year's budget. It has been CFIB's position, and supported by a number of studies, that increasing the basic personal exemption is an important poverty reduction tool. Over the past number of years, personal income tax exemptions and brackets have been eroded by inflation. To prevent

this from happening in the future, **CFIB recommends automatic indexation of the personal income tax system with the Consumer Price Index (CPI) every year.**

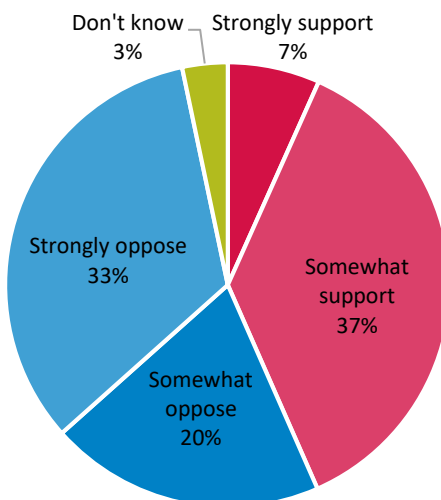
Carbon Pricing

Environmental issues are a concern for many small business owners and the vast majority of small business owners are already making environmentally-friendly changes in their businesses. While 80 per cent believe it is possible to growth the economy and protect the environment at the same time, small businesses are concerned about the impacts carbon pricing may have on their operations PEI (see Figure 7). Since many small businesses will, as a result, face higher tax bills, implementing a carbon tax may well make it harder for small businesses to make further changes to reduce their environmental footprint if offsetting tax measures are not also implemented.

Figure 8:

To what extent do you support or oppose the following government approaches to deal with environmental issues? (% response)

Introduce taxes and fees (e.g. carbon tax, levies on tires and electronics)



Source: CFIB, National Environment Survey, July 21-August 29, 2016, PEI n= 30

In addition to general tax measures to offset the negative impacts on small businesses, CFIB strongly urges government to thoroughly assess the impacts carbon pricing will have on the competitiveness of our industries and put in place specific plans to ensure economic growth is not sacrificed. **The introduction of carbon pricing would be an opportune time for government to conduct a full tax review with the aim of improving our competitiveness as a province.**

Tax Recommendations:

1. Reduce the small business corporate income tax rate to the Atlantic Canadian average of 3 per cent over two years to help small businesses invest in their operations and increase employee wages.

2. Introduce automatic indexation of personal income tax brackets and deductions.
3. Work with industries to ensure competitiveness and economic growth are not sacrificed with the introduction of a carbon pricing.
4. Launch a full-scale tax review with the aim of identifying the most competitive tax system for the province.

Reducing “red tape”

While government may have a limited fiscal capacity to reduce taxes, reducing red tape makes good business sense. Reducing paperwork requirements, using plain language, providing excellent customer service and streamlining processes can all go a long way to saving businesses time and money and helping them to be more productive.

CFIB has been encouraged by the momentum built around Project ART and the Joint Office of Regulatory Affairs along with passing the Regulatory Accountability and Reporting Act. **We encourage government to continue with these initiatives and ensure evaluation of efforts so that successes can be measured.**

In addition, **PEI should consider piloting the Business Navigator model that was recently established in Nova Scotia.** Figuring out the rules and regulations that apply to a business can be complex and time-consuming and the navigator model used in Nova Scotia helps new and existing businesses find and understand the information that they need.

Red Tape Recommendations:

1. Introduce a broad-based measure to evaluate the current regulatory burden on the Island and ensure that regulatory reduction efforts are contributing to an overall reduction for Island businesses.
2. Explore launching a Business Navigator service in PEI based on the Nova Scotia model.

Summary of Recommendations:

1. Age-test programs to make sure the long-term spending implications are understood and publicly report findings so that taxpayers are aware of the extent of challenges;
2. Continue to focus on spending restraint to ensure that debt is contained and that overall spending is sustainable over the long-term;
3. Look to increased regional cooperation as a means of finding spending efficiencies as is currently seen in areas of health care and joint procurement initiatives;
4. Focus on labour force and economic growth to help offset the impacts of an aging population. This should include productivity improvements and better matching of training and immigration programs to the labour needs of small businesses.
5. Reduce the small business corporate income tax rate to the Atlantic Canadian average of 3 per cent over two years to help small businesses invest in their operations and increase employee wages.
6. Introduce automatic indexation of personal income tax brackets and deductions.
7. Work with industries to ensure competitiveness and economic growth are not sacrificed with the introduction of a carbon pricing.
8. Launch a full-scale tax review with the aim of identifying the most competitive tax system for the province.
9. Introduce a broad-based measure to evaluate the current regulatory burden on the Island and ensure that regulatory reduction efforts are contributing to an overall reduction for Island businesses.
10. Explore launching a Business Navigator service in PEI based on the Nova Scotia model.