CAMIC ACCAM
CANADIAN ASSOCIATION OF MUTUAL INSURANCE COMPANIES
ASSOCIATION CANADIENNE DES COMPAGNIES D'ASSURANCE MUTUELLES

RECOMMENDATIONS FOR THE 2017 FEDERAL BUDGET

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Executive Summary

Mutual insurance companies insure 65% (115,000) of Canadian farms and fishing enterprises. Insurers doing more than 20% of their business with farms and fishing enterprises benefit from a tax deduction and typically return their tax savings to the farmers and fishermen. Those which do not meet the 20% threshold do not receive and cannot transfer the benefit to about 30,000 farmers and fishermen. Under the Income Tax Regulations, three (3) companies are not subject to the same rules; this distorts the insurance market. Combined, the two tax measures recommended are cost neutral to the federal government and would benefit an additional 30,000 farmers and small fishing enterprises.

History of the insurance provided to Canadian farmers and fishermen

One of the main concerns of Canadian farmers and fishermen has always been the adequate protection of their assets. Before Confederation and for a few decades after Confederation, farm insurance was not available or not available at a fair price. As a response, Canadian farmers decided to create their own insurance companies under the mutual ownership structure. Having their own mutual insurance companies ensured farmers that the insurance products they needed would be available, at a fair price, and would come with the level and type of service desired.

The premium charged to the members (farmers) was first paid at the end of the year and the amount paid was exactly what was needed to cover claims and expenses of the past year. Subsequently, mutual insurers started charging their premium (an estimate of claims and expenses) at the beginning of the year, which meant that in some years a profit would be generated, profit that would be transferred to the surplus of the company to better manage rainy days and ensure the long-term sustainability of the company. However, making a profit also meant paying taxes.

1) Tax deduction for insurers of farmers and fishermen (Paragraph 149(1)(t) of the Income Tax Act)

In 1945, the Report of the Royal Commission on Co-operatives recognized that the main mandate of mutual insurers was not principally to earn a profit but rather to provide a service to their constituency, the farmers and the fishermen. The Commission recommended that an insurer, mutual or otherwise, not pay tax when 50% of its business was done with farmers and fishermen. That recommendation was adopted by Parliament in the 1954 Federal Budget. In keeping with the objective of not making a profit with the insurance of farmers, mutual insurers have since typically returned their tax savings to farmers and fishermen in the form of reduced premiums.

Over time, due to the steady reduction in the number of farms in Canada and the increased underwriting of non-farm/non-fishing risks, a number of mutual insurers started generating more than 50% of their premium revenues from non-farm/non-fishing business and, consequently, became fully taxable. To maintain the incentive to insure farmers and fishermen, the government responded by replacing the tax exemption with a tax deduction equivalent to the percentage of business done with farmers as long as that percentage of business exceeded 25%. Under this arrangement, rather than not being eligible to any tax relief, an insurer doing say 40% of its business with farmers and fishermen could and still can deduct 40% of its income taxes otherwise payable.

In 1996, the Income Tax Act was further modified to allow insurers doing between 20 and 25% of their business with farmers and fishermen to claim a tax deduction equivalent to half of their percentage business done with farmers and fishermen. For instance, rather than not being eligible to any tax relief, an insurer doing 24% of its business with farmers and fishermen can deduct 12% of its income taxes otherwise payable.

While the farm component of the total book of business of farm mutual insurers is diminishing, the involvement of farmers in the oversight of their mutual insurance companies continues to be very strong. Indeed, farmers and fishermen still represent the majority of board members sitting on mutual insurance companies' board of directors.

Today, Canadian farmers and fishermen continue to recognize the value of doing business with their own local mutual insurance company as more than 65% of them do business with mutual insurers. However, as the number of farms and fishing enterprises continues to diminish, the farm component of mutual insurers' portfolios now averages about 15% of their book of business. That has meant more companies failing to meet the 20% threshold and more fish and farm clients not realizing the saving in their premiums that they would have accrued from the limited tax deduction.

Recommendation

That insurers, mutual or otherwise, be allowed to deduct from their income tax otherwise payable the proportion of their business done with farmers and fishermen as long as that proportion exceeds 5%.

Impact Analysis

According to Federal Government data, the current tax deduction costs the Federal Government in the neighborhood of $9 million/year in forgone tax revenues. CAMIC estimates that a reduction of the threshold from 25% to 5% would increase the tax expenditures by $2.5 million/year and benefit up to 30,000 additional farms and fishing enterprises currently insured with mutual insurers that do between 5% and 25% of their business with farmers.

2) Special tax measure applicable to three (3) insurers of farmers and fishermen (Subsection 4802(2) of the Income Tax Regulations)

On May 12, 1994, subsection 4802(2) of the Income Tax Regulations was put in place to allow three (3) prescribed insurers not to take into account the gross premium income of affiliated insurers when determining their eligibility for the tax deduction under paragraph 149(1)(t) of the Act. The measure was retroactive to the 1989 taxation year and applicable to subsequent years. There was no public explanation of that decision.

The list of prescribed insurers was then, and remains as follows: 1) Union Québécoise, compagnie d'assurances générales inc.; 2) Les Clairvoyants Compagnie d'Assurance Générale Inc.; and 3) Laurentian Farm Insurance Company Inc. None of these three companies still exists. However, all three companies have been sold to other insurers. The three current successor companies have seen the tax benefit extended to them, even though the percentage of the farm/fishing business of each respective consolidated company is much less than the 20% threshold required of other insurers in the Income Tax Act. Their status distorts the competitive marketplace without any tax policy rationale.

Recommendation
That subsection 4802(2) of the Income Tax Regulations be repealed

Impact Analysis
The elimination of the special treatment afforded to the successor companies of companies prescribed in the Income Tax Regulations would reduce tax expenditures by an excess of $2.5-$3.0 million/year. In addition, insurers would from thereon be operating on a level playing field.

Combined recommendation
That both recommendations be implemented simultaneously to make the combined measures *cost neutral for the Federal Government*.