



Ontario Independent Appraisers Association

**2017 Pre-Budget Submission
to the
House of Commons Standing Committee on Finance**

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Executive Summary

Canada's independent appraisal industry supplies vehicle damage appraisal services to the property and casualty insurance industry. Like so many businesses, appraisers have adapted to changes in technology and consumer demands.

In response to these forces of change, Canadian businesses have adopted new technologies, embraced new business models and structural change. As Canadian businesses adapt, so must associated laws and regulations. This is particularly true of the country's tax system.

The independent appraisal industry is an example of an industry that has adapted to technological and structural change, but tax laws have not kept pace. As a result, the industry is now facing considerable negative consequences with potential job losses, business closings and increased insurance costs.

To meet their "expansion, innovation and prosperity goals," the federal government must ensure that laws, regulations and policies accommodate industries' technological and structural changes while *retaining the original policy intent*.

Canada's independent appraisal industry

Canada's independent appraisal industry provides the country's property and casualty insurance industry with appraisals of damaged vehicles such as automobiles, trucks, RVs and trailers, boats, ATVs and motorcycles.

There are approximately 350 independent appraisers across the country of which 250 are sole operators – true small businesses. Many of these appraisers live in rural areas of Canada, where insurance companies rely on independent appraisers rather than staff.

The Ontario Independent Appraisers Association is the only formally organized voice for the industry. Nonetheless, it represents the views of appraisers from across Canada.

The Technology Challenge

For many entrepreneurs and small businesses, technological change has brought new opportunities and new challenges. For some industries, technology has brought entrants with new business models - Uber being the most obvious example of these economic 'disruptors'.

Canada's appraisal industry met its "Über" over a decade ago with the advent of digital cameras and affordable data transmission. Technology was the industry's real disruptor. The advent of digital technologies vastly changed how appraisers interact with their end-users.

Responding to demands by governments and consumers to reduce auto premiums, insurance companies have been driving cost reductions. Less days to repair a vehicle equals lower costs and increased customer satisfaction.

Innovative solutions such as digital imaging, specialized management software, online access and data sharing with claim stakeholders have all significantly supported the reduction of appraisal costs and repair times.

The Tax Policy Challenge

For Canada's personal and commercial insurance industry, expenses associated with adjusting and appraising automobile losses are GST exempt. Paragraph (j.1) of the Excise Tax Act was added to the "financial service" definition, effective from the beginning of the GST in January 1991, in order to exempt the provision of damage appraisal services provided to insurers.

At that time, appraisal services were provided directly by appraisers to insurance companies and the wording of paragraph (j.1) reflected this direct, single-tier relationship.

As discussed, the advent of digital technologies vastly changed how insurers and appraisers do business. The insurance industry no longer operates through local offices but, instead, operates through centralized corporate structures with few, if any, regional offices.

The wording of paragraph j.1 reflects the structure of the appraisal service industry during the 1990's. The organization of appraisal services to support insurance claims adjusting has evolved to reflect technological advances and the need for efficiency improvements – moving from a direct relationship between an insurance company and independent appraisers to one where larger appraisal companies typically handle assignments from insurance companies or adjusters through a national network of local appraisers.

In most cases, appraisers now provide their services to insurers on a "multi-tier" basis. The local appraiser still provides the appraisal service, just as they did in the 1990s, but today this service can be supplied to an appraisal company, which is contracted to supply the appraisal to the insurer or licensed independent adjuster. However, the essence of appraisal services and their critical role in claims adjusting has not changed, such that they remain an essential component of the financial provided by P&C insurers to their customers.

However, in the Fall of 2011 a Revenue Canada regional office issued an interpretation to an independent appraiser indicating that his appraisal services did not come within the existing exemption, that is, he was not supplying it directly and should be charging HST on the service. In 2011, roughly two thirds of all appraisals were conducted by independent appraisers providing their services to larger appraisal firms who, in turn, ultimately were dealing with the property and casualty insurance companies

In January of 2013, the Canada Revenue Agency (CRA) published GST/HST Information Sheet - "Insurance – Appraisals of Damage Caused to Property" suggesting that restructuring in the appraisal industry that started over ten years prior meant that appraisal services should be taxed despite the fact there was no change in the actual service provided and no change in the end-user, the insurance industry.

This interpretation is in direct opposition to the original policy intent. Moreover, it would cause serious harm to many independent, small businesses across Canada.

Federal Action to Support Prosperity and Economic Growth

The Standing Committee on Finance has asked what federal actions would assist Canada's businesses meet their expansion, innovation and prosperity goals, and contribute to Canada's economic growth.

As discussed, just as industry must change and adapt to 'disruptors' or other external the federal government must complement these actions with fair, flexible and adaptable tax policy, as required.

The situation Canada's appraisal industry is currently facing illustrates the negative consequences of a rigid tax system. Without change, the original tax policy intent can be lost, resulting in negative economic consequences.

A technical amendment to bring paragraph *j.1* in line with the current market structure for appraisal services is needed to prevent adverse cost and efficiency consequences for the consumers of P&C insurance products. These consequences arise from the disruption caused to the current claims processing supply chain, which will in turn require insurance and adjusting companies to make costly and functionally unnecessary structural changes. A further cost implication would occur if the current GST/HST rules remain and are applied retroactively to appraisal services.

The amendment proposed by the OIAA and supported by Canada's P&C industry would address this situation by ensuring that both single-tier and multi-tier arrangements would qualify under paragraph (j.1).

The amendment would also be in accordance with the tax neutrality principle in the OECD VAT/GST Guidelines because the revised wording of the exemption would provide equal treatment to the economic operators (the appraisers) that carry out the same functions and would have minimal impact on business decisions of the insurers.

If the amendment is not made and the insurers are required to pay GST/HST on appraisals, it would impact the decisions made by the insurers and thereby would not be in accordance with the tax neutrality principle. Insurers would often decide to *not* send an appraiser to inspect the damages and would instead try to manage their exposure remotely from a desk in a Toronto office. The risk profile of the insured losses would change, and the small businesses of the independent appraisers would be seriously jeopardized and a number of them would have to close.

Our recommendation

The OIAA recommends the federal government work with all industries to ensure tax policies reflect the adaptive changes that industries must make to remain a strong contributor to the Canadian economy.

The OIAA supports the governments' approach to sound fiscal and tax policy. We support efforts by the government to close tax loopholes, eliminate tax losses and avoid unintended consequences of tax policy changes. We also recognize that any change to the Excise Tax Act must be made with caution and concern about setting precedents that could lead to other requests for tax changes.

As set out below, it is our view that the OIAA's proposed technical change to the wording of paragraph (j.1) would not constitute a precedent for additional changes to the "financial service" definition.

The OIAA's proposed amendment would *not* be a "precedent" because the OIAA is not seeking a *new* exemption. Rather, the OIAA is seeking a technical amendment to restore the functionality and tax neutrality of the already existing exemption in paragraph (j.1), reflecting the adaptive changes the industry has made.

Further, the proposed amendment would remain applicable to the same type of appraisals as was intended when paragraph (j.1) was first enacted. It does not seek to expand the exemption to other types of appraisals.

Finally, the function of the amendment would not be new. It would parallel the existing adjuster exemption in paragraph j by focusing on the nature of the service and the ultimate beneficiary. Just like the adjuster exemption, it would apply in both single and multi-tier situations.

In summary, fixing the appraisal exemption would not be precedent setting because, in the OIAA's situation, there is an already existing exemption and restoring its intended functionality would simply be maintaining the *status quo ante*.

Conclusion

The Ontario Independent Appraisers Association has been working with the Department of Finance and the Office of the Minister of Finance to find a workable solution. After *three years* of constructive work, we believed a solution had been reached that would keep the exemption in place for our industry. Regrettably, the 2015 election put a temporary stop to the work on this matter.

It is through adaptive and responsive tax policy that the federal government can support prosperity and economic growth.

We submit, given that the appraisal industry has adapted to accommodate change, the federal government continues to work with industry to establish a technical amendment that would restore the functionality of the exemption in line with its original intention.