



Chemistry Industry
Association of Canada
canadianchemistry.ca

Association canadienne
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chimiecanadienne.ca

CANADA'S CHEMISTRY INDUSTRY

SUBMISSION TO THE HOUSE OF COMMONS STANDING COMMITTEE ON FINANCE

PRESENTED BY THE CHEMISTRY INDUSTRY ASSOCIATION OF CANADA

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Responsible Care®
Our commitment to sustainability.



Gestion responsable™
Notre engagement envers le développement durable.

WHO WE ARE

WE ARE CANADA'S CHEMISTRY INDUSTRY

The Chemistry Industry Association of Canada (CIAC) represents leading companies engaged in the business of chemistry. Member companies apply the science of chemistry to create innovative products and services that make people's lives better, healthier and safer. Responsible Care[®], a continuous improvement program, is a requirement of membership in CIAC. Through Responsible Care, member companies dedicate themselves, their technology and business practices to sustainability. This commitment involves working with all stakeholders in support of innovation for safer products and processes, which conserve resources and improve people's lives and the environment, and to ensure the stewardship and security of chemistry products through their lifecycles.

WE ADD VALUE TO CANADA'S RESOURCE BASE

Chemistry is an enabling industry and is uniquely positioned within energy and downstream manufacturing value chains. Our members take energy products (oil and gas components, electricity) and convert them into value added manufactured products, adding 5 and 10 times to the initial value of the commodities. When these products are further upgraded by our many customers such as the auto parts, packaging, medical devices, textiles and communication equipment industries, the value added is considerably more. Chemistry is innovative and values inputs that are often considered as waste or residual products by other industries such as energy. For example, our members can take off gases from oil sands upgraders as well as natural gas liquids, which form a very small portion of natural gas, and convert these relatively minor components of energy into high value manufactured products. They also convert electricity, minerals and agricultural bio-mass into chemical products that are used in a wide range of industrial and consumer applications. A significant service sector has grown up around and evolved from the chemistry sector which is highly knowledge-intensive. This service sector, which includes many of our member companies, depends upon the growth and continued health of the business of chemistry in Canada. At the public policy level, moving up the value chain through chemistry means that governments at all levels and Canadians benefit from the collection of taxes on higher value sales and jobs.

WE PROVIDE SOLUTIONS AND JOBS

The business of chemistry is a \$19 billion a year enterprise for CIAC industrial chemical manufacturers through which they provide the basis for the broader \$45 billion a year chemical and chemical products sector (this includes pharmaceuticals, paints and coating, etc). The chemical industry is the fourth largest in the manufacturing sector, creating close to 80,000 direct jobs. After information technology (IT), chemistry is the biggest employer, within the manufacturing sector, of university graduates as a percentage of its total workforce. In addition, each job in the chemical industry creates 4.8 additional jobs elsewhere in the economy¹. Chemistry jobs are well-paying and require skilled workers whose knowledge is often applied to other sectors of the economy. Our member companies provide solutions to many energy conservation, environmental and health-related societal issues. For more information and specific examples, please consult our webpage at: www.canadianchemistry.ca.

OUR RECOMMENDATIONS

CIAC, on behalf of its membership welcomes the opportunity to provide input into the House of Commons Standing Committee on Finance (the Committee) as it conducts its 2011-2012 pre-budget consultations. CIAC looks forward to meeting with the Committee to discuss the Canadian economy and our industry's role as an innovative, value-added manufacturer and creator of jobs and wealth. As a natural resource-based and developed economy, Canada needs to continually attract investment in value-added resource upgrading to improve productivity and environmental performance and generate wealth for future

¹ National & Provincial Multipliers, 2005, Catalogue No. 15F0046XDB

generations. Within the context of creating sustainable jobs, maintaining announced and scheduled corporate tax reductions, and restoring a balanced budget, we urge the Committee to adopt the following recommendations:

- **Five years Accelerated Capital Cost Allowance (ACCA) extension** - Stimulate new investment in manufacturing, put new and improved tools into the hands of Canadian workers and encourage the adoption of new technology to achieve environmental goals, through one specific investment-enhancing policy measure; a five-year extension of the ACCA for new machinery and equipment (two-year rapid write-off).
- Maintain the Scientific Research and Experimental Development (SR&ED) tax credit program and streamline its administration
- **Focus on a value-added manufacturing strategy** We need government commitment to work on rebuilding and growing value-added manufacturing in the country, creating jobs and restoring wealth creation.

BACKGROUND

Canada is envied the world over for its rich portfolio of natural resources, skilled workers and proximity to the world's largest market. This portfolio and its elements need to be managed for the long term. This requires careful consideration of what is needed to continue generating healthy returns, or in other words, wealth and quality of life for Canadians today and tomorrow. It is believed by many that manufacturing is declining in economic importance. This is absolutely false and is a misconception that needs to be addressed if Canada is to continue to benefit from investment and innovation. Manufacturing has traditionally been and will continue to be a significant and essential part of the Canadian economy and wealth creation for generations to come. The manufacturing sector plays essential roles: It adds value to our natural resources and in doing so creates employment in all economic sectors including the service and high-tech sectors. It provides diversity to our economy and helps smooth out the bumps during commodity swings which are a risk given our continued and growing dependence on resource exports.

When we focus on extracting and shipping our resources elsewhere to be upgraded, we lose out on the demand and associated job opportunities. We become less innovative and productive as a nation. Canada's resource base has generated significant industrial clusters such as chemistry based on resource upgrading. The linkages between industries such as chemistry and Canada's natural resource base need to be recognized and supported through policies that allow for growth. The Committee needs to ask how to keep these industries here and continue to drive innovation through the value chain and into competitive advantage. Clearly resource abundance is not enough. We need investment in upgrading and innovation and the remainder of this submission identifies tax policy and government leadership as essential elements of a strategy.

Chemistry is a highly capital-intensive business. It is also global. This means that we must recognize that capital is mobile and global production is shifting. Facilities in Canada are in constant competition within their corporate families for investment capital that is allocated worldwide. Therefore, our focus is on measures which will ensure that Canada attracts a necessary share of investment to grow and renew its value-added industrial base to generate jobs and wealth for today and tomorrow. We firmly believe that the Committee should focus on key policy measures that work to enhance investment and ensure that Canadian industry is ready and equipped to take on what is increasingly tougher competition for future investments.

We commend the Committee and the government for extending the ACCA for a further two years in the last budget. This is an important tax lever to attract new capital and investment in Canada. However, we believe that the ACCA and subsequent extensions have not been sufficient in duration to stimulate enough investment in machinery and equipment (M&E) to raise labour productivity levels in our sector and across the manufacturing sector. Already our sector is more productive than its U.S. counterpart but this

advantage is narrowing as the productivity enhancing effects of large investments made in the early 1990's taper off. We need more to sustain our advantage and drive innovation. In particular, an emphasis needs to be made on the upgrading of energy products (in line with sector growth) to ensure that valuable feedstocks are available to the chemistry industry so that it can supply its customer base. The ACCA is an important part of this mix but to attract major new investments it needs to be in place for the necessary amount of time to be factored into investment planning decisions that are more often than not made at the global level with many locations under consideration.

Investment cycles do vary depending on the type of industry but a period of **five years** is a minimum. It is important to note that the ACCA is only available when machinery has been ordered and put in place. This is because, there is an inherent construction time lag built into the investment decision process for projects. Large projects have to go through development phases such as detailed engineering design, construction and major regulatory reviews which collectively can last several years before the M&E becomes operational. A typical board of directors will look at the entire time horizon for a project. If the ACCA is only available at the front end and not when the machinery is installed, it will not be factored into the decision making process. Therefore, an eligibility period of less than five years is just too short to impact investors' decisions on the large-scale capital intensive projects that Canada needs.

Our need for an extended ACCA is based on the fundamental view that services and manufacturing do not compete for the same capital. Service industries are subject to different regulatory structures, standards and have different capital/labour ratios. A lower corporate tax rate for all is good but we must also consider the huge capital requirements of manufacturing industries and their markets and investment environments which are truly global. We must also look to the competition and the role of government policies that impact the opportunities for extracting maximum value from Canada's natural resources such as energy. For example, oil sands upgraders that convert bitumen into synthetic crude oil do not qualify for the temporary ACCA in Canada. Meanwhile, U.S. refineries are making large scale capital investments to retool to handle Alberta bitumen as they take advantage of a five-year ACCA that was put in place in 2007. And that measure has recently been extended a further three years, maintaining a five-year investment planning horizon. It would seem therefore that U.S. tax policy is designed to encourage and favour the upgrading of Canadian natural resources in the U.S.

Another important component of Canada's tax policy mix is the SR&ED tax credit program. Research and development (R&D) is important to value creation in the Canadian economy and our industry plays a significant role. The manufacturing sector accounts for over 50% of all R&D investments in Canada, of which 14% is generated by the chemistry industry. The SR&ED tax incentive program is cited by many member companies as a critical factor in their decisions to locate R&D facilities in Canada. It yields economic benefits and is viewed by many other countries as a model for success. Finance Canada estimates that for every dollar of assistance provided via the SR&ED tax incentive, there is a net economic gain of 11 cents. We believe that this return could be even higher if administration of the program was streamlined. This would bring down costs and provide greater certainty to investors as to the value of the tax incentive. Businesses need to be confident about what R&D is eligible; however, at times they find the administration of the program unpredictable and inconsistent. As a result many companies have to exclude R&D tax incentives from return on investment (ROI) calculations because of uncertainty. Other issues such as inconsistent technical interpretations, increasingly complex requirements for compliance and delays in claim processing diminish the value and efficiency of the SR&ED tax credit system. In recommending streamlining of the program, we believe that this Committee needs to ensure that Revenue Canada does not move forward with any changes to the program in isolation and prior to completion of the comprehensive review of federal support to R&D.

Each year CIAC prepares competitiveness scorecards with supporting texts for Canada as well as the key chemical producing provinces. [Federal and provincial scorecard documents](#) can be found on our website.

The scorecards identify the key priority issues for our members and what needs to be done to address them. Tax policy and measures such as the ACCA and SR&ED tax credit are key components of a strategy to attract new investment in value-added manufacturing and resource upgrading but more needs to be done.

The rapid development of shale gas is providing new opportunities for petrochemical development in North America and we need to ensure that Canada gets its share. Complexes such as the one in Sarnia, Ontario are getting new life and an opportunity for growth as a result of the new feedstock supply from shale gas. Tax policy can help leverage these new opportunities into investments but government also needs to have strategies and policies to develop value-added resource upgrading complexes. We need more timely regulatory policies and policy alignment.

That is why we believe that there needs to be a government commitment to value-added manufacturing in Canada. Canada needs to develop a value-added manufacturing strategy. Canada needs a realistic assessment of the future of manufacturing and what government can do and what role industry must play. The [Alberta Competitiveness Act](#) and the [Alberta Competitiveness Initiatives](#) associated with that legislation is one example and one way to proceed. Reclaiming manufacturing for Canada is a worthy partnership to embark on.

CONCLUDING REMARKS

New sources of feedstock such as shale gas promise a once in a generation opportunity for growth. We need to seize this with new investment to create wealth and jobs and strengthen and grow our manufacturing base. As mentioned earlier, chemistry is what we call a keystone industry because we are part of so many different value chains in the economy. We transfer knowledge and deliver value and solutions through products and services. These are provided from and to other sectors of the economy including oil and gas extraction; petroleum refining; mining; forest products; metals; plastics; motor vehicles; telecommunications; computer and electronic products; electrical equipment; pharmaceuticals and food. Therefore when we grow, the benefits are spread throughout the economy.

Our goal as an industry is to become the North American leader in value-added resource upgrading. We need more innovation and upgrading. That is why we are recommending measures to encourage investment such as the five-year ACCA and improvements to the SR&ED tax credit program that will provide an upfront incentive to invest in Canada and add value to our natural resource base here rather than elsewhere.

It is appropriate to ask what the added cost of a five year ACCA will be. Since this measure has now been in place several years and been extended by a year or two in several Budgets, the incremental cost of a further five year extension is relatively small. Estimates by the Canadian Manufacturers and Exporters (CME), using investment figures from Finance Canada, suggest costs in the order of \$594 million over the next five years. This estimate does not credit any incremental investments that will result from the five year extension. CIAC urges the government to measure current machinery and equipment investments (average over the past three years) and compare it to the next five years to establish the real and incremental net benefit/cost to Canada. On top of this will be the added co-benefits of improved energy efficiency, reduced environmental footprint and increased productivity.