



## **Proposals to Deliver Greater Canadian Economic Efficiency and Innovation**

**To: The House of Commons Standing Committee on Finance  
2012 Pre-Budget Consultations**

**Guyanne L. Desforges, Clerk Standing Committee on Finance**  
House of Commons  
Ottawa, ON  
fina@parl.gc.ca

**Re: Submission of Spectra Energy Corp.**

**Date: August 11, 2011**

**Contact Information:**

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Mr. James Rajotte, MP  
Chairman  
House of Commons Standing Committee on Finance  
Ottawa, ON K1A 0A6

Dear Mr. Rajotte and Committee members:

Thank you for the opportunity to submit Spectra Energy's recommendations to the House of Commons Standing Committee on Finance's Pre-Budget Consultations.

Natural gas is the balanced energy of choice for North America: it is cleaner-burning, abundant, cost effective and reliable. More than ever, natural gas represents the most efficient and affordable way to heat our homes, generate electricity, and power industry. Recently, North American shale gas has dramatically altered the natural gas market, offering more continental gas supply than ever before, meaning natural gas prices for consumers are poised to remain stable and cost effective compared to other energy alternatives. For Canada, natural gas is well-positioned to advance shared energy, environmental and economic needs.

Today, due to highly competitive corporate tax rates, Canada is an attractive place to invest and we encourage the federal government to continue to advance policies, programs and instruments that stimulate investment in both the production and demand for natural gas, and the technological innovation that is the foundation for a cleaner energy future.

As a leading North American natural gas processing, transportation and delivery company, Spectra Energy would like to make several recommendations to the Committee to ensure that Canada continues to make the best use of these resources. Our recommendations are the following:

**Summary of Recommendations:**

- 1) ***Strengthen Economic Efficiency:*** Change Part VI.1 of the *Income Tax Act* to address discrepancy in rates between recent changes in Federal Corporate Tax Rates and unchanged VI.1 rates
- 2) ***Enhance Innovation:*** Address restrictions on ability to flow Investment Tax Credits (ITCs) to other partners besides the General Partner in a Limited Partnership under the SRED program

**About Spectra Energy:**

*Spectra Energy is one of North America's premier natural gas infrastructure companies serving three key links in the natural gas value chain: gathering and processing, transmission and storage, and distribution. Based in Houston, Texas, with operations in seven provinces and twenty-six states, Spectra Energy and its predecessor companies have processed, transported and delivered natural gas to customers across North America for more than a century.*

*Spectra Energy employs 3,400 people in Canada. Its operations include Spectra Energy Transmission West operating 5,700 km of natural gas gathering and transmission pipelines and sixteen natural gas processing plants in western Canada; an Ontario gas distribution company, **Union Gas**, that serves 1.3 million customers in 400 communities; and the **Maritimes & Northeast Pipeline**, a joint venture based in Halifax.*

*Spectra Energy is poised to continue investing in Canada. For 2011, Spectra Energy is devoting half its total capital expansion program to natural gas infrastructure development (pipelines, compressors, natural gas processing) in British Columbia.*

## **Recommendations:**

### **1. Part VI.1 of the *Income Tax Act: Finalizing a simple change first proposed in 2003***

**Recommendation:** Reduce tax rates in Part VI.1 of *Income Tax Act* to keep up with corporate tax reductions in order to not penalize companies that use Preferred Shares.

**Issue:** We offer one recommendation on the tax side, and that is to enact a tax deduction that was first proposed in 2003. In particular we would like to bring to your attention the matter of proposed tax changes to Part VI.1 and related legislation in the *Income Tax Act*.

We believe this initiative to be a non-contentious housekeeping initiative that complements and supports the federal government's economic policy towards encouraging investment in Canada and ensuring there is a very competitive tax environment to support jobs and investment.

Since 2003, the government has embarked on a campaign to ensure Corporate Tax Rates are low and competitive which we have supported in the past and commend the government for its leadership in this area. *The rate of the Part VI.1 tax and the corresponding tax deduction for this tax has not kept up with the reduction in corporate tax rates over the years.* The inequity has been recognized and draft legislation has been out in circulation in various forms over the past few years to rectify this issue. However, it has not been passed.

Utilities and Spectra Energy in particular, often use Preferred Shares as part of the mix of debt and equity in their operations. Under Part VI.1 of the *Act*, a tax is imposed on certain preferred dividends paid by a company. As part of this taxing regime a deduction is also provided under paragraph 110 (1) (k) for the amount of part VI.1 tax paid. The rate of the Part VI.1 tax and the deduction under 110 (1) (k) was set at a time when corporate tax rates averaged 40%.

**Benefits:** When Part VI.1 tax was introduced it was designed to leave a taxable corporation tax neutral, meaning the reduction of Part 1 tax would be more or less equal to the Part VI.1 tax payable. With the reduction of corporate tax rates under Part 1 the deduction no longer reduces Part 1 tax equivalent to the Part VI.1 tax. If it is not corrected preferred share issuers will continue to be unfairly penalized and it will reduce an option available for corporations in raising capital for further investing in Canadian jobs.

### **2. SR&ED: Making innovation more efficient and attractive for Limited Partnerships**

**Recommendation:** Allow for SR&ED tax credits to flow to other partners rather than solely the General Partner for innovation investments undertaken by Limited Partnerships.

**Issue:** Under the Scientific Research & Experimental Development ("SR&ED") program companies can earn Investment Tax Credits ("ITCs") on expenditures relating to its SR&ED activities. The ITCs earned can then be applied against income tax payable in the entity which carried out the SR&ED activity. When the SR&ED activity is carried out by a Limited Partnership ("LP") entity 100% of the ITCs flow to the general partner ("GP") under the Income Tax Act ("ITA"). Generally LP entities are structured so that the GP holds less than a 1% interest in the LP with the limited partner holding the remaining interest. *This can make it difficult or impossible for the GP to use the ITCs as usually the GP's only source of income is the income allocation from the LP.*

A secondary issue arises when the LP carrying out the SR&ED is in a tax loss position. When a LP makes a SR&ED submission the ITA prevents the SR&ED expenditures from increasing the loss allocated to the limited partner with no ability to carry forward the loss or reallocate to the GP and as a result losing the

tax loss. As an example had Spectra Energy submitted a SR&ED claim for one of its projects that had been carried out in one of its LPs the GP would have been allocated approximately \$1 million of ITCs and the limited partner would have had a tax loss allocation of approximately \$5 million. As the GP could not utilize the ITCs and the limited partner would have lost the tax loss, Spectra Energy did not submit the SR&ED claim for this important innovation project.

**Benefits:** Studies have shown that private sector R&D spending can lead to a more innovative economy and higher productivity growth and living standards. Society also benefits from new discoveries that serve as a catalyst for the creation of new or improved products, services, technology and processes. Canada does not have consolidated tax filings and as a result partnerships are often used to effectively achieve a consolidated tax filing with a limited partnership structure generally preferred to limit legal liability in a similar manner as a corporation does. The choice of the legal structure should not reduce the tax effectiveness of the structure under the SR&ED program and the current SR&ED application system does penalize the limited partnership structure.