PRE-BUDGET CONSULTATION REPORT & RECOMMENDATIONS

SUBMISSION TO THE STANDING COMMITTEE ON FINANCE

BY THE CANADIAN VEHICLE MANFACTURERS' ASSOCIATION

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The Canadian Vehicle Manufacturers' Association (CVMA) is the industry association that has represented Canadian manufacturers of light and heavy duty motor vehicles for more than 85 years. Its membership includes Chrysler Canada Inc.; Ford Motor Company of Canada, Limited; and, General Motors of Canada Limited. Collectively its members account for 63% of vehicles produced in Canada, operate five vehicle assembly plants, engine and components plants, and have over 1,300 dealerships. Approximately 120,000 jobs are directly tied to vehicle assembly in Canada.

The CVMA is submitting this consultation paper on behalf of its members offering fiscal policy recommendations that will support the competitiveness of the Canadian auto manufacturing industry and its ability to provide good quality jobs for thousands, contribute millions in tax revenues to all levels of government and support prosperous communities. The following is a summary of the recommendations put forward for the consideration by the Standing Committee on Finance as part of the 2015 budget planning process:

Competitiveness of Auto Manufacturing is Important to Canada

Canadian auto manufacturing:

- Employs over 120,000 people and each assembly job has a multiplier of 9 additional jobs that add benefit to the surrounding community.
- Contributes over 11% of total manufacturing GDP
- Contributing billions of dollars in Government tax revenues
- Provides good jobs for families; contributes to fiscal sustainability of communities and to their overall economic prosperity.
- Contributes to a vibrant research, development, innovation and commercialization presence in Canada.

Auto manufacturing is undoubtedly a critical contributor to Canada's economy. At the same time, it is also under immense pressure from increasingly aggressive global competition. The report, *"A Call for Action: II"*, released by the Canadian Automotive Partnership Council (CAPC) in November 2013, provided an overview of the current competitive environment and listed key recommendations to both the public and private sectors to help Canada position itself to better respond to aggressive competition. A copy of the report has been enclosed as a separate document with this submission.

Other Jurisdictions are Successfully Competing for Manufacturing Investment

With the increasing global competition to attract investment, Canada needs to reassess its investment support strategies in order to ensure that they remain globally competitive.

- The Office of Automotive and Vehicle Research at the University of Windsor reported that auto makers spent $17.6 billion (U.S.) around the world in 2013 to increase vehicle-making capacity but none of this was placed in Canada.

This marks the third year in a row that Canada has missed investment decisions underlining the need to put reinvigorated focus on ensuring the right incentives and policies in place to support Canada's competitiveness going forward.

Given the intense global competition to attract these economically beneficial automotive investments, it is critical for Canada to have globally competitive investment support strategies in place to secure re-investment in its existing automotive production footprint. These investments incentives provide rapid returns on investment for both the Government and taxpayers, even in times of fiscal restraint. A clear illustration of the return on investment has been developed by Magna International Inc. and we would be pleased to provide this on request. This ROI illustration clearly provides evidence that there is much to be achieved through strategic investments and partnership between government and industry.

CVMA RECOMMENDATIONS TO THE STANDING COMMITTEE ON FINANCE PRE-BUDGET CONSULTATIONS

Given the importance of auto manufacturing to the Canadian economy and in response to fierce global competition, the following recommendations are presented for the Government's consideration and which address each of the 2015 budget planning themes.

RECOMMENDATION 1 – *Change the AIF to a non-repayable investment incentive and ensure the level of incentive is sufficient to ensure Canadian auto assembly plants are able to compete for investment. All elements of the AIF should be benchmarked against competing jurisdictions to ensure that Canada has the most competitive tools available including: the magnitude and form of AIF, its tax treatment, required conditions, and speed of approval for eligible proposals.*

a) Magnitude and Form of AIF:
Government incentives in Canada have typically reached a maximum level of 30% of the total investment proposal, jointly split between the federal and provincial Government, with the federal portion in the form of a long-term zero interest loan or repayable contribution.

This model was successful in helping to previously attract billions of dollars of automotive investment to Canada, however the requirement to repay this contribution and recent rulings by CRA to tax the repayable contribution in the year the loan is received, results in a federal incentive in Canada that is uncompetitive when compared with other jurisdictions in North America and globally.

From an accounting perspective, a repayable contribution or loan is a balance sheet transaction. As such, these incentives do not reduce the cost of an auto investment in Canada as the funds are repayable. Depending on the company's borrowing cost, taxing these repayable funds in the year received may actually completely eliminate any potential benefit of this type of funding.

Today, most competing jurisdictions offer non-repayable contributions in many different forms, including cash grants, refundable tax credits, and infrastructure and training credits and grants, with contribution levels that can exceed 50% of the total investment spending. No additional taxes are incurred as a result of the incentives, the conditions are flexible and performance-based, and project evaluation and approval is relatively fast.

Canada's auto industry appreciates the renewal and funding of the AIF, however, the terms of the program also need to change in order to keep up with changes in competitive jurisdictions for auto investment. The fact that the last several large investments were made outside of Canada should be a sign that Canada's Auto Innovation Fund needs to change in order to become competitive. Making an enhanced and globally competitive AIF permanent would also improve Canada's ability to compete for future investment decisions by providing certainty and predictability for decision-makers when examining where to place new investments.

b) Tax Treatment of Loans and Repayable Contributions from AIF and Similar Programs
It is recommended that the Government of Canada change the Income Tax Act to provide for the tax-free status of the repayable amounts received under the AIF programs to provide greater financial benefit to the recipient company making the prospective investment in Canada.

Taxing the fully repayable contribution in the year that the funds are received significantly reduces the value of the incentive, and also reduces the value of any potential SR&ED credits, thereby reducing the value of the AIF, and similar funds. Under the current tax treatment of the repayable loans incentive, only half of the benefit of such a loan is realized by a recipient.

Providing tax free status of AIF funding will help improve the competitiveness of the AIF and will provide support to Canadian vehicle manufacturers (including CVMA members as well as Toyota and Honda) and the Canadian supplier community, which together accounts for over 120,000 direct jobs in the industry. As such, the economy at large will benefit.

If this change cannot be made, then the overall contribution share provided to any one OEM from the AIF should be significantly increased.

c) Greater flexibility
Ongoing assessment of AIF is required to evaluate the comparative incentives offered by competing jurisdictions. Adaptation must continue and be planned for with a mid-to-long term vision. Canadian vehicle manufacturers need to have clarity on the conditions and applicability of the investment tools and mechanisms available at any moment. Consistency in approach is recommended and investment incentives that take the form of grants tend to enhance the flexibility needed by large scale manufacturing.

d) More effective and efficient coordination
More efficient and transparent coordination is needed between federal, provincial and municipal government stakeholders. It is recommended that governments institute a single window of entry approach, similar to that successfully employed by ProMexico.

e) Certainty of Investment Incentives
Automotive manufacturers require certainty. The ability for companies to receive an early signal or response from Government as to the level and type of incentives available for a proposed investment is crucial. Investment incentives must be sufficiently flexible to recognize the speed at which company investment decisions are being made. A clear indication of what each level of government would contribute to any one planned investment can have a marked impact on how a company prioritizes investment decisions and site location. Further to this, contributions to investment funds need to be continuous so that a company has the ability to plan accordingly to obtain new product mandates.

f) Prompt response time

In the fierce competition for plant investment among jurisdictions, the availability of incentives is essential. Government must be in a position to respond quickly to demonstrate to investors that it will assist with their needs to early launch into markets and work with the company to secure new investment in Canada.

g) Accelerated Capital Cost Allowance (ACCA)

The industry has been very supportive of the ACCA as an important measure that has enabled companies to update machinery and equipment for auto manufacturing. To be competitive, Canadian auto manufacturing companies must be able to demonstrate leadership in productivity, utilizing leading edge technology in both products and processes. The ACCA has been an effective measure to spur investment in machinery and equipment. However, as this measure will sunset in 2015, it is strongly recommended that the government commit to a depreciation rate of 30% to 50% on a declining balance basis to ensure Canadian auto manufacturers have the ability to compete with other jurisdictions (especially with the U.S.) with investments in productive assets.

h) Scientific Research & Experimental Development (SR & ED)

The SR&ED has been an effective competitive measure and consideration of how advanced manufacturing companies could access unused credits at a time when they could best be allocated is encouraged. The CVMA recommends that large companies should be able to exchange unused SR&ED tax credits in exchange for direct funding when used for new R&D projects. Ideally, this would also include capital assets for research and development facilities, building of new R&D facilities and/or to invest in machinery and equipment for R&D purposes. Providing the ability for companies to repurpose unused tax credits to invest in research and development would enhance industry innovation and competitiveness.

i) Better communication mechanisms

A government investment strategy must also support an effective and consistent communications mechanism to ensure company global investment decision-makers are aware of current tools and strategies available to them in Canada in an ongoing, time sensitive manner.

RECOMMENDATION 2 - *The CVMA recommends the establishment of a Canadian Automotive Research Institute (CARI) technology initiative to support the research, development, innovation and commercialization of new products and manufacturing processes that will lead to improved productivity and profitability for the auto industry (both suppliers and OEMs) as well as increased employment opportunities.*

The CVMA members support a CARI initiative that would provide a competitive level of assistance to encourage and support the research, development, innovation and commercialization of new products and manufacturing processes that will lead to improved productivity and profitability for the auto industry (both suppliers and OEMs) as well as increased employment opportunities.

This initiative would improve auto manufacturing competitiveness by proving support to auto companies of all sizes to make Canada a centre for product and manufacturing process development which is a critical aspect of an overall auto strategy for Canada to protect its auto manufacturing footprint.

Canada already provides similar support to the aerospace sector through various mechanisms, most recently the Technology Demonstration Fund established in Budget 2013 as part of the Strategic Aerospace Defence Initiative, and the auto industry believes that a similar approach for the automotive sector would bolster the Government's economic agenda to support jobs, economic growth and competitiveness.