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# **Canadian Vehicle Manufacturers' Association**

**Submission to the 2004  
Pre-Budget Consultation Process**

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## **INTRODUCTION AND BACKGROUND:**

On behalf of the members of the Canadian Vehicle Manufacturers' Association (CVMA), thank you for the opportunity to provide our comments as part of the 2004 pre-budget consultation process. The CVMA is the national association for Canada's largest automotive manufacturers; our membership includes DaimlerChrysler Canada Inc., Ford Motor Company of Canada, Limited, General Motors of Canada Limited, International Truck & Engine Corporation, and Volvo Cars of Canada Ltd. Our member companies are the leaders in an industry that employs over 500,000 Canadians, accounts for roughly 16% of Canada's manufacturing GDP and generates a trade surplus of \$11.5 Billion annually as Canada's leading exporting sector. Over the past decade, DaimlerChrysler Canada Inc., Ford Motor Company of Canada, Limited, General Motors of Canada Limited invested over \$20 Billion in new technology and facilities in to Canada

Strategic public policies, such as the Autopact and free trade, have played a crucial role both in developing this large and productive automotive industry and in terms of creating assembly and auto parts jobs in Canada. These policies, along with economic and business realities, have resulted in an automotive sector that has become highly competitive and truly global in nature. However, significant changes to domestic and international policy throughout the 1990s has undermined the effectiveness of these policies' ability to draw new investment into Canada. The result is that Canada's automotive industry is at a critical juncture. With unprecedented competition, excess capacity and the elimination of most of the key policy tools to encourage automotive manufacturing investment, the future of much of Canada's automotive manufacturing industry is at risk. To ensure that Canada remains a competitive location for automotive production and investment we have been working with the federal government, the governments of Ontario and Quebec, labour and academia, through the Canadian Automotive Partnership Council, to create and implement a strategic automotive policy for our future.

The Canadian Automotive Partnership Council's (CAPC) mandate has been to develop a new policy framework that will create an environment that facilitates the strengthening and growth of our industry in Canada. This includes recommendations for both investment and innovation as well as for creating a competitive and fair marketplace for consumers to purchase new vehicles. Many recommendations have been put forward

by CAPC that will help sustain the hundreds of thousands of jobs and billions of dollars of government revenue which depend on a vibrant and competitive auto industry. While some of these recommendations have begun to be implemented, such as the elimination of the Large Corporations Tax (LCT) announced in the 2003 Canadian budget, we must ensure that a complete package of economic and social policies are fully and expeditiously implemented by government. This should include policies in the areas of taxation, innovation, and infrastructure as well as policies that will address the dramatically increasing costs for health care and employee benefits incurred by the private sector. This submission highlights many policy options that we feel would help strengthen the automotive industry in Canada.

## **RECOMMENDATIONS FOR THE 2004 BUDGET:**

### **1. Alternative Fuel Vehicle Rebate**

Traditional gasoline internal combustion engine vehicles (ICEs) have evolved significantly over the last number of decades and have made significant advances in both fuel economy improvement and emissions reductions. Improvements of this nature are expected to continue and therefore, ICEs are expected to dominate the Canadian fleet for the foreseeable future. Concurrently, vehicle manufacturers have spent billions of dollars developing and bringing to market traditional alternative fuel vehicles (AFVs) and advanced technology vehicles (ATVs), such as hybrid electric and fuel cell vehicles. Although they have been available for many years, alternative fuel and more recently advanced technology vehicles have not been significantly adopted by the Canadian marketplace. This is primarily because consumers are very familiar with gasoline ICEs, which are efficient, reliable, durable and relatively low cost compared with ATF and ATV vehicles which have a significant cost premium and limited refueling infrastructure may exist for these vehicles.

Cleaner, more fuel efficient advance technology vehicles have a role to play in achieving Canada's air quality goals and will contribute to reducing vehicle-related green-house gas emissions. The magnitude and speed of the contribution is largely related to how quickly they these technologies are adopted by consumers. Due to the associated advanced vehicle technologies involved, the costs to manufacture these vehicles is many thousands of dollars higher than a comparable ICE vehicle. This premium is significant because for every \$100 increase in the cost of a new vehicle there is a

corresponding .8% reduction in demand. Surveys show that consumers indeed want ‘greener-cleaner’ products including cars, but their enthusiasm quickly dissipates when it is evident they might have to pay a more to obtain those products. To assist consumers with these price premiums, the government should provide consumers with meaningful incentives to purchase advance technology vehicles. Creative options could include direct consumer rebates, sales tax rebates, or perhaps income tax credits that would allow consumers to effectively offset the higher costs associated with these vehicles. The level of incentive should reflect the cost premium and level of benefit offered by the vehicle. As a result, the CVMA recommends that:

- **The federal government should establish meaningful consumer incentives for the purchase of AFVs and ATVs to create market pull and assist early consumer adoption of these vehicle technologies.**
- **The federal government should encourage the development of refueling infrastructure for ATVs and AFVs.**

## **2. Air Conditioning Excise Tax Elimination**

In 1976 the federal government introduced an excise tax on vehicles sold with air conditioners. At that time, air conditioners were not ozone friendly and were considered luxuries. Today, consumers pay \$100 on each new vehicle with an air conditioner despite the fact that modern air conditioners are environmentally friendly and are no longer considered luxuries. As a result, the CVMA recommends that:

- **The federal government should eliminate the \$100 excise tax on air conditioners designed for vehicles.**

## **3. Fiscal and Investment Policy**

Multiple factors drive investment decisions by corporations including market access, labour and other costs of production, political stability, and after-tax return on investment (corporate tax policy). Within NAFTA, the United States has the advantage of market size to encourage investment while Mexico has labour cost advantages. One clear area for Canada to become a more attractive location for investment is by creating a hemispheric competitive tax policy that improves after-tax return on investment.

By leveraging the corporate tax system to encourage capital investment, Canada can maintain and create a large volume of high skilled, high wage, high tax stream jobs. Canada has made significant progress to date on various fiscal issues including eliminating deficits, improving the debt-to-GDP ratios and beginning to reduce corporate taxes. While a good beginning, the focus should now move to policies to further stimulate domestic and foreign investment in order to generate growth and jobs. Such policies will cultivate a corporate tax base that will assist in providing revenues for other priority areas such as health care, education, infrastructure and the environment. We believe that the areas of focus for an automotive investment tax policy must include the following:

- The federal government announced in the 2003 budget that it would phase out the Large Corporation Tax by 2008. This tax, more than any other, unfairly targets capital intensive industries and acts as a disincentive to investment. **The CVMA recommends that the phase out of the LCT be accelerated.**
- A general corporate tax reduction would stimulate the economy as a whole and would encourage greater foreign investment. Multi-national corporations are encouraged to leave earnings in lower tax jurisdictions. This could result in a growth of tax revenues as companies seek a net reduction in overall corporate taxes globally by structuring their activities to pay more tax in Canada. The federal government rate reductions for non-manufacturing and processing profits will be fully phased in next year, however, we believe that they should be lowered further and that the corporate surtax should be eliminated. **The CVMA recommends that the federal corporate tax rate be lowered to 17.5%**, which would be the lowest rate within North America.
- **The CVMA recommends that an investment tax credit for new manufacturing equipment be reintroduced.** These credits would apply on eligible new equipment and would be refundable. These credits improve the cash flow and return on investment to tax paying entities.

- Increasing the rate of capital cost allowances would improve the competitiveness of the tax system as well as Canadian companies because it would encourage investment in new technology and equipment. **The CVMA recommends the rates of Capital Cost Allowances on manufacturing equipment be increased.**
- Taxes are generally required to be withheld when Canadian companies issue payments in respect to interest and dividends to non-resident investors. This creates a significant disincentive to foreign companies that are contemplating investing in Canada. Eliminating the requirement to withhold tax on such non-resident payments would encourage greater direct foreign investment. **The CVMA recommends that future tax treaties provide for the elimination of the withholding tax on interest and dividends payments between Canada and the foreign country in order to promote direct investment in Canada.**

#### **4. Trade and Infrastructure Policy**

As a highly-integrated industry across North America, the automotive industry relies on seamless transportation between Canada and the U.S. to ensure that our facilities efficiently operate. As a result of our production and level of industry integration, our sector accounts for roughly 25% of the two-way trade between Canada and the U.S. The majority of these shipments are production parts that feed assembly facilities on both sides of the border which require streamlined and efficient border crossings to accommodate the just-in-time delivery systems.

As a result of this high level of integration we have been actively engaging the governments of both Canada and the U.S. to implement changes in customs regulations to streamline the processing of shipments crossing the border. We have worked with both governments to implement the 30-point action plan and our members have been the first to implement new programs such as Free And Secure Trade (FAST) into their operations. However, the programs aimed at expediting border crossings do very little if the physical infrastructure that carries goods and people to the border is outdated and inadequate to handle current volumes. Canada's auto industry has long advocated for strategic infrastructure investments to effectively process existing trade volumes

between Canada and the United States and also future trade growth as our economies become further intertwined. The money announced in the 2002 federal budget for infrastructure was a good start, however, it is insufficient to meet current or future demands. **The CVMA recommends that the federal government increase funding for physical transportation infrastructure that will sustain current and future trading demands.** These efforts should be aimed at:

- Expeditiously implementing previously announced investments, such as the \$300 Million for border infrastructure, which were designed to support the 30-point action plan. This must include taking leadership in implementing the 9-point plan developed jointly with the Province of Ontario for the critical Windsor gateway.
- The creation of a new border crossing into the U.S. in the critical southern Ontario region.
- Creating an uninterrupted access from highway 401 through to the U.S. interstate system.
- Working with provincial governments to improve critical trade corridors.

## **5. Innovation Policy**

Given that investment and innovation are effectively two halves of the same whole, the government needs to ensure that in addition to having an efficient R&D tax credit system, Canada has a complementary product commercialization strategy to help bring new goods to market.

To support strategic innovation, the CVMA recommends that:

- **An Early Commercialization Investment Tax Credit be created.** This tax credit would be stackable on top of other available incentives/assistance for early modules of production of a new technology to attract new technology (such as alternative fuel and propulsion technologies) production opportunities to Canada.

- **Funds be specifically earmarked for automotive R&D, with particular focus on lightweight materials, hybrids, fuel cells and pilot programs involving hydrogen refueling infrastructure.**
- **Establish meaningful tax credits to assist consumers to adopt new technologies by offsetting premium costs.**
- **Vigorously expand process review within the SR&ED directorate.** This will allow companies to spend their resources on SR&ED rather than defending their SR&ED claims.
- **Enhance the definition of eligible SR&ED activities to better address and encourage automotive product development and manufacturing process innovations.**

#### **CONCLUSION:**

The implementation of a strategic and comprehensive policy that supports investment and innovation in the automotive sector, such as those put forward by CAPC, is vital to the sustainability of our sector in Canada. CVMA members believe that creating a climate for economic growth must be a fundamental priority of the 2004 budget. Implementing the recommendations included in this submission would send a signal that the government is serious about fostering an environment that promotes growth in the automotive industry. Thank you again for the opportunity to provide input into the pre-budget consultation process for 2004.

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## **SUMMARY OF RECOMMENDATIONS:**

### **Alternative Fuel Vehicle Rebate:**

- Establish meaningful consumer incentives for the purchase of AFVs and ATVs to create market pull and assist early consumer acceptance of these vehicles.
- Encourage the development of refueling infrastructure for ATVs and AFVs.

### **Air Conditioning Excise Tax Elimination:**

- Eliminate the \$100 excise tax on air conditioners designed for vehicles.

### **Fiscal and Investment Policy:**

- Accelerate the phase out of the Large Corporations Tax (LCT).
- Lower the federal corporate tax rate to 17.5%.
- Eliminate the corporate surtax.
- Reintroduce an investment tax credit for new manufacturing equipment.
- Increase the rates of Capital Cost Allowances on manufacturing equipment.
- Eliminate the withholding tax on interest and dividends payments between Canada and foreign countries.

### **Trade and Infrastructure Policy:**

- Increase funding for physical transportation infrastructure that will sustain current and future trading demands.

### **Innovation Policy:**

- Create An Early Commercialization Investment Tax Credit.
- Specifically earmark funds for automotive R&D, with particular focus on lightweight materials, hybrids, fuel cells and pilot programs involving hydrogen refueling infrastructure.
- Establish meaningful tax credits to assist consumers to adopt new technologies by offsetting premium costs.
- Vigorously expand process review within the SR&ED directorate.
- Enhance the definition of eligible SR&ED activities to better address and encourage automotive product development and manufacturing process innovations.