TAX POLICY TRENDS

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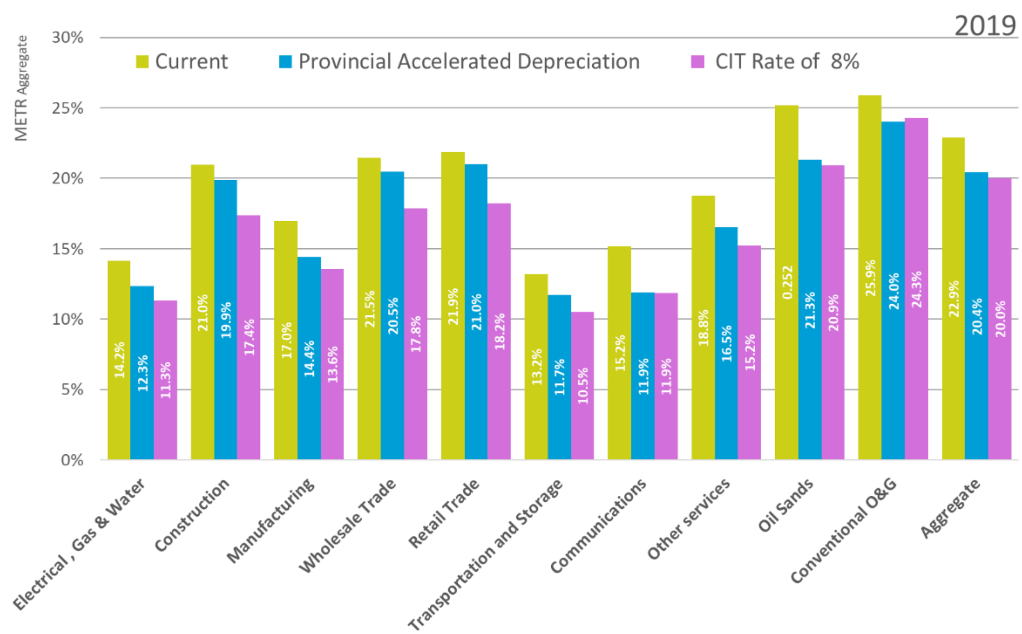
CORPORATE TAX POLICY: ALBERTA GOES ITS OWN WAY

By Philip Bazel and Jack Mintz[1]

When it comes to corporate tax policy, Alberta is taking a different path than the federal government and other provinces. Alberta's May 28th *Job Creation Tax Cut* will reduce the provincial corporate income tax rate from 12% to 8% in lieu of introducing accelerated depreciation that was adopted by federal government November 2018[2], including a 100% write-off for clean energy and manufacturing.

All provinces, except Alberta and Quebec that collect their own corporate income tax, have adopted the federal amendments, consistent with Tax Collection Agreements. In December 2018, Quebec agreed to the same federal accelerated depreciation package, scaling back its generous additional capital cost allowance implemented by the province prior to the Federal announcement. Prior to the April 16th 2019 election, Alberta's NDP government made no announcement and the UCP platform was silent on accelerated depreciation. Now, the only proposal adopted in Alberta is the corporate tax rate reduction.

Figure 1: Marginal Effective Tax Rates on Capital by Industry for Pre-July 1 2019 (current), provincial accelerated depreciation and Job Creation Tax Cut[3]



*Aggregate includes agriculture and forestry.

This *Tax Trends* compares the impact of the *Job Creation Tax Cut* with temporary accelerated depreciation for Alberta. We specifically examine impacts on investment and economic distortions.

In the figure, we present the combined federal-Alberta marginal effective tax rate[4] (METR) for greenfield investments by industry for three cases: the pre-July 1 current system, provincial accelerated depreciation (that would be fully in place for 5 years before being phased out) and fully implemented corporate rate cut to 8%.

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Compared to the current corporate tax system, the legislated 4-point Alberta corporate tax rate reduction will reduce the METR from 22.9% to 20% when fully implemented. While all industries benefit, the largest reductions in the METR or more will take place in construction (3.6 points), manufacturing (3.4 points), wholesale trade (3.7 points), communications (3.3 points), other services (3.6 points) and oil sands (4.3 points).

For most industries, *Job Creation Tax Cut* will be more beneficial for investment than adopting federal accelerated depreciation except for conventional oil and gas.

The rate reduction also slightly reduces tax distortions while accelerated depreciation increases them substantially by favouring shorter-lived investments (especially manufacturing and clean energy). The dispersion index (the variance in METRs across assets and industries as a percentage of average METR) rises by three-quarters from 0.032 to 0.056, resulting a greater misallocation of resources under accelerated depreciation.

The rate reduction, being permanent, also provides greater long-run confidence that Alberta's tax system will be more conducive to investment than temporary accelerated depreciation. It serves as a better response to U.S. tax reform that has made it more attractive to invest and keep profits in the U.S.

Since January 1, 2018 the largest oil and gas producing state in North America, Texas, has a federal-state corporate income tax rate of only 21 percent.

The UCP must be fans of Fleetwood Mac's song "Go your Own Way". Perhaps it makes sense they did.

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[2] Federal accelerated depreciation provides 100 percent write-offs for machinery investments in clean energy, manufacturing and processing as well as increasing the first year write-off for other depreciable assets from one-half to one-and-half times the regular capital cost allowance rate.

[3] Excluding oil and gas, aggregate values are: Current at 16.3%, Provincial Accelerated Depreciation at 14.5%, and CIT Rate of 8% at 13.1%

[4] The METR is the amount of corporate income tax, sales tax on capital purchases, asset-based taxes and resource levies paid as a percentage of the pre-tax rate of return on capital. For model details, see P. Bazel and J. Mintz, "2015 Tax Competitiveness Report: Canada is Losing its Attractiveness", *SPP Research Papers*, 9(37), The School of Public Policy, University of Calgary, 2016.

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