CANADIAN MANUFACTURERS & EXPORTERS

CME 2023 ONTARIO PRE-BUDGET SUBMISSION

Submission to: Hon. Peter Bethlenfalvy, Minister of Finance

February 2023

PILLARS OF AN ADVANCED MANUFACTURING STRATEGY

Pillar 1: Establish Competitive Investment Incentives to Address the IRA

- Introduce a 30 per cent refundable "Ontario Made" manufacturing investment tax credit
- Broaden and extend the Ontario Job Creation Investment Incentive
- Establish positive incentives to reduce emissions
- Enable Carbon Capture, Utilization and Storage (CCUS)
- Bolster energy and charging infrastructure
- Champion Ontario Made
- Boost incentives to innovate

Pillar 2: Get the Workers We Need

- Support work integrated learning
- Accelerate the transition to skilled trades
- Connect employers to opportunities
- Reconsider the income surtax

Pillar 3: Lower the Cost of Doing Business

- Create a new industrial electricity rate
- Provide tax and program incentives for new energy options
- Provide relief for employment lands
- Reduce red tape

INTRODUCTION

Manufacturing is critical to Ontario's economy. The industry's 36,200 firms directly generate almost 11% cent of the province's GDP and close to 80 per cent of its merchandise exports. Including indirect and induced impacts, the sector's footprint amounts to one-quarter of Ontario's total economic activity. As well, the sector directly employs 772,400 Ontarians and supports nearly 2 million more of the province's workers through supply chain activity and employee spending.

As critical as the sector is, its development has not kept pace with Ontario's North American competitors. Over the last 15 years:

- Investment increased by 36% in the US but fell by 15% in Ontario
- Real GDP rose 14% in the US but decreased 19% in Ontario
- Exports climbed 53% in the US compared to only 10% in Ontario

To reverse these long-term trends, the government must make an Advanced Manufacturing Strategy a key focus of the 2023 provincial budget, underpinned by the following three pillars.

PILLAR 1 – ESTABLISH COMPETITIVE INVESTMENT INCENTIVES TO ADDRESS THE IRA

Adopted by Congress in August 2022, the IRA added $369 billion to funding previously committed under the CHIPS and Science Act and the 2021 Infrastructure Investment and Jobs Act. Combined, these initiatives represent almost half a billion over ten years in clean energy and technology supports. Of particular significance, the Advanced Manufacturing Production Credit (Section 45X) supports the development of a domestic clean technology supply chain, providing incentives valued at $30.6 billion.

To compete, Ontario's manufacturing sector needs to embrace the Industry 4.0 revolution – the integration of advanced technologies such as the Internet of Things (IoT), robotics, cloud computing, and big data analytics into manufacturing. This integration allows for greater automation, improved communication and decision making, and more efficient, productive use of resources.

Unfortunately, Ontario's manufacturers are slow adopters of advanced manufacturing technology, especially relative to their counterparts south of the border. Over the last 15 years, machinery and equipment (M&E) investment in the US manufacturing sector increased by a total of 16.7%, but it fell by 14.9% in Ontario's manufacturing industry.

→ RECOMMENDATIONS

- **Introduce a 30 per cent refundable "Ontario Made" manufacturing investment tax credit** to assist companies with plant expansion, upgrades, technology adoption, onshoring, re-tooling, improving environmental performance, and exporting.
- **Broaden and extend the Ontario Job Creation Investment Incentive.** Also known previously as the Accelerated Capital Cost Allowance (ACCA), this measure allows companies to immediately write-off the full cost of investing in productivity enhancing M&E. The phase-out of the tax credit (currently planned to begin in 2024) should be postponed for at least three years considering the IRA and the pandemic's disruptive impact on capital projects. Eligibility for the accelerated depreciation should be reviewed to include strategic mining and metal manufacturing activities.
- **Establish positive incentives to reduce emissions.** This could be accomplished by allowing manufacturers to access proceeds paid under the Emissions Performance Standards (EPS) to fund technology investments to reduce greenhouse gas (GHG) emissions in their business. This company-specific allowance could be administered and disbursed through the tax system and be held for five years. After this period, funds could be used by other manufacturers for GHG reduction initiatives.
- **Enable Carbon Capture, Utilization and Storage (CCUS).** The IRA increased the existing 45Q tax credit to \$85 per tonne for permanent geological sequestration of CO_2 and to \$60 per tonne for utilization of CO_2. To prevent a flight of financial and human capital to projects in the US, Ontario should accelerate the regulatory process to enable CCUS in the province and consider more generous incentives on par with the IRA, including operational expenditures.
- **Bolster energy and charging infrastructure.** According to the *2022 IESO Annual Planning Outlook,* Ontario will face an electricity generation capacity shortfall as early as the mid-2020s due to nuclear retirements and refurbishments, expiring contracts, and rising demand from electrification. Ontario should consider appropriate grid improvements based on industry input to power the energy transition across the province. Similarly, we need to dramatically ramp up financial incentives to establish the charging infrastructure needed for the broad adoption of electric vehicles.
- **Champion Ontario Made.** Ontario must lead the Buy Ontario revolution, leveraging the \$29 billion in goods and services purchased annually through the Building Ontario Businesses Initiative (BOBi). Key to the success of this initiative is CME's Ontario Made program, which can be used by procurement officials to better assess available local supplies. However, annual funding renewals have limited the program's ability to reach its full potential. Emulating the success of Foodland Ontario, the province should commit to permanent funding to broaden the program's scope and reach.
- **Boost incentives to innovate:** Ontario's Innovation Tax Credit (ITC) is based on outdated federal definitions that are over 40 years old and is set at such a low rate that it only offsets income tax on the equivalent federal SR&ED credit. To provide a proper incentive, the credit should be increased incrementally, to 15%, 20% and 25% once fully ramped-up. Eligibility should also be expanded beyond early-stage research and development (R&D) to include capital improvements and product or process innovations, which have become crucial to compete in the age of Industry 4.0.

PILLAR 2 – GET THE WORKERS WE NEED

To succeed in tomorrow's economy, employers must develop stronger capacity to upskill their workforce to adapt to evolving manufacturing workplace trends – digitalization, automation, and greater emphasis on problem solving. While significant energy has been dedicated to training initiatives, broader incentives are needed to benefit employers across the sector, large or small, unionized or not. There is urgency. In a recent survey conducted by CME, Ontario manufacturers reported that labour and skills shortages in the sector cost Ontario's economy almost $4 billion resulting from lost sales, penalties for late delivery, and delayed or cancelled capital projects.

→ RECOMMENDATIONS

- **Support work-integrated learning** by introducing a new refundable tax credit to support employer-led training and the shift to automation (covering 50% of expenditures, for the first five years on the job). This measure will provide sector-wide benefits that will not only increase productivity but maintain employment during the widely anticipated economic slowdown.
- **Accelerate the transition to skilled trades.** In CME's fall labour survey, 71% of Ontario respondents identified skilled production occupations (millwrights, machinists, welders or electricians) as the most urgent area of labour shortage. Despite that reality, less than 60% of employers said they had used apprenticeship programs and tax incentives in the past or were planning on using them in the future. Of those that did, only 39% said the incentives helped them find skilled workers. This calls for a more aggressive approach to continue to publicize and streamline programs under the stewardship of Skilled Trades Ontario. One approach could be to invest in shorter pathways, allowing students testing well on key competencies to enter the market sooner, or giving them the option to pursue a lower tier of certification than is currently required for full Red Seal Qualification.
- **Connect employers to opportunities:** In Fall 2022, the Government announced its Level Up Fairs to more effectively attract students to consider STEM careers. This outreach should be supplemented with financial support for workplace school visits by manufacturers and an online single window system that matches prospective apprentices with manufacturing employers. The Skills Development Program (SDF) should be resourced appropriately to continue building those initiatives.
- **Reconsider the income surtax.** In 2007, Ontario implemented a surtax on personal incomes over $75,000. Originally envisioned as a temporary measure, this surtax is levied on previously taxed income and was not adjusted to inflation, therefore acting as a punitive and growing disincentive to attract in-demand and mobile skilled workers such as software engineers, electricians, or plant managers. This surtax should be phased out, or at least adjusted to factor in the effects of inflation and remove double taxation.

PILLAR 3 – LOWER THE COST OF DOING BUSINESS

In the span of just 11 months, the Bank of Canada has increased its policy target rate by 425 basis points, representing the most aggressive tightening cycle in 25 years. This rapid increase in the cost of financing adds to the other high costs of doing business in Ontario, including having among the highest electricity rates in North America.

While the Comprehensive Electricity Plan has provided welcome relief from the escalation of Global Adjustment charges seen between 2008 and 2018, this gain is being partly offset by a recent increase of the Hourly Ontario Energy Price (HOEP). As neighbours like Michigan and Quebec already offer special electricity rates designed to attract investment, those jurisdictions are now well positioned in the race to diversify heat sources and invest in energy-intensive production of hydrogen or battery cell manufacturing.

To be competitive, Ontario must provide immediate rate relief to avoid missing on key investment.

→ RECOMMENDATIONS

- **Create a new industrial electricity rate:** Leveraging the work of the newly formed Electrification and Energy Transition Panel, Ontario should implement a subsidized electricity rate to attract and retain manufacturing investment to Ontario. This rate should be competitive with comparable rates offered by neighbouring provinces and US states (i.e., in the $0.06 to $0.10/KWh range).
- **Provide tax and program incentives for new energy options.** Mirroring similar incentives in the IRA, the province should support company efforts to diversify toward more sustainable or cost-effective solutions to generate heat and power for industrial operations, which may include hydrogen, biodiesel, renewable natural gas, heat pump, hybrid heating systems or others.
- **Provide relief for employment lands:** Eliminate the Business Education component of the property tax system and phase-in assessments to avoid compounding the real estate shock when values are re-assed for the first time since 2016. To provide better certainty going forward, Ontario should harmonize with other Canadian jurisdictions and announce a transition to annual assessments. The province should also work on a balanced framework of incentives to preserve access to industrial lands for business expansions while also building the houses needed for the next generation of manufacturing workers.
- **Reduce red tape:** Regulatory modernization and simplification remains necessary to create the stable environment needed for business to thrive. Building on the $576 million reduction achieved between 2018 and 2022, and the helpful consultation process announced in the 2022 Fall Economic Statement, Ontario should commit to further reducing regulatory red tape by $700 million in the next four years. This would represent a 20% increase in the burden reduction over the government's last mandate.

ABOUT CME

Since 1871, we have made a difference for Canada's communities.

Fighting for the future of manufacturing in Canada. Helping manufacturers invest and grow at home and abroad.

From the first industrial boom in Canada, CME has advocated for and representing member interests. 150 years strong, CME have earned an extensive and effective track record of working for and with 2,500 leading companies nationwide.

More than 85 per cent of CME's members are small and medium-sized enterprises. As Canada's leading business network, CME, through various initiatives including the Canadian Manufacturing Coalition, touches more than 100,000 companies from coast to coast, engaged in manufacturing, global business, and their integrated supply chains. CME's membership network accounts for an estimated 82 per cent of total manufacturing production and 90 per cent of Canada's exports.

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Questions?

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