Railway Association of Canada

September 8, 2023

RAC RESPONSE TO CONSULTATION ON CERTAIN BUDGET 2023 MEASURES

Hon. Chrystia Freeland
Department of Finance Canada
90 Elgin Street
Ottawa, Ontario K1A 0G5

Dear Minister Freeland,

The Railway Association of Canada (RAC) is pleased to participate in consultations regarding *Budget 2023 measures to grow the clean economy, close tax loopholes, and deliver tax relief for Canadians*.

Rail is the greenest mode of ground transportation. Despite moving 50% of Canada's exports and $350 billion of goods per year, railways represent only 3.6% of Canadian transportation emissions. Canada's freight railways have reduced their emissions intensity by over 25% since 2005. Through constant innovation, the rail sector is actively supporting Canada's climate objectives.

Just one locomotive can haul a tonne of goods more than 220 kilometres on a single litre of fuel while removing 300 trucks from our congested public highways. Each passenger train replaces dozens of cars, reducing emissions and improving commute times.

Rail is the backbone of Canada's transportation system. In the past decade, railways have invested over $20 billion into the 43,000-kilometre Canadian rail network, moving more goods and more people while generating increased tax revenues for governments.

By investing over 20% of revenues back into the rail network, RAC's Canadian Class 1 members are generating economic benefits for the entire country. A recent Conference Board of Canada study found that rail contributes $17.6 billion to Canada's GDP, generates $7.2 billion in tax revenue, supports 182,000 jobs, and lifts incomes by $10.1 billion.

This is a critical time for Canadian supply chains, manufacturers and producers, and families struggling with the cost of living. Given recent and highly damaging strikes at B.C. ports, practical solutions and supply chain certainty are more important than ever.

The government's recent resurrection of extended interswitching risks chasing unionized Canadian jobs and investment dollars to the U.S. This could lengthen transit times, increase greenhouse gas emissions, and add to the transportation costs of goods and resources that move by rail, fueling inflation. Extended interswitching undermines this consultation's stated objectives and should be immediately abandoned.

Canada's railways urge the federal government to develop a policy and regulatory framework that incentivizes private investments and supply chain fluidity over congestion. The below proposals will ensure that RAC members can continue to support the government's key objectives of building a cleaner Canadian economy and creating new opportunities for Canadian workers.

Sincerely,

Marc Brazeau
President and Chief Executive Officer
Railway Association of Canada

SUMMARY OF RECOMMENDATIONS

1. Abandon extended interswitching and planned anti-replacement workers legislation
2. Incentivize rail investments through accelerated (or 100% immediate) depreciation, a tax credit (like the 45G credit in the U.S.) to support shortline railway infrastructure, and other tax measures
3. Ensure the rail sector has access to clean technology investment tax credits
4. Develop policies that enable modal shift to rail
5. Confront the growing administrative burden of the tax system
6. Modify share buyback proposal to match the lower U.S. tax rate, avoid double taxation, and broaden exemption provisions for repurchase of shares issued for corporate financing purposes (e.g., M&A)
7. Delay EIFEL measures and/or exempt the rail sector to reflect its unique circumstance (e.g., the requirement for significant investment in capital and maintenance programs to enhance safety of privately funded infrastructure)

Railway Association of Canada

Measures to Grow Canada's Clean Economy

RAC members are driving a cleaner Canadian economy and are at the forefront of green innovation. Railways are always working to build on their already impressive record of emissions reductions, including by piloting the use of clean hydrogen locomotives, battery locomotives, and 100% biofuel.

A recent study by Delphi Group and Pollution Probe (supported by Transport Canada and RAC), highlights these projects and explores the feasibility of scaling up these (and other) technologies.

The federal government can play an elevated role in supporting clean technology scaling. Investments related to the production, distribution, storage, and use of hydrogen and other clean technologies should be eligible under the Clean Hydrogen Investment Tax Credit, the Tax Credit for Clean Technologies, or some other taxation vehicle.

As Canada enhances its capabilities in hydrogen and other zero-emission technology manufacturing, railways agree that support for production facilities is essential. But eligibility of related tax credits and supports should be broad and inclusive, with the objective of developing the entire ecosystem (up- and down-stream). Investment support for downstream users, including railways, will help ensure a growing customer base for Canada's hydrogen, biofuel, and zero-emission technology manufacturers.

The RAC recommends that the Department of Finance regularly consult the RAC and its members in its reviews of new technologies that may be eligible for accelerated or immediate depreciation, reduced income tax rates, or tax credits. As technology evolves and advances, the commercially viable clean technologies with application in the rail industry must be included and supported. This will enable the rail sector to further drive the decarbonization of Canada's transportation system.

An investment in rail is an investment in the green economy. The federal government should support investment in the rail industry through tax policies and accelerated (or 100% immediate) depreciation measures. Investments in rail provide immediate emissions reductions through modal shift and significant benefits to Canadian supply chains and should therefore be eligible for 100% immediate depreciation. This approach would complement the National Trade Corridors Fund to quicken the pace of investment in supply chains to help sustainably move more Canadian goods to international and domestic markets.

By providing accelerated capital cost allowance for investments in all forms of cleaner energy locomotives and related equipment, reductions in greenhouse gas emissions will be achieved. These locomotives and equipment include hydrogen locomotives, battery-powered locomotives, catenary systems, tiered locomotives, use of low-carbon fuels as well as liquified natural gas and compressed natural gas, and the various types of equipment that are used at yards, terminals, and ports.

Locomotives are long-lived assets often in service for several decades. As such, it does not make commercial sense for fleet turnover to occur as rapidly or swiftly as it may in other industries. Railways already invest over 20% of their revenues into rail assets each year. To quicken the adoption of clean, low- and zero-emission technologies, federal government support through accelerated (or 100% immediate) capital cost allowance and other supportive tax policies is essential.

The federal government should lead the way in incentivizing modal shift to rail. Shifting just 10% of freight from trucks to rail would reduce greenhouse gas emissions by approximately four megatonnes of carbon dioxide equivalent – enough to take more than one million cars off the road every year.

Shortline railways provide critical first-mile, last-mile services that connect customers to Class 1 railways and global markets. Shortlines face many of the same challenges as larger railways but they have fewer financial and technical resources. They compete directly with trucks on publicly funded highways for traffic while operating lower density lines than their Class 1 counterparts.

Shortlines need stronger government support to remain a viable alternative to trucking. Greater shortline infrastructure would contribute to regional economic development, improve supply chain fluidity, lower costs for businesses, and enhance safety while lowering emissions and reducing the strain on public infrastructure. The federal government should a) look to the U.S. model, where the federal government recognizes the unique circumstances and critical role of shortline railways and provides a permanent 45G tax credit to support shortline infrastructure, or b) create a dedicated, multi-year capital funding program to support shortline infrastructure investments similar to other jurisdictions (U.S., Québec).

Passenger railways connect communities and provide unique tourism experiences that showcase Canada. The federal government should leverage the tax system and boost capital investments to increase support for passenger railways. Dedicated tracks are essential for growing both passenger and freight capacity. The federal government should augment its support for passenger rail to bolster their economic and sustainability impacts and allow for recovery from drastic pandemic ridership shocks.

Measures to Deliver Tax Relief for Canadian Workers and Businesses

While the RAC does not have specific comments on the proposed measures under this section at this time, it should be noted that extended regulated interswitching will do the exact opposite of providing relief to workers and businesses. In fact, it will introduce inefficiencies into supply chains and chase unionized jobs and investment to the United States. More details can be found in the RAC's submission to the House of Commons Standing Committee on Finance.

Canada's railways would also like to register significant concern regarding proposed anti-replacement workers legislation. This policy could cause severe disruptions to essential supply chains in the event of a labour dispute. Other layering on of costly regulations further jeopardize stated government goals.

Tax Improvements and Other Tax Measures

Accelerated (or 100% immediate) tax depreciation is one of the best tried and tested options for the federal government to boost private sector investment. The current class rates and depreciation rules are not supportive of investment in the green rail industry and should be improved to support the critical investments that railways make to enhance safety, reduce emissions, and benefit Canadian supply chains and the broader economy. The table below, from RAC's paper *Railways, Taxation, and the COVID-19 Recovery,* highlights the differences between the Canadian and U.S. tax regimes as they relate to railway capital cost allowance; and the tax treatment of railways versus select capital intensive industries in Canada.

Tax Treatment of Canadian Railways vs U.S. Railways and Select Canadian Industries

	Canadian Railways		U.S. Railways		Canadian Trucking Industry		Cdn Manufacturing & Processing (M&P)	
	Class Rates	CCA Claimed	Class Rates	CCA Claimed	Class Rates	CCA Claimed	Class Rates	CCA Claimed
	Track Infrastructure		Track Infrastructure		N/A*		M&P Plant	
Year 1	10%	15%	100%	100%			10%	15%
Total by Year 4		38%		100%				38%
	Rail Yard Facility (Building)		Rail Yard Facility (Building)		N/A		N/A	
Year 1	4%	6%	100%	100%				
Total by Year 4		17%		100%				
	Railcars		Railcars		Trailers		M&P Kiln/tank/vat	
Year 1	15%	23%	100%	100%	30%	45%	100%	100%
Total by Year 4		52%		100%		81%		100%
	Locomotives		Locomotives		Hauling trucks		M&P Equipment	
Year 1	30%	45%	100%	100%	40%	60%	100%	100%
Total by Year 4		81%		100%		91%		100%

*As infrastructure used to move freight (inter-provincial roads) for the trucking industry is already fully funded by the Government.

Considering that Canadian supply chains require massive investments to sustain growth in our economy, the measures we propose here should apply to all supply chain participants which make investments to maintain or expand capacity. This would promote Canada's global competitiveness in support of economic growth.

Suggested Changes to Certain Proposed Measures

As a general comment, the Canadian tax system is becoming more burdensome, and companies are increasingly required to dedicate greater resources to tax administration at the expense of productive activities to grow Canada's clean economy. The government should confront the growing administrative burden of the tax system.

The United States has a lower share buyback tax rate than the proposed federal tax rate. The federal government should, at the very least, reduce its proposed rate to 1% to match the U.S. rate. It is also necessary that an exception or offset between Canada and the U.S. be created to avoid any double taxation of Canadian companies, since Canadian companies that have operations and generate profits in the U.S. may also be captured under the new U.S. share buyback tax. Further, the government should exempt repurchase of shares that are associated with share financing (e.g., funding used for capital acquisitions, M&A, etc.), which is an alternative to debt financing. Such is different from the stated intent of this tax, which is to encourage re-investment and tax the wealthiest individuals.

The RAC is also concerned that, through its fixed ratio, the Excessive Interest and Financing Expenses Limitations (EIFEL) regime could discourage investment and limit the rail industry's ability to help Canada meet its ambitious emissions reduction targets. The EIFEL measures must be delayed until Canada's investment and productivity levels improve to rival those of its direct competitors, notably the United States.

Amid high inflation, extreme weather events, the recovery from B.C. port strikes, competitive U.S. policy actions, and a clear need for significant supply chain investment, now is no time to introduce measures that limit capital investment. The EIFEL measures could limit railways' ability to finance investments, capping the amount of interest expenses they can use in each tax year to reduce their taxable income. Railways make significant capital investments each year to strengthen the extensive cross-Canada rail network, enhance safety, and green the fleet of 60,000 railcars and nearly 4,000 locomotives.

Canada's investment and productivity performance has long lagged the United States, and the EIFEL regime may constrain the ability for Canada to catch up with its southern neighbour. The government should be supporting capacity-enhancing investments in rail, not imposing additional regulations or limitations. Since the final details of the EIFEL rules are still not confirmed through legislation, and compliance will require changes to business plans, Canadian businesses should be provided with adequate lead time to prepare. Implementation should be delayed as recommended by the Tax Executives Institute (TEI) to taxation years beginning on or after December 31, 2024.

If the government proceeds with the measures, the government must exempt the rail sector from a fixed ratio under the EIFEL regime. The RAC requests that an exemption be granted to the rail sector given its unique circumstance as a mode of transportation operating on private infrastructure, as opposed to public infrastructure.

This unique situation necessitates a higher fixed ratio, as the EIFEL regime could produce the unintended consequence of constraining railway investment in network enhancement, capacity expansion, and climate resilience, among others.

About RAC

The Railway Association of Canada (RAC) represents close to 60 freight and passenger railway companies. The RAC also counts a growing number of industrial railways and railway supply companies in its associate membership. As part of the fifth largest rail network in the world, RAC members are the backbone of Canada's transportation system.