

CTA BRIEFING NOTE



June 2016

Application of Federal Excise Tax to Diesel

Economic and Financial Background

The trucking industry employs over 450,000 Canadians – two thirds of which are employed as truck drivers. Over 70% of Canada-US trade, measured by value, moves by truck. All products on Canadian stores' shelves were on a truck at least once. It goes without saying the Canadian economy moves by truck. The trucking industry is also highly competitive. The operating ratio (OR) – which is an expression of operating expenses as a percentage of revenue in which a lower value is better – of Canadian Class 1 railways are in 0.63-0.65 range. For most trucking companies an acceptable OR would be 0.95. Trucking is a high revenue, low margin business where the difference between profit and loss on a load can be measured in dollars, not hundreds of dollars. The elimination of \$800-\$1000 in federal excise tax refunds per tractor-trailer per year when considered across an entire fleet is a significant sum of money for many trucking operations. It could even total the difference between hiring additional employees or not. In Canada, that could translate into thousands of jobs across the country.

Issue: Federal Excise Tax Exemptions

The 2016 federal budget's Notice of Ways and Means Motion has made two fundamental changes to the application of the FET to diesel:

- Heating oil is now defined under the Excise Tax Act. It now means any fuel oil that is consumed exclusively for providing heat to a home, building, or similar structure and that is not consumed for generating heat in an industrial process, including any commercial process that involves removing moisture from a good.
- Diesel fuel is still exempt from FET if it is purchased for use in the generation of electricity. However, the exclusion from this exemption has been changed to "... unless the diesel fuel is used in or by a vehicle, including a conveyance attached to the vehicle, of any more of transportation."

These amendments will come into effect on July 1, 2016. It is intended that these changes would eliminate the FET exemption for diesel fuel consumed by the temperature control units ("TCU") used to transport food and other goods, the auxiliary power units ("APU")/ in-cab heaters and the power takeoff units ("PTO") of the trucks. The Canadian Trucking Alliance is opposed to eliminating FET exemptions on these technologies.

Technologies Impacted & What Duties They Perform

- TCU. A vehicle designed to carry perishable freight at specific temperatures. These configurations could be heated (protect from freeze service) or cooled. Some examples of freight moved by these vehicles include food products, pharmaceuticals, cosmetics, adhesives, chemicals; and electronics.
- PTO. Equipment added to a licensed motor vehicle to perform loading/offloading functions. Technology examples include: cement mixers, aerial buckets, lifts, cranes, refrigeration units, power vacuums, pumps and blowers.

- APU/In cab heater. Technology that provides hotel services for long-haul truck drivers who use tractors with sleeping quarters. This technology removes about 9 to 20 metric tons of carbon dioxide and particulate matter emissions. In-cab heaters also reduce carbon.

Eliminating FET Exemption Taxes Food & Housing

The excise taxes are generally intended to be imposed on luxury products such as jewelry, tobacco and alcohol. Excise taxes are not meant to increase the cost of basic provisions such as food, pharmaceuticals and shelter. Even when FET was imposed on diesel in 1982, the intention was for it to apply to transportation fuel only. Eliminating FET refunds on temperature controlled and PTO units will increase the transportation cost of the food and other important products Canadian families rely on. Furthermore, the budget measure unfairly targets transportation companies in the food, pharmaceutical and consumer goods supply chain. On the other hand, entities providing building storage services for food products, pharmaceuticals or consumer goods will not be subject to the FET on diesel fuel. APUs and In-cab heaters provide hotel services for over 200,000 Canadians. The policy behind all consumption taxes is to not impose tax on shelter. This is evidenced by the fact these taxes do not apply to residential rent, and to residential heating oil or electricity. For many truck drivers who drive across the continent, their truck cabin is their shelter and home. The Proposed Amendments will result in diesel fuel used in APUs being subjected to the FET. This is wrong.

Using a Policy Sledge Hammer Instead of a Scalpel

CTA understands that this FET budget measure was introduced to address a sector that was stretching the intent of the FET exemption. This sectoral attempt made it difficult for Canada Revenue Agency to also audit claims. The technologies raised by CTA – PTO, TCU and APU/in-cab heaters – are not only consistent with the FET exemption, they are easily auditable and have separate fuel tanks and meters. If there are problems with a particular sector and technologies, Finance should identify them and impose sanctions directly on those sectors, rather than lump in trucking under a blanket policy.

CTA Position

The Department of Finance recognizes the elimination of the FET exemption is not a significant revenue matter. For the trucking industry it is a significant revenue matter. CTA also believes our industry's technologies and claims are consistent with the historic practice of FET claims. As such, the Department of Finance should specifically create a FET exemption for diesel fuel used in TCUs, PTOs and APUs in the ETA. If a specific exemption is not made, then the Canada Revenue Agency should adopt a written policy that it would interpret the ETA to exclude the application of FET to diesel used in TCUs, PTOs, and APUs. CTA would like to meet with the Department of Finance in July to develop this written policy.

June 3, 2016

Mr. Stephen Laskowski
Senior Vice President
Canadian Trucking Alliance
555 Dixon Road
Toronto ON M9W 1H8

Re: Application of the federal excise tax to diesel fuel – heating oil and diesel used to produce electricity

Dear Mr. Laskowski:

You have asked us to provide the Canadian Trucking Alliance ("CTA") with arguments supporting its position that the proposed amendments to the application of the federal excise tax ("FET") under the *Excise Tax Act* (the "ETA") to diesel fuel in the federal budget 2016 will negatively affect businesses, especially the trucking industry in Canada.

We have divided our arguments into two main sections. In the first section, we provide you with arguments supporting that the amendments will hurt Canadian businesses and the Canadian economy. Under the second section, we provide you with arguments more specific to the trucking industry. Our position is that both arguments should be presented to the Department of Finance in order for them to be effective.

I. BACKGROUND

The federal budget 2016's Notice of Ways and Means Motion has made two fundamental changes to the application of the FET to diesel (the "Proposed Amendments"):

- Heating oil is now defined under the ETA. Heating oil is defined to mean "any fuel oil that is consumed exclusively for providing heat to a home, building, or similar structure and that is not consumed for generating heat in an industrial process, including any commercial process that involves removing moisture from a good." [emphasis added]
- Diesel fuel is still exempt from FET if it is purchased for "use in the generation of electricity." However, the exclusion from this exemption has been changed to "... unless the diesel fuel is used in or by a vehicle, including a conveyance attached to the vehicle, of any mode of transportation." [emphasis added]

These amendments will come into effect on July 1, 2016. It is intended that these changes would eliminate the FET exemption for diesel fuel consumed by the temperature control units ("TCU") used to transport food and other goods, the auxiliary power units ("APU") and the power take-off units ("PTO") of the trucks.

The reasons provided by the Department of Finance for the Proposed Amendments is that "court decisions have expanded these relief provisions (i.e., relief for heating oil and diesel used to produce electricity). To ensure that the scope of these relief provisions remains targeted, Budget 2016 proposes two measures to clarify instances in which relief is provided."

The Department of Finance has indicated that any tax relief for heating oil is intended to be limited to "heating in respect of buildings." The purpose of the changes to the exemption for diesel fuel used to produce electricity is to simplify the legislation so that no relief applies to fuel "used to produce electricity in any vehicle" as opposed to fuel used to produce electricity "primarily (i.e., over 50%) in the operation of the vehicle."

II. EXECUTIVE SUMMARY OF THE MAIN ARGUMENTS RELATED TO TRUCKING INDUSTRY

The Proposed Amendments will make Canada less competitive by increasing the tax on business inputs. By increasing the tax on business inputs, including the diesel used in the TCUs, APUs and PTOs, businesses will try to pass on the cost to the consumer. This will result in the increase in the price of many products for consumers, including food products and pharmaceuticals.

The Department of Finance has chosen the worst time to introduce the Proposed Amendments. During the last few years, the cost of groceries has steadily been increasing in Canada due to a number of factors including in the fall in the Canadian dollar, drought in some parts of the country and use of fuel products for making biofuels. People living in poverty spend 50 percent of their income, and the people living below the poverty line spend as much as 75 percent of their income on food.¹ The Proposed Amendment will further exasperate the situation for low-income families.

In cold Canadian winters or hot Canadian summers, the APUs are absolute necessities for the drivers as they control the temperature in the cabin during the legislated rest time. The APUs significantly reduce fuel consumption of the vehicles and reduce greenhouse gas emissions. For many truck drivers, their cabin is their shelter. The Proposed Amendments will result in the diesel fuel used in APUs to be subject to the FET. Thus, they will increase the cost of shelter for these truck drivers.

The Proposed Amendments unfairly target transportation companies in the food, pharmaceutical and consumer goods supply chain. Entities providing building storage services for food products, pharmaceuticals or consumer goods will not be subject to the FET on diesel fuel. The only entities that are required to pay the additional FET on diesel fuel for heating or refrigeration in the supply chain of food products, pharmaceuticals and consumer goods would be the transportation companies. The Department of Finance has provided no valid reason for this inequitable treatment. This is not consistent with the principle of fairness in tax policy.

There is little support for the Proposed Amendments on the basis that the courts have expanded the scope of the exemption for heating oil to beyond what was initially intended. The FET was imposed on diesel in 1979. In 1979, the Minister of Finance's speech and the exemptions in the legislation confirm that the intention was for the FET to apply to fuel used in transportation only. The Proposed Amendments significantly narrow the scope of the exemption for heating oil and electricity from what was initially intended in 1979.

III. ARGUMENTS AGAINST THE PROPOSED AMENDMENTS

A. The Proposed Amendments will work to the detriment of competitiveness and the consumer

(i) The Proposed Amendments will make Canada less competitive

The Proposed Amendments will result in FET applying to various business uses of diesel including diesel used in TCUs and PTOs for the transportation and loading of food and other products in Canada, diesel fuel used in the APUs of trucks that provide heat and electricity to truck drivers, diesel used for mining exploration and exploitation, diesel used to produce heat in oil production and processing, and other similar business inputs.

¹ Oxfam Canada - http://www.oxfam.ca/grow/learn/why_food_prices_are_rising

The changes to the ETA and imposing FET on diesel used in industrial processes as well as narrowing the exemption for diesel used for electricity production will directly lead to a significant hidden cost of doing business in Canada and constrain the ability of Canadian firms and industries to compete effectively.² For example, the trucking industry will see the cost of diesel used in TCUs used to transport food and certain consumer goods increase. This would mean that the industry will have less to invest in purchasing new and more energy efficient vehicles and equipment and create new employment opportunities. Accordingly, the Proposed Amendments will make Canada less competitive.

(ii) The Proposed Amendments will hurt the Canadian consumer

The Proposed Amendments will work to the detriment of consumers.³ By increasing the tax on business inputs and increasing the cost of doing business in Canada, the same businesses would ultimately pass on the cost to consumers. Wholesale and retail markups are applied to prices that reflect the FET on diesel fuel used as an input. Accordingly, it is expected that the Proposed Amendments will increase the cost of consumer goods, from food to electronics and petroleum products in Canada.

B. Even if the Department of Finance intends to impose FET on diesel, it should not apply to FET on diesel used in TCUs and PTOs for the transportation and loading of food, pharmaceuticals and goods and in APUs for shelter heating

Even if the government intends to implement the Proposed Amendments, the government should not apply the FET to diesel fuel used in TCUs and PTOs used for the transportation and loading of food, pharmaceuticals and goods and in the APUs of trucks.

The excise taxes are generally intended to be imposed on luxury products such as jewelry, tobacco and alcohol. The excise taxes are not meant to increase the cost of basic provisions such as food and shelter. Even when FET was imposed on diesel in 1979, the intention was for it to apply to transportation fuel only.

(i) Effect of Imposing FET on diesel used in TCUs and PTOs

The TCUs are used to transport food products and pharmaceuticals across the country. PTOs are used to load and unload these products. Food items and pharmaceuticals are required to be maintained in an environment with a controlled temperature for transportation, or the food products or the medication will spoil. The Proposed Amendments will significantly increase the cost of diesel fuel used in TCUs for the transportation of food products and pharmaceuticals as well as the cost of diesel fuel used in PTOs for loading and unloading these products in Canada.

Effect on food prices for consumer

Transportation companies, including the trucking industry, will either absorb the cost of the additional FET at the detriment of investing in new technologies and employment or will pass on the cost to the shippers. The shippers will apply markups to prices of food, pharmaceuticals or other goods that reflect the FET on diesel fuel used for transporting the food to the detriment of the consumer, and the Canadian consumer will eventually be paying for the increased cost of transportation by paying more for food, pharmaceuticals or other temperature-sensitive consumer goods.

The Department of Finance has historically been very sensitive to the effect of sales and excise taxes on food products. Even when the GST was introduced in 1991, the ETA ensured that the cost of food products at grocery

² The White Paper Tax Reform 1987, June 18, 1987, Department of Finance, pages 14 - 15.

³ The White Paper Tax Reform 1987, June 18, 1987, Department of Finance, page 15.

stores was not increased as the result of the new tax, and most types of food products purchased were considered to be zero-rated supplies. This was to ensure that the introduction of a very broad-based sales tax would not result in an increase in the cost of food. However, the Proposed Amendments have not considered the effect of the increase in the cost of FET on the food products.

Moreover, the Department of Finance has chosen the worst time to introduce the Proposed Amendments. During the last few years, the cost of groceries has steadily been increasing in Canada due to a number of factors including in the fall in the Canadian dollar, drought in some parts of the country and use of fuel products for making biofuels.⁴ People living in poverty spend 50 percent of their income, and the people living below the poverty line spend as much as 75 percent of their income on food.⁵ The Proposed Amendment will further exasperate the situation for low-income families.

Effect on food prices for consumer

The Department of Finance has also been very sensitive to the effect of sales taxes on pharmaceuticals. Under the ETA, the GST does not apply to prescription drugs. Provincial sales taxes do not apply to prescription drugs either. These measures ensure that the sales taxes do not increase the cost of pharmaceuticals. However, the Proposed Amendments have not considered the effect of the increase in the cost of FET on pharmaceuticals.

Effect on fairness

A tax system should treat businesses in similar circumstances equitably. Where a tax system does not treat businesses in similar circumstances equitably, "there should be valid reasons for different treatment."⁶ However, the Proposed Amendments unfairly target transportation companies in the food, pharmaceutical and consumer good supply chain. Entities providing building storage services for food products, pharmaceuticals or consumer goods will not be subject to the FET on diesel fuel. This is because these businesses will use natural gas, electricity or diesel fuel for heating or refrigeration. Natural gas and electricity do not attract FET, and the diesel fuel used as heating oil in a building will continue to be subject to the exemption (unless the Canada Revenue Agency would interpret such use as an industrial process). Thus, the only entities that are required to pay the additional FET on diesel fuel for heating or refrigeration in the supply chain of food products, pharmaceuticals and consumer goods would be the transportation companies. The Proposed Amendments unfairly target the transportation companies in the food and consumer good supply chain, and the Department of Finance has provided no valid reason for this inequitable treatment. This is not consistent with the principle of fairness in tax policy.

Effect on simplicity of tax administration

One reason provided for the Proposed Amendments is to simplify the administration of the FET. However, imposing FET on diesel fuel used in TCUs and PTOs will not greatly simplify the administration of the tax. Most TCUs and many PTOs have separate fuel tanks and are unique cost centres. As such, the transportation companies have a separate record of the TCU and PTO fuel and use that information for claiming refunds. The transportation companies will continue to keep track of their fuel consumption separately for business reasons even after the Proposed Amendments come into force.

For transportation companies using electrical TCUs, the generator producing the electricity for the generators also have their own fuel tanks with their own cost centres. The transportation companies owning these types of

⁴ Oxfam Canada - http://www.oxfam.ca/grow/learn/why_food_prices_are_rising

⁵ Oxfam Canada - http://www.oxfam.ca/grow/learn/why_food_prices_are_rising

⁶ The White Paper Tax Reform 1987, June 18, 1987, Department of Finance, page 3.

equipment will continue to keep track of their fuel consumption for these generators separately for business reasons. Therefore, the Proposed Amendments will not really impact the simplification of the tax system but instead will only unfairly eliminate tax relief in its entirety.

There may be some types of PTOs that do not have their own separate fuel tanks. These PTOs may use the diesel from the general tank of the truck. These PTOs have their own fuel consumption rates, and the truck drivers keep track of their use. These figures have been used in the past for claiming refunds. The transportation companies will continue to keep track of the diesel used in the PTO even after the Proposed Amendments come into force. Therefore, the Proposed Amendments will not contribute to the simplification of the tax system in respect of the PTOs.

(ii) Effect of imposing FET on diesel used in APUs

The Proposed Amendments will increase the cost of shelter

Trucks generally have APUs that produce heat and electricity for the cabins of the trucks while in legislated rest time. In cold Canadian winters or hot Canadian summers, the APUs are absolute necessities for the drivers. The APUs significantly reduce fuel consumption of the vehicles and reduce greenhouse gas emissions. Without the APUs, the truck driver must use the main engine of the truck to produce heat and electricity at rest spots, which significantly use more diesel and emit more greenhouse gases than the APUs.

The policy behind all consumption taxes, including the FET, GST and also the provincial sales tax is to not impose tax on shelter. This is evidenced by the fact that these taxes do not apply to residential rent, and FET and many provincial sales taxes do not apply to residential heating oil or electricity. For many truck drivers who drive across the continent, their truck cabin is their shelter and home. The Proposed Amendments will result in the diesel fuel used in APUs to be subject to the FET. Imposing tax on the cost of shelter is generally contrary to the long-standing policy of the Department of Finance. Accordingly, the Proposed Amendments will increase the cost of shelter for these truck drivers.

Effect on simplicity of tax administration

Imposing FET on diesel fuel used in the APUs will not simplify the administration of the tax. APUs have their own fuel consumption rates, and the truck drivers are required under the transportation laws to keep track of their rest time (i.e., when the APU is operating). These figures have been used in the past for claiming refunds. The transportation companies will continue to keep track of their downtime for regulatory reasons even after the Proposed Amendments come into force. Therefore, the Proposed Amendments will only impact on simplification of the tax system for the purpose of the APUs by eliminating tax relief in its entirety.

(iii) The Proposed Amendments will expand the application of FET beyond what was intended in 1979

There is little support for the Proposed Amendments on the basis that the courts have expanded the scope of the exemption for heating oil to beyond what was initially intended. The FET was imposed on diesel in 1979. In 1979, one of the main policies was to constrain/limit the demand for oil by imposing a tax on "gasoline, diesel and other transportation fuels"⁷. Minister Crosbie [as he then was] specifically indicated that the "tax will not apply to heating oil in the home or elsewhere ... The tax will apply to all users of transportation fuels and will replace the current tax of 7

⁷ House of Commons Debates for December 11, 1979 and Imperial oil v R, 2007 CF 464.

cents a gallons on gasoline which applied only to non-commercial users⁸." From the Minister's speech, it is apparent that the intention was for the FET to apply to fuel used in transportation only.

To minimize the impact of imposing FET on diesel fuel on taxpayers and ensure that the FET would only apply to transportation fuels, heating fuel was given a tax-exempt status. In addition, diesel used to produce electricity was also exempt from the FET, unless the diesel was used primarily in the operation of the vehicle. These measures were meant to ensure that FET would only apply to diesel used for transportation purposes.

By limiting the definition of heating oil to only the diesel fuel that is used in homes, buildings and similar structures and that is not consumed for generating heat in an industrial process, the Proposed Amendments significantly narrow the scope of the exemption for heating oil from what was initially intended in 1979. Therefore, there is little support for the Proposed Amendments on the basis that the courts have expanded the scope of the exemption for heating oil to beyond what was intended in 1979.

(iv) Other jurisdictions

The United States of America (the "US") is Canada's number one trading partner and competitor. The US provides a refund of the US equivalent of the excise tax on diesel fuel used in TCUs since that country recognizes the tax will increase the cost of food, as well as discourage investments in new technology and employment.

IV. REQUESTS

The CTA should make the following requests:

- The Department of Finance should specifically create a FET exemption for diesel fuel used in TCUs, PTOs and APUs in the ETA.
- If the Department of Finance does not make a specific exemption from FET for diesel fuel used in TCUs, PTOs and APUs in the ETA, the Canada Revenue Agency should adopt a written policy that it would interpret the ETA to exclude the application of FET to diesel used in TCUs, PTOs, and APUs. Given the ambiguity in the wording of the ETA, this is not the preferred approach as it would still put all taxpayers at risk of an assessment.

If you have any questions, please contact me at 403-267-1702.

Yours truly,



R. Jason Riche
Tax

⁸ House of Commons Debates for December 11, 1979 and Imperial oil v R, 2007 CF 464.



Application of FET to Diesel Fuel Used to Produce Electricity

Canadian Trucking Alliance
Department of Finance Office
June 6, 2016

Canadian Trucking Alliance

- Canadian Trucking Alliance (CTA) is a federation of the country's provincial trucking associations
- CTA represents a broad cross section of the trucking industry – about 4500 carriers and industry suppliers
- A large majority of provincial carrier members are family-run small and medium sized operations
- CTA Board is made up of carriers from every province and all sectors.

Trucking & The Economy

- Trucking is the dominant mode of transport in both domestic and international lanes. The same commodities dominate both exports and imports: automotive products, machinery and electrical equipment, other manufactured products and agricultural products. In 2015 trucks carried 66.5 percent of U.S.-NAFTA freight and continues to be the most heavily utilized mode for moving goods to and from both U.S.-NAFTA partners. Trucks accounted for \$US28.4 billion of the \$US44.6 billion of imports (63.7 percent) and \$US26.4 billion of the \$US37.9 billion of exports (69.7 percent).
- The Canadian agriculture and agri-food system (AAFS) is a complex and integrated supply chain that includes input and service suppliers, primary producers, food and beverage processors, food retailers and wholesalers, and foodservice providers. Trucking services are a key part of this supply chain. Canadian processed food and beverage products are exported to some 190 countries with a significant proportion exported to a few countries. In 2014, 89% of the total went to six major markets with the United States (71%) being the largest. Trucking dominates this market place in terms of shipments – with 100% of the retail marketplace moving by truck.

The Competitive Business of Trucking

- Operating ratio (OR) is defined as a company's operating expenses as a percentage of revenue – commonly used for industries that require a large percentage of revenues to maintain operations. The smaller OR, the more profitable the company. Large class 1 railways perform in the 0.63-0.68 range. In contrast, 0.95 or lower is considered healthy for trucking carriers. Trucking is a highly competitive business with extremely tight margins.
- Nearly 87% of productivity gains in for-hire trucking have been passed along to the industry's customers in the form of lower prices (Conference Board of Canada, 2013)
- Recently, fuel costs have declined precipitously due to oversupply in crude oil. The for-hire trucking industry, though, passed on much of these savings through reductions in fuel surcharges. It's estimated that fuel charges fell recently to under 13% of base freight costs, down from 22% in 2014. Meanwhile, total freight costs (including fuel surcharges) have declined trend since early 2015 (CPCS, 2016).
- There is no reason to expect changes in competitiveness. Despite ongoing consolidation the industry has relatively low barriers to entry. As a result, any time there appears to be significant increases in industry rates.(Conference Board of Canada, 2013).

FET Policy Impact on Trucking Technology

- **Temperature Controlled Unit (TCU).** A vehicle designed to carry perishable freight at specific temperatures. These configurations could be heated (protect from freeze service) or cooled. Some examples of freight moved by these vehicles include food products, pharmaceuticals, cosmetics, adhesives, chemicals ; and electronics.
- **Power-take Off Unit (PTO).** Equipment added to a licensed motor vehicle to perform loading/offloading functions. Technology examples include: cement mixers, aerial buckets, lifts, cranes, refrigeration units, power vacuums, pumps; and, blowers. Sectors would include bulk trailers moving agriculture/food products/cement/oil/gas.
- **Auxiliary Power Unit (APU)/In cab heater.** Technology that provides hotel services for long truck drivers who utilize tractors with sleeping quarters. A typical long-haul combination truck can idle between 1600 and 2400 hours per year, which would use about 3400 and 5300 litres of fuel, respectively. Depending on area and type of operation idling could burn up to 9000 litres. Saving fuel annually through idle reduction by installing an APU would remove about 9 to 20 metric tons of carbon dioxide, reduce nitrogen oxide and particulate matter emissions. In-cab heaters would save slightly based on there are no cooling benefits.

Budget Amendment to FET

The 2016 federal budget's Notice of Ways and Means Motion (**NWMM**) has made two fundamental changes to the application of the FET to diesel (the "Proposed Amendments"):

- Heating oil is now defined under the ETA. Heating oil is defined to mean "any fuel oil that is consumed exclusively for providing heat to a home, building, or similar structure and that is not consumed for generating heat in an industrial process, including any commercial process that involves removing moisture from a good." (emphasis added)
- Diesel fuel is still exempt from FET if it is purchased for "use in the generation of electricity." However, the exclusion from this exemption has been changed to "... unless the diesel fuel is used in or by a vehicle, including a conveyance attached to the vehicle, of any more of transportation." (emphasis added)

These amendments will come into effect on July 1, 2016. It is intended that these changes would eliminate the FET exemption for diesel fuel consumed by the temperature control units ("TCU") used to transport food and other goods, the auxiliary power units ("APU")/ in-cab heaters and the power takeoff units ("PTO") of the trucks.

Policy Rationale

Department of Finance

- The reason for the Proposed Amendments, according to the Dept. of Finance is “court decisions have expanded these relief provisions (i.e., relief for heating oil and diesel used to produce electricity). To ensure that the scope of these relief provisions remains targeted, Budget 2016 proposes two measures to clarify instances in which relief is provided.”
- The Department of Finance has indicated that any tax relief for heating oil is intended to be limited to “heating in respect of buildings.” The purpose of the changes to the exemption for diesel fuel used to produce electricity is to simplify the legislation so that no relief applies to fuel “used to produce electricity in any vehicle” as opposed to fuel used to produce electricity “primarily (i.e., over 50%) in the operation of the vehicle.”

CTA Response to Ways & Means Proposal

- The Department of Finance should specifically create a FET exemption for diesel fuel used in TCUs, PTOs and APUs in the Excise Tax Act (ETA).
- If the Department of Finance does not make a specific exemption from FET for diesel fuel used in TCUs, PTOs and APUs in the ETA, the Canada Revenue Agency should adopt a written policy that it would interpret the ETA to exclude the application of FET to diesel used in TCUs, PTOs, and APUs. Given the ambiguity in the wording of the ETA, this is not the preferred approach as it would still put all taxpayers at risk of an assessment.

Rationale for CTA's Proposal

Improper Application of Tax

- The excise taxes are generally intended to be imposed on luxury products such as jewelry, tobacco and alcohol. Excise taxes are not meant to increase the cost of basic provisions such as food and shelter. Even when FET was imposed on diesel in 1982, the intention was for it to apply to transportation fuel only.
- Even when the GST was introduced in 1991, the ETA ensured the cost of food products at grocery stores did not increase as a result of the new tax, and most food purchases were considered to be zero-rated supplies.
- By limiting the definition of heating oil to only diesel fuel used in homes, buildings and similar structures not consumed for generating heat in an industrial process, the Proposed Amendments significantly narrow the scope of the exemption from what was initially intended in 1979. Therefore, there is little support for the Proposed Amendments on the basis that courts have expanded the scope of the exemption for heating oil to beyond what was intended in 1979/1982.

Effect on Fairness

- A tax system should treat businesses in similar circumstances equitably. Where a tax system does not treat businesses in similar circumstances equitably, "there should be valid reasons for different treatment." However, the Proposed Amendments unfairly target transportation companies in the food, pharmaceutical and consumer good supply chain. Entities providing building storage services for food products, pharmaceuticals or consumer goods will not be subject to the FET on diesel fuel. This is because these businesses will use natural gas, electricity or diesel fuel for heating or refrigeration. Natural gas and electricity do not attract FET, and the diesel fuel used as heating oil in a building will continue to be subject to the exemption (unless the Canada Revenue Agency would interpret such use as an industrial process).

Rationale for CTA's Proposal

Technology Understanding

- One reason provided for the Proposed Amendments is to simplify the administration of the FET. However, imposing FET on diesel fuel used in APUs, TCUs and PTOs will not greatly simplify the administration of the tax. Most APUs TCUs and many PTOs have separate fuel tanks and are unique cost centres. As such, the transportation companies have a separate record of the APUs, TCU and PTO fuel and use that information for claiming refunds.

Simplicity of Tax Administration

The transportation companies will continue to keep track of their downtime for regulatory reasons even after the Proposed Amendments come into force. Therefore, the Proposed Amendments will only impact on simplification of the tax system for the purpose of the APUs by eliminating tax relief in its entirety.

Rationale for CTA's Proposal

Less Competitive Canada

- Changes to the ETA and imposing FET on diesel used in industrial processes as well as narrowing the exemption for diesel used for electricity production will lead to a significant hidden costs of doing business and constrain the ability of Canadian firms and industries to compete effectively.
- For example, the cost of diesel used in TCUs used to transport food and certain consumer goods will increase, meaning the trucking industry will have less to invest in new and more energy efficient equipment and creating new employment opportunities. Accordingly, the Proposed Amendments will make Canada less competitive.

Canadian Consumer Hurt

- By increasing the tax on business inputs and increasing the cost of doing business in Canada, the same businesses would ultimately pass on the cost to consumers. Wholesale and retail markups are applied to prices that reflect the FET on diesel fuel used as an input. Accordingly, it is expected that the Proposed Amendments will increase the cost of consumer goods, from food to electronics and petroleum products in Canada.

Rationale for CTA's Proposal

Increase Cost to Shelter

- APU's and In-cab heaters provide hotel services for over 200,000 Canadians.
- The policy behind all consumption taxes, including the FET, GST and the provincial sales tax is to not impose tax on shelter. This is evidenced by the fact these taxes do not apply to residential rent, and FET and many provincial sales taxes do not apply to residential heating oil or electricity. For many truck drivers who drive across the continent, their truck cabin is their shelter and home. The Proposed Amendments will result in diesel fuel used in APUs being subjected to the FET. Imposing tax on the cost of shelter is generally contrary to the long-standing policy of the Dept. of Finance. Accordingly, the Proposed Amendments will increase the cost of shelter for truck drivers.

Living Essentials

- People living below the poverty line spend as much as 75 percent of their income on food.
- The Department of Finance has been very sensitive to the effect of sales taxes on pharmaceuticals. Under the ETA, the GST does not apply to prescription drugs. Provincial sales taxes do not apply to prescription drugs either. These measures ensure that the sales taxes do not increase the cost of pharmaceuticals. However, the Proposed Amendments have not considered the effect of the increase in the cost of FET on pharmaceuticals.

Summary

CTA Position

- The Department of Finance should specifically create a FET exemption for diesel fuel used in TCUs, PTOs and APUs in the ETA.
- If the Department of Finance does not make a specific exemption from FET for diesel fuel used in TCUs, PTOs and APUs in the ETA, the Canada Revenue Agency should adopt a written policy that it would interpret the ETA to exclude the application of FET to diesel used in TCUs, PTOs, and APUs. Given the ambiguity in the wording of the ETA, this is not the preferred approach as it would still put all taxpayers at risk of an assessment.

CTA Policy Rationale

- Inconsistent application of excise tax and historical application.
- Motion will have negative impact on tax fairness.
- Motion will not have desired effect on simplicity of taxation.
- Motion will make Canada less competitive and send wrong environmental message.
- Motion will hurt consumers and 200,000+ truck drivers.