



November 2, 2025

From: Don Drummond
To: Budget Watchers
Re: HOW THE BUDGET COULD DELIVER A COMPETITIVE CORPORATE TAX SYSTEM

Mark Carney has said tomorrow's budget will include measures to give Canada a "highly competitive corporate tax system" though he offered few details.

The Liberal election platform included some scattered tax measures intended to enhance competitiveness, but they alone fall short of making Canada truly competitive. Several C.D. Howe Institute's publications have **advanced** ideas that could make a **greater** impact.

The election platform pledged to:

- Increase the annual limit for the scientific research and development tax credit for small and medium-sized companies.
- Establish a patent box with a preferential tax rate for income derived from certain types of intellectual property.
- Expand tax incentives for critical minerals exploration and extraction.
- Reintroduce a tax incentive for investors in multi-unit residential buildings.
- Introduce a 20-percent artificial intelligence tax credit for small and medium-sized businesses.
- Expand flow-through shares to corporations operating in the AI, quantum computing, biotechnology and advanced manufacturing industries.
- Extend the expiry of the carbon capture, utilization and storage tax credit.
- Continue the six clean-economy tax credits.
- Establish a review of the corporate income tax system.

All positive, but still short of what will be required to bolster productivity and reverse Canada's weak investment in machinery and equipment. Output per hour worked in Canada is now just barely above the OECD average, after once ranking among the top three.

The idea of trading more with Europe is optimistic, given that Canada's productivity now trails Ireland, Norway, Luxembourg, Belgium, Switzerland, Denmark, Austria, the Netherlands, Germany, Sweden, France, Finland, the United Kingdom and Italy.

In the second quarter of 2025, real **investment** in machinery and equipment reached \$12,800 per worker at an annual rate in the United States compared with only \$4,100 in Canada. Without stronger investment, Canada will remain dependent on a weaker dollar and lower wages to compete, both of which depress real incomes.

Four quick steps to give productivity and investment the jolt they need include:

- Cutting the general corporate income tax rate from 15 to 13 percent.
- Introducing a broad-based investment tax credit.
- Reforming the SR&ED tax credit so firms receive it shortly after outlays are made and bringing up the rate for large corporations to better align with that for small firms.
- Introducing targeted incentives to support seed- and early-stage venture capital.

Proceeding with the corporate income tax review promised in the Liberal's election platform could be highly valuable, especially if it focuses on lowering taxes on reinvested profits and modernizing small business tax incentives to better promote scale and growth.

As new Nobel laureate Peter Howitt **noted** in a 2015 opinion piece "new firms, not necessarily small firms, are the agents of creative destruction. We would have higher economic growth if governments gave preferences to new firms instead of supporting firms only because they are small. . . (yet) federal and provincial political parties of all stripes offer tax breaks for small businesses."

The Liberal election platform deepens the imbalance by excluding larger, more productive corporations from several of the proposed tax measures, despite their higher productivity and greater propensity to research and export.

C.D. Howe Institute analyses have also warned against the risk of persistent large federal deficits and a heavy and growing debt burden. It recommends paying for more substantial income tax relief through a higher GST rate and deeper spending restraints.

The November 4 budget should aim to boost competitiveness while staying within fiscal limits. A good starting place would be to scrap most of the remaining 100-odd election platform promises yet to be fully implemented, which together add up to more than \$20 billion this fiscal year alone. And the budget should show deeper spending cuts in lower priority and inefficient areas than so far hinted.

To truly restore Canada's competitive edge, the budget will need to go well beyond the platform's scattered tax commitments and tackle the deeper structural tax and regulatory barriers to investment and productivity.

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