

Income Tax Act

tive; it is in fact that they will be taxed on the lesser of 5 per cent of capital employed or one-third of profits. It automatically operates in their favour; there is no election.

Mr. Burton: I appreciate the point made by the parliamentary secretary, Mr. Chairman. Certainly a co-operative would take whichever option operated best for it. Two options are open and, of course, the amendment states that the taxable amount would be the lesser of those two options as spelled out. It would appear that one option provides for the 5 per cent of capital employed formula as contained in the original bill, and the other would be one-third of the amount of taxable income that might be determined in the ordinary way.

It is very difficult to pass judgment on this change and to see what impact or benefit it will have on co-operatives until detailed study has been given to it. I should like to make a few preliminary comments, however. First of all, I note that the government has left the "capital employed" concept in the bill. Thus it would appear that the government has some rationale for this concept. They feel it is a suitable basis for determining taxation of co-operative organizations. But I think it was pointed out many times during the debate on second reading, Mr. Chairman, that it was very difficult to determine the rationale.

What is the concept of "capital employed"? What sense does it make? It would appear that the government took no heed of the representations, because they have left the "capital employed" concept in the bill while providing another alternative to co-operatives. I think it was pointed out in some of the submissions by the co-operatives that there really is no suitable rationale that would justify the use of the "capital employed" concept, but it has been left in the bill. The 5 per cent figure also has been left in the bill. Hon. members know that up to the present the figure has been 3 per cent of capital employed to be used as a basis in determining taxable income.

I believe this has been in the Income Tax Act since 1946 when certain amendments were passed which affected co-operatives. The figure was changed from 3 per cent to 7 per cent in the white paper, but it was pointed out that this was disastrous for most co-operatives. It now appears that there has been a compromise and the figure in the bill, which remains in the amendment tabled this afternoon, is 5 per cent of capital employed.

Mr. Chairman, I fail to see what rationale there is in the 5 per cent figure. The only rationale that I can think of is that it is half way between 3 per cent and 7 per cent. If the government finds that it can justify that sort of compromise position and defend it, then of course that is what they will have to try to do. However, it does not make sense to me.

Similarly, I suggest that we must look at the long-run implications of the option which has been provided to co-operatives, namely, that one-third of the amount calculated as taxable income would be subject to taxation. It is difficult to determine the rationale for that one-third figure. I am not sure what it is and I am not sure that the minister dealt with it in his remarks this afternoon. If he did, then I did not understand. We are told there is to be a complex phasing-in rule as well, which we will have to study before passing judgment.

[Mr. Mahoney.]

I do not understand why the government could not accept the very simple proposition put forward by the co-operative movement. They suggested that patronage dividends as they applied to the dividend paid out by production co-operatives, which amounts to about 95 per cent of the total dividends paid out, should be taxable in the hands of the recipient at his marginal rate of tax. This means that a member of a co-operative will be taxed on the reward he obtains as a result of patronizing his own organization and making use of the services which he helped establish. Apparently this suggestion was rejected by the government, as were other suggestions which I think would have taken into account the objections raised regarding the tax position of co-operatives.

The parliamentary secretary will be aware that a withholding tax will be imposed on patronage dividends no matter whether the dividend was paid out in cash. So long as it is credited to the member of the co-operative, he will be subject to the withholding tax payment and can deal with it from there in his personal income tax return, as is the case at present with respect to other types of payments which are taxable in the hands of the recipient. For example, a lump sum payment to an individual where he receives a refund of pension contributions is subject to a withholding tax of 10 per cent and is subject to a special tax rate in the hands of the recipient. That 10 per cent is withheld at the time the money is paid out to the recipient.

• (5:00 p.m.)

There is also a proposal that co-operatives be taxed on their undistributed earnings, that is, the earnings which are retained by them, and also on earnings derived as a result of business with those who are not members of the co-operative. There is no question about such earnings being subject to taxation. It seems to me, Mr. Chairman, that this was a very reasonable set of proposals. On initial examination I am disappointed that the government did not see fit to accept those recommendations and adopt what I think was the sensible approach suggested by the co-operative movement.

There are other areas of concern regarding the bill. We shall deal with those when discussing the individual clauses. Of course, I am concerned about the impact that tax changes will have on agriculture and on farming, and we are particularly concerned about the way in which the taxation of capital gains will apply to farms. This, of course, is a complex subject. I do not propose to deal with it at present, except to note that farmers, as all hon. members no doubt are aware, are in a very special and unique position in terms of the type of operation they undertake, the economics of their position and the underlying realities which apply to their operations. These factors must be taken into account in any system in which capital gains are to be taxed.

There are other areas of concern as well. Some of them have been alluded to. I am referring to the proposed changes with regard to basic herds and to the depreciation of farm equipment and farm assets. We shall have to consider these in greater detail when we come to the appropriate clauses of the bill.

This afternoon as we move toward the clause by clause consideration of the bill I wish to make a few general comments. I note that as we are examining this bill in