



Strengthening Canada's Industrial Competitiveness Through Strategic Tax Benchmarking

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This study was commissioned by the Centre for Civic Engagement. The CCE is a non-partisan Canadian charity dedicated to conducting original research on public policy issues related to Canadian prosperity, productivity, and national flourishing. The CCE's research informs an active program of policy seminars, events, conferences, and lectures all aimed at providing the policy making community with actionable insights that encourage informed decision making on issues that matter to Canadians.

Introduction

A fundamental challenge behind Canada's stagnating GDP per capita is weak business investment. Between 2014 and 2021, private-sector investment per worker declined by approximately 20%, contrasting sharply with peer countries.¹ In 2024, Canadian workers were estimated to receive only 55 cents in investment for every dollar received by U.S. counterparts.² This divergence in investment behaviour undermines Canada's capacity to enhance labour productivity and economic output.

Notably, during the same time both federal and provincial governments have increasingly relied on largescale business subsidies, with federal business subsidies growing 140% between 2014 and 2024.³

While politically visible, business subsidies have significant drawbacks, and at best have been an inefficient use of government spending power. In 2024, Canada's federal business subsidies were about 1.4% of GDP, over double the U.S. level of 0.6%, yet productivity growth in Canada remains below the U.S. and the OECD averages.^{4,5} These subsidies are often narrow in scope, duplicative, and lack evidence of sustained economic benefit. Research shows that subsidies alone rarely generate jobs or growth and may even harm economic development by distorting markets and misallocating resources.⁶ Moreover, the financing of subsidies through higher general tax burdens may inadvertently deter broader investment, thus limiting overall economic impact.

Provinces wield primary authority over many competitiveness-related policies, including taxation, labour regulations, and land use. However, they operate within a fiscal environment largely shaped by federal funding and policy. Federal business subsidies frequently overlap with provincial programs, creating inefficiencies and limiting provinces' fiscal flexibility. Thus, provinces lack the fiscal space to conduct strategic tax benchmarking effectively on their own, to compare their tax competitiveness with U.S. counterparts, and guide meaningful reforms.

Therefore, to address Canada's structural productivity challenge it is recommended that the provincial governments, in coordination with the federal government, advance a three-pronged tax reform program to enhance industrial competitiveness:

1. Canadian provinces establish **strategic tax benchmarking** initiatives, comparing their corporate tax regimes to peer U.S. states, implementing tax-based reforms to improve competitiveness.

¹ Tegan Hill & Joel Emes. (June 29, 2023). *Comparing Business Investment per Worker in Canada and the United States, 2002-2021*. Fraser Institute. <https://www.fraserinstitute.org/studies/comparing-business-investment-worker-canada-and-united-states-2002-2021>

² William B.P. Robson & Mawakina Bafale. (September 12, 2024). *Underequipped: How Weak Capital Investment Hurts Canadian Prosperity and What to Do about It*. C.D. Howe Institute. <https://cdhowe.org/publication/underequipped-how-weak-capital-investment-hurts-canadian-prosperity-and-what/>

³ John Lester. (March, 2024). *Federal Business Subsidies: Explosive Growth Since 2014*. School of Public Policy, University of Calgary. https://www.policyschool.ca/wp-content/uploads/2024/03/FP6-FedBusSubsidies.Lester.Mar7_.pdf

⁴ Ibid.

⁵ Chris Edwards. (March 4, 2025). *Corporate Welfare in the Federal Budget*. CATO Institute. <https://www.cato.org/policy-analysis/corporate-welfare-federal-budget-0#:~:text=Recently%2C%20corporate%20welfare%20soared%20with,year%20on%20aid%20to%20businesses.>

⁶ Tegan Hill, Joel Emes & Jake Fuss (March 12, 2024). *The Cost of Business Subsidies in Canada: Updated Edition*. Fraser Institute. <https://www.fraserinstitute.org/sites/default/files/cost-of-business-subsidies-in-canada-updated-edition.pdf>

2. The federal government offers conditional **tax point transfers** to provinces that pursue benchmarking. These transfers provide economic incentives to the provinces to yield greater value from benchmarking and/or provide provinces with the fiscal room to lower taxes without compromising services or fiscal stability.

3. Governments **phase out industrial subsidies**, with savings redirected toward the tax point transfers and provincial tax reductions, ensuring the program remains financially sound.

Empowering provinces to establish strategic tax benchmarking against industrially comparable U.S. states and to pursue targeted tax reforms based on these comparisons offers a promising pathway. Such benchmarking would provide provinces with the necessary data and framework to implement evidence-based tax reforms that enhance competitiveness.

Supporting these provincial initiatives with conditional federal tax point transfers, in lieu of less effective subsidies, would provide fiscal space and incentives for reform. This approach aligns fiscal responsibility with structural competitiveness, offering a sustainable means to raise Canada's productivity and close the growing economic gap with the United States.

Key Considerations

The following are key considerations which inform the policy mechanism and provide a qualitative rationale for its efficacy:

Fiscal Federalism – Aligning responsibilities across government levels improves economic development efficiency. Phasing out overlapping federal subsidies and redirecting funds to conditional tax point transfers gives provinces the fiscal flexibility to implement targeted tax reforms. This approach ensures federal support complements provincial action, enhancing the effectiveness of public spending.

Subsidiarity – Programs are most effective when delivered locally. Reducing federal subsidies and providing provinces with data and fiscal space empowers them to design tax reforms tailored to their economies. This strengthens local accountability, encourages industrial growth, and supports innovation, reinforcing the principle of subsidiarity.

Global Tax Competitiveness – Attracting investment requires understanding Canada’s position globally. Strategic tax benchmarking equips provinces with evidence on competitiveness relative to comparable U.S. states, allowing reforms that enhance investment attractiveness and focus on long-term economic opportunities.

Lower Taxation for Competitiveness – Investment decisions are highly sensitive to taxes. By redirecting subsidies to tax point transfers, provinces gain fiscal space to lower industrial taxes. Benchmark-informed reductions increase returns on capital, stimulate business investment, and improve Canada’s productivity and global competitiveness.

Policy Mechanism

The strategic tax reform program is conceptualized to progress through six steps which are grouped into three phases:

Phase 1

1. Provinces Undertake Benchmarking Analysis

Participating provinces conduct a benchmarking study comparing their tax regime to key U.S. competitor states. The analysis identifies competitive gaps, evaluates investment impacts, and proposes target reductions in distortionary taxes. This Competitive Tax Benchmark becomes the province's measurable objective and eligibility basis for federal tax point transfers.

2. Provinces Identify High-Value Tax Reductions

Provinces determine which tax reductions deliver the greatest competitiveness gains. This may include consultation with municipalities to address fees affecting business location decisions. Focusing on the most distortionary taxes ensures reductions drive higher investment returns and productivity.

3. Provincial Government Communicates Benchmark

Provinces formally notify the federal government of their benchmark and proposed reductions. The federal government then calculates the maximum eligible tax point transfer, creating a transparent, rules-based process so provinces know their fiscal support before reforms begin.

Phase 2

4. Provinces Lower Taxes and Remove Ineffective Subsidies

Provinces amend tax systems to reduce or eliminate distortionary taxes. These changes improve tax neutrality, reduce compliance costs, and strengthen long-term investment incentives.

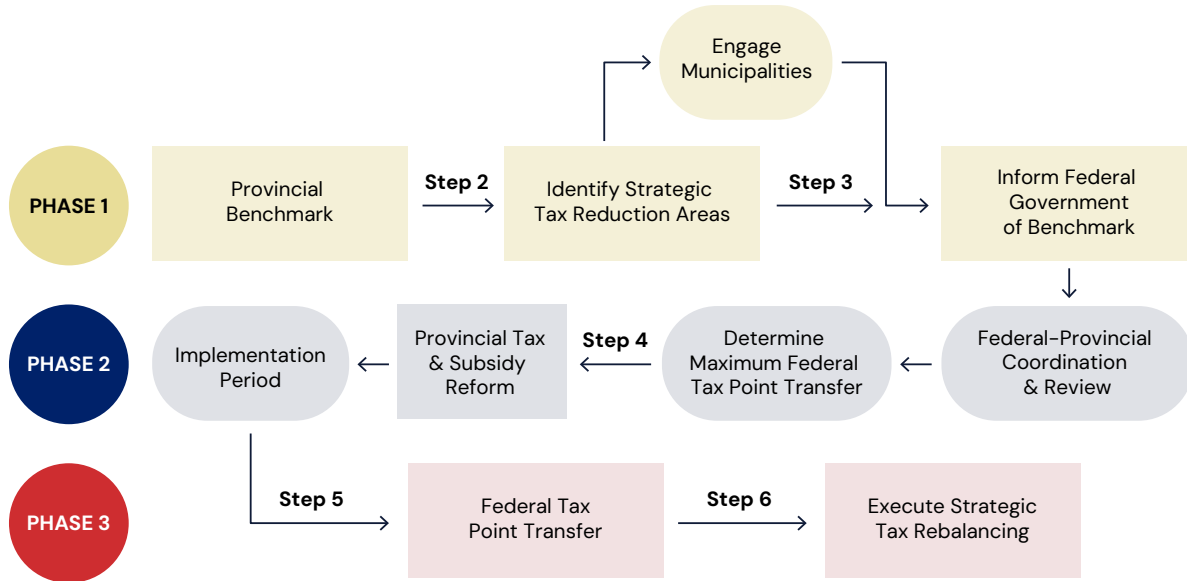
Phase 3

5. Federal Government Provides Tax Point Transfer

After verification, the federal government delivers the agreed tax point transfer, supported by the phase-out of federal industrial subsidies.

6. Provinces Execute Strategic Tax Rebalancing

Provinces use the new fiscal space to finalize targeted tax reductions while maintaining budget neutrality. Reforms are measured against the benchmark to ensure competitiveness gains.



Strategic Tax Benchmarking

Lack of strategic direction, combined with the political appeal of direct subsidies, has led governments to adopt costly and inefficient policies that fail to deliver sustained economic growth. The status quo harms economic development by distorting markets and misallocating resources, which highlights the need for a new, strategic, and integrated approach to tax and subsidy policy.

Jurisdictions with lower structural tax burdens have leverage in attracting investment capital. As a mid-size economy, Canada cannot compete on industrial subsidies alone – bigger economies can always offer bigger subsidies. This has been made evident by recent U.S. policies, like the *Inflation Reduction Act* (IRA) and the *One Big Beautiful Bill Act*, both of which included generous business subsidies and some tax reductions that Canada cannot match.

Therefore, the goal of this policy is for provinces to gain strategic insight to inform tax burden reduction, developing a competitive edge on identified industrially competitive U.S. states. This shifts both the federal and provincial competitiveness strategy from targeted subsidies to general tax reductions.

| POTENTIAL BENCHMARKING COMPARISONS | |
|------------------------------------|---|
| PROVINCE | U.S. STATES |
| Ontario | New York, Michigan, Illinois, Alabama, Tennessee |
| Alberta | Texas, Wyoming |
| Nova Scotia | Maine, Rhode Island, New Hampshire, Massachusetts |

*Provinces would undertake qualitative and quantitative analysis to identify comparable U.S. states.

Based on these insights, provinces would design reform plans aimed at reducing tax-induced economic distortions and phasing out low-yield subsidies. Provincial governments would retain full autonomy over policy design but would be expected to demonstrate material improvements in tax competitiveness to receive federal tax point transfers.

To maximize the impact of tax reform, provinces should move beyond headline rates and adopt a more detailed benchmarking approach that considers the marginal effective tax rate (METR) and the total net tax burden after accounting for credits and subsidies. This would provide a clearer picture of the province’s true competitiveness relative to comparable U.S. states.

A carefully calibrated tax premium could then be evaluated to determine the most economically efficient point of reduction, ensuring that tax policy directly counterbalances these disadvantages. This would allow provinces to strengthen their unique competitive position by strategically adjusting their corporate tax frameworks to attract investment and talent while reducing reliance on costly subsidies.

While this proposal focuses on corporate tax benchmarking, a similar process could be undertaken to benchmark personal and sales taxes.

Example Analysis: Ontario Benchmarking Analysis

While Ontario’s combined corporate tax burden (26.5%) is already slightly below the average of economically comparable U.S. states (28.13%), further targeted reductions could make Ontario a more attractive destination for business investment, particularly in manufacturing and high-value sectors. This would capitalize on its existing advantage, signaling to multinational and domestic firms that Ontario is a low-friction environment for capital deployment.

| ONTARIO | SELECTED STATES AVERAGE |
|------------------------|-------------------------|
| Total corporate: 26.5% | Total corporate: 28.1% |

*For the purposes of this example analysis we rely on headline rates.

** Selected States: New York, Michigan, Illinois, Alabama, Tennessee.

Ontario, through the benchmarking exercise, would determine an optimal tax target that accounts for the effect of the net tax burden and other negative pressures on attracting investment income. This target would guide the design of a tax reduction measure aimed at maximizing Ontario’s economic competitiveness with comparable U.S. states.

Once the target is set, it will be communicated to the federal government. The federal government and Ontario would then collaborate on an implementation plan that reflects the total revenue reduction possible through reduced subsidies. Specifically, the federal government would reduce business subsidies by an amount equal to the provincial revenue lost in achieving the optimal tax target. This fiscal room would then be reallocated to Ontario through a conditional tax point transfer, ensuring the province has the capacity to implement the tax reduction. Ontario would then have two options:

Option 1: With this reallocation, Ontario would be able to adjust its existing corporate tax so that the province can return the rate to its original provincial thresholds, thereby maintaining provincial revenue neutrality while still reducing the overall tax burden to meet the target.

Option 2: Ontario could choose to go further. It could maintain the federal reallocation and reduce its own revenues, thereby achieving a larger combined tax reduction (with a maximum of doubling the tax impact).

Ultimately, the approach gives Ontario the flexibility to achieve a net reduction in taxes while preserving revenue neutrality, or if desired, to generate a more substantial impact on tax competitiveness by combining both provincial and federal reductions.

Tax Point Transfers

Tax point transfers facilitate mutual investment between Ottawa and the provinces in the pursuit of lower taxes in the service of strategic competitiveness. The policy mechanism ensures that provinces retain fiscal autonomy while being incentivized to reform their tax systems to enhance competitiveness. The program would encourage provinces to move in the same general direction by lowering distortional taxes while leaving space for local variation.

Central to the incentive of this proposal is the avoidance of a provincial revenue cliff induced by tax reductions. Given that this program would invite provinces to reduce their share of taxes while receiving an offsetting federal tax point transfer, it will be the federal government that must reduce its spending to deliver the fiscal capacity for the overall reduction. This is premised on the federal government's phase-out of industrial subsidies, where the fiscal space would be redirected toward the tax point transfer.

This mechanism preserves provincial fiscal capacity, shifts support from firm and industry specific subsidies to broad-based tax reductions, and enhances vertical fiscal alignment within Canada.

The federal government will have to reduce the fiscal cost of industrial subsidies commensurate with the total value of federal tax space to be devolved to the provinces that undertake and execute a tax benchmarking. This should be achieved by:

- Reviewing all industrial subsidies delivered through the tax system, direct investments, and the activities of government business enterprises with the goal of winding down all subsidies which do not explicitly and verifiably solve for a market failure.
- Evaluating all temporary tax credits – like the suite of clean economy credits – and reduce their rates and accelerate their wind downs.
- Eliminate any subsidies which are duplicative of provincial programs to enhance and respect provincial autonomy and responsibility in economic development initiatives.

Upon initiating the policy mechanism, the federal government should commence an audit of its business subsidy programs to ascertain the maximum fiscal recalibration it could harness through the phase out of industrial subsidies. This exercise would guide the intergovernmental negotiations of tax point transfers.

Federal industrial subsidies in 2023–24 amounted to roughly \$40 billion or 1.4% of GDP and are forecasted to reach about \$50 billion in 2027–28.⁷ Therefore, the maximum fiscal recalibration derived from total subsidy phase-outs would be in the order of \$40–\$50 billion. While subsidy savings cannot be transferable to tax reductions or transfers on a 1:1 basis, this maximum figure offers a reference point to the magnitude of fiscal capacity that could be reoriented to tax point transfers.

The phase out of federal industrial subsidies would represent both a strategic policy shift – from distortional subsidies to broad base tax reductions – and a measure of fiscal recalibration. Phasing out direct subsidies has a value, but only intermediary in comparison to the full potential harnessed by simultaneously reducing tax burdens.

⁷ John Lester. (March, 2024). *Federal Business Subsidies: Explosive Growth Since 2014*.

Economic Analysis

While a comprehensive economic analysis would require further assessment, presented here are three scenario cases of differing magnitudes to provide reasonable references of the fiscal costs and economic opportunities from the program.

Scenario A: Ontario

| ONTARIO BENCHMARKING FISCAL IMPACT | |
|------------------------------------|--|
| Current Total Tax Rate | Total corporate: 26.5% (Federal 15% + Ontario 11.5%) |
| Selected States Average Tax Rate | Total corporate: 28.1% (Federal 21% + Average State 7.1%) |
| Actual Provincial Revenue | \$27.8 B |
| Target Reduction Rate | 2% |
| Revised Total Tax Rate | 24.5% |
| Tax Reduction Cost | \$4.83 B |

* For the purposes of this example analysis we rely on headline rates.

** Selected States: New York, Illinois, Michigan, Tennessee, Alabama.

*** Ontario revenues sourced from 2024-2025 Public Accounts.⁸

⁸ Government of Ontario. (August 29, 2025). *Public Accounts 2024-2025: Annual Report*. <https://www.ontario.ca/page/public-accounts-2024-25-annual-report>

Scenario B: Nova Scotia

| NOVA SCOTIA BENCHMARKING FISCAL IMPACT | |
|--|--|
| Current Total Tax Rate | Total corporate: 29% (Federal 15% + Nova Scotia 14%) |
| Selected States Average Tax Rate | Total corporate: 28.7% (Federal 21% + Average State 7.7%) |
| Actual Provincial Revenue | \$1.1 B |
| Target Reduction Rate | 2% |
| Revised Total Tax Rate | 27% |
| Tax Reduction Cost | \$0.158 B |

* For the purposes of this example analysis we rely on headline rates.

** Selected States: Maine, Rhode Island, New Hampshire, Massachusetts.

*** Nova Scotia revenues sourced from 2025 Public Accounts.⁹

⁹ Government of Nova Scotia. (September 22, 2025). *Public Accounts*.
<https://notices.novascotia.ca/files/public-accounts/2025/pa-volume-1-financial-statements-2025.pdf>

Scenario C: Alberta

| ALBERTA BENCHMARKING FISCAL IMPACT | |
|------------------------------------|--|
| Current Total Tax Rate | Total corporate: 23% (Federal 15% + Alberta 8%) |
| Selected States Average Tax Rate | Total corporate: 21% (Federal 21% + Average State 0%) |
| Actual Provincial Revenue | \$8.1 B |
| Target Reduction Rate | 2% |
| Revised Total Tax Rate | 21% |
| Tax Reduction Cost | \$2.03 B |

* For the purposes of this example analysis we rely on headline rates.

** Selected States: Texas and Wyoming.

*** Alberta revenue sourced from 2024–2025 Final Results.¹⁰

If these three provinces each pursued a 2 % corporate tax reduction, the combined fiscal impact would total about \$7 billion in foregone revenue:

- **Ontario:** 2% drop from 26.5% to 24.5% total tax burden would cost roughly \$4.83 billion, or about 17% of provincial corporate tax revenues.
- **Nova Scotia:** 2% cut from 29% to 27% total tax burden would cost approximately \$160 million, or about 14% of provincial corporate tax revenues.
- **Alberta:** 2% reduction from 23% to 21% total tax burden would cost roughly \$2.03 billion, or 25% of provincial corporate tax revenues.

These estimates represent a significant portion of the Canadian economy, indicating that if the policy were widely adopted, it would be consistent with the scale of current federal spending on business subsidies. But if additional provinces pursue deeper rate cuts, the fiscal burden could rise substantially. This highlights the need for federal–provincial coordination following the benchmarking process to preserve fiscal stability and establish a clear understanding of the maximum fiscal space that can be supported through tax point transfers.

¹⁰ Government of Alberta. (June 2025). 2024–25 Final Results. <https://open.alberta.ca/dataset/9c81a5a7-cdf1-49ad-a923-d1ecb42944e4/resource/8b2a1431-b31d-4a6f-8a50-d1eaaa638280/download/tbf-go-2024-2025-final-results-year-end-report.pdf>

Conclusion

Canada's long-term economic performance depends on creating the conditions for sustained private investment, innovation, and productivity growth. The current reliance on business subsidies has proven to be an inefficient and unsustainable strategy, yielding limited economic benefit while requiring growing shares of public resources. Redirecting these funds toward broad-based tax reductions, enabled through conditional tax point transfers, represents a more effective and fiscally responsible path forward.

By empowering provinces to undertake strategic tax benchmarking and reform their tax systems based on the evidence of international competitiveness, this policy proposal advances a structural solution. It strengthens fiscal federalism by aligning the responsibilities of both orders of government, promotes subsidiarity by enabling provinces to tailor reforms to their unique economic strengths, and enhances transparency and accountability through a clear and verifiable process.

Non-Economic Outcomes

- The right sizing of the federal government's role in economic development through the reduction in the size and scope of business subsidies.
- A restoration of fiscal federalism that respects Section 91 and 92 responsibilities.
- A new tone and approach from Ottawa, signaling that the federal government will step back and allow provinces to take greater responsibility for their economic destinies.
- Alignment of major tax reduction policies with both federal and provincial priorities through coordination.

Economic Outcomes

- A reduction in the overall combined federal and provincial tax rates, improving Canada's structural competitiveness.
- Bringing provincial tax rates at least to parity with U.S. peer jurisdictions to strengthen investment attraction and retention.
- Improved capital allocation by replacing narrow, firm-level subsidies with broad-based tax reductions focused on long-term competitiveness.

This approach leverages existing fiscal capacity to drive long-term structural reform. It respects provincial jurisdiction while incentivizing coordinated action consistent with national economic objectives. It achieves these goals without new federal spending or program creation, offering a fiscally sustainable, economically coherent, and federatively balanced response to Canada's competitiveness challenge.

Annex

ONTARIO: Benchmarking State Average Sources

New York Corporate Income Tax Rate: 6.9% (*average of the two major business tax rates)

Illinois Corporate Income Tax Rate: 9.5%

Michigan Corporate Income Tax Rate: 6%

Tennessee Corporate Income Tax Rate: 6.5%

Alabama Corporate Income Tax Rate: 6.5 %

NOVA SCOTIA: Benchmarking State Average Sources

New Hampshire Corporate Income Tax Rate: 7.5%

Massachusetts Corporate Income Tax Rate: 8%

Maine Corporate Income Tax Rate: 8.4% (*average of three major non-small business tax rates)

Rhode Island Corporate Income Tax Rate: 7%

ALBERTA: Benchmarking State Average Sources

Texas Corporate Income Tax Rate: 0%

Wyoming Corporate Income Tax Rate: 0%

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