PRE-BUDGET SUBMISSION

TO

THE HOUSE OF COMMONS STANDING COMMITTEE ON FINANCE

From

Direct Sellers Association of Canada

Association de ventes directes du Canada

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INTRODUCTION

The Direct Sellers Association of Canada (DSA), founded in 1954, is the national association of Canadian direct selling companies and their independent sales contractors (ISCs). The mission of the DSA is to further enhance trust, confidence and growth in the Canadian direct selling industry through self-regulation and ethical conduct.

The DSA and its 55 member companies are committed to operating in accordance with the comprehensive industry standards set out in the DSA's Code of Ethics and Business Practices (Appendix A). The Code governs the direct sale practices and procedures used by DSA member companies in marketing their products and services to the public and refers to the relationship all DSA members and their ISCs should strive to obtain with the community. The purpose of the Code is to emphasize the sense of responsibility and commitment all DSA members should express and exhibit towards Canadian consumers and the general public, thereby bettering the individuals they serve and the community as a whole.

The direct selling companies and their ISCs market and distribute a wide variety of products and services directly to the consumer, usually but not exclusively in the consumer's home, rather than in traditional retail establishments. Generally, these products and services are sold by ISCs in the context of group presentations (party plan), or on a personal consultation basis.

The strength of direct selling lies in its tradition of independence, its simplicity, and its commitment to a free market system, providing accessible business and career opportunities to people whose entry is not restricted by gender, age, education or previous experience. It is a significant fact that direct selling is a manageable economic opportunity, which can further family income with minimal disruption and minimal investment. This opportunity is accessible to all women and men, everywhere in Canada, whether they live in urban or rural communities.

During the past year, more than 1 million ISCs were engaged in operating their own direct selling businesses, selling more than $1.6 billion of retail goods and services. The products and services sold by these individuals are as diverse as the individuals themselves, and include cosmetics and personal care items, clothing and accessories, home appliances, houseware specialties and decorations, household cleaning products, candles, natural health food products, toys, educational products and telecommunication services just to mention a few. In terms of the ISCs, it should be noted that 73% are women, 77% are married, 66% have full-time jobs - using this business opportunity to earn extra income, and approximately 33% work full or part-time and have no other occupation.

The DSA has always shared its expertise and knowledge with all levels of government. For example, the DSA has worked closely with Revenue Canada (now the CCRA), in educating and encouraging ISCs to comply with Canada's income tax laws by assisting in the preparation of the *Tax Filing Information for Independent Sales Contractors* Income Tax Guide. The DSA is also continually working with Consumer Protection Agencies across the country, in promoting the harmonization of Provincial direct selling legislation, and the Canadian Competition Bureau, in promoting the principles set out in the *Competition Act* to the members and ISCs. Internationally, the DSA has asked the Canadian representative at the APEC Ministerial Forum for Small and Medium Enterprises to support the Consumer Education and Protection Initiative aimed at enhancing consumer protection across APEC economies. The DSA proudly notes that this initiative was endorsed by APEC in 1999.

SUMMARY OF RECOMMENDATIONS

The DSA believes that the following recommendations will assist the Committee in preparing a Pre-Budget report that (i) ensures that Canada remains a major player in the New Economy; (ii) provides Canadians with an equal opportunity to succeed; and (iii) creates a socio-economic environment where Canadians can enjoy the best quality of life and standard of living.

I. Maintaining Competitiveness by Reducing Taxes

The DSA recommends additional personal and corporate tax reductions be implemented immediately.

II. Ensuring Canadians are Adequately Saving For Retirement

The DSA recommends the introduction of retirement savings plan alternatives, such as tax-prepaid savings plans (TPSPs), and increasing the current RRSP contribution limits to $17,500.

III. Job Creation and Transitioning to Independence

The DSA recommends that existing social programs be amended to allow transitional relief to all individuals moving from a position of dependence to a position of independence in operating his or her own small business.

IV. Providing GST/HST Relief for Natural Health Products

The DSA recommends that the *Excise Tax Act* be amended immediately to zero-rate all natural health products.

V. GST/HST and the Direct Sellers Mechanism

The DSA recommends that the Direct Sellers Mechanism be expanded so that it is equally available to direct sellers and ISCs who operate on a sales agent basis (currently, only direct sellers and ISCs who operate on a buy-and-resell basis may use the DSM).

RECOMMENDATIONS

I. <u>Maintaining Competitiveness by Reducing Taxes</u>

The DSA applauds the Canadian government for its commitment to lowering taxes and strengthening the Canadian economy. Notwithstanding the government's recent tax reductions, the fledging U.S. economy has negatively impacted Canada causing, among other things, layoffs and the postponement (and elimination) of capital investment decisions.

Recommendation

Given the unforeseen deterioration of the U.S. economy, the DSA recommends further tax reductions be implemented effective January 1, 2002. In particular, the DSA recommends that corporate tax rates be cut 6 per cent immediately (as opposed to the proposed 2 per cent per year over the next 3 years) and that personal income tax rates be further reduced 1 per cent for each marginal tax bracket. These actions will contribute to the long-term strength of our economy and, as acknowledged by the Honourable Paul Martin, will "also provide stimulus in the short term when we need it now, by putting more money in the hands of Canadians, by spurring business, sparking investment and creating jobs".

II. <u>Ensuring Canadians are Adequately Saving For Retirement</u>

As the Honourable Paul Martin has recognized, many Canadians "wish for a secure retirement and a health care system that's there when you need it". These same concerns are also prevalent amongst ISCs and other self-employed persons.

Unlike many employees in the public and private sector, self-employed persons, such as ISCs, do not have company/government pensions to rely on to satisfy their retirement needs and, as such, rely entirely upon their own savings. Currently, the only government sponsored retirement savings alternative available to most Canadians is a registered retirement savings plan ("RRSP"), with maximum yearly contributions of $13,500. Recent studies have shown, however, that the current RRSP system is not adequately or effectively enabling Canadians to satisfy their objectives of providing themselves with a "secure retirement".

Recommendation

A. Canadians Need More Retirement Savings Options

As indicated in a recent C.D. Howe Institute Study, *A New Option for Retirement Savings: Tax Prepaid Savings Plans*, Kesselman and Poschmann, "Canadians are saving less than they should, and in economically distorted forms, which raises the risks for public finances in meeting the income support levels of the coming boom of retirees".

Giving these observations, the DSA is in substantial agreement with Professor Kesselman and Mr. Poschmann's conclusions that "Canada's tax treatment of retirement savings needs to be improved" and recommends that Canada implement an alternative means for enabling all Canadians to effectively save for retirement. In this regard, the DSA recommends that the government follow Professor Kesselman and Mr. Poschmann's recommendations by implementing TPSPs, with an initial annual contribution limit of $10,000.

The DSA finds TPSPs to be an appealing alternative to RRSPs, particularly, because TPSP contributions are made with tax paid income resulting in no immediate tax deferral costs to the government. Furthermore, unlike RRSPs, which are of limited benefit to low and moderate income earners, TPSPs are beneficial to all income earners as they enable all income earned on contributions to accrue tax-free. Accordingly, TPSPs will encourage more and more Canadians to seriously consider their retirement goals and implement a savings plan to meet those goals.

B. RRSP Contribution Limits Need to be Increased Immediately

Even though the Canadian economy has been growing at unprecedented rates, RRSP contribution limits have decreased from $14,500 in 1995 to its current limit of $13,500 per annum. This decrease, compounded with the negative inflationary effects, significantly hinders Canadian taxpayers' abilities to adequately provide for their retirement through an RRSP. The government's 1996 announcement, freezing RRSP contribution limits until the year 2004, is equally discouraging to the average Canadian taxpayer, falsely implying that saving for retirement should not be a top priority.

Consistent with the Standing Committee's report for the year 2000 Budget, and the federal government's 1999 "five-year tax reduction plan", the DSA recommends that the current RRSP contribution limits be increased immediately from $13,500 to $17,500 so that all Canadians can more adequately provide for their retirement.

III. Job Creation and Transitioning to Independence

The DSA believes it is important for the government to understand that the direct selling industry is a vital part of the small business sector in Canada. We have a tremendous capacity to create jobs and reduce dependence on social assistance programs by providing accessible earning opportunities, with little or no investment, to a broad spectrum of Canadians. The accessibility of these earning opportunities is highlighted by the fact that 57% of all ISCs have only a high school education (or less).

One of the cornerstones for success in the direct selling industry has been the quality and availability of training for ISCs, who learn to properly present the products, guarantees and business opportunities of the companies which they represent.

By providing such training and educational assistance to people who have the ability to succeed in a sales career, the direct selling industry is contributing to the Canadian economy in a positive fashion while reducing the burden on the public sector. The direct selling industry provides an opportunity for all Canadians to increase their knowledge and skills set, providing benefits to the Canadian economy in the process.

With 73% of the more than one million ISCs being women, operating their businesses usually on flexible hours within their own homes, there is a reduced burden on the already severely strained child care system then there would be if these women were working in more conventional jobs with fixed hours. A previous study, "Women in the Labour Force", published by Statistics Canada, focused on the challenges encountered by single mothers in their attempts to re-enter or remain in the labour force and some of the negative perceptions associated with their particular status.

The report raised the question as to the new and growing barriers that are keeping single mothers on welfare when they would rather be productive working members of society. Some of the barriers include: limited employment options, absence of day care facilities during early and late hours of the day, time off for family problems, etc.

The direct selling industry <u>can</u>, and <u>will</u> meet the needs of hundreds and thousands of Canadians, who find themselves in these familiar situations, offering flexibility of hours, a wide variety of earning situations, and the opportunity of maintaining, or returning to, a meaningful and fulfilling standard of living.

We believe that the small and medium-sized business sector will continue to be the engine for Canadian economic growth. It is this area which continues to create jobs when the economy is at a standstill. ***The direct selling industry has an unlimited capacity to***

transform individuals who are dependent on social programs, such as employment insurance, into successful small business operators.

The present rules for employment insurance and social assistance, however, create a barrier to entering the direct selling industry for those who are receiving such benefits. While there is now a provision which allows for a certain level of additional income to be earned from employment before social benefits are reduced, there is only uncertain and limited transitional relief for earnings from self-employment.

When an unemployed man or women becomes self-employed and begins operating their direct selling business as an ISC, they are required to complete a Human Resources Development Canada (HRDC) "self-employment" questionnaire. The purpose of this questionnaire is to determine whether the individual is still eligible to collect EI while operating their own business as an ISC. Factors which are considered by HRDC include whether the ISC will be working more than 35 hours per week, whether they are capable of working at another job, whether staff will be hired, whether any investment in capital is required, etc.

In situations where HRDC determines that the ISC is still eligible to continue claiming his or her EI benefits, certain restrictions are imposed. The more stringent requirements include a work week of less than 35 hours and earnings of less than 25% of the total EI benefits received. Once the 25% threshold is surpassed (earnings equalling approximately $50/week), the claimants will have their EI benefits deducted dollar per dollar with every additional dollar earned as an ISC.

The current rules respecting eligibility do not apply with a sufficient degree of certainty for ISCs. Although there is a slight transition period (i.e., until earnings reach 25% of their EI benefits), ISCs who have a solid, reliable business plan for self-employment, and who plan on making direct selling their full time job, become ineligible for EI benefits, where they are devoting more than 35 hours per week to their businesses.

Thus, the current rules discriminate against the direct selling industry, and inhibit the transition from dependency to independence, by discriminating against those who are serious from the outset in establishing their direct selling business, denying these persons any transitional EI relief during the start-up phase of their small businesses, and thus discouraging these persons from making the transition from dependence on social assistance to independence.

In addition, the current rules do not take into account the fact that, like any business venture, there are certain risks/costs associated with establishing a business venture. An individual entering the direct selling industry has some start-up costs, such as a small investment in a new business starter kit, and usually requires a reasonable period of time (which, in the beginning is often time intensive requiring in excess of 35 hours per week) before a customer base is established and income is generated.

Recommendation

The DSA recommends that existing social programs be amended to allow <u>all</u> individuals, including those starting their own businesses, the transitional relief needed to move from a position of dependence on social assistance to a position of independence in operating one's own small business. Additionally, once a taxpayer's earnings have surpassed the allowed level of transitional relief (currently 25% of EI earnings), the DSA recommends that social programs be amended by providing additional pro-rata relief, through only deducting 50% of additional earnings from EI eligibility (i.e., for every dollar earned EI eligibility is reduced by only 50 cents).

IV. <u>Providing GST/HST Relief for Natural Health Products</u>

With the globalization of the Canadian economy and the diversification of the Canadian population, more and more Canadians are using natural health products as part of their daily health routine. Whether it is to manage a specific concern, or as part of an overall wellness-centred approach to health and diet, natural health products play an integral role in many Canadians' health and well being decisions.

In using such products, factors taken into consideration include the benefits of prevention, wellness and self-care, and how these and other factors impact on their overall lifestyle. It is important to note that many natural health products serve as a cost-effective alternative to more traditional and expensive pharmaceutical medicines.

Under Health Canada's March 2001 Proposed Regulatory Framework for Natural Health Products, natural health products will no longer be regulated as "food" or "drugs" under the *Food and Drugs Act*. Rather, these products will be subject a separate set of regulations designed especially for natural health products. Under the proposed regulations, natural health products will be defined, in part, as follows:

> Products manufactured sold or represented for use in
>
> (i) the diagnosis, treatment, mitigation or prevention of a disease, disorder, or abnormal physical state or its symptoms in humans;
>
> (ii) restoring or correcting organic functions in humans, or
>
> (iii) maintaining or promoting health or otherwise modifying organic functions in humans.
>
> Specifically, medicinal ingredients of natural health products are those set out below, alone or in combination:
>
> (a) a herb set out in Table 1 (to be developed)
>
> (b) a homeopathic preparation,
>
> (c) a substance or substances used as a traditional medicine, including, but not limited to, a substance used as a traditional Chinese medicine, a traditional Ayurvedic medicine or a North American aboriginal medicine, and
>
> (d) a mineral or a trace element, a vitamin, an amino acid, an essential fatty acid or other botanical, animal or microorganism derived substance.

Recommendation

Unlike food products and prescription drugs – which are zero-rated under the *Excise Tax Act*, natural health products are generally subject to GST/HST. Given the benefits these products possess, the DSA recommends that the *Excise Tax Act* be amended to zero-rate all natural health products. This will effectively lower the costs in using such products, and will encourage more and more Canadians to manage their own health and dietary needs, preventing unnecessary illnesses and ailments, and freeing up Canada's provincial health care systems for more productive and efficient uses.

V. GST/HST and the Direct Sellers Mechanism

The Direct Sellers Mechanism (DSM) is a classic example of government and business working in partnership to develop a policy which has been beneficial to consumers, the government, the direct selling industry and the more than 1 million ISCs across the country. It is this type of cooperation between government and business which is necessary to strike the proper balance among the competing concerns of raising revenue and ensuring broad-based voluntary tax compliance, while freeing business from unnecessary administrative burdens.

Subject to the important concern noted below, the DSA is pleased to state that the needs of the member companies and the ISCs have generally been met by the DSM contained in sections 178.1 through 178.5 of the *Excise Tax Act*, in that it relieves much of the burden for ISCs in terms of filing and collecting GST/HST. This mechanism is based on pre-collection of GST/HST on the suggested retail price, with the result that (a) there is a cash-flow advantage to the government and (b) there is no "underground economy" with respect to GST/HST in the direct selling industry. The DSM has significantly reduced government administrative costs by negating the need for ISCs to be GST/HST registered, while maintaining the same level of GST/HST revenues and allowing more tax "bang" for every administrative "buck". The DSA member companies and affiliated ISCs have collected and remitted in excess of $700 million in GST/HST revenues since the inception of the GST/HST in 1991.

While the DSM is operating in a positive fashion, it currently only applies to those direct selling companies whose ISCs operate on a buy-and-resell basis. The 20-25% of the direct selling industry which operates through sales agents, who earn commissions for arranging the sales of the products involved, are currently excluded from using the DSM.

These companies and their sales agents have indicated that they feel discriminated against by not having the DSM equally available to them. This is because GST/HST must be charged by the direct selling companies on sales aids supplied to the ISCs and because needless administrative costs are incurred in determining whether GST/HST should be paid by the direct selling companies on the commission payments, which are ultimately recoverable in any event by way of an input tax credit.

Notwithstanding the fact that most ISCs are "small suppliers" and, as such, are not required to be GST/HST registered, many ISCs are becoming GST/HST registered, generally to enable them to claim input tax credits. This obviously unnecessarily increases the administrative costs of the direct selling companies, the ISCs and the CCRA.

Recommendation

The DSA recommends that legislative action be taken to extend the Direct Sellers Mechanism so that it will be available, not only to those direct sellers and their ISCs who operate on a buy-and-resell basis, but also to direct sellers and their ISCs who operate on a sales agent basis.

The benefits of extending the DSM to this sector of the direct selling industry would be significant: (i) the GST/HST rules would apply on the same basis throughout the industry with minimal, if any, impact on government revenues; (ii) the companies and their sales agents would face a significantly reduced administrative and compliance burden; and (iii) the CCRA's administrative costs would be reduced as the sales agents would no longer be required to be registered for GST/HST purposes simply so they can recover the GST/HST they paid on sales aids through an input tax credit. Additionally, consistent treatment regarding the availability and application of the DSM will reduce uncertainty and confusion which has resulted within the industry.

CONCLUSION

The Direct Sellers Association appreciates the opportunity to appear before the Committee and believes that its recommendations are consistent with the Committee's objective to prepare a Pre-Budget report that (i) ensures that Canada remains a major player in the New Economy; (ii) provides Canadians with an equal opportunity to succeed; and (iii) creates a socio-economic environment where Canadians can enjoy the best quality of life and standard of living.

As always, the Direct Sellers Association is prepared to provide its support to the government to help achieve these goals. The DSA, and all its members, thank the Standing Committee of Finance for allowing it to participate in the 2002 Budget making process.

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