TEN TAX MYTHS

by Murray Dobbin

October 1999
ISBN: 0-88627-200-9

Ten Tax Myths

by Murray Dobbin

About the Author

Murray Dobbin is a B.C.-based writer and broadcaster, a CCPA Research Associate, and a member of the CCPA's Board of Directors. He is the author of several best-selling books, including his latest, now available in paperback, **"The Myth of the Good Corporate Citizen."**

October 1999

ISBN: 0-88627-200-9

Introduction

"Taxes are the price of civilization."
—U.S. Supreme Court Justice Oliver Wendell Holmes Jr.

❖ ❖ ❖

Canada's business élite and their influential academic and media allies have launched another campaign against social programs and democratic government. Earlier in the decade, government debts and deficits were misrepresented to convince Canadians they had no choice but to drastically scale back their hard-won social programs. Now, with the disappearance of the deficit in fiscal 1997-98, Canada's élite have conjured up a new campaign to advance their cause: tax cuts.

Couched in terms of job creation and "relief" for ordinary citizens, this campaign is designed to permanently lower government revenues and thus further weaken the ability to deliver social programs, redistribute income, and manage the economy in a way that benefits all of us and not just a privileged few.

The tax cut campaign rests on one of the most enduring myths in our society: the notion that "everybody" hates paying taxes. In truth, the vast majority of Canadians recognize that, if we want good government and the services it provides, we **must** pay taxes. The idea that we "hate" paying taxes makes about as much sense as saying we "hate" having to pay for restaurant meals, a new television set, or a vacation. It isn't a matter of liking it or disliking it. It is just a fact of life. If we want something, we have to pay for it, whether it's a public service or a private good.

And, in poll after poll and in every province, Canadians say they **do** want the things that their taxes pay for. They are even prepared to pay **more** taxes if they have to. Even in Alberta, where conventional wisdom suggests people are most suspicious of government and hostile to taxes, the vast majority of citizens polled by the Klein government repeatedly said that Alberta's government surplus should go back into the Medicare and education programs slashed by the government. Only a handful said they wanted more tax cuts.

Canadians say this because they know that, if we are to have a civilized society, one not determined exclusively by the dictates of the private marketplace, we must be willing to pay for it. And they say this in spite of the relentless attack on government by neo-liberal and neo-conservative media commentators, political parties, and business think-tanks. What is remarkable is that, in the face of the efforts of all these powerful and well-funded organizations, Canadians' values have not fundamentally changed.

It is still necessary, however, for Canadians to know the facts about taxes so that they can counter the myths perpetuated by those who want to permanently downsize government. While Canadians generally understand that they must pay taxes, that the tax system is unfair, and that corporations don't pay their fair share, information on these and other tax questions is rarely to be found in the mainstream media. The truth is out there. But it's not always easy to find.

The big tax scare: Another assault on equality

For over 15 years, Canada's business élite have been attacking the very idea of government as a positive force in society, as a democratic counter-balance to the unequal marketplace. This attack has been relentless in its intensity, and multi-faceted.

First, we were pummeled for years by what many referred to as "debt terrorism"—the belief that government debt was so serious that it threatened our very survival as a country. Every other national objective and social value had to be sacrificed to deal with it. While the deficit *was* a problem and the debt remains an issue, much of what was said on this subject was either false or misleading (see the CCPA's **10 Deficit Myths)**. The campaign was designed to lower Canadians' expectations of government.

To some extent, it succeeded. Many Canadians, while they maintained their conviction that government was a force for good and that it should provide for its citizens, came to accept the proposition that we could "no longer afford" good government. This is despite the fact that between 1979 and 1997 the wealth created in Canada (i.e., Gross Domestic Product, or GDP, per capita) increased by 50% in real terms. This suggests that we could afford far better social programs than we had in the 1970s if we had the political will to implement them. Instead, we saw them slashed throughout the first half of the 1990s.

The attack on government continued on several other fronts. One persistent theme expressed in the editorials of the Conrad Black and Thomson newspapers—and on television—was that public services were inferior, too expensive, and controlled by lazy, overpaid "bureaucrats." This attack, too, relied on deliberately misleading and often false declarations about Canadian social programs and educational standards (see the CCPA's **"In Defence of Public Services"**).

The goal was transparent. If Canadians were led to believe that their social programs were no good, and that the public employees delivering them were somehow violating their public trust, they would no longer support those services.

Here the attack on government has been much less successful. While there has been a decrease in support for government in the most general sense, people have not been fooled. To the extent that the quality of Medicare and public education has been eroded, Canadians know that it is because the funding for these vital services has been cut to the bone. Support for those actually providing services, including teachers and nurses, remains high.

Now that the deficit problem has been successfully dealt with, those determined to reduce the role of government have been forced to take another tack. With the end of the deficit era, people's expectations are again reflecting their values. They want the surpluses spent on social programs. The neo-liberal counterattack to this renewed support for social spending is the call for across-the-board tax cuts.

If they are successful in this campaign, we will see a dramatic reduction in government revenues. Once made, these tax cuts will be extremely difficult to reverse and the government's capacity to fund programs and intervene in the economy could be permanently reduced. In effect, tax cuts are meant to bind the hands of any future government that wants to invest in Canada's social infrastructure. Such a government might have a mandate from the people, but will be hamstrung by a tax system unable to provide the revenue to carry it out.

The tax cut advocates cast their proposals in terms of relief for ordinary citizens, as well as job creation. There is an enormous hypocrisy in this sales pitch, given that these same forces have for over a decade supported the government's policy of keeping unemployment high to fight inflation. Even with inflation at or around 1%, the government still adheres to a policy determined by what it calls the Non-Accelerating Inflation Rate of Unemployment (NAIRU)—the so-called "natural rate" of unemployment.

In effect, this policy places low inflation (which primarily benefits the wealthy) ahead of low unemployment as a government priority. Currently, the Bank of Canada believes the NAIRU rate is between 8% and 8.5%. That means the economy and the money supply is controlled to keep unemployment from going *below* 8%. Business voices arguing that tax cuts are needed to create jobs, at the same time that they call for near-zero inflation/high unemployment, cannot be taken seriously. Tax cuts serve the same purpose as deficit-fighting: to reduce government revenues in order to reduce its social and economic role.

The debate over tax cuts versus reinvesting in our social programs promises to be the next big political fight in this country. The outcome of this battle will be determined by how many Canadian citizens are able to engage in the debate on the basis of strong, sound counter-arguments to the myths, distortions and outright falsehoods being used by the other side of the debate.

Ten Tax Myths is intended to equip citizens with the information and analysis needed to debunk the many myths about taxes being put forward by those determined to dismantle democratic government.

Glossary of tax terms

- **regressive vs. progressive taxes:** These terms refer to the relative impact of a given tax on low-income earners. The GST is criticized for being a regressive tax because it is not based on ability to pay and thus has a disproportionate effect on the poor. They pay the tax on all their income (because they spend all their income) while the wealthy pay it only on the portion of their income they spend. Graduated income tax is classified as progressive because it is based on the ability to pay.

- **statutory tax rate:** The rate at which an individual or corporation is taxed before tax deductions, special concessions or incentives are applied. The federal statutory corporate income tax rate is 28%, but few corporations pay this much tax on their net profits because they use many tax breaks and loopholes to reduce the amount actually paid.

- **effective tax rate:** This is the rate of tax *actually* paid, as opposed to the official (or statutory) tax rate. For example, the **statutory** corporate income tax rate, combining federal and provincial rates, averages 42%, but, after tax breaks and deferments, the **effective** rate drops to just 27.4%.

- **payroll taxes:** These taxes are paid by employees, employers, or both, and include such things as UI, Canada Pension Plan premiums, and workers' compensation.

- **consumption tax:** Just what it says, these taxes are collected whenever an individual (and sometimes companies) purchase goods or services. These include provincial sales taxes, the GST, and taxes on cigarettes, alcohol and fuel (these latter are called excise taxes).

- **capital gains tax:** Those who make money in the stock market, in real estate, or by selling a business for more than they paid for it, pay income tax on the money they made in these transactions. While there is no special, lower capital gains tax, those who make income this way only have to pay income tax on 75% of the capital gains they make.

- **marginal tax rate:** The marginal tax rate is the rate of income tax an individual pays on the last dollar he or she earned. If your taxable income is $29,590 or less, you pay the lowest federal rate (17%) on all that income. Starting with the next dollar of income above $29,590, you pay the next highest rate, 26%, and you pay that on all taxable income up to $59,180. Every dollar of taxable income *over* $59,180 is taxed at the top federal rate of 29%. Your marginal tax rate is the rate you paid on the *last* dollar you earned.

- **tax brackets:** Refers to the particular statutory tax rates for various income levels. Currently, Canada has three federal income tax brackets for individuals earning wages or salaries: 17%, 26% and 29%.

- **flat tax:** Refers to an income tax rate that is the same for all levels of income. There would be only one tax bracket, applying to everyone.

- **bracket "creep" and tax "indexing":** Up until 1985, the income threshold for moving from a lower into a higher tax bracket was indexed to inflation. This meant that, if your income just kept pace with inflation, you would not be pushed into a higher tax bracket. Let's say your income was $30,000, the threshold at which you paid 15%, and above which you paid 20%. Let's also assume that inflation for the year was 5% and your income just kept pace—increasing to $31,500 with no increase in buying power. If personal taxes were fully indexed, the threshold for moving into the higher bracket would move you up to $31,500 in the next tax year. You would still be paying the same tax rate (15%) because you had no "real" increase in income. But in 1985 indexing limited to inflation above 3%. Continuing our example, the threshold would only increase to $30,600 and you would pay a higher (20%) rate on the amount over $30,600, or $900: a tax increase of $45. This is bracket "creep"—the process by which a higher tax bracket creeps incrementally lower each year by an amount equal to inflation. Brackets have been creeping in this way since 1985, in effect increasing the effective tax rates paid by all Canadians.

- **tax expenditures:** In lay terms, these are called tax breaks, incentives, or, pejoratively, loopholes. They are government spending programs that are delivered through the tax system. Instead of handing a corporation a grant, a tax expenditure might allow a special tax deduction for research and development. The tax reduction is the equivalent of a government expenditure. Another very large tax expenditure is the RRSP deduction. It is a government "expenditure" because it is the equivalent of paying you the amount you save on your income tax.

- **financial transactions tax:** Such a tax, not implemented in Canada as yet but in place in several countries, would tax every domestic financial transaction from stocks and bonds to currency trades, just as goods and services are now taxed, though at a much lower rate.

Myth 1
"Canadians are overtaxed."

This declaration fits the classicmodel of propaganda: a deliberately oversimplified statement designed to elicit an emotional response instead of a rational one. It generates resentment at government, implies a whole range of bad intentions from irresponsible politicians and a "bloated" bureaucracy, and promotes isolation between government and citizens.

This blanket declaration begs many questions. Which Canadians are overtaxed? All, or just some? Overtaxed compared to what and whom? Other countries? Does it mean we are overtaxed compared to what we get for our taxes? Compared to what we *used* to pay in taxes? Overtaxed in relation to the revenue we need for good public services? Or might it mean, if we actually examine the situation, that low-income Canadians are overtaxed compared to wealthy Canadians and large corporations?

This deceptively simple statement that we are overtaxed is designed to make people jump to the simple answer: lower "our" taxes. Such a solution ignores all the above questions about public services, tax fairness, and the overall objectives of a tax system. That makes a real debate about taxes more difficult, allowing governments to reduce taxes on high-income earners and corporations without public opposition—which is exactly what happened in the 1980s.

The assumption implicit in the blanket statement is that tax levels, particularly on middle-income families, are still rising. This is simply not the case. To be sure, the total amount of personal income taxes collected by Ottawa and the provinces has been rising in recent years (although it is projected to fall in the next few years because of tax cuts introduced in the 1998 and 1999 budgets).

In 1995, the total personal income tax bill was about $94 billion. In 1996, that figure rose to $99 billion. This increase, however, largely reflects growth in the economy and the extra taxes collected from *high-income* individuals as a result of large increases in capital gains and dividend payments. As Table 1.1 reveals, while the total income assessed by Revenue Canada rose 3.6% between 1995 and 1996, the largest increase by far came in the form of taxable capital gains, the vast bulk of which were earned by people at the top of the income ladder.

Table 1-1
The Rise in Tax Revenue

	1995	1996	% change (1993-96)
Total Number of Tax Returns	20,514,590	20,805,980	1.4
Employment income ($)	346,341,166	354,167,957	2.3
Capital Gains ($)	7,471,180	9,834,166	31.6
Taxable Dividends ($)	9,312,338	10,335,607	11.0
All Income ($)	530,085,394	549,101,590	3.6

Source: Author's calculations based on Revenue Canada data.

Table 1-2
Percentage of household budget spent on four major categories, 1997

	Lowest quintile	2nd quintile	3rd quintile	4th quintile	Highest quintile
Food	18	15	13	11	9
Shelter	32	24	21	19	16
Transportation	11	14	13	13	11
Personal income taxes	3	10	17	21	30

Source: Statistics Canada

Employment income rose just 2.3%, a figure that barely kept ahead of the increase in the number of tax filers. In short, a disproportionate share of extra tax revenue has been coming from upper-income earners profiting from a booming stock market and larger bonuses. These developments have little effect on middle-income earners, yet that is precisely what many tax critics have presumed.

To further support their claim that Canadians are over-taxed, anti-tax crusaders routinely make reference to the "average taxpayer" to illustrate their argument. The right-wing Fraser Institute uses this approach to make the case that personal income taxes now make up the largest share of average household spending. And statistics do appear to show that, on average in 1997, Canadian families spent 21 cents of every dollar on personal income taxes, followed by 20 cents for shelter, 12 cents for transportation, and 11 cents for food.

There is a problem, however, in using averages this way, which is easily explained by the following example. Suppose four families with $30,000 incomes each pay $4,500 in income tax—or 15% of their incomes. Now, add in a wealthy family with $250,000 in income that pays $92,500, or 37% of its income. Using an approach based on averages, one would conclude that these five families pay an average 30% of their income on taxes (total tax payments of $110,500 divided by total income of $370,000 equals 30%). The trouble is that the 30% figure is completely misleading. The majority of people (the four middle-income families) pay 15% of their income in income tax, not 30%.

So, based on *averages,* Canadians appear to spend more on personal income taxes than any other expenditure, but the truth is that most of us do not. Table 1.2 illustrates the percentage of household budgets spent on food, shelter, transportation, and personal income taxes. Rather than using averages, however, the data are broken down into five equal-sized income groups or quintiles, ranging from the 20% of households with the lowest income to the 20% with the highest income.

Using this approach, we find that, for 40% of Canadian households, income taxes represent the *smallest* share of expenditures. For the third or middle quintile, shelter remains the largest expenditure. In fact, it is only for the top two income groups that taxes are the major household expenditure. When critics use averages to describe taxes paid by Canadians, it produces skewed results that ascribe tax rates to the average person that are in fact paid only by taxpayers at considerably higher income levels.

Nevertheless, there is no question that some Canadians are overtaxed. Tens of thousands of low-income Canadians end up with income tax bills. Between 1980 and 1990, the average income tax rates increased for all quintiles, but the largest proportionate increase was for the lowest quintile—an increase of 43% (from 2.3% to 3.3%). Consequently, the overall progressivity of Canada's income tax system, when measured as the ratio of the effective rate payable by the top quintile to that payable by the bottom quintile, declined from 1980 to 1990. It has only been in the 1990s that the ratio has widened again.

What about wealthy Canadians? Are they overtaxed? It's true that wealthier Canadians pay a greater share of their taxable income in taxes—that, after all, is the principle of progressive taxation. Revenue Canada figures for the 1996 tax year show that those Canadians with taxable income above $250,000 paid on average about 37% of that in federal and provincial income taxes. Canadians with taxable incomes of between $30,000 and $40,000,

Table 1-3
Effective Income Tax Rates by Quintiles, 1980-1997

Year	Lowest	Second	Third	Fourth	Highest	Ratio of top quintile to bottom
1980	2.3	9.7	14.0	16.2	19.8	8.6
1985	2.3	9.4	14.3	17.4	21.4	9.3
1990	3.3	12.0	17.5	20.5	25.5	7.7
1993	2.6	10.6	16.6	20.0	25.1	9.7
1997	3.1	11.4	17.5	21.1	26.0	8.4

Source: Statistics Canada, Income after tax, distributions by size in Canada, 1997.

by contrast, paid just over 15% of their income in taxes.

However, this doesn't give us the complete story, since these rates are based only on *taxable* income. Many wealthy Canadians have income from sources not taxed, such as inheritances and gifts. In fact, Canada eliminated its inheritance tax in 1970. When you include these other sources of income and wealth, then wealthy Canadians are clearly *undertaxed* when compared to other groups.

As a broad-based share of all sources of income, Canadians with income over $300,000 paid just 14.4% of that in personal income tax. That's only slightly more than what people earning $50,000 paid.

Are corporations overtaxed? Corporate lobbyists complain loudly that governments are undermining their profitability through taxes. But this is far from the truth. The corporate tax rate fell dramatically throughout the 1950s and 1960s, and has remained fairly stable since the 1970s. Perhaps most importantly, Canadian corporate income taxes compare favourably with those of other countries, including the United States.

Are we overtaxed with respect to the other developed countries to which we normally compare ourselves? The question is far more complex than commonly assumed. International tax comparisons raise countless problems. Tax rates are notoriously difficult to measure on a strictly comparative basis, since numerous tax expenditures, credits, shelters and write-offs can significantly lower the amount of tax actually paid. Consequently, many researchers measure effective tax rates, most commonly by calculating total tax revenue as a share of GDP.

By this approach, Canada comes in right in the middle of the pack—higher than some, but lower than others. Nevertheless, even with this approach, problems continue to abound. What is classified as a tax in one country might be classified as a user fee in another. The costs of what is provided as a publicly-funded service in one nation may have to be borne privately in others. Some countries even include in their revenues taxes paid by governments themselves, such as sales taxes on purchases.

Problems arise even when we compare ourselves to the United States. While the overall tax burden is higher in Canada, it does not necessarily mean that all Canadians are left with less disposable after-tax income than their American counterparts. The OECD records that the disposable income of families earning the average industrial wage, expressed as a percent of gross pay, is actually higher in Canada than in the United States.

Other data confirm this. In 1995, the median family in Canada had $30,200 to spend after taxes, compared with $29,500 for the median U.S. family (both in Canadian dollars). The Canadian family is even better off than the $700 difference because it has already paid for health care in its taxes, while the American family may have to pay private premiums or bear the costs of sizeable medical bills if it is among the 43 million Americans without health insurance.

Moreover, the other burden faced by American families is the cost of education. Most private colleges charge tuition fees of US$25,000. State schools charge considerably less, but still average more than tuition at Canada's colleges and universities.[1]

How do we determine if we are overtaxed? How much tax revenue does Canada require to meet the needs expressed by the majority of its citizens? This is a complex question tied to issues of Canadians' values, their commitment to community, their strong support for Medicare and public education, the protection of the environment, and decent pensions. And, in answering the question of how much revenue do we need to pay for desired public services, we must ask: just how should we raise that revenue?

Most Canadians have always displayed a strong commitment to the principle of fairness, and that principle must be key to any tax system designed to meet the needs of society and community. That principle of fairness was enshrined historically in the principle of taxing people based on their ability to pay—i.e., a progressive tax schedule that charged increasingly higher tax rates as income increased.

Much of our revenue leaks out of the system by means of what are called tax expenditures—incentives, breaks and tax shelters. Many of these tax breaks are provided disproportionately to wealthy individuals and corporations. As Table 1.4 shows, those earning over $80,000 a year, while making up just 2.9% of all tax-filers, claimed 21.5% of all RRSP and RPP deductions and 83% of all capital gains deductions in 1996.

Ordinary working Canadians are paying more and getting less because regressive changes in the tax system in the 1970s and 1980s reduced revenues to such an extent that Canada began to build up significant annual deficits. Businessmen were allowed to deduct the cost of expensive lunches as business expenses; developers are still allowed to claim a depreciation expense, even though their buildings are appreciating in value; corporations are able to depreciate their capital assets faster for tax purposes than they do for purposes of their own financial statements.

The Bank of Canada's ill-considered high interest rate policies in the 1980s caused those deficits to balloon because the government had to pay those high rates on the money they borrowed to service the deficits.

The interest on that debt is being paid largely from working Canadians' taxes and goes almost exclusively to financial institutions and wealthy investors. Ironically, wealthy Canadians gain at both ends of this so-called debt crisis. They gain, first, by having their taxes lowered (helping to cause the crisis by lowering government revenues) and secondly, by reaping the investment benefits of interest payments on the bonds the government had to sell to make up for the lost revenue.

As we will see in the remainder of this study, the Canadians who are truly overtaxed are poor and working Canadians whose tax burden has increased dramatically over the past 15 to 20 years. Here are just some of the numbers that show how low-income Canadians have seen their tax burden increase.

- The principle of progressive taxation based on ability to pay is virtually dead in Canada after 20 years of neo-liberal tax reform. Taking all taxes into account, Canada now has a nearly flat tax system, with everyone paying a similar percentage of their income in taxes.

- In part because of the tax system, wealthy Canadians have gained an ever-increasing share of the

Table 1.4
RRSP/RRP and Capital Gains Deductions, 1996

Income Level	% of all tax filers	% of total RRSP and RPP deductions	% of total capital gains deduction
Less than 20K	52.4	5.6	1.2
$20K - 40K	27.8	27.7	4.1
$40K - 60K	12.6	31.4	6.7
$60K-80K	4.4	17.6	5.3
$80K - 100K	1.3	11.0	5.1
$100K - 150K	0.9	5.9	14.4
$150K - 250K	0.4	2.9	24.9
$250K +	0.3	1.7	38.5

Source: Calculations based on Revenue Canada data.

total national income since the early 1970s. In 1993, the top 30% of income earners in Canada took home $14.3 billion more income than they would have, had their percentage share of national income stayed the same as it was in 1973. Virtually all of this extra income was transferred from the bottom 50% of income earners.[2]

- One way of looking at the fairness of the tax system is to examine the distribution of wealth. A progressive tax system is supposed to even out incomes over time by taxing high incomes at a relatively higher rate. But Canada's unbalanced system has allowed the high-income earners to become extremely wealthy, and the gap keeps growing. Although statistics Canada has not conducted a wealth survey since 1984, according to recent estimates, the wealthiest 1% of Canadians owned 25% of all wealth and close to 40% of all financial wealth (i.e. stocks, bonds, etc.).[3]

Are Canadians overtaxed? It depends. On what we want taxes to pay for, on how fair we want our society to be, on how we stack up to the other developed nations we normally compare ourselves to, on what the actual effect of various taxes is on economic growth and sustainability.

It depends, ultimately, on what values we choose to have as a people and how we incorporate those values into public policy. The question should be reformulated: **"Does our tax system reflect the values, aspirations and needs of the majority of Canadians and their communities?"**

Myth 2

"We have one of the highest tax rates among the 29 countries in the OECD—the Organization for Economic Cooperation and Development—and the G-7."

This allegation has been repeated over and over again by business representatives and conservative media pundits, to the point that it is now the conventional wisdom. While it shows that business thinks it appropriate to compare Canada to other OECD countries, the claim itself is completely false—and always has been. As Table 2.2 illustrates, Canada places very close to the middle of the OECD countries, no matter what kind of tax is compared—a ranking that has been steady for many years. If we compare ourselves to European countries, we collect a lower percentage of our GDP in tax revenue.

- The OECD's 1998 report (based mostly on 1996 figures) shows that Canada's total tax revenue equals 36.8% of its GDP. That's just below the average for the entire OECD, but below the European average of 42.4%. Fourteen countries collected more than Canada, and 14 countries, including the U.S., collected less.
- As a share of GDP, Canada collected a higher portion of its total tax revenue from individuals than the OECD average: 13.9% compared with 10.1%. This means that Canada relies more on the personal income tax system for its revenues, and less on regressive levies like sales taxes and social security contributions.
- Our payroll taxes—e.g., UI and Canada Pension Plan contributions—are about 25% less than the OECD average, and are the lowest of any of the G-7 countries.
- Canada collects less of its revenue from taxes on goods and services—provincial sales tax, the GST, gasoline, liquor and tobacco taxes—than the OECD average, 9.1% versus 12.3%. Of the G-7 countries, only the U.S. and Japan collect less.
- The OECD figures do not take into account Canada's public investments in health and education. A study by Standard and Poors DRI found

Table 2.1
Tax Revenue as a share of GDP, 1996

	Personal Income Tax	Corporate Income Tax	Social Security	Taxes on Goods and Services	Other Taxes	Total Tax Revenue
Canada	13.9	3.3	5.9	9.1	4.6	36.8
United States	10.7	2.7	6.7	4.9	3.5	28.5
European Union	11.0	3.2	11.2	13.3	3.7	42.4
OECD average	10.1	3.1	8.4	12.3	3.8	37.7

Source: OECD Revenue Statistics, 1965-1996.

Table 2.2
How Canada Compares Internationally (1996)

	Total Taxes (% of GDP)	Highest Personal Income Tax Rate	Lowest Personal Income Tax Rate	Average Disposable Income (% of gross pay)
France	45.7	54.0	41.7	78.6
Italy	43.2	46.0	37.0	74.5
Germany	38.1	55.9	58.2	77.9
New Zealand	35.8	33.0	33.0	83.8
CANADA	36.8	54.1	46.1	81.8
UK	36.0	40.0	31.0	76.5
Japan	28.4	65.0	50.0	90.4
USA	28.5	46.6	39.5	81.7
Mexico	16.3	35.0	34.0	98.6
OECD Average	37.7	47.8	35.1	85.1

Source: OECD in Figures, 1998.

that, "[o]nce private medical and education expenditures are added to total government receipts, the difference between Canada and the United States disappears."[4]

- In terms of high marginal tax rates on individuals, Canada again places close to the middle, with 10 countries having higher marginal rates on high income earners. The OECD only measures taxes on income, not wealth, and thus does not take into account inheritance taxes which all but three OECD countries impose on upper-income individuals. About half of these countries also have a yearly tax on net worth. Canada has neither of these taxes, and as a result our mid-range marginal income tax rate actually exaggerates the tax burden placed on high-income earners because their accumulated wealth is never taxed.

- Disposable income after taxes is a good measure of the tax paid by individuals. Measuring this figure for a family with two children, Canada's average disposable income is 81.8% of total income. Again, this is just slightly below the OECD average of 85.1%, and higher than the U.S. Fifteen countries have a higher disposable income as a percentage of total income, and 13 have lower.

While these OECD figures are useful to know, given the frequent repetition of this tax myth, they are not particularly meaningful unless we also compare what we get for those taxes. For example, while our governments collect a higher portion of GDP than does the U.S., we get a great deal more in government services, most significantly universal, publicly-funded Medicare. Americans pay an enormous amount for their profit-oriented medical care system (whose overall per capita cost is 50% higher than ours to account for the high administrative costs and the profits being made).

The same is true of education, although Canada is headed in the wrong direction in education spending. A meaningful comparison of taxes paid would add the costs of Medicare to the average American family's tax bill.

We pay less in taxes as a percentage of GDP than do people in most European countries, but they in turn enjoy social programs of far greater generosity and comprehensiveness for their higher taxes. Most of the more developed countries in Europe have social programs that Canadians can only dream of: Universal, publicly-funded child care; maternity leave with full or nearly full pay for all working mothers; weeks of legislated time off to care for sick children; up to twice the number of weeks of paid vacation; well-funded universities with low or no (as in Britain, even under Thatcher) tuition fees. Our UI program now ranks below even that of the U.S., and is one of the most miserly of the OECD countries.

Myth 3

"Taxes on corporations in Canada are too high, especially compared to those in the U.S., discouraging foreign investment and even driving corporate investors from the country."

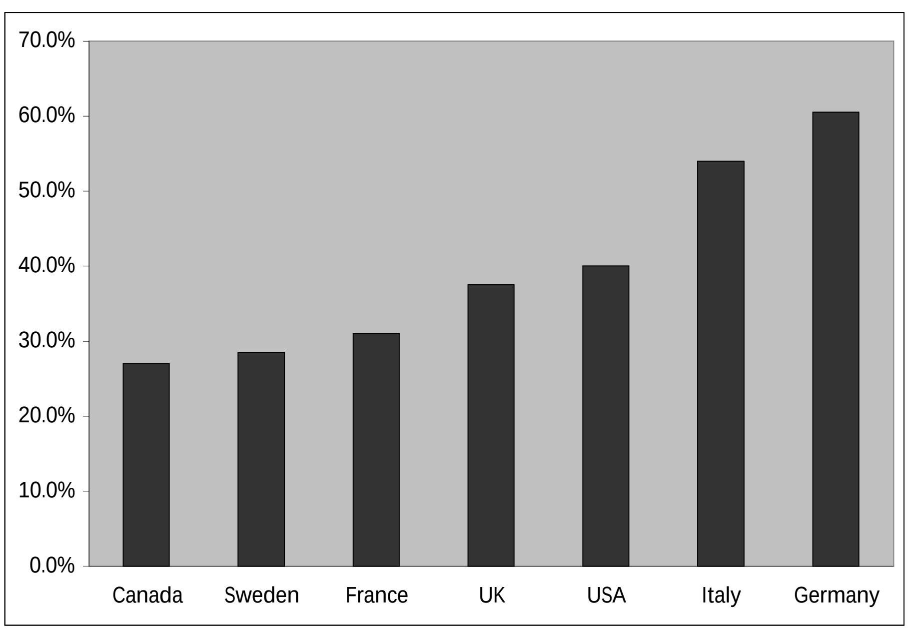
This argument fails to stand up to scrutiny, for three reasons.

First, it assumes that taxes are a major factor in a company's decision regarding whether or not to invest. Surveys of CEOs making actual decisions on where to invest and locate show that taxes rank from 5th to 7th place in terms of priority, behind things like an educated labour force, access to resources and markets, electricity costs, land costs, borrowing costs, labour costs, the strength of the local currency, and social infrastructure and quality of life. As we will see below, Canada does extremely well in these categories compared to our competitors.

Secondly, even if taxes were a critical factor in investment decisions, we still compare very favourably in terms of our actual tax rates on corporations. When examining virtually every kind of tax that is regularly identified as slowing down investment or preventing job creation, Canada's taxes are very competitive, particularly with those in the U.S., to which we are most often compared unfavourably.

Thirdly, the attack on taxes is very often aimed at their alleged negative impact on foreign investment. Yet this argument uncritically accepts the assumption that all foreign investment is good for Canada, all the time. This simply isn't supported by the evidence. Foreign investment can enhance areas of the economy that need development, or it can simply capture the domestic market and send prof-

Effective Combined Corporate Income Tax Rate (percentage of net profit before tax)



Source: "The Competitive Alternative: A Comparison of Business Costs in Canada, Europe and the United States," KPMG, published by Prospectus Inc., October 1997.

its out of the country. In profitable domestic sectors, it can even drive local investors out of business, as Wal-Mart has done.

Trying to make Canada "attractive" to foreign investors by lowering taxes can mean we lose both ways. We undermine our ability to collect the tax revenue we need for social programs, and we encourage predatory investment in which foreign corporations simply buy up existing Canadian operations.

- A number of studies undertaken by the Canadian international accounting and management consulting firm, KPMG, reveal that taxes affecting corporations in Canada are extremely competitive with those in other developed countries. The 1997 KPMG study, "The Competitive Alternative," compared the costs of doing business in Canada, the U.S., the U.K., France, Germany, Italy and Sweden.[5] It showed that Canada had the lowest effective corporate income tax rate—i.e., the tax rate actually paid after all the tax breaks and credits were deducted. Canada's rate (which included federal and provincial taxes) was 27.4%. The U.S. rate was 40%, good for fifth place and nearly 50% higher than Canada's. Sweden was second lowest with 28.5%.

- Germany and France had high rates of corporate taxation (60.5% and 54% respectively). But neither of these countries is considered "uncompetitive" with Canada or the U.S. in attracting investment. This demonstrates the point argued earlier: that corporate income tax levels are well down the list of factors considered by corporations when they are deciding whether or not to invest.

- The same KPMG study showed that two other taxes that are often the target of criticism by corporate think-tanks and business associations are relatively low in Canada. Payroll taxes—nearly always described as "job killers" because they are paid regardless of how well a company is doing—are actually low in Canada, both as a percentage of all tax revenue and in comparison with our major competitors. In particular, they are 30% lower than they are in the U.S.

- The third type of tax that affects corporations is local property taxes, and here, too, Canada is very competitive. In the KPMG study, Canada had the lowest property taxes among the five countries that levy such taxes. The Canadian average was $2.16 per square foot, compared to the next cheapest, the U.S. Its property tax rate averaged $2.92, 35% higher than Canada's.

- The OECD's 1997 analysis lumped all other taxes, including capital taxes, together under "other" and in this category Canada was slightly higher than the OECD average, but virtually identical to our main competitor, the U.S.

Foreign Direct Investment

Over the past 20 years, the Canadian government, mimicked by most provincial governments, has transformed the Canadian economy in an effort to compete in the global economy. Both Tory and Liberal governments have followed a policy of deliberately high unemployment to keep inflation and labour costs down, have allowed minimum wages to drop well below the poverty line, and have gutted the UI program so that fewer than 36% of those who pay premiums are actually eligible for UI when they lose their jobs. And they have signed free trade deals.

All of this was in an effort to "create the conditions" for private enterprise to invest. And now they want to lower taxes, too. It is hard to believe that this will bring the promised prosperity, any more than the other measures listed above. In fact, Canadian workers are far worse off now than they were 15 years ago and have seen their real (after inflation) incomes actually decline over that period.

If we examine the impact of foreign direct investment (FDI), this trend is not surprising. One figure used repeatedly among advocates of being "open for business" is the claim that, for every billion dollars in foreign investment, Canada gains 45,000 jobs over the succeeding five years. But this figure is simply not credible. It ignores too many questions, most importantly, what kind of foreign investment? Foreign direct investment can include new plant and equipment, buying up existing factories, or buying shares in publicly-traded companies.

Figures from Industry Canada's Investment Review Division (IRD) suggest that FDI in Canada actually creates very few jobs. Examining the actual investments made by foreign corporations, the IRD identified $21.2 billion in foreign investment in Canada in 1997, the second highest on record. This suggests, first of all, that Canada is having no trouble attracting foreign investment. But, more importantly, the analysis shows that 97.5% of that investment was directed at "acquisitions"—i.e., the takeover of existing Canadian companies. Just 2.5% was invested in new productive capacity. Over a 12-year period, from 1985 to 1997, 93.4% of the $183.6 billion in foreign investment went to acquisitions.[6]

In most cases, such acquisitions actually result in a **decrease** in jobs as the new owners pay for the cost of their acquisition by laying off workers. But, in any case, even using the analysis of those promoting FDI, only $530 million of the $21.2 billion was new—creating under 24,000 new jobs over five years, fewer than 5,000 jobs a year. This is a minuscule number, given that there are about one-and-a-half million Canadians out of work, and especially insignificant given the decline in our standard of living that is the indirect cost of trying to attract such investment.

We are asked to accept the notion that taxing corporations is somehow counterproductive, without recalling that corporations get a lot for the taxes they pay: an educated, healthy, secure work force; one of the best communications system in the world, much of it public or publicly subsidized; a very large domestic market; easy access to the U.S. market, the largest in the world; and political and social stability. These are things that corporations cannot buy at any price in many countries in the world. Why should they get them for free or at a discount here in Canada?

Myth 4

"The standard of living of ordinary Canadian working people has decreased over the past 20 years, and rising taxes are largely to blame."

There is no question that poor and low-income Canadians are unfairly taxed, compared to wealthy Canadians and large corporations. But, in examining inequality in Canada, it is not primarily the tax system that impoverishes people. While the income tax structure is far less progressive than it was in the 1960s and 1970s, it still has the effect, along with government transfers, of modestly evening out incomes in Canada (see Table 4.1). Without income taxes and transfers, the gap between the top and bottom 20% of income earners would be four times greater than it is.

The principal source of the decreasing living standards is the decline in personal income, largely as a result of the poor labour market. Average after-inflation personal disposable incomes were no higher in 1997 than they were in 1980. In fact, they declined by over 7% between 1990 and 1997. While this drop is routinely ascribed to higher taxes, Table 4.2 shows that it has been the decline of *before-tax* incomes that is the principal factor behind the fall in disposable income.

Average personal taxes per capita rose by just $177 in real terms between 1990 and 1997—hardly grounds for a tax revolt. Meanwhile, in the face of growing unemployment, reduced wages, and government cutbacks to UI and income assistance, before-tax income plunged by $1,129.

The lowered standard of living of Canadian workers is actually the result of a deliberate policy of governments to lower the wage and salary rates of Canadians in order to weaken the power of labour vis-à-vis capital. Policies maintaining high levels of unemployment mean that millions of workers compete for an inadequate number of jobs, and they compete by accepting less pay that they would in an economy closer to full employment.

Systematically reducing labour costs is also part of the government's strategy to become "internationally competitive" by restructuring the Canadian economy along the lines of free trade and liberalized investment rules. This strategy has made it easier for capital and goods (and good jobs) to move freely across borders.

This effort to suppress wages and salaries, and to weaken social programs that support working people, goes back to the mid-1970s. Years of strong union organizing and aggressive collective bargaining meant that working people had actually made major gains and shared a bigger slice of the economic pie. That meant there was less for the owners of capital—corporations and their shareholders. Profits slipped and there was a determination by influential corporate leaders to reverse the trend and recapture capital's historic share of wealth.

The means chosen to reach this goal was the pursuit of what has become known as "labour flexibility." Corporations began a concerted move away from providing the traditional job—40 hours a week, 9 to 5, on weekdays—and towards temporary, just-in-time, and part-time jobs, and to sub-contracting by large firms. And they successfully pressured governments to pass legislation and regulations that made such "flexibility" possible.

Free trade and NAFTA have restructured the economy to such an extent that Canada now has the highest proportion of low-paid jobs of any of the 29 industrialized countries. While literally millions try to put together a series of temporary and part-time jobs to survive, others are overworked through forced overtime. The Canadian economy is increasingly characterized by a good job/bad job phenomenon.

The impact is especially dramatic when it comes to young workers, particularly young men. According to a study by the Centre for Social Justice, young men's earnings are declining relatively and absolutely, regardless of education level, geographic area, or the industry they work in. This trend continued even during the boom period of the 1980s and when the economy came out of recession in the min-1990s.

- The relative market incomes of the top 10% and bottom 10% in Canada have gone through a staggering change in the past 25 years. In 1973, the top 10% of families with children under 18 earned an average income 21 times higher than the those 10% at the bottom ($107,000 compared to $5,200 in 1996 dollars). By 1996, the top 10% made 314 times as much...(an average $136,737 compared to an average market income of less than $435).[7]

- In just seven years, between 1989 and 1996, the number of firms using part-time workers rose from 33% to 50%. Part-timers made up 29% of the average firm's work force, three times the figure for 1989. In 1997, 20% of workers worked part-time, compared to half that percentage in the mid-1970s.[8]

- In 1995, just over half of Canadian workers were employed in traditional 35-hours-per-week jobs, compared to 67% in the mid-1970s.

- Part-time and temporary workers lose out, not only because of lower pay and financial insecurity, but because under current labour standards laws employers are not obliged to pay them fringe benefits such as paid holidays, maternity leave, sick leave, and the other benefits that full-time employees might enjoy, such as health and pension benefits.

- In 1996, 5.4 million Canadians earned less than $10,000 in the private market economy.

- Canada has the second highest incidence of low-paid jobs—23.7%—among the 29 industrialized nations of the OECD), second only to the

Table 4.1
Family Income Shares, Before and After Taxes and Transfers, 1997

	Market Income	Income After Tax and Transfers
Lowest Quintile	2.1	7.4
Second Quintile	10.1	13.2
Middle Quintile	17.7	18.1
Fourth Quintile	25.8	23.9
Highest Quintile	44.3	37.5
Ratio of Highest/Lowest	21:1	5:1

Source: Statistics Canada, Income after tax, distributions by size in Canada, 1997.

Table 4-2
Household Incomes, Spending, and Saving ($1,992 per capita)

	Personal Income	Personal taxes	Consumer Spending	Saving	Saving Rate
1990	$22,491	$5,107	$15,450	$1,934	11.1%
1997	$21,362	$5,284	$15,816	$262	1.6%
Change	-$1,129	+$177	+$366	-$1,672	-9.5 pts.
Proportion of decline in savings accounted for by:	68%	11%	22%		

*Source: Jim Stanford, **Paper Boom** (Ottawa: CCPA/Lorimer), 1999.*

U.S. at 25%. The comparable figure for New Zealand is 16.9%, France and Germany 13.3%, Italy 11.9%, and Sweden 5.2%. (Low-paid is defined as less than two- thirds of the median earnings for all full-time workers.)[9]

- Workers in the bottom 20% of income earners saw their average market income drop from $7,817 in 1984 to $5,325 in 1994, an astonishing 31.9% decrease. In the next fifth, incomes declined from $29,276 to $26,291. The third fifth lost some income, as well. If this 60% of the Canadian work force had maintained its 1984 share of national income, they would have had an additional $5.2 billion in 1993.[10]

While employers have been putting an ever-tighter squeeze on employees, governments have aided and abetted this process by not adjusting labour laws to protect this new just-in-time work force. For example, they could pass laws requiring employers to provide benefits on a pro-rated basis to part-time workers, as an incentive to hire full-time workers. They could make overtime voluntary, opening up jobs for the unemployed, and implement a shorter official work week, thus lowering the overtime threshold.

Not only have governments not made these positive changes, but they have actually made life even more insecure for wage-earners by gutting existing laws on welfare, minimum wage and UI, which are intended to give working people a measure of economic security not provided by the unregulated private labour market.

- In 1978, the minimum wage levels in every province and in the federal jurisdiction provided an income above the poverty line—up to 118% (in Saskatchewan). By 1994, not a single minimum wage in Canada provided an income above the poverty line. The best was 89% in Ontario; the worst, the federal government, was at 53%.[11]

- Welfare rates in Canada have become cruelly low and, despite the image of the U.S. as having worse social programs, Canada has now surpassed the U.S. for punitive welfare rates. Almost one-third of U.S. states are more generous than our most generous provinces.[12]

- Unemployment Insurance, a major safety net for people losing market income, has also been slashed to levels below those in many U.S. states. On average, just 36% of those who pay into the fund are now eligible to collect when they lose their jobs, compared to 74% in 1989. The benefit levels for some workers is as low

Table 4.3
The Permanent Recession

	The "Golden Age"	The Age of "Permanent Recession"	
	1950-1960	1981-1997	1990-1997
Real interest rates, short term (%)	0.9	5.6	5.1
Real interest rates, long term (%)	1.6	6.5	6.8
Change in gov't program spending (as % of GDP)	+16.3	+1.1	-2.5
Average annual real GDP growth (%)	4.7	2.4	1.8
Average annual employment growth (%)	2.8	1.1	0.5
Average unemployment rate (%)	5.4	9.8	10.0

*Source: Jim Stanford, **Paper Boom** (Ottawa: CCPA/Lorimer),1999.*

Table 4.4
Average Family Income Before Transfers (Families with Children) ($1996)

	1973	1984	1990	1996	% change 1973-90	% change 1990-96
Bottom 5th						
Decile 1	5,204	2,062	2,760	435	-47	-84
Decile 2	19,562	14,930	16,599	11,535	-15	-31
Middle 5th						
Decile 5	40,343	42,495	46,477	42,829	+15	-8
Decile 6	46,136	49,664	54,561	51,494	+18	-6
Top 5th						
Decile 9	71,611	79,628	88,426	86,497	+23	-2
Decile 10	107,253	123,752	134,539	136,737	+25	+2

Source: Centre for Social Justice

as 25% of lost income, a far cry from the 70% the program was originally designed to pay.[13]

- Cuts to medicare, education and municipal services, and sky-rocketing tuition fees for post-secondary education, mean that services that were once almost completely public are becoming increasingly privatized, taking money out of the pockets of working people and their children.

Taxes do play a role in the decreased standard of living of low-income Canadians. Families earning $10,000 should not be paying any income tax. Bracket creep, whereby inflation pushes people into a higher tax bracket, even when real income down not go up, has hurt millions of working people. But the general decline in living standards is caused primarily by corporate pressure on wages, Ottawa's high unemployment policy, massive cuts to social programs and the social safety net, and free trade deals that allow companies to threaten to leave the country if their employees don't accept management's demands for wage freezes and rollbacks.

Myth 5

"Canada needs a flat tax. Our current income tax system penalizes high-income people. This results in a 'brain drain' to the U.S., and it discourages wealthy individuals from investing."

In fact, Canada's income tax system is not very progressive any more, which means that high-income people are not being taxed excessively, or even appropriately. After years of regressive tax changes, the income tax system now has just three personal tax brackets—17%, 26% and 29% (the provinces add between 45-52% of these rates). The highest marginal rate combining both (as well as various surtaxes) is 53.7% in Newfoundland. This compares to 10 different tax brackets and a top marginal rate of 80% on very high incomes in the 1960s. Tax reform by the Mulroney government raised the lowest rate and decreased the highest rate when it reduced the number of brackets from 10 to three in the mid-1980s.

As noted above, when all taxes (income, GST, payroll, property, sales tax) are taken into account, Canada already has a virtually flat tax system. In other words, everyone pays nearly the same rate of tax, regardless of income. We can illustrate this by looking at some concrete examples.

Let's take the case of three families of four living in British Columbia. All three families have two income earners. One family earns $30,000, the second $55,000, and the third $90,000. The two-income family with $30,000 is assumed to have each spouse earning $15,000; the family with $55,000 is assumed to have one spouse earning $35,000 and the other $20,000; and the family with $90,000 is assumed to have one spouse earning $50,000 and the other $40,000.

It is further assumed that each family pays CPP and UI premiums, as well as federal and provincial income taxes based on basic personal credits, applicable provincial credits, and typical major deductions at each income level. Each family owns a home and pays property tax amounts based on the Canada Mortgage and Housing Corporation review of prop-

Table 5-1
Taxes Paid by Three Families, British Columbia, 1998

	$30,000 income	$55,000 income	$90,000 income
Federal income tax	2,347	6,191	13,176
Prov'l income tax	1,162	3,065	6,522
Child Benefits	(766)	0	0
Net property tax	1,168	1,168	1,168
Prov'l sales tax	480	724	969
Fuel tax	165	165	165
Net GST	266	1,086	1,454
Health premiums	691	864	864
CPP	736	1,536	2,138
EI	885	1,623	2,106
TOTAL TAXES	**7,134**	**16,422**	**28,562**

Source: Calculations based upon Revenue Canada and Government of British Columbia, Budget Reports 1999

Table 5-2
Taxes as a Share of Family Income, 1998

	$30,000	$55,000	$90,000
Net income taxes	9.1%	16.8	21.9
Sales and fuel taxes	3.0%	4.0	2.9
Property taxes	3.9%	2.1	1.3
Social Security and Health Premiums	7.7%	7.3	5.7
Total taxes	23.8%	29.9	31.7

Source: As in Table 5.1.

erty taxes buyers are likely to pay in major cities in each province. Sales and fuel tax estimates (including sales tax on meals, liquor and accommodation) are calculated based on expenditure patterns from Statistics Canada's 1996 Survey of Family Expenditures. GST estimates are reduced by the GST credit, where applicable. The total tax bill for each family is shown in Table 5.1.

Table 5.2 presents the taxes paid by the three families as a share of their total income. From this, it can be seen that the personal income tax system is relatively progressive—i.e., that the effective rates at which tax is applied rises along with income. On the other hand, sales and fuel taxes as a share of total income remain the same among all three families, while property taxes and social insurance premiums are clearly regressive. Consequently, when all taxes and premiums are added up, the overall progressivity of the personal income tax system is muted.

Yet there are proposals in Canada for a completely flat income tax system that would make an already inequitable situation even worse. The Alberta government announced in March, 1999, that it would phase in such a system by the year 2002. It would be the first provincial government to decouple its income tax system from the federal government's system. Currently, provinces base their tax system on a percentage of the federal income tax.

Alberta's planned flat tax system would impose a flat provincial rate of 11% on all income earners. Critics have pointed out that middle-income earners, who pay most of the tax revenue, get very little relief, while the wealthiest Albertans gain a great deal. A single person earning $30,000 will get a tax break of $16 a year, whereas a single person earning $250,000 will get a break of over $6,000.

While the Alberta government says the plan will knock 78,000 low-income people off the tax rolls, this could be done without introducing a flat tax. Most of the $600 million in sacrificed revenue from the new tax structure will find its way into the hands of high-income earners.[14]

An examination of the arguments put forward by flat-tax promoters shows that none of them stand up to any sustained scrutiny. According to Osgoode Hall Law professor Neil Brooks, flat tax proponents claim to want greater simplicity, but the section of the Income Tax Act that sets out tax rates is "one of the most straightforward: it is scarcely a dozen lines...[O]nce someone's taxable income is calculated on their tax return, a Grade 3 student can calculate the tax owing, no matter how many rates there are."[15]

Another argument made in favour of a flat income tax rate is that it would reduce tax evasion. As Brooks points out, this is just a subtle form of blackmail. The rich are in effect saying that, if you force us through the will of the majority to pay taxes we think are too high, we will engage in criminal activity to get our way. Giving in to blackmail is hardly a sound basis for public policy.

Even so, the argument itself is false and implies that a so-called "fairer" flat tax is less likely to be avoided. In fact, it is the GST—a flat 7% tax—that is the most evaded in the country.

The argument flat-taxers use to make their proposal sound progressive is that it will lead to increased economic prosperity for everyone. This is the old "trickle-down" theory that has been thoroughly discredited by both prominent economists and all available evidence. As Brooks points out, the last 50 years have been marked by ever lower taxes on the wealthy and lower rates of economic growth—"a troubling coincidence to those who argue that reducing the top marginal tax rate is the key to spurring economic growth."

In the 1940s and early 1950s, the top marginal rate was 90% and GDP increased at a yearly rate of 6.2%. In the late 1950s and early 1960s, the top rate was 80% and growth averaged 5.1%. In the 1970s, the top rate was reduced to 60% and growth slipped to 4.2%. Since 1981, the highest rate has been about 50% and growth has averaged just 2.4%.

Brooks points out that these correlations do not imply causation. While the precise relationship between tax rates and economic growth is not clear, there is no evidence that lowering top marginal rates promotes economic growth. If anything, the evidence suggests the opposite—that low taxes retard growth. According to Cornell University economist Robert Frank, "If you only look at the evidence, countries with low taxes on the wealthy—and here the U.K. and U.S. stand out—have slower growth rates than countries in which the tax system is more progressive.

"Countries in which the inequality of reward is lower actually have higher growth rates in productivity. If you look over time, in the U.S., the inequality between rich and poor has grown over the past 25 years, and yet that period has been a period of slower growth than in the past."[16]

Of the 29 industrialized countries in the OECD, only Canada, New Zealand and Australia have no inheritance tax. These taxes typically kick in at a very high rate and affect only the wealthiest 5-to-10% of the population. The absence of an inheritance tax (also called a wealth transfer tax) in Canada is an enormous advantage to the wealthy, a gift from other taxpayers of $3 billion a year to the richest Canadians.

Nearly half the OECD countries also apply a net wealth tax on their wealthiest citizens, amounting to 1-to-2% of their net worth each year. These taxes, applied to a person's net assets or net worth, have a very high exemption rate so that they apply only to the wealthiest 5-to-10% of the population. According to Brooks, such a tax in Canada would easily bring in $1 billion in additional revenue.

The effect of not having these two taxes has been a huge and growing gap in wealth—a gap that is far greater even than the income gap in the market part of our economy. The failure to tax wealth contributed to a tripling of the number of millionaires in Canada between 1989 and 1997, to 220,000. Estimates are that this number will triple again by 2005.[17] And, as the Centre for Social Justice documented in its 1999 study *The Growing Gap*, the gulf between rich and poor is growing at an unprecedented rate, especially since 1993. This growing gap is in part due to the failure of the tax system to moderate the inequities of the market as it used to do, and in part to the erosion of transfer programs.

The tax system, the calls for deep cuts notwithstanding, has clearly not had a negative affect on the investment activities of wealthy Canadians. On the contrary, they are getting increasingly wealthy as a result of that system. In part, this is because capital gains and dividends income from stocks, a major source of income for the wealthy, are still taxed at preferential rates so that income from investing is taxed at a lower rate than income from working. In addition, the interest paid on money borrowed in order to invest is tax deductible.

In any case, there is no evidence for the claim that wealthy people will automatically invest in job-creating, productive activity if we reduce their taxes. It is not simply the availability of extra savings that determines the level of productive investment. Demand for goods domestically, and demand for Canada's exports abroad, determine whether or not new plant and equipment come on stream.

In the absence of new demand, investment goes abroad or into speculative activity in the stock market, currency markets, and the like. While individual investors may benefit from this activity, the country as a whole does not.

The brain drain

One of the most popular myths being promoted by business think-tanks such as the C.D Howe Institute and the Fraser Institute, is the notion that our tax system is so out-of-whack with that of the U.S. that it is causing a huge brain drain to that country.

Canada's income tax rate is significantly higher than it is in the U.S. and this is the alleged source of the "exodus" of high-income earners to that country.

This claim, however, is grossly misleading, focusing as it does on a very small part of the picture, in a very short time frame, and intended to create a crisis atmosphere. Once created, the "crisis" can only be dealt with by an immediate and dramatic decrease in taxes.

According to an October 1998 StatsCan study, there has been a net outflow of university-educated people from Canada to the U.S. in the 1990s of approximately 8,500 per year. But, overall, Canada benefits from an enormous brain **gain** from other countries. During this same period, Canada received 32,800 university educated immigrants—a net gain of 24,300 highly educated workers. This holds true for engineers, computer scientists and natural scientists.

The StatsCan study concluded that, while Canada was losing a small number of skilled workers in key occupations to the U.S., "the numbers are: small in a historical sense, small relative to the stock of workers in these occupations, small relative to the new supply of workers in these disciplines, manifold smaller than the influx of immigrants into these occupations."

It is not at all clear that even those who are leaving are doing so because of high taxes. The fact is that U.S. universities and some high-tech companies are prepared to pay higher salaries, sometimes much higher, to get skilled labour. The U.S. is 10 times the size of Canada and has that many more opportunities, so it is hardly surprising that some Canadians would be attracted there.

The extent to which there is a small brain drain now has more to do with Canada's macroeconomic policies than with its tax policy. The Canada-U.S. free trade deal and NAFTA have made it easier for professionals to work in the US. And our disastrous zero-inflation policies of the 1990s were in large part responsible for driving our unemployment rate up nearly twice as high as the rate in the U.S.

Add to that the draconian deficit reduction policies that gutted the civil service, and you have the explanation for the vast majority of the so-called brain drain. Most are not leaving private sector employment; they are unemployables in a public service cut to the bone.

StatsCan figures show that cuts to Medicare, the slashing of university budgets, and the gutting of federally-funded research and development have left thousands of highly educated Canadians with nowhere to work. Tax levels don't even enter the picture. As much as 40% of the graduating classes of nursing colleges go directly to the U.S. If Canada were serious about reversing the current net outflow of skilled workers to the U.S., it would reverse the severe cuts to post-secondary institutions and research councils, and implement policies explicitly aimed at reducing unemployment.

The constant whining by high-tech firms about the exodus of highly-skilled workers tells more about the firms themselves than about the tax system. First, they are unwilling to pay as much as their American counterparts. The low Canadian dollar is partly to

Table 5.3
Canadian Immigration and Emigration, Selected Occupations (1996)

	Emigration to US	Immigration from US	Worldwide Immigration into Canada	Net Gain or (Drain)
Engineers	506	93	8,278	7,772
Computer Scientists	148	113	6,467	6,319
Natural Scientists	195	61	2,194	1,999
Nurses	1,104	28	421	(683)
Physicians	522	7	342	(180)

Source: Statistics Canada

blame; but Canadian firms could still afford to compete overall because the Canadian corporate income tax system is more generous —27.4% compared to the U.S. effective rate of 40%.

Labour costs in Canada are also much lower than those in the U.S. in general, in part because our publicly-funded Medicare saves employers millions in medical premiums that U.S. employers are obliged to pay.

As Neil Brooks points out, the arguments about flat taxes—and taxes in general—reflect fundamental differences in definitions about what is a good society. He asks: even if there was a significant exodus of high-income individuals because of our higher taxes, "is the loss so serious…that Canadians ought to yield to the pressure…and refashion their public policy to accommodate them?" According to Brooks, this isn't just a matter of tinkering with a single tax policy, but goes to the heart of what we as a democratic society wish to do about the unfair distribution of our national wealth.

The brain drain issue, though exaggerated, highlights what anti-free trade activists argued throughout the debates about the FTA and NAFTA: that these agreements would put pressure on Canada to harmonize its policies with the more free-market policies of the U.S. This is exactly what has happened. Not only are standards of health and education declining toward American standards, but we are now told that we have to harmonize our tax system downwards, as well, to match the U.S. system.

Fortunately, the vast majority of Canadians do not make their decisions exclusively on the basis of how much income they can make or the level of taxes they pay. Most are not attracted to the U.S. because it has a weaker communitarian value system, higher crime rates, and impoverished social programs—particularly with respect to Medicare.

Those who stay regardless of higher pay in the U.S. do so because they value what we have built in Canada. Perhaps the real story is not how many Canadians are enticed to move to the U.S., simply on the basis of economic gain, but how many more choose to stay in Canada.

Myth 6

"Canada is a very expensive country in which to do business. One way of getting around this barrier to investment is to provide tax breaks and special tax deductions as incentives."

There are actually two myths included in this neo-liberal claim. They are easily refuted by two facts: First, Canada is one of the least expensive countries in the developed world in which to set up and run a business. And second, tax breaks, of which there are still dozens in the Canadian system, are extremely ineffective in promoting new investment.

The study by KPMG referred to earlier, "The Competitive Alternative," compared the costs of doing business in Canada, the U.S., the U.K., France, Germany, Italy and Sweden. In nearly every category of costs, Canada came out lowest. It ranked No. 1 in lowest initial investment costs, 15% cheaper than the U.S., and No. 1 as well in lowest annual costs following initial set-up. The U.S. ranked fourth, the U.K. third, Sweden second, Italy fifth, Germany seventh, and France sixth.[18]

Comparing Canada with the U.S., our main competitor for investment dollars, Canada had lower costs in the areas of labour, electricity, marine transport, telecommunications, interest, depreciation, income and other taxes. The only area where Canada was more expensive was land transport. Overall, Canada came in almost 6% cheaper than the U.S., a significant cost difference when you consider that most industries do well to make a return on investment of 12%.

Part of the advantage enjoyed by Canadian companies is Canada's publicly-funded Medicare system. A study by Bryne Purchase of Queen's University shows that employer-paid health benefits account for between 5% and 20% of total payroll costs for U.S. companies. "For the Big Three U.S.-owned automakers, the employee health care cost differential between Canada and the United States is reportedly over $8 per hour." In the agri-business sector, health care costs are as much as $13,000 a year higher south of the border.[19]

The KPMG study reinforced a yearly survey done by KPMG comparing the costs of doing business in the U.S. and Canada. The study looks at between six and 13 locations in each country. In each year that the study has been done, starting in 1995, all of the Canadian cities studied were cheaper than any of the American locations. In other words, even the most expensive Canadian city was a cheaper location in which to do business than the cheapest American location surveyed.

Even if it were true that Canada was an expensive place to do business, the use of tax breaks and incentives to spur investment is notoriously ineffective. The history of using the tax system to encourage investment is one of wasted billions in government revenue and citizens' tax dollars.

The most comprehensive effort at tax incentives was undertaken in the early 1970s by then Finance Minister John Turner. Reduced corporate taxation and a series of tax breaks, including the rapid depreciation of new machinery for tax purposes, were intended to give a significant boost to manufacturing capital investment and a big increase in employment.

In 1977, some eight years after the first measures were introduced, employment in manufacturing had actually **dropped** by 1.5%—a far cry from the 250,000 new jobs the minister claimed would be the result. Most manufacturing sectors were plagued by overcapacity and no company in that situation was going to put extra cash flow (through tax breaks) into new productive capacity. Most of the money found its way into corporate coffers and ended up going to shareholders' dividends.

According to numerous studies of the effectiveness of investment tax incentives, surveyed by Memorial University's Douglas May, for every dollar forgone in tax revenues to spur investment, only 20 cents worth of actual new investment was created. Some studies suggested that the figure was even lower.

Even worse was their record at "reducing unit costs"—an objective aimed at making Canadian manufacturers more competitive internationally. In this area, May demonstrated that the tax incentives reduced unit costs by a minuscule 0.5%.

One of the unforeseen results of these tax incentives was their negative impact on employment. By giving tax breaks to companies buying new equipment and machinery, the government made such machinery relatively less expensive than labour. Where a company might otherwise have hired more workers, or kept them on, this particular tax break made it more economical to upgrade the equipment and lay off workers.

Yet, despite these extremely poor results, the tax incentives have continued to this day—and every year the Canadian government loses many millions in revenue it would otherwise collect. In the first half of the 1980s, the big five banks alone were given $2.8 billion in tax breaks that brought their effective tax rate down to about 2% (compared to the statutory rate of about 40%).[20]

A study by Kirk Falconer showed that, over an eight-year period, from 1980 to 1987, the amount of untaxed corporate profits totalled nearly $127 billion. These untaxed profits arose because corporations are able to take advantage of perfectly legal provisions of the corporate income tax system. But, had the statutory rate of taxation been applied, the additional revenue for that period would have amounted to nearly $60 billion.

In the final year of that study, 93,405 profitable corporations paid no tax at all. Most of the tax breaks—84% of the total amount—went to corporations earning over $1 million in profits.[21]

While some tax reform was implemented in the mid-1980s, in 1995, the last year for which figures are available, there were still 90,415 profitable corporations with total profits of $18.6 billion[22] that paid no income tax. And these numbers reflect just those corporations that paid no tax at all (or even received a tax credit). Thousands more had their tax bill reduced.

How do these untaxed profits arise? The most detailed analysis of this phenomenon was conducted by the Ontario Fair Tax Commission in 1992. The Commission found that, of $18.5 billion earned by profitable corporations that paid no tax, $2 billion was non-taxable because of prior years' losses, $9 billion was non-taxable because inter-corporate dividends are not taxed, $850 million represented equity income that is taxed at a corporation's subsidiary, and another $700 million was untaxed for various other reasons. That left $6 billion in untaxed profits.

It is worth noting that the lost revenue from these tax breaks were a major contributor to Canada's national debt. Several studies have shown that declining government revenues in the 1970s and 1980s, and not increased spending, laid the foundation for the large accumulated deficits of the 1980s and 1990s. The burden of paying off that debt has fallen, not on the corporations, but on ordinary working people, through their taxes and through eroded social programs.

Myth 7

"Governments can't create jobs. All they can do is help and encourage the private sector to create jobs."

It is important to look at this argument not only on its merits, but from where it comes. The political parties, commentators, and corporate think-tanks promoting this notion have for over 10 years demonstrated a complete lack of interest in Canada's appallingly high unemployment rate. In fact, they have all supported our high-interest rate policy that deliberately maintains a high unemployment rate.

Instead of any real concern about unemployment, the tax-cutters are much more interested in ensuring that social programs and transfers to the provinces are increasingly starved of their necessary funding. The best way to ensure this is to systematically reduce the government's revenue. That would, in addition, maintain Canada's high debt level, always a useful tool to support the demand for more spending cuts.

But do tax cuts really create jobs and stimulate growth? It depends. It depends on who gets the tax cuts. Personal tax cuts at the lower end of the income scale do have a stimulating effect because poor people tend to spend every extra dollar they receive.

Tax cuts at the high end, however, have a much less stimulative effect because wealthy individuals are already saving much of their income. Any extra income is likely to be saved, as well. It is argued that the wealthy will invest their extra money and create jobs but, as we saw earlier, this argument doesn't hold up in an economy where demand is stagnant—and kept stagnant by government policies—and export markets are down.

If those recommending tax cuts were really interested in creating jobs, they would be calling for revenue-neutral tax changes—i.e., reform of the tax structure that would maintain the current levels of total revenue necessary for government programs, but shift the burden away from low- and moderate-income earners. But this is not what they are calling for. Common to all these proposals is the **lowering** of total revenue, and thus of the ability of the government to provide for citizens. The more honest of the would-be tax cutters, like the Reform Party, call for simultaneous tax cuts **and** lower government spending.

The other problem with tax cuts to higher- and even middle- income earners is that Canadians now have record levels of debt, a result of trying to maintain their standard of living on ever-decreasing real incomes. Much of the tax cut money would likely go to paying down these high debt levels and decreasing the level of new borrowing.

Governments do create jobs - millions of them

If you think about the argument that governments can't create jobs, it's pure nonsense. Teachers, university professors, nurses, doctors, parks workers, civic employees, those employed by Crown corporations such as utilities—all are doing jobs "created" by government and paid for with tax revenue.

The question really comes down to which is the best and most socially useful way to create jobs. Tax cuts can have a stimulative effect, but how do tax cuts compare to government spending on hiring more nurses and teachers and child care workers? Or maintaining highways and buying new transit buses?

A study by the Ottawa economic forecasting firm Informetrica compared the job-creation effectiveness of government spending to that of tax-cutting. Government spending turns out to be a far more effective job creation tool, especially in the areas of social spending, than cutting taxes. The study compared the job-creating effectiveness of tax cuts of $100 million to government spending of the same amount, tallied over three years. Spending on additional government employment, health and education would each result in 70,000 new jobs over the three years. The same amount spent on day care would create 130,000 jobs, and on goods and services in the private sector, 59,000 jobs.

Tax cuts didn't do nearly as well. The best job creation tax cut was in the GST, where a $100 million cut would produce 53,000 new jobs. An across-the-board personal income tax cut creates 40,000 jobs, and a corporate tax cut 22,000.[23]

Besides the actual numbers, Canadians need to judge these job creation techniques by what else they produce. Tax cuts are not neutral; they mean fewer public services, poorer communities, a weaker safety net for the most vulnerable, fewer public parks—in other words, less public space. Private, individual consumption would go up, yes, but part of this increase would be spent to make up for the lost public services. What good does it do poor people to get a small tax cut if they have to spend more on health services that used to be covered by Medicare, or school supplies that used to be paid for by the school?

The assumption behind tax cuts is that people only want choices in their private purchases. But clearly people want choices in public services just as much: witness the strong support for Medicare and public education. As tax policy professor Neil Brooks asks, where is the evidence that people want more cars and fewer buses, more private theme parks and fewer wilderness areas, more toll roads and fewer public highways, more private clinics and fewer hospitals? In fact, the evidence strongly suggests just the opposite.

Part of the call for tax cuts is tied to the notion that the government is taking money "out of the economy." The Reform Party repeatedly talks about government jobs not being "real jobs." Both these notions are just silly. If true, we would have to see a job in tobacco advertising as a "real job" and that of a nurse treating cancer patients as not real. In fact, government jobs are so prevalent in the economy that 23 of the 51 Reform MPs elected in 1993, now so critical of government jobs, had themselves previously worked at such jobs.

As for taxes taking money out of the economy, just the opposite is true. Millions of jobs result from government spending. A study done by David Robertson in 1985 demonstrated just how many jobs. While the study is now somewhat dated, the conclusions still hold. That year, governments in Canada spent $86 billion in the private sector—accounting for 6% of the total output of all services, 14% of utilities and transportation; 21.6% of publishing and printing; 48% of redimix concrete—and so on, throughout the economy.[24]

This government spending in the private sector accounted for over one million jobs. In addition, $30 billion in government salaries spent in the economy created another half million jobs, and transfer payments (another $30 billion) a similar number. These were direct jobs and did not count the multiplier effect of those government dollars working their way through the economy. If UI payments were included, the numbers would be even larger.

Another action the government could take is to further lower interest rates. While we often hear that Canada is now enjoying the lowest interest rates in 15 years, this is extremely misleading. Real interest rates are calculated by subtracting the inflation rate from the official rate set by the Bank of Canada. With the inflation rate under 1%, the real interest rate in Canada at the end of 1998 was 5.5%—over twice the historic rate maintained through most of the post-war period up until 1980.

The long-term real interest rate averaged 1.6% between 1950 and 1980. Between 1990 and 1997, it averaged 6.8%. In fact, real interest rates are now higher than they were in the early 1980s when nominal rates were up to 20%. **(See Table 4.3.)**

If we are to deal seriously with the jobs issue, we must examine where Canada's unemployment—twice the U.S. rate—comes from. Analysts of all political

The productivity connection

One of the more recent buzz-words in the anti-tax campaign has been productivity. This is the measure of how productive the average worker is, usually calculated as output per employed person. Measuring and comparing productivity between countries is complicated, and not without controversy. The OECD claimed in a 1999 report that Canada's productivity was lagging far behind that of the U.S. But, subsequently, Statistics Canada produced figures that showed just the opposite, confirming numbers produced by the Ottawa-based Centre for the Study of Living Standards.

In the midst of this debate, anti-tax crusaders selectively relied on the OECD data to make the case that Canada must lower taxes to increase productivity. In truth, tax levels have very little to do with productivity.

Productivity is determined by a number of factors, including the skill of the work force, the modernization of plant and equipment, and the application of new technologies. Increasing productivity therefore depends upon private and public investments in technology, research, education and training. Taxes simply have no discernible impact. A Standard and Poor's DRI study notes that "[l]ow-tax countries have widely varying productivity performances. This implies that there are a number of other factors...that are important."[22]

In fact, if low taxes were the solution, there would be no controversy over Canada's productivity performance. There are already very generous tax breaks for corporate research and development in Canada. Large companies, like Nortel, which grab the lion's share of such tax breaks, end up with extremely low effective income tax rates. For example, Nortel paid income tax at an effective rate of 6% on its profits of $583 million in 1994. But Nortel uses its tax breaks to develop technology and then export production jobs to low-wage countries, thus **undermining** efforts to improve Canadian productivity. As of 1995, the Canadian taxpayer had subsidized each job remaining at Nortel's Canadian operations to the tune of $140,000.[26]

stripes have identified Canada's extremely aggressive deficit reduction efforts and its high interest policies as the key culprits. Jeff Rubin, chief economist with CIBC's Wood Gundy brokerage firm, stated in 1997 that Canada would have been much closer to the "full-employment U.S. economy" had governments not gone overboard on cuts to government spending.

The enormous cuts to social spending, combined with ruinously high interest rates, created a completely unnecessary high level of unemployment that cost the Canadian economy $400 billion in forgone national income between 1990 and 1996, according to Professor Pierre Fortin, former President of the Canadian Economics Association. It stands to reason that bringing interest rates down to the historic real rate (inflation plus 2%, or about a 3% Bank of Canada rate) and reinstating social spending to 1980s levels would do more for job creation and economic stimulus than any combination of tax cuts.

A recent example of the power of governments to affect jobs and growth was the B.C. economy in 1998. Widely characterized as being in a recession because of weak resource sectors, the province's economy baffled pundits by scoring the fastest job growth in the country, even ahead of alleged powerhouses Alberta and Ontario, to which it was unfavourably compared.

The puzzle was not that difficult to solve. The B.C. government increased funding in health and education, and, partly because of that, job growth in the public sector rose by 11.7% with only a minor increase in the deficit. The result was a 3.6% job growth rate, compared to Alberta's 3.1% and Ontario's 3.5%.

Myth 8

"The stimulative effects on the economy of reducing taxes—especially on the wealthy—would lead to an increase in government revenue, not a decrease."

Those calling for major tax cuts have anticipated that public support for social programs translate into public resistance to cuts—so they claim we can have both. This seemingly contradictory argument promises the sky: lower taxes (appealing to tax-cutters) and *more* revenue (appealing to those concerned about funding for social programs.) It is an attractive idea, except that it's a promise that can't be kept. In times of high economic growth rates, revenue can increase *in spite* of tax cuts. But there is simply no evidence that revenue increases *because* of tax cuts.

This argument is part of the ideological arsenal of what in the 1980s were called economic "supply-siders." Until the advent of these neo-liberal economic theorists, it was widely accepted that it was the level of demand in an economy that determined whether or not economic growth took place. Up until the late 1970s, governments were concerned about the level of unemployment because people who weren't working weren't spending money in the economy (or were spending less) and that meant "demand" was down.

It also meant that tax revenue was down because unemployed workers paid less in taxes, as did companies selling fewer goods and services and making lower profits. Policies to lower unemployment were seen by "demand-siders" as the way to increase tax revenue.

Supply-siders, on the other hand, argued that, if you freed up money by lowering taxes on the wealthy, they would invest that money (to make more money) and in the process create new productive capacity. In other words, if you stimulated the supply side of the economic equation (create more goods and services and people will buy them), the economy would grow and so would tax revenue (as well as jobs and investment).

In this scenario, the stimulation of demand was much less important, and in fact the whole question of unemployment became less important. Controlling inflation was seen as paramount because inflation ate into the value of assets, which were the key to supply-side stimulation.

When the numbers were in, particularly in the U.S. where this economic experiment was conducted with the greatest enthusiasm, the supply-siders were simply proven wrong. President Ronald Reagan made major tax cuts, claiming they would stimulate growth and increase government revenues. Instead, over Reagan's two terms, revenues fell and annual federal deficits and resulting debt soared to record levels. The wealthy did not go on an investment spree. Far from it. Gross investment in relation to total GDP actually fell. Supply-side policies were subsequently ridiculed as "voodoo economics" by pro-business U.S. President George Bush.

A recent study conducted by the B.C. office of the CCPA came up with similar conclusions about tax cuts and revenue growth. In *A Tale of Two Provinces: A Comparative Study of Economic and Social Conditions in British Columbia and Alberta,* Seth Klein and Catherine Walshe show that government revenues grew faster in B.C., where tax cuts were minimal, than they did in Alberta, where tax cuts were deep and extensive.

The study revealed that, while revenue in both provinces grew between 1993-94 and 1996-97, it actually grew faster in B.C. than it did in Alberta. This was the case even though Alberta enjoyed faster economic growth, and growth in corporate profits. Both corporate and personal income tax revenues increased at a slower pace. Given that the Alberta economy was growing due to other factors (the ideal situation for the supply-side theory to prove itself), the fact that revenue grew relatively slowly suggests that supply-siders have it completely wrong. The evidence suggests that tax cuts had exactly the effect one would expect: they slowed revenue growth well below the pace it would have achieved without the cuts.

The decline of revenue from general tax reductions is paralleled in the record of selected tax breaks for corporations. Here, too, tax breaks failed to encourage new investment. Responsible CEOs don't invest in new plant and equipment unless they know there is potential new demand for their goods. But, of course, corporations and the wealthy will happily take advantage of tax loopholes and tax cuts if governments are misguided enough to offer them.

The evidence over the years suggests that revenue increases as population increases (increased demand) and as real economic growth occurs. The latter is determined by domestic demand and by the demand for exports, and by where we are in the business cycle. Tax cuts can do nothing to change the lowered demand for Canada's natural resources caused by the Asian economic crisis. Lowering high-end taxes in this situation has a completely predictable effect: lower government revenue.

Myth 9

"Cancelling the GST now would be too difficult. It raises a large amount of revenue and is an easy tax to collect. It is fair because it is applied equally to everyone."

The arguments against abolishing the GST simply don't stand up to scrutiny—not even those advanced by some advocates of progressive taxation. They have suggested that the tax is now a permanent feature of the tax system and that it provides such a large piece of the revenue pie that it should be left alone. Its extremely regressive features, they say, can be moderated by other policies, such as the existing GST rebate to low-income earners.

It is also argued by some of those initially critical of the GST that, unlike some other taxes, it is a difficult tax to evade. And, while the GST is unquestionably regressive, the $18 billion a year that it raises helps pay for social programs, which are Canada's most effective redistributive mechanisms.

Nevertheless, there are very good reasons to call for the gradual elimination of the GST. First, no one disputes that it is among the most regressive of all taxes,one that puts a disproportionate financial burden on those least able to pay.

It is largely because of the GST and other consumption taxes that Canada now has an almost flat tax system when all taxes are taken into account. Because poor and low-income Canadians spend virtually all of their earnings, they pay the GST on their total disposable income. Middle- and upper-income Canadians escape the tax on that portion of their income they are able to save or invest. The more you earn, the less onerous the GST.

A Carleton University study found that, for those earning less than $10,000, the GST and other consumption taxes took 14.6% of their income. In sharp contrast, those earning $100,000 to $150,000 had only 7% of their incomes eaten up by these taxes. The notion that we can moderate the impact of this tax on the poor implies that we will always have governments in place with the political will to implement such policies. The current GST rebate falls far short of cushioning the harsh impact on the poor, and the rebates have been getting smaller each year, due to inflation. (The rebates are indexed to inflation only if inflation reaches 3%, so that the value of the rebate decreases every year by the amount of inflation below 3%.)

The GST is just one of many measures that, in their effect, transfer wealth from the bottom 80% of the population to the top 20%. By implementing a tax that falls most heavily on those who have to spend all or most of their income to support their families, the government has been able to reduce the tax burden on wealthy Canadians.

As detailed elsewhere in this report, the wealthy in Canada are becoming ever-wealthier, and at an unprecedented rate. The decrease in the high marginal tax rates on the rich has been largely financed by the GST. The GST benefits the wealthy, not just because it is a regressive tax, but also because it transfers billions of dollars in taxes from corporations (replacing the old Manufacturers' Sales Tax) to individuals. Improving the bottom line of corporations benefits the wealthy, the primary beneficiaries of corporate profitability.

There is another reason for targeting the GST for eventual elimination. Of all the taxes that could be cut or eliminated, the GST would have the largest impact on job creation. It is the only tax cut that comes close to the job-creation impact of increased government spending. As indicated above, a cut in the GST of $100 million would result in an increase of 53,000 jobs over three years—more than twice as many as would a corporate tax cut.

Replacing the GST

There is no question that the government would have to find a major new source of taxation to replace the $18 billion that the GST currently raises. And there are no simple, one-stop solutions to replacing the GST revenue. Numerous tax reforms need to be implemented—wealth taxes, a minimum corporate tax, additional high rates on very high incomes, and the elimination of questionable tax breaks.

The proposal for a domestic financial transactions tax has attracted some attention from proponents of progressive tax reform. The idea of taxing financial transactions comes from Nobel prize-winning economist James Tobin, whose "Tobin tax" proposal is aimed at currency speculation world-wide. Taxing the $1.5 - 2 trillion traded every day would raise billions for Third World debt relief and would cool the hot money markets that triggered the Asian financial crisis of 1998.

A domestic version of the Tobin tax, however, is problematic. Such a tax is already being implemented in several countries, including some of the most open free market economies in the world, such as Hong Kong, Singapore and Britain. But the tax raises relatively small amounts of money when compared to the billions brought in by the GST—revenue in the range of $150-200 million annually. Although the potential tax base is huge— nearly $20 trillion when all financial transactions are considered—much of this would disappear if a tax were levied. Some would move to other jurisdictions, some would be disguised as non-taxable transactions, and others would no longer take place.

More importantly, nearly three-quarters of such transactions in Canada involve federal and provincial government bonds. The burden of the tax would end up being paid by Canadian citizens, since it would make Canadian bonds less competitive. According to the CCPA's Alternative Budget analysis, such a tax would also destroy the market for 90-day Treasury Bills, a key source of revenue for the federal government. The government would be forced to buy longer-term bonds at higher interest rates.

The goal of eventually getting rid of this regressive tax is nonetheless still achievable, and in the short term it can be made less regressive. As the debt-to-GDP ratio continues to decline, federal finances will improve and less of our revenue will go to paying interest on the debt. That would allow for gradual elimination of the GST through a staged reduction of the 7% rate.

Reforming the tax system to bring in greater revenues from wealth taxes, minimum corporate taxes, and additional tax brackets for very high income earners—and even a moderate financial transactions tax—would accelerate this process.

Alternatively, the GST could be changed into a European-style value-added tax that would build in higher rates of tax on luxury items, while lowering it on necessities. Such a tax could be used to achieve environmental as well as redistributive objectives, e.g., giving tax breaks for products made from recycled materials and taxing toxic products or those putting other stresses on the environment, at higher rates. This would in effect mean a tax shift to green taxes; something environmentalists have been advocating for many years.

Myth 10

"When asked what governments should do with their surpluses, Canadians say that they want tax cuts. Individual consumers know better than governments how to spend their money."

This myth, for the most part, is neo-conservative wishful thinking. After years of calculated deficit hysteria and huge cuts to social programs, those wanting to "downsize" government were hoping that people would be eager to demand tax cuts. In Reform Party parlance, the product is no good, so give the customers their money back.

Conrad Black's *National Post* has taken this wishful thinking to its most absurd level, declaring in an editorial that Canada is in the grip of "tax rage...[which] has many of the characteristics of a forest fire about to jump a lake." (April 1999).

As it turns out, Canadians' strong communitarian values—and sheer practicality—are very resilient. Some directed polls, in which people are given a list of options to choose from, suggest tax cuts are popular. But, given open-ended choices, Canadians consistently choose to put governments' surpluses into Medicare, education, job creation, child poverty, child care, and debt reduction before they choose tax cuts.

A **Globe and Mail**/Environics poll in late 1996 showed that only 9% of respondents wanted tax cuts—and this figure was only slightly higher (11%) for upper-income Canadians. Thirty-one percent wanted money to go to job creation, 25% to health care, and 13% to children of poor families.

Even in Alberta, where the government is committed to a neo-liberal agenda of downsizing government, polls have shown scant support for tax cuts. The government, in fact, conducted poll after poll in the late 1990s, hoping for better results to justify its ideological commitment to such cuts. In every poll, however, tax cuts were rejected.

Typical of the results was an Environics poll in 1997, in which 37% wanted the Alberta government surplus to go to education (where cuts had been severe), 29% to health care, and 22% to job creation. Only 11% wanted to pay down the debt, and a minuscule 5% wanted tax cuts. It wasn't until 1998, after years of government and media promotion of tax cuts, that opinion began to shift in favour of cuts.[27]

And in Ontario, where the Harris government cut provincial income taxes by 30%, the population is not in favour of further tax cuts. Even at the height of the 1999 provincial election in which the Conservatives were re-elected, an Angus Reid poll showed that only 23% of Ontarians wanted the government to go ahead with its promised additional tax cut. Over half (53%) said they wanted the government to forget the tax cut and spend the equivalent amount of money on health care and education, while 22% said it should be applied to the deficit.[28]

In general, Canadians in 1997 began to turn decisively against neo-liberal ideology and the policies that flow from it. Having been told for a decade that they couldn't have social programs because of the deficit, Canadians are demanding a return to social spending as deficits disappear. The Ekos consulting firm does polling for the federal government, and produces a yearly study called "Rethinking Government." The results in 1997 showed a dramatic turn in favour of activist government.

For example, in the Ekos 1996 poll, 34% supported two-tier medicare. A year later, that figure had plummeted to 23%, statistically a huge drop. According to the authors of the report, "Despite deep scepticism about the effectiveness, efficiency and fairness of government, Canadians are now looking for a return to an active agenda... On virtually every public indicator and test we examine, the neo-conservative wave—always overstated in terms of public support—is in collapse."[29]

The Ekos poll shows a steadily declining concern about the level of taxes since the agency began its yearly study in 1994—a result that parallels the decreasing deficit and the concern about the erosion of social programs.

Who pays taxes, and how much we need to collect overall, are questions relating fundamentally to the collective life of Canadians. They are questions about how much of our space we want to be public and how much private. The notion that the "customer wants his/her money back" seeks to portray Canadians not as citizens wanting community solutions to social questions, but simply as customers in the private marketplace, keen to make private consumer choices.

All the polls relating to this broad question show this claim to be false. The Ekos poll (which also shows a major gap in attitudes toward government between the governing élite and the rest of us) demonstrates a strong sense of collective life and an accompanying desire for strong (though fiscally responsible) government. In the words of the Ekos poll authors, "We are finding evidence of rising concern for others and increased receptivity to the role of government as an agent to address the problems in our collective life."

A large majority (82%) of people polled disagreed with the statement that a stronger economy meant that we didn't have to worry as much about child poverty; 72% said too many people have been hurt by cuts to social programs and "it's now time to strengthen our commitment to the social safety net."

Those forces in Canadian society committed to gutting social programs and ending any progressive role for government see tax cuts as their guarantee that we will not have the money for such activist government. And it is in their interests to portray Canadians as eagerly awaiting the tax-cut windfall. While the poll results are mixed, with many Ontarians supporting the Harris government's cuts, the clear message that governments get when asked is that Canadians are acutely aware of the connection between paying taxes and having a civilized society in which to live.

In fact, they have demonstrated that they are actually willing to pay **higher** taxes if that is what it takes to ensure that key social objectives are met. According to a poll by Vector Research, this willingness to pay more in taxes attracted 74% of respondents when dealing with child poverty; 57% regarding publicly-funded child care (so that poor parents could work or get training); 68% for training, and 58% for improving public schools.[30]

Canadians clearly are not persuaded that they need only have choices as customers in the marketplace to achieve their aspirations. They see themselves as citizens in a collective undertaking and are willing to pay to make it work.

Notes

[1] Andrew Cohen, "So you wanna live the dream," *Report on Business Magazine*, July 1999.

[2] *The CCPA Monitor* (Ottawa: Canadian Centre for Policy Alternatives), March 1995.

[3] Stanford, Jim, *Paper Boom*, CCPA, Ottawa, 1999, p. 269-70.

[4] Eric Beauchesne, "Canadian tax load same as US," *Vancouver Sun*, May 26, 1999.

[5] *The Competitive Alternative: A comparison of business costs in Canada, Europe and the United States*, KPMG, Published by Prospectus Inc., October, 1997.

[6] Mel Hurtig, "How much of Canada do we want to sell?", *Globe and Mail*, Feb 5, 1998.

[7] Armine Yalnizyan, *"The Growing Gap: A report on the growing inequality between rich and poor in Canada,"* The Centre for Social Justice, Toronto, October, 1998, p.45.

[8] *Globe and Mail Report on Business*, Feb, 1997.

[9] op.cit. Yalnizyan, p. 23.

[10] Clarence Lochhead and Vivian Shalla, "Delivering the Goods: Income Distribution and the Precarious Middle Class," in *Perceptions*, Canadian Council on Social Development, spring, 1997.

[11] National Council of Welfare, Province of Manitoba.

[12] *The Monitor*, the CCPA, Sept, 1996.

[13] Kevin Hayes, *"Left Out in the Cold,"* Canadian labour Congress, January, 1999.

[14] *Edmonton Journal*, Mar 16, 1999.

[15] Brooks, *CCPA Monitor*, July/Aug. 1999.

[16] "Drowning in Stuff," Part 1 by Jill Eisen, Ideas, CBC Radio, May 4, 1999.

[17] Survey by Ernst and Young, quoted in the *Globe and Mail*, Nov 11, 1997.

[18] op. cit., The Competitive Alternative.

[19] Bryne Purchase, *"Health Care and Competitiveness,"* Kingston, Ont.: Queen's University School of Policy Studies.]

[20] Gordon Ternowetsky, University of Northern B.C.

[21] Kirk Falconer, "Corporate taxation in Canada: A Background Paper," in *Canadian Review of Social Policy*, Nov, 1990.

[22] *"Unfair Shares,"* Ontario Federation of Labour, 1998.

[23] Infometrica, *"Economic effects of selected fiscal and other initiatives,"* 1997.

[24] David Robertson, *"The Facts,"* publication of the Canadian Union of Public Employees, July-Aug, 1985.

[25] Cited in E. Beauchesne, "Canadian tax load same as US," *Vancouver Sun*, May 26.

[26] Canadian Auto Workers, Parliamentary submission regarding the future of Canadian manufacturing operations at Nortel, 1995.

[27] *Edmonton Journal*, July 25, 1997.

[28] *Globe and Mail*, May 17, 1999.

[29] News release, Ekos Research Associates, Feb 26, 1998.

[30] Vector Research and Development, National Poll, December, 1994.