Progressive Tax Options for BC

Reform Ideas for Raising New Revenues and Enhancing Fairness

by Iglika Ivanova
and Seth Klein

JANUARY 2013

CCPA
CANADIAN CENTRE
for POLICY ALTERNATIVES
BC Office

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ACKNOWLEDGEMENTS

The authors would like to thank Lynell Anderson, Marcy Cohen, Shannon Daub, Marc Lee, Ben Parfitt, Claire Young and four anonymous peer reviewers for their helpful comments and suggestions on an earlier draft of this report.

This research was carried out as part of a broader CCPA project on tax policy. The project is supported by the individual members and donors who contribute to the CCPA's core funding, the BC Government and Service Employees' Union, BC Teachers' Federation, Hospital Employees' Union, Canadian Federation of Students, BC Nurses' Union, BC Retired Teachers' Association, and Canadian Union of Public Employees.

The opinions expressed, and any errors, are those of the authors, and do not necessarily reflect the views of the publishers or funders of this report.

Copyedit and design: Nadene Rehnby, www.handsonpublications.com

ISBN 978-1-77125-051-1

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Progressive Tax Options for BC

THE IDEA THAT WE SHOULD DEBATE WHETHER taxes are 'good' or 'bad' is old. As most of us understand, taxes are the price we pay for the high quality of life we enjoy in Canada. At their root, taxes come down to a simple question: Which goods and services do we want to pay for together as a society, and which do we want to pay for privately as consumers?

Recently, the CCPA conducted extensive opinion research into what British Columbians think about taxes, including a poll conducted with Environics Research. It turns out we aren't nearly as divided on these issues as one might think.

The overwhelming majority of British Columbians (90%) think there should be income tax increases for those at the top. As to where those higher taxes should kick in, a clear majority (57%) says at $100,000 per year of income. A majority (67%) also think major corporations are asked to pay less tax than they should.

Of course it's easy to say someone else should pay more taxes. But most British Columbians are also willing to consider the idea of paying slightly higher taxes themselves, if it can bring about new or expanded public services, such as greater access to home and community-based health care for seniors. (For more information, see: www.policyalternatives.ca/bc-tax-opinion.)

These results are hopeful. British Columbians know we face a budget crunch. We know more revenues are required if we are going to tackle the major challenges we face, like growing inequality and persistent poverty, climate change, and the affordability crisis squeezing so many families (in housing and child care in particular). And we know higher revenues are needed to sustain and enhance the public services so vital to our quality of life and the prospects of our children, like health care, education, and environmental protection.

In short, British Columbians are ready for a thoughtful, democratic conversation about how we raise needed revenues and ensure everyone pays a fair share. This report examines the case for tax reform, highlighting the ways in which BC's tax system has become increasingly unfair. It compares BC taxes to other provinces. And it models various provincial tax policy options, focusing mainly on personal income taxes and corporate taxes. A final section refutes some of the common arguments against tax increases.

The overall finding: There is a clear need to raise more tax revenues. There is considerable room to do so. And the options for doing so are many.

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THE CASE FOR TAX REFORM

FISCAL CAPACITY: BC's finances are squeezed because a series of cuts to both personal income taxes and business taxes since 2000 have steadily eroded provincial revenues.

- If BC collected today the same amount in tax revenues as a share of the economy (GDP) as we did in 2000, we would have $3.5 billion more in public funds this year alone. Meaning, no deficit, and the ability to invest in enhanced or even new public services.

FAIRNESS: Significant cuts to personal and corporate income taxes, combined with increases to regressive taxes like sales tax and Medical Services Plan (MSP) premiums, have produced a tax system that is much less fair. Taxation has been shifted from corporations to families, and from upper-income families to middle- and modest-income ones.

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- Provincial tax cuts since 2000 have delivered the lion's share of benefits to the richest. The richest 1% of BC households have seen their taxes cut by an average of $41,000 per year. That's more than the average income for the poorest 30% of households.
- BC's overall tax system is now remarkably regressive. When all personal taxes are considered (income, sales, property, carbon, and MSP premiums), the higher your income, the lower your total provincial tax rate.
- MSP premiums increased by 85% between 2000 and 2013. A two-earner family with an average household income of $60,000 now pays more in MSP ($1,536) than it does in personal income taxes ($1,190). The provincial government now collects more money from MSP premiums (BC's most unfair tax) than it does from corporate income taxes.
- British Columbians now pay more out-of-pocket for a host of public services, through school fundraisers, rising tuition and seniors care fees, etc., which impose a larger burden on lower-income families.

Tax Terms

PROGRESSIVE taxes are based on the principle of ability to pay — the more you make, the more you pay as a share of income. For example, a progressive income tax system applies higher tax rates to income above a series of thresholds.

REGRESSIVE taxes, on the other hand, take up a bigger share of income for lower-income people than higher-income people. In practice, taxes that charge everyone the same dollar amount (such as MSP premiums) or the same percentage amount (such as sales taxes) end up being regressive. For example, MSP costs $768 per year for a single individual. That's a much bigger cost, as a share of income, for someone making $40,000 per year than it is for someone making $250,000. Sales taxes end up costing upper-income people less as a share of income, because they are more apt to save and invest their money, which is not subject to sales taxes.

ECONOMIC PERFORMANCE: The provincial government is currently inundating the public with ads trumpeting that BC's taxes are the lowest in the country. But set against underfunded public services and growing inequality, this is nothing to boast about. There is also no evidence that lower taxes have delivered on their economic promise.

- BC's economic performance, employment rates and business investment levels are all around the middle of the pack compared to other provinces, and no better than when taxes were higher.

BC's low taxes are not a source of strength — instead, they are part of what's holding us back. Simply put, our province's taxes are too low, and there is plenty of room to increase taxes without undermining economic "competitiveness."

- If BC collected the same amount of personal income tax (as a share of GDP) as the *average* for other Canadian provinces, we'd have an additional $2.4 billion in revenues. (This includes BC's MSP premiums, which no other province uses).
- Last year, the global accounting firm KPMG examined businesses taxes in 55 major cities in 14 countries. Their finding: Vancouver was found to have the second lowest taxes after Chennai, India.

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TAX OPTIONS TO RAISE REVENUES AND REDUCE INEQUALITY

The table on the following page outlines a menu of tax policy options that would help create the budgetary room to meet our most pressing needs, and reduce income inequality. To be clear, this is not an exhaustive list and we are not recommending that the province adopt all these options. Rather, we aim to support an informed public debate by highlighting a range of possibilities, with estimates of the revenues each could raise. There is much room for different formulations.

PERSONAL INCOME TAX REFORM: We focus primarily on income tax (the most progressive element of any tax system) as it represents the best way to ensure all British Columbians pay a fair share of tax. The table below shows BC's current income tax brackets, the statutory tax rates, and the percentage of British Columbians impacted by each.

BC's personal income tax brackets, 2012

Tax bracket	Applies to taxable income of	Current tax rate	% of BC tax-filers in each tax bracket*
1	Under $37,013 (with zero tax on the first $11,354 of income)	5.06%	59%
2	$37,013 to $74,028	7.7%	27%
3	$74,028 to $84,993	10.5%	4%
4	$84,993 to $103,205	12.29%	4.5%
5	Over $103,205	14.7%	5.5%

* Based on Canada Revenue Agency taxfiler data for 2009, the most recent data available.

Summary of Tax Options for BC

Tax change *Note these are single changes, not cumulative*	Potential provincial revenues raised	Could fund... *Note these are merely a selection of possibilities, not specific recommendations*
Increase the current top (5th) bracket rate from 14.7% to 17%	$375 million	Increases to welfare benefit rates of $200 to $400 per month
New tax bracket at $150,000 of income set at 18%	$400 million	2,000 units of new social housing per year
Two new brackets at the top: 18% on income $150,000–$200,000; and 21% on income over $200,000	$700 million	2,000 units of new social housing per year plus restore K–12 class sizes, composition, and specialist teacher staffing to levels that prevailed five years ago
Increase the current top (5th) bracket rate to 17%, and add two new upper income brackets: 20% on income $150,000–$200,000, and 22% on income over $200,000	$930 million	Welfare benefit increases, a major funding increase to the Ministry of Children and Family Development, plus restore K–12 class sizes, composition, and specialist teacher staffing to levels that prevailed five years ago
Two new upper-income brackets (at 20% and 22%) plus increases to the existing top three brackets of 2% of income *OR* Reintroduce a two-level surtax modeled on Ontario's surtaxes (an extra tax on one's provincial tax once certain thresholds are passed)	$1.1 billion	2,000 units of new social housing per year plus restore K–12 class sizes, composition, and specialist teacher staffing to levels that prevailed five years ago *PLUS* the first phase of a comprehensive, publicly funded child care plan
Increase the tax rate in each bracket by 20%,* and add two new upper-income tax brackets (20% on income $150,000–$200,000 and 22% on income over $200,000)	$2.3 billion	2,000 units/year of new social housing; welfare benefit increases; restore class sizes, composition and specialist teachers to where they were five years ago; first phase of child care plan; needed investments in community health care for seniors and people with disabilities; Ministry of Children and Family Development budget increases; increase in post-secondary education funding; and substantial increase to environmental protection *OR* Eliminate MSP premiums (in this scenario, even with the income tax increases in column one, a majority of British Columbians would be net beneficiaries)
Reduce personal tax deductions	$100–500 million	Various poverty reduction initiatives
Return corporate income tax rate to 12%	$400 million	Investments in public transit and building retrofits
Return corporate income tax rate to 13.5%	$700 million	A more ambitious Climate Action Plan
Reduce corporate tax deductions	$300 million	Green industry investments
Increase natural gas royalties	Amount would depend on the rate and production levels	Establish a Heritage Fund from which to pay for future job re-training for energy workers and alternative energy development
Increase forestry stumpage	$26 million	Forest restoration
Increase the BC carbon tax to $50 per tonne of CO_2	$2.2 billion	$1.1 billion for an expanded low and middle-income carbon credit (making the bottom half of BC households net beneficiaries even with a high carbon tax) and $1.1 billion for public transit and/or building retrofits to reduce greenhouse gases

*Note that a 20% increase sounds like a lot. But the vast majority of British Columbians pay less than 5% of their income in provincial income taxes, and thus such an increase represents less than 1% of income. For most people, a 20% increase amounts to between $200 and $800 a year. Detailed descriptions of all personal income tax reform scenarios discussed in this report are provided in Appendix 2 along with estimates of their distributional impacts by income level.
Source: Authors' calculations. Tax revenue estimates calculated using Statistics Canada's Social Policy Simulation Database/Model for 2012.

One of many possible tax reform scenarios...

If the **TOP 6%** of British Columbians (incomes over $103,000) paid a fair share of taxes, we could raise

$930 million

and

INCREASE welfare rates to cover basic food and housing needs

\+

SUPPORT families by properly funding Ministry programs

\+

RESTORE smaller class sizes in public schools

The reforms presented are not an exhaustive list, and we are not recommending that the province adopt all these options. Rather, we aim to inform the public debate with a range of possibilities and estimates of the revenues that each could raise.

Most of the options we have modeled would impact only a minority of upper-income British Columbians. For example, if we increase the tax rates in the current top three brackets, only about 14% of BC tax-filers would be affected. An increase to the current top bracket would impact only the richest 5.5%. A new tax bracket at $150,000 of income would impact the richest 2%. And a new bracket at $200,000 of income would impact only BC's top 1%.

These tax increases for higher income British Columbians could raise as much as $1.1 billion in new revenues. But if we also modestly increase the bottom two brackets — which in practice would mean about the cost of a cup of coffee a day for most of us — we could raise as much as $2.3 billion a year in new revenues. This would be enough to fund substantial investments in a number of important areas.

Tax brackets: Statutory tax rates vs effective income tax rates

BC has five tax brackets, or **STATUTORY** tax rates that apply to peoples' taxable income (that is, after deductions like RRSPs, child care fees, and business investment losses). These rates kick in at a series of set thresholds. No one pays any tax on their first $11,354 of income. A rate of 5.06% applies to taxable income between $11,354 and $37,013. A rate of 7.7% applies to taxable income between $37,013 and $74,028. And so on. It is a common misconception that once a person's income hits the threshold for the next tax bracket, the higher rate applies to their *entire* taxable income. This is not the case. The higher tax rate applies only to the dollars *above* that threshold. In addition, various refundable and non-refundable tax credits reduce total income tax payable.

The **EFFECTIVE** income tax rate is the actual amount of income tax paid as a share of a person's total income. The vast majority of British Columbians pay an effective provincial income tax rate of less than 5%.

OTHER OPTIONS: The report examines many other progressive tax reform options, including:

- Closing personal and corporate tax deductions. For example, the federal RRSP program costs the BC treasury almost half a billion dollars in foregone revenues each year. It is also one of the most inequitable social programs in Canada — most high-income people make extensive use of it, while few middle and modest earners can afford to do so.
- Making property taxes more progressive.
- Increasing and expanding the carbon tax, and restructuring the credit to ensure it leaves the bottom half of families better off.
- Increasing corporate taxes (currently the lowest in Canada).
- Reforming resource royalties (for forestry, water and natural gas) to ensure a fair return to the public. For example, natural gas production is at an all-time high in BC, but our royalty revenues are near an all-time low.
- Regulating and taxing cannabis, which could generate $500 million per year in new revenues.

The scope of unmet social and environmental needs in our province should compel us all to consider pitching in a little bit more to strengthen our communities and build a province we can all be proud of.

For most of us, our provincial income taxes are remarkably low, given the high quality of life we enjoy. The scope of unmet social and environmental needs in our province should compel us all to consider pitching in a little bit more to strengthen our communities and build a province we can all be proud of.

Ultimately, what British Columbians deserve is a comprehensive and thoughtful conversation about our overall tax system, such as a deliberative citizen-led decision-making process. The core questions we need to answer as a province are: What are the things we want to pay for together, and how can we raise the money needed in a way that ensures everyone pays a fair share? We hope this report can help kick-start that conversation.

PART 1

Introduction

BRITISH COLUMBIA NEEDS TO RAISE NEW REVENUES. If we are to truly rise to the challenges we face — climate change, growing income inequality, persistent poverty, and the affordability squeeze felt by so many families — we will need to take bold action together as a province, and that will require an increase in what we collectively raise and invest. Yet we are told repeatedly by our government and business lobby groups that we cannot afford it. We are told that we cannot even afford to sustain existing public programs like health care and education upon which we all rely, and that enhancing them or introducing vital new ones such as universal early learning and child care is out of the question.

This report makes the case for progressive tax reform in BC and presents a menu of possible tax policy options that would increase BC's fiscal capacity, create the budgetary room to meet our most pressing needs, and reduce income inequality.

Are our choices—in one of the richest provinces of one of the richest countries in the world—really so limited?

BC's finances are currently squeezed because, for more than a decade, a series of cuts to both personal and corporate taxes has steadily eroded our fiscal capacity. Relative to the total income generated in BC (our Gross Domestic Product or GDP) the provincial government raises less tax revenues than it used to. Moreover, it does so through a tax system that is much less fair. Taxes have been shifted from corporations to families, and from upper-income families to middle and modest-income ones. As a result, British Columbians now pay more out-of-pocket for a host of services, from school fundraisers and post-secondary tuition to seniors care fees. This cannot continue.

This report makes the case for progressive tax reform in BC and presents a menu of possible tax policy options that would increase BC's fiscal capacity, create the budgetary room to meet our most pressing needs, and reduce income inequality, which is higher in BC than in the rest of the country.[1] This is not an exhaustive list and we are not recommending that the province adopt all of the options we present. We merely aim to enrich the public debate by highlighting the broad range of tax policy options available, and estimating the revenues that each option could raise. Note, however, that there is room for countless specific formulations.

1 BC has the most unequal distribution of total income and after-tax income in Canada, as shown in Andrew Sharpe and Evan Capeluck, *The Impact of Redistribution on Income Inequality in Canada and the Provinces, 1981–2010* (Ottawa: Centre for the Study of Living Standards, 2012). See also Dan Schrier, *Infoline Report – Mind the Gap: Income Inequality Growing* (Victoria: BC Stats, 2012); and TD Economics, *Income and Income Inequality – A Tale of Two Countries* (2012).

Much of this paper focuses on personal income taxes—the most progressive element of any tax system—because they are a vital tool for reducing income inequality. However, personal income tax is only one element of the overall provincial tax system; the only way to ensure we collect the right amount of revenues from the right taxpayers is to examine all taxes on persons and businesses. Therefore we also outline progressive tax reform ideas for other areas of the provincial tax system, including corporate taxes, resource royalties, and the carbon tax.

WHY TAXES MATTER

Taxes are essential in a modern society. Taxes are how we:

- Fund public services and infrastructure—we buy things together that we cannot buy on our own. Pooling our resources through taxes is more efficient and allows us to provide equitable access to much needed services and infrastructure. This creates a safe, stable environment for communities, businesses and individuals to thrive.
- Meet a moral obligation to look after one another—by providing supports and services to one another when facing illness, unemployment, poverty or old age.
- Enhance economic security for all by spreading payment for certain high-cost needs (such as education and health care) across our lifetimes and our society. Progressive taxes ensure that we pay for the services we use when we're best positioned to do so—during our prime earning years—instead of paying at the point of use.
- Redistribute income in the face of market-driven inequality.
- Strengthen democracy by transferring some investment decisions from the private to the public sphere, where decisions can be made through a democratic process, not just by those wealthy enough to be shareholders.

Taxes are fundamentally about our quality of life. At their root, taxes come down to a simple question: Which goods and services do we want to pay for together as a society, and which do we want to pay for privately as consumers?

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Ultimately, what British Columbians deserve is a broad and thoughtful conversation about our overall tax system; a fulsome and deliberative citizen engagement process that allows us to consider these questions in a comprehensive manner. The core questions we need to answer as a society are: What are the things we want to pay for together, and how can we raise the money needed in a manner that ensures everyone pays a fair share? We hope this report can help kick-start that conversation.

PART 2

The Case for Progressive Tax Reform

THE HIGH PRICE OF TAX CUTS

BC now has the lowest provincial income taxes for individuals earning up to $120,000 and the lowest corporate income tax rates in the country (on par with Alberta and New Brunswick).[2] But a decade of tax cuts has produced few "savings" for most families, while out-of-pocket user fees for public services have risen (such as residential care fees for seniors and people with disabilities, university and college tuition, park use permits, etc.).

A decade of tax cuts has produced few "savings" for most families, while out-of-pocket user fees for public services have risen (such as residential care fees for seniors and people with disabilities, university and college tuition, park use permits, etc.).

At the same time, a number of public services have been scaled back or suffer from declining quality due to underfunding. Class sizes in our schools have increased and a large number of special needs children do not receive the supports they need to learn well. Many public schools now charge extra fees not just for field trips but for children to participate in sports teams, for instruments in music class or for materials in trades or arts classes. Hospital emergency rooms are overcrowded. Waiting lists for residential care and other community health services for seniors are so long that many seniors spend weeks and sometimes even months in hospital waiting for a spot.

Out-of-pocket user fees and deteriorating public services affect British Columbians differently depending on their particular age and circumstances, which makes it difficult to compare the increases in fees with tax cuts for an average BC family. However, they have eaten up a large portion of the tax "savings" for many if not most, and they weigh more heavily on lower-income families.

The BC government claimed that tax cuts would boost the economy, creating so many jobs they would pay for themselves. Instead, tax cuts have opened up a gaping hole in our public finances. Reduced fiscal capacity is the inevitable flip side of lower taxes, as foregone revenue is no longer available to meet our collective needs.

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2 BC Budget 2012. Interprovincial comparisons of personal income taxes are presented in Appendix 1. Notably, all provinces charge higher income tax rates than BC at incomes lower than $120,000. BC has the second lowest income taxes at incomes between $120,000 and $340,000 (after Alberta) and the third lowest for incomes between $340,000 and $730,000 (after Alberta and Newfoundland).

Six Waves of Tax Cuts/Changes Have Eroded BC's Fiscal Room

2001/02

- Personal income tax rates reduced by 25% across the board (the tax rate in each bracket was reduced by approximately 25%).
- Corporate income tax rate reduced from 16.5% to 13.5%.
- Corporation capital tax eliminated for non-financial corporations.

TOTAL COST: $2.1 billion

2005/06

- New non-refundable tax credit reduced or eliminated personal income taxes for lower-income British Columbians (income up to $26,000).
- Corporate income tax rate reduced from 13.5% to 12%.
- Small business tax threshold increased from $300,000 to $400,000.

TOTAL COST: $0.3 billion

2007/08

- Personal income tax rates in the first four brackets reduced by about 10%.

TOTAL COST: $0.5 billion

2008/09

- Carbon tax introduced alongside a package of tax cuts and credits aimed at making the tax "revenue-neutral" (i.e., returning all revenues to taxpayers):
    - Low-income carbon tax credit that is phased out above incomes of $30,000 for individuals and $35,000 for families;[3]
    - Personal income tax cuts in the bottom two brackets (i.e., on the first $70,000 of income);
    - Corporate income tax rate reduced from 12% to 10% over four years;
    - Small business income tax rate reduced from 4.5% to 3.5%.
- Corporation capital tax on financial institutions eliminated.
- Small business income tax rate reduced from 3.5% to 2.5% (as part of October 2008 economic plan).

TOTAL COST: $0.3 billion.[4]

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3 Like the GST credit, the low-income carbon tax credit is, technically speaking, a tax *benefit*: the amount for the current year is calculated based on income from the previous year's tax return.

4 While the carbon tax was intended to be revenue-neutral, it has proven to be, in practice, revenue-negative, largely due to the escalating cost of corporate income tax cuts phased in over its first four years. When the tax was introduced in the 2008 Budget, corporate income tax cuts were projected to cost $133 million in 2011/12, but the 2012 Budget reveals that the costs were more than double, $271 million. Personal income tax cuts, in contrast, cost less than projected.

2010/11

- HST introduced along with a series of rebates and credits intended to make the shift from PST "revenue-neutral":[5]
    - BC HST low-income credit introduced.[6]
    - Basic personal amount (i.e., the threshold for paying income tax) increased from $9,373 to $11,000.
- Small business tax threshold increased from $400,000 to $500,000.

  TOTAL COST: $0.1 billion

2012/13

- A number of income tax credits for individuals and corporations introduced, including exempting jet fuel from fuel tax, the children's fitness credit, the children's arts credit, and the BC seniors' home renovation tax credit.
- Plans announced to transition back to PST over 2013/14 (including a one-year BC first-time new home buyers' bonus and an increase in the BC HST new housing rebate threshold to $850,000 from $525,000). While the HST was introduced as a revenue-neutral tax change, it turned out to generate more revenues than anticipated. As a result, a shift back to PST is projected to reduce government revenues by $500 million in the first year.[7]

  TOTAL COST: $0.6 billion

Personal and corporate income tax rates in BC, 2001 and 2012

Tax bracket	Taxable income range (2012 dollars)*	January 2001 tax rates	January 2012 tax rates
1	$0 to $37,013	8.40%	5.06%
2	$37,013 to $74,028	11.90%	7.70%
3	$74,028 to $84,993	16.70%	10.50%
4	$84,993 to $103,205	18.70%	12.29%
5	Over $103,205	19.70%	14.70%
Corporate tax rate	Large corporations	16.5%	10%
	Small corporations	4.5%	2.5%

* Tax brackets are adjusted for inflation yearly. There have been no other changes to the income thresholds for BC provincial tax brackets over this period. The basic personal exemption (currently $11,354) is the effective threshold for paying income tax. The amount is also adjusted for inflation every year, and it was increased once over the period from $9,373 to $11,000 (effective January 2010). This increase is slated to be reversed with the return to PST (effective April 1, 2013).

5 The transition to HST was originally announced in the summer of 2009 instead of being introduced with a provincial budget as is customary for major tax changes. The full fiscal implications of the tax were presented in the 2010/11 BC Budget.

6 The HST low-income credit is technically a tax benefit like the GST credit and the low-income climate action tax credit, as explained in Footnote 4.

7 According to the Independent Panel's report on HST, *HST or PST/GST? It's Your Decision* (2011, 18), www.pstinbc.ca/independent_panel/

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To curb budget deficits in the early 2000s (after the first round of expensive tax cuts), the government introduced a round of steep spending cuts in all ministries. These cuts had far-reaching impacts on seniors' care, hospitals and schools, welfare, services to children and families, legal aid, women's shelters and a host of other program areas, which have been documented in previous CCPA research.[8] Despite five consecutive budget surpluses in the mid-2000s, many of these services have not been restored.

BC's taxation revenues have fallen significantly relative to the size of the provincial economy, from 11.6% of GDP in 2000/01 to 10% of GDP by 2011/12. This may seem like a small change, but 1.6 percentage points of provincial GDP in 2011 amounts to about $3.5 billion. In other words, if we collected in 2011 the same taxes as a share of our provincial economy as we did in 2000, we would have $3.5 billion more in the public treasury. This is revenue that could be used to fund much-needed programs and services.

THE EROSION OF TAX FAIRNESS

If we collected in 2011 the same taxes as a share of our provincial economy as we did in 2000, we would have $3.5 billion more in the public treasury. This is revenue that could be used to fund much-needed programs and services.

We need to restore fiscal capacity and raise new revenues, but we also need to ensure that any reforms result in a tax system that is fair and progressive overall. Over the past decade, the province has cut taxes in a way that fundamentally eroded the fairness of BC's overall tax system.

Most British Columbians would agree that everyone should pay their fair share of taxes. And most assume that the wealthy pay more, not only in straight dollars, but also a higher tax *rate* as a share of their income. This is how income taxes work. But other taxes we pay — sales, carbon, property, and MSP premiums — are regressive, which means that they cost lower and middle-income households more as a share of their income. Most British Columbians would probably be surprised to learn that when all personal taxes are considered, the richest BC households now pay a *lower* total provincial tax rate (when all provincial taxes are combined) than the rest of us.

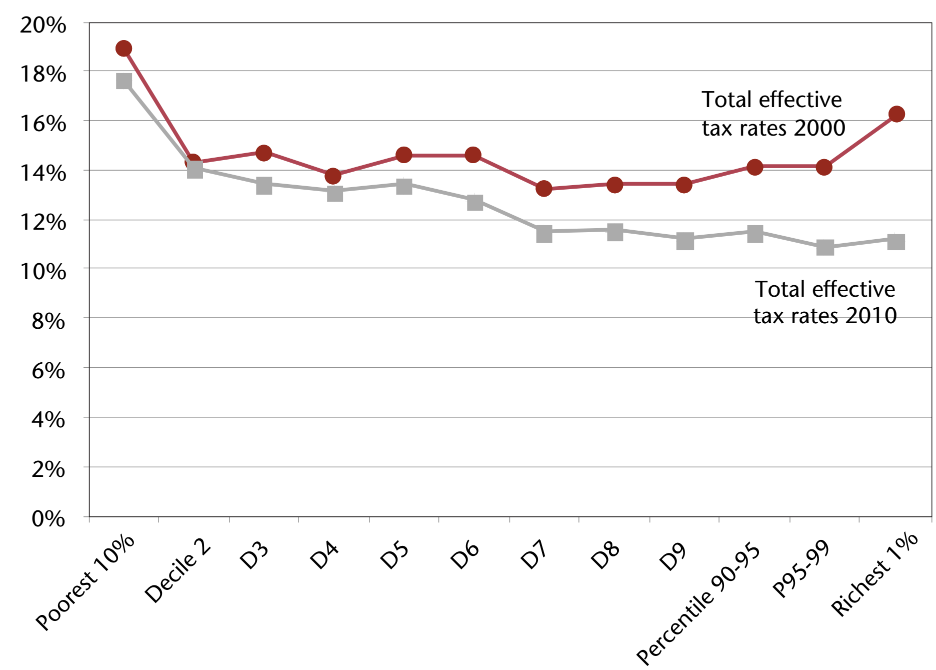
This trend is documented in a recent CCPA report, *BC's Regressive Tax Shift: A Decade of Diminishing Tax Fairness, 2000 to 2010*.[9] Using Statistics Canada's Social Policy Simulation Database and Model, a database that draws on tens of thousands of tax files, the report examined how tax policy changes over a 10-year period affected the total provincial tax rate paid by households at different income levels (the actual tax bill as a share of household income for all personal provincial taxes combined — income, sales, carbon and property taxes, and MSP premiums).

In 2000, most BC households paid about the same total tax rate, with the richest 10% paying a little more. By 2010, however, the tax system had become regressive — the higher your income, the lower your overall BC tax rate. The result can be seen in Figure 1.

8 See, for example, the CCPA–BC publications: Marcy Cohen, Jeremy Tate and Jennifer Baumbusch, *An Uncertain Future for Seniors: BC's Restructuring of Home and Community Care, 2001–2008* (2009); Seth Klein and Jane Pulkingham, *Living on Welfare in BC: Experiences of Longer-Term "Expected to Work" Recipients* (2008); Bruce Wallace, Seth Klein and Marge Reitsma-Street, *Denied Assistance: Closing the Front Door on Welfare in BC* (2006); Marc Lee, Stuart Murray and Ben Parfitt, *BC's Regional Divide: How Tax and Spending Policies Affect BC Communities* (2005).

9 Marc Lee, Iglika Ivanova, and Seth Klein, *BC's Regressive Tax Shift: A Decade of Diminishing Tax Fairness, 2000 to 2010* (Vancouver: CCPA–BC, 2011).

Figure 1: BC Total Personal Tax Rates by Income Group, 2000 and 2010



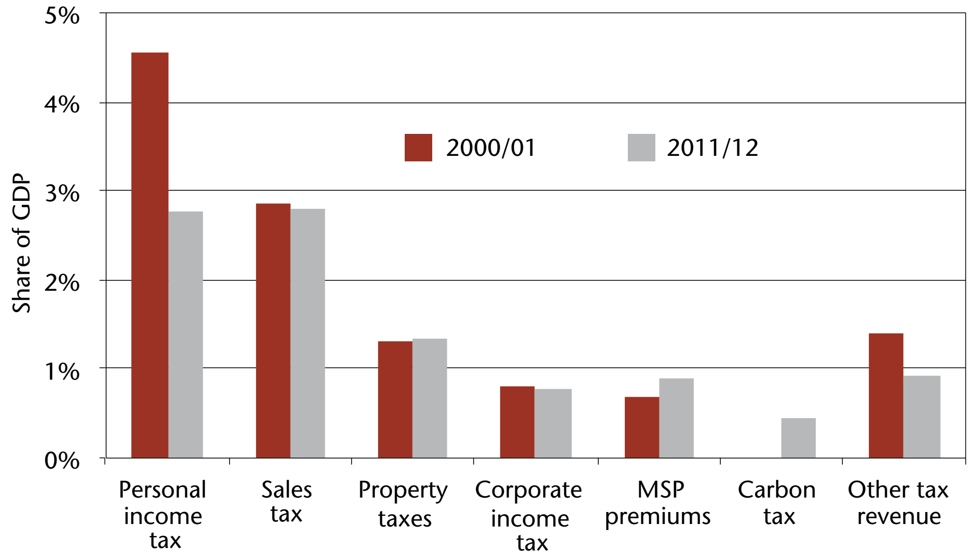
Source: Marc Lee, Iglika Ivanova and Seth Klein, *BC's Regressive Tax Shift: A Decade of Diminishing Tax Fairness, 2000 to 2010* (CCPA–BC 2011, Figure 2).

By 2010, the tax system in BC had become regressive—the higher your income, the lower your overall BC tax rate.

In dollar terms, over the past decade lower-income households received an average tax cut of a couple of hundred dollars per year, those in the middle benefitted from a tax cut of just over $1,200, and those in the top 10% pocketed on average over $9,000 per year in combined tax savings. For the top 1% of BC households, the tax cut was worth more than $41,000 per year. Notably, their tax cut was larger than the average incomes for the poorest 30% of households.

The last decade of tax policy has also fundamentally shifted the mix of sources of provincial revenues. The BC personal income tax system remains mildly progressive, meaning, as household income rises, so too does the tax rate. But, as seen in Figure 2 on page 18, because income taxes have been cut, income tax revenues have dropped by one third over the last decade (when compared to the size of the provincial economy) and now raise about the same amount as sales taxes. And notably, the provincial treasury now collects more from Medical Service Plan premiums than it does from corporate income taxes.

Figure 2: BC Tax Revenues by Source as a Share of GDP, 2000/01 and 2011/12



Source: Authors' calculations based on *BC Financial and Economic Review – July 2012*, Table A2.5.

Income tax revenues have dropped by one third over the last decade (when compared to the size of the provincial economy) and now raise about the same amount as sales taxes. And notably, the provincial treasury now collects more from Medical Service Plan premiums than it does from corporate income taxes.

The province's greater reliance on highly regressive MSP premiums is particularly troubling. Between 2000 and 2013, MSP premiums increased by $366 for a single person, and by $732 for a family of three of more—both increases of a dramatic 85%. According to BC Ministry of Finance calculations, a family of four with an annual income of $60,000 in 2012 will pay more in MSP premiums ($1,536) than in provincial personal income tax ($1,190).[10] BC is alone in the country in choosing to raise revenues in such a regressive manner, using what is effectively a head tax, with all but low-income households paying the same dollar amount regardless of their means. $1,536 is a significant amount for a modest income family with children, but it is negligible for a family among the top 10%.[11]

The point here is not that income tax should be the only provincial tax, replacing all other taxes (though we model a plan to replace MSP premiums with income taxes later in this report), but that we need to readjust the tax mix to establish a system that is in total progressive.

Overall, BC has witnessed a number of core shifts in how it raises revenues:

- From corporations to households;
- From upper-income households to middle and modest-income households; and
- From progressive income taxes to regressive consumption taxes, MSP premiums, and out-of-pocket user fees for public programs and services.

10 *BC Budget 2012,* Table A3.

11 Alberta had a very similar health premium, but it was eliminated effective January 1, 2009. Quebec charges a health premium, but instead of a flat amount, the premium depends on one's income.

BC'S INCOME TAXES ARE WELL BELOW THE NATIONAL AVERAGE

For too long, BC political leaders have boasted about having the lowest taxes in the country for almost all individuals (see Appendix 1 for a detailed comparison of provincial income tax rates at different income levels). This is nothing to be proud of, especially when we also have the highest poverty rate of any province, the second-highest child-poverty rate, and the highest rate of income inequality in the country. BC clearly pays a fiscal price for this choice in diminished government revenues and reduced fiscal capacity to meet pressing needs.

If anything, BC's experiment in tax cutting provides evidence that lower taxes do not lead to a stronger economy. BC's economic and employment record has been fairly average in Canada despite our considerably lower taxes. In 2010, BC ranked fifth out of 10 provinces according to economic performance, fourth according to personal income, seventh in jobs and ninth in social conditions.[12] Similarly, BC's economic performance since 2001 has not been stronger than the decade prior to large tax cuts: real GDP grew by 31% over the 1990s (when taxes were higher) compared to 25% over the 2000s, while total employment grew by 22% over the 1990s compared to 19% during the 2000s.[13]

If anything, BC's experiment in tax cutting provides evidence that lower taxes do not lead to a stronger economy. BC's economic and employment record has been fairly average in Canada despite our considerably lower taxes.

A recent report from the BC Business Council confirms that BC's economic performance over these two decades is comparable and finds that investment in machinery and equipment grew more slowly over the 2000s than it did over the 1990s, when corporate taxes were considerably higher.[14] This is because other factors, such as the decline of the forest industry in BC, the ups and downs of global commodity prices, and changes in the value of the Canadian dollar have a much larger impact on BC's economy than our tax rates.

BC would be in a much better position if we pooled a little more of our collective resources through taxes and used them to invest in public services that improve our quality of life. These public investments would also benefit businesses that operate in our province: our public health care system provides a competitive advantage to businesses operating in Canada compared to their US counterparts who face much higher employee benefits costs.[15] Given that we currently have the lowest income tax rates in the country, a lot could be done if we simply matched the average taxes other provinces collect.

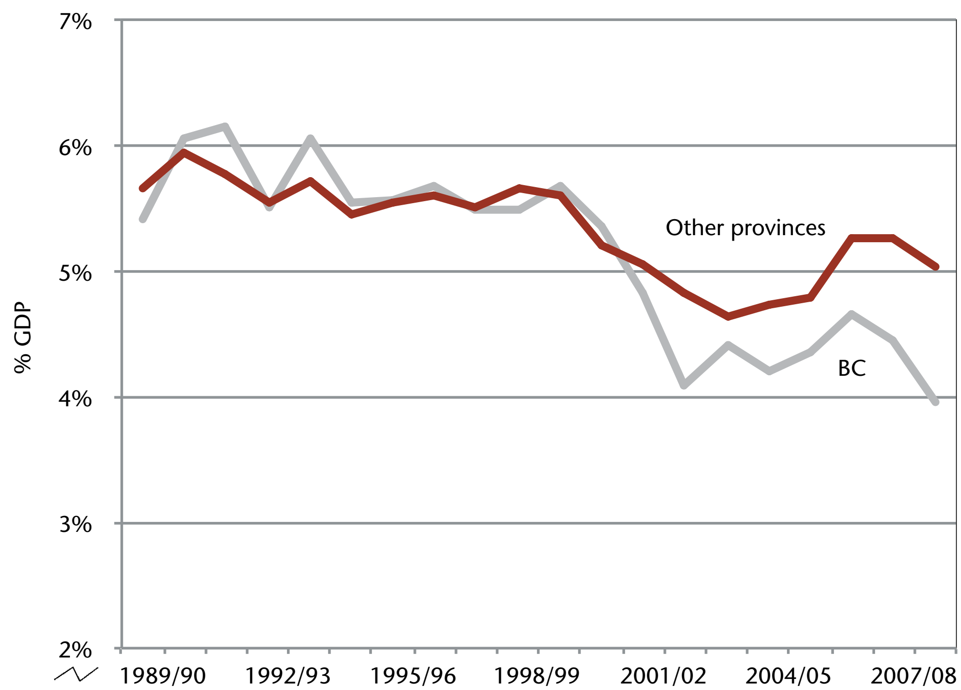
12 BC Progress Board, *2011 Benchmark Report* (2012). "Social conditions" includes indicators of quality of life for marginalized citizens such as poverty rate (as measured by Statistics Canada's LICO), proportion of the population relying on income assistance, crime rates, low birth weight rate, and long-term unemployment. According to the BC Progress Board Rankings, over the first decade of the 2000s, BC lost ground relative to other provinces in economic performance, jobs and personal income and remained second to last in social conditions.

13 Authors' calculations based on Statistics Canada data on employment and GDP.

14 Peter Severinson, Jock Finlayson and Ken Peacock, *A Decade by Decade Review of British Columbia's Economic Performance* (Vancouver: Business Council of British Columbia, 2012).

15 See, for example, Guy Caron and Jan Malek, *Best Kept Secret: Canada's Health Care Competitive Advantage* (Ottawa: The Council of Canadians, 2008).

Figure 3: Provincial Income Tax Revenue and Health/Drug Insurance Premiums as a Share of GDP



Source: Statistics Canada, CANSIM Table 385-0001: Consolidated federal, provincial, territorial and local government revenues and expenditures and CANSIM Table 384-0001: Gross domestic product (GDP), income-based, provincial economic accounts. Note: 2008/09 is the final year for which data on government revenues are available on a Financial Management System (FMS) basis as Statistics Canada is in the process of moving to a new accounting standard and will not be producing data on government revenues until 2014.

In 2008/09, the last year for which Statistics Canada data is available, BC collected 3.9% of its GDP in income tax (including MSP premiums), compared to 5% for all other provinces. If BC collected the same level of personal income tax revenues as a share of GDP as the other provinces, the BC treasury would have $2.4 billion more every year.

As seen in Figure 3, during the 1990s, BC tracked the national average with respect to the collection of personal income taxes (including MSP premiums). Since the early 2000s, however, BC has collected significantly less personal income tax as a share of GDP than other provinces.[16] While all provinces have reduced their personal income taxes over the last decade, tax cuts have been steeper in BC. In 2008/09, the last year for which Statistics Canada comparative data is available, BC collected 3.9% of its GDP in income tax (including MSP premiums), compared to 5% for all other provinces. If BC collected the same level of personal income tax revenues as a share of GDP as the other provinces, the BC treasury would have $2.4 billion more every year.

16 BC is the only province that charges MSP premiums as a per-person amount regardless of income or employment situation. Alberta used to charge a health care insurance premium similar to MSP, which was eliminated as of January 2009 (so the last year of data available 2008/09 includes three quarters of a year worth of health premiums).

THE PUBLIC IS READY FOR A THOUGHTFUL CONVERSATION ABOUT TAXES

The good news is that British Columbians increasingly understand that we need to raise new revenues, that taxes pay for services that improve our quality of life, and that BC's tax system has become much less fair and is in need of reform. A major new opinion poll commissioned by the CCPA (conducted by Environics Research) reveals that public opinion is shifting.[17] On the whole, British Columbians appear ready to consider tax reform — and even tax increases — with more openness than political leaders seem to appreciate.

British Columbians want to see a significant redistribution of income — away from the richest 20%, towards the middle and the bottom. The overwhelming majority of British Columbians (90%) think there should be income tax increases for those at the top. A clear majority (57%) believe that should kick in at $100,000 per year of income. A majority (67%) also think major corporations are asked to pay less tax than they should.

These responses cut across party lines. It is not just those who would vote NDP or Green in a provincial election who think high-income individuals and corporations should pay more tax. A majority of Liberal and Conservative voters say the same.

A major new opinion poll commissioned by the CCPA reveals that public opinion is shifting. On the whole, British Columbians appear ready to consider tax reform — and even tax increases — with more openness than political leaders seem to appreciate.

A further surprise is the degree of openness British Columbians show when it comes to potential tax increases for *themselves*. When initially asked a general question about their own level of taxation, most people feel they pay too much — no surprise given the cost of living challenges many wrestle with. But, when taxes are linked to concrete policies that can reduce inequality and improve our quality of life, the story changes.

Respondents were asked if they would consider paying a slightly higher share of their own income to provincial income tax (for most people representing a few hundred dollars per year) in order to help bring about 11 different policy changes. The changes included things like providing more access to home and community based health care for seniors, increasing welfare benefit rates, creating a $10 per day child care program, protecting BC's forests and endangered species, or reducing class sizes in schools.

The results are striking: 68% said they are willing to pay a higher share of their income to help bring about four or more of the 11 policies. And once again, this held true for majorities regardless of which political party people intended to vote for in the next provincial election.

That said, this opinion research also made clear that people aren't interested in writing a blank cheque to government. They are prepared to entertain tax increases, but only under the right conditions. People want greater transparency and accountability from their governments. They want to know the money will be well spent on needed programs. And most importantly, they want to have a say in how decisions are made.

17 Shannon Daub and Randy Galawan, *Beyond the 1%: What British Columbians Thinks About Taxes, Inequality and Public Services* (Vancouver: CCPA–BC, 2012), www.policyalternatives.ca/bc-tax-opinion

PART 3

Options for Raising New Revenues and Reducing Inequality

Tackling income inequality requires that we increase BC's high-income personal tax rates to strengthen the redistributive role of the provincial tax system.

THERE ARE NUMEROUS WAYS TO RAISE MORE REVENUES for needed public programs and services. To illustrate the range of possibilities, we present a selection of possible tax reforms with respect to both personal and business taxes.

Personal Tax Options

Growing inequality over the last 20 years has been driven by big gains at the very top. Our tax system has reinforced market income disparities with generous tax cuts for the wealthy and an erosion of income support programs for the less well off.[18] Tackling income inequality requires that we increase BC's high-income personal tax rates to strengthen the redistributive role of the provincial tax system.

18 Welfare rates have eroded over the 2000s and new eligibility criteria have made it harder for many marginalized British Columbians to qualify for support.

INCREASE TAX RATES AND CREATE NEW BRACKETS

There are a number of ways to raise income taxes. First, one must decide at what income level taxes should be increased. There is no one right answer here. But if reducing inequality is the goal, increases for the highest-income 20% of individuals should be considered, with rates progressively increasing for the top 10%, 5%, 2% and 1%. This would entail increases in the top three provincial income tax brackets, as well as new high-income tax brackets on incomes above $150,000 and $200,000 to capture the richest 2% and 1% respectively.

BC currently has five income tax brackets, and in 2012 the top rate kicked in at a taxable income of $103,205. Table 1 shows the share of tax-filers whose income (before deductions) puts them in each tax bracket (the tax brackets are annually adjusted for inflation, and so back in 2009, the last year for which we have detailed tax filer data, this top bracket kicked in at an income of $99,588).

If reducing inequality is the goal, increases for the highest-income 20% of individuals should be considered, with rates progressively increasing for the top 10%, 5%, 2% and 1%.

Table 1: Selected BC income tax statistics, 2009 tax year

Tax bracket	Taxable income range	2009 tax rates	Approximate share of individuals in this income range*
Up to basic personal exemption	$0 to $9,373	0%	19%
1	$9,373 to $35,716	5.06%	40%
2	$35,717 to $71,433	7.70%	27%
3	$71,433 to $82,014	10.50%	4%
4	$82,014 to $99,588	12.29%	4.5%
5	Over $99,588	14.70%	5.5%

Notes: *Income range is approximate and reflects the share of tax filers with total income in the nearest income group as listed in the CRA data (under $9,999, $10,000 to $34,999, $35,000 to $69,999, $70,000 to $79,999, $80,000 to $99,999, and over $100,000). British Columbians pay income tax on their individual income, not on their combined family income, which is why all tax filers are represented as individuals in this table.

Source: Authors' calculations based on latest available CRA data, T1 Final Statistics, 2009 tax year, Final Table 2: All Returns by Total Income Class, British Columbians. Note also that total income is as reported on tax forms and includes only the taxable amount of capital gains (50%) and dividends, but excludes non-taxable government transfers (low income credits such as GST credit, CCTB, etc).

While the range of possible adjustments to BC's tax brackets and rates is endless, we model 16 scenarios overall to illustrate how much revenue can be expected from each and how taxpayers at different income levels would be affected. [19] These scenarios are presented in detail in Appendix 2 along with estimates of their distributional impacts by income level. The following sections highlight a few examples.

19 Unless otherwise noted, all tax revenue estimates in this report are calculated using Statistics Canada's SPSD/M model for 2012. See the Technical Appendix for details.

TERMINOLOGY

A Quick Guide to BC Income Tax Terms

While all British Columbians are obliged to report the income they receive from wages, salaries, self-employment and other sources (their **TOTAL INCOME,** as listed on page 2 of their tax return), they do not necessarily pay taxes on all of it. Certain deductions are subtracted from total income, such as registered pension plan deductions, RRSP deductions, union dues, child care expenses, business investment losses, and security options deductions (see page 3 of a federal tax return).

British Columbians pay income tax only on their income after allowable deductions; that is, on their **TAXABLE INCOME.**[20] In addition, various refundable and non-refundable tax credits reduce total income tax payable. Depending on family circumstances and major sources of income (wages versus business or investment income), there may be a large gap in taxes paid at the same level of total income.

BC has five tax brackets with rates increasing from 5.06% in the bottom bracket to 14.7% in the top bracket. No income tax is paid on the first $11,354 of income. The rate assigned by law to each bracket is known as the **STATUTORY TAX** rate. The BC income tax system has five different statutory rates, as shown in Table 1 on page 23.

The **EFFECTIVE TAX RATE** is the total income tax paid as a share of total income. For example, the top bracket tax rate in BC is currently 14.7% but a single individual earning half a million dollars per year currently pays an effective tax rate of only 13.1% of their total income in provincial income tax (and that's without any deductions for RRSP contributions or charitable donations, which would additionally reduce one's effective tax rate). BC's effective tax rates for individuals at different income levels between $10,000 and $1,000,000 are presented in Appendix 1, alongside the corresponding effective tax rates of each Canadian province.

The tax rate charged on income in the highest bracket is referred to as the **TOP MARGINAL TAX RATE.** This is the tax rate that applies to the last dollar earned by higher-income individuals. Notably, because BC's statutory tax rates in the bottom two brackets are so low relative to other provinces, even if BC's top marginal tax rate were substantially higher than in other provinces, the overall **EFFECTIVE** tax rate even for very high-income earners would still remain relatively low (at least until one reaches well into the top 1% of earners).

20 If you take a look at your tax forms from last year, you can find your *total income* on line 150 and your *taxable income* on line 260.

INCREASE INCOME TAX FOR HIGHER INCOME INDIVIDUALS

Table 2: Income Tax Options at the Very Top

Tax change (note these are single changes, not cumulative)	Potential provincial revenues raised	Would impact (% of tax filers)
Increase the current top (5th) bracket rate from 14.7% to 17%	$375 million	Top 5.5%
New tax bracket at $150,000 of income with a tax rate of 18%	$400 million	Top 2%
New tax bracket at $200,000 of income with a tax rate of 22%	$725 million	Top 1%
Two new brackets at the top: 18% on income $150,000–$200,000; and 21% on income over $200,000	$700 million	Top 2%
Increase the current top (5th) bracket rate to 17%, and add two new upper income brackets: 20% on income $150,000–$200,000, and 22% on income over $200,000	$930 million	Top 5.5%
Two new upper-income brackets (at 20% and 22%) plus increases to the tax rates in the existing top three brackets (to 12.29%, 14.7% and 17%, respectively)	$1.1 billion	Top 14%

The vast majority of British Columbians would be unaffected by these tax increases. As seen in Table 1, close to 60% of all tax filers fall in the first tax bracket or pay no income tax at all because their income is so low it is below the basic personal exemption. About 86% of BC tax-filers have income below $70,000, and thus only pay taxes under the first two brackets.

Yet our analysis shows that higher income tax rates for top earners could yield some much-needed income to the public treasury. The amount would depend on the exact rated adopted, but for example, a new 18% tax rate on income over $150,000 could generate about $400 million in new provincial revenues — enough to build about 2,000 new units of social housing per year, to give but one comparison.

Adding a second new tax bracket with a rate of 21% on income over $200,000 could generate an additional $300 million on top of that. This could provide a long-overdue increase to welfare rates, which have been eroded by inflation since the last increase over five years ago.[21]

A new 18% tax rate on income over $150,000 could generate about $400 million in new provincial revenues — enough to build about 2,000 new units of social housing per year. Adding a second new tax bracket with a rate of 21% on income over $200,000 could generate an additional $300 million on top of that. This could provide a long-overdue increase to welfare rates.

21 For example, increasing welfare benefit rates by $200/month for single recipients, $300 for couples, and $400 for families with children would cost approximately $383 million a year. See Seth Klein, Lorraine Copas and Adrienne Montani, *BC's welfare recipients need immediate relief* (CCPA–BC, April 24, 2012), www.policyalternatives.ca/publications/commentary/bcs-welfare-recipients-need-immediate-relief

INCREASE INCOME TAX FOR THE TOP 20%

If we wanted to increase taxes for the top 20% of BC tax filers, it would be necessary to split what is currently the second tax bracket (as the threshold income for the top 20% of British Columbians is about $60,000 a year,[22] and the second tax bracket currently spans $37,013 to $74,028).

Table 3: Income tax options for the top 20%

Tax change (note these are single changes, not cumulative)	Potential provincial revenues raised	Would impact (% of tax filers)
Lower the threshold of the second tax bracket from $74,028 to $60,000	$200 million	Top 20%
Combine the above tax bracket change with two new upper-income brackets (with tax rates of 20% and 22%) plus increases to rates in the existing top three brackets (to 12.29%, 14.7% and 17%, respectively)	$1.4 billion	Top 20%

INCREASE ALL TAX RATES

All of the above scenarios would impact only the top 20% of BC tax filers. However, as the CCPA/Environics poll indicated, under the right conditions, a substantial majority of British Columbians are prepared to pitch in a little more in taxes.

Table 4: Income tax options for broad-based tax increases

Tax change (note these are single changes, not cumulative)	Potential provincial revenues raised	Would impact (% of tax filers)
Increase the tax rate in each current tax bracket by 10% (meaning, the first bracket would go from 5.06% to 5.57%, the second from 7.7% to 8.47%, etc.)	$890 million	81%
Increase the tax rate in each bracket by 20%	$1.8 billion	81%
Increase the tax rate in each bracket by 20%, and add two new upper-income tax brackets (20% on income $150,000–$200,000; and 22% on income over $200,000)	$2.3 billion	81%

Of course, a 20% increase to tax rates sounds like a lot. But as noted above, the vast majority of British Columbians pay an overall effective tax rate of less than 5% in provincial income taxes, and thus such an increase represents less than 1% of their total income. For most people, a 20% increase amounts to between $200 and $800 a year.

22 According to CRA data, T1 Final Statistics, 2009 tax year, Final Table 2.

Indeed, right up to individuals with taxable income of $150,000, all the tax options we model generate income tax increases of 2% or less of taxable income. BC would remain the lowest or second lowest tax jurisdiction in Canada for individuals earning less than $120,000 under all the scenarios modeled in this report. Appendix 2 details the impact of the changes we model in dollar terms and as percentage of income for individuals earning from $10,000 to $1 million.

RE-INTRODUCE SURTAXES

An alternative approach to raising rates or introducing new brackets would be for BC to adopt one or two upper-income *surtaxes*. Surtaxes are surcharges levied on the provincial income tax payable above a certain threshold (for example, above provincial tax of $5,000), rather than being a tax on income above a certain income threshold. Surtaxes affect individuals at the top of the income ladder because they are the ones who pay higher provincial taxes that can place them above the surtax threshold. The exact income level at which a surtaxes kick in depends on how the threshold is set and what kind of tax deductions and credits are available to tax filers. The federal system used to include two surtaxes (put in place as part of Canada's deficit reduction plans in the late 1980s), as did the BC tax system until the year 2000. Ontario and PEI still have income surtaxes.

Introducing a two-level surtax, similar to Ontario's, of 20% on provincial tax over $4,213 and an additional 19.65% on provincial tax over $5,392 would raise about $1.02 billion in new revenues.

BC could consider upper-income surtaxes specifically linked to poverty and homelessness reduction measures (to reduce income inequality),[23] or to climate action measures (given that upper-income households have higher greenhouse gas emissions).[24] Introducing a two-level surtax, similar to Ontario's, of 20% on provincial tax over $4,213 and an additional 19.65% on provincial tax over $5,392 would raise about $1.02 billion in new revenues.[25]

Such surtaxes would kick in at incomes of about $85,000 and $95,000 respectively, although in practice the exact income threshold would vary by individual depending on the deductions and credits for which they are eligible. In most cases, the surtaxes would take effect at higher income levels and the extra tax would be very modest until incomes reach well beyond $100,000.

For example, a person with taxable income of $90,000 (i.e. after deductions) owing $5,756 in provincial income tax would pay an extra surtax of $380 (20% of the difference between $5,756 and $4,213 and 19.65% of the difference between $5,756 and $5,392), which is a mere 0.4% of their taxable income (and likely a smaller share of their total income). More details on the dollar impacts of such surtaxes on individuals by taxable income are available in Appendix 2.

Alternatively, surtaxes could be designed to kick in at slightly higher income levels, such as to affect only the top 5% of filers—those with income over $100,000. For example, a two-level surtax charging 20% on provincial tax over $6,000 and 19.65% on income over $8,000 would kick in at incomes of about $100,000 and $120,000 with typical deductions and credits claimed by individuals at these income levels. Such a surtax would raise $850 million in new revenues for BC.

23 Poverty reduction measures should include policies such as increased welfare rates, enhanced community health care for frail seniors and people with disabilities, steps toward a comprehensive child care plan, and improved education and training opportunities for low-income people.

24 Marc Lee and Amanda Card, *Who Occupies the Sky? The Distribution of GHGs in Canada* (Ottawa: Canadian Centre for Policy Alternatives, 2011).

25 Ontario's surtax on income over $5,392 is 36%, but we model a lower surtax of 19.65% to match Ontario's top marginal tax rate. This is one way to set surtax rates, but BC need not be overly constrained by other provinces' tax systems.

The possibilities for setting surtax rates are numerous. In general, increasing the tax rate at the first surtax threshold and lowering the rate at the second threshold would generate higher revenues for the same top marginal income tax rate, albeit in a less steeply progressive way (though still more progressive than the current system of five tax brackets).[26]

The two examples above model surtax rates based on Ontario's current system, matching Ontario's current top marginal tax rate (which is lower than Nova Scotia and Quebec's rates), although BC should consider going further.

REDUCE LOOPHOLES AND BOUTIQUE TAX CREDITS

A core factor undermining the progressivity of our income tax system is the vast array of tax deductions, exemptions and other credits that disproportionately benefit high-income individuals. These credits and deductions represent forgone government revenues—technically known as "tax expenditures." Tax expenditures are considerably less transparent than other government spending measures, and their amounts are generally not subject to discussion and debate in the legislature. While some of these tax credits are available to all or most tax filers (such as the basic personal exemption, the age amount for seniors, the deduction for children and other eligible dependents, or the child care deduction), and some specifically benefit lower-income households (such as the Canada Child Tax benefit or the BC sales tax credit), a large number of deductions and credits can be claimed only by those with very high incomes and/or income from businesses or capital (that is, financial and real estate investments).

A core factor undermining the progressivity of our income tax system is the vast array of tax deductions, exemptions and other credits that disproportionately benefit high-income individuals.

For example, only half of capital gains (i.e., the profit earned from selling a capital asset such as real estate, a bond, or a stock, at a price higher than the original purchase price) are treated as taxable income, while the other half is earned tax free, a tax expenditure that costs the federal government approximately $3.6 billion per year, and mainly benefits upper-income people. Sales of primary residences are entirely exempt from capital gains tax at a cost of $4.2 billion per year, even though considerable gains have been made in hot urban real estate markets like Vancouver. There is a lifetime capital gains exemption of $750,000 for small businesses and farms, which costs $560 million per year.[27]

RRSP deductions are another example of a tax expenditure than disproportionately benefits the affluent. RRSP contributions (up to an annual limit) are tax deductible and the income generated by the contribution is fully sheltered from tax as long as it remains in the plan. The maximum RRSP deduction for 2012 was $22,970, and this does not include any unused room from previous years. Only someone with a very high income would have over $22,000 in extra income to put into this publicly-subsidized savings plan. In contrast, a minimum-wage earner working full-time all year would have an entire annual income of only about $20,000.

26 At first glance, setting a lower tax rate at the second surtax level may make the system seem regressive, but this is not actually the case. Surtax rates are applied to all provincial tax above each of the surtax thresholds, with the two surtax levels entirely independent of one another.

27 As estimated by Finance Canada, *Tax Expenditures and Evaluations 2011* (2012).

The RRSP is one of the most expensive and inequitable social programs in Canada, and it has proven inadequate as a mechanism to generate sufficient retirement savings for most Canadians.[28] The program costs the federal treasury about $10 billion a year in net foregone revenues, that is, after taking into account taxes paid on RRSP withdrawals in retirement, with additional costs to each province.[29] Yet, while more than two-thirds of those making over $100,000 a year contribute to RRSPs, less than a quarter of those making less than $50,000 are able to contribute.[30]

Even tax deductions that seem like they help middle or lower-income people (like the children's fitness and arts tax credits) amount to very small savings for each family ($25 for each of fitness and arts, but only after spending $500 on eligible programs per child). They are often of no help to the poor who cannot afford the program fees to begin with, and are predominantly used by middle or upper income families who would engage in these activities anyway.[31] Eliminating these tax credits and investing in actual programs available to all children, for example, would benefit a lot more British Columbians.

Incorporation rules for self-employed professionals also merit reconsideration. Under the current system, self-employed professionals, including doctors, dentists, lawyers and accountants, often incorporate. This allows them to pay corporate tax on the income they earn, which is much lower than personal income tax. In addition to paying less tax on their income, incorporation allows high-earning self-employed professionals to essentially defer their income until later when their total income is less (similar to RRSPs but with unlimited room for deferred income). There is no economic reason for this. Self-employed professionals should be taxed at the same rate as all other British Columbians who earn income from working — through our progressive personal income tax system. This would improve fairness in the system and raise more revenue, while helping to address income inequality at the very top.[32]

If we eliminated or at least scaled back some of these tax expenditures, our tax system would become more equitable, and we could raise significant revenues without altering statutory tax rates at all.

The problem for BC is that most of these breaks (particularly the most costly and regressive tax expenditures) are provided under the *federal* tax system. Yet they severely undercut BC's tax revenues. For example, the federal RRSP program costs close to half a billion in foregone provincial income tax revenues to BC each year.[33] That's because these federal deductions are used for calculating an individual's "net taxable income," which in turn is the figure used for calculating one's BC income taxes (as well as federal income taxes).

If we eliminated or at least scaled back some of these tax expenditures, our tax system would become more equitable, and we could raise significant revenues without altering statutory tax rates at all. For example, the federal RRSP program costs close to half a billion in foregone provincial income tax revenues to BC each year. Much new revenue could be raised if BC were to liberate itself from federal tax policy choices that undermine progressivity and our fiscal capacity.

28 See, for example Michael Wolfson, *Projecting the Adequacy of Canadians' Retirement Incomes: Current Prospects and Possible Reform Options* (Montreal: Institute for Research on Public Policy, 2011). Most current research points to the unsuitability of voluntary programs such as the RRSP to serve as a basis of a retirement income security program, due to low participation rates. Compulsory contribution programs, such as the CPP/QPP, are much better suited for the task.

29 $9.9 billion in 2011, as estimated by Finance Canada, *Tax Expenditures and Evaluations 2011* (2012).

30 According to the CCPA's 2012 Alternative Federal Budget.

31 John Spence, Nicholas Holt, Julia Dutove, Valerie Carson. "Uptake and Effectiveness of the Children's Fitness Tax Credit in Canada: The Rich Get Richer," *BMC Public Health* 10:356 (2010). See also Kevin Milligan, "Fitness a Worthy Goal – But Not With Gimmicky Tax Credit," *Globe and Mail: Economy Lab,* April 3, 2011.

32 A recent study from the University of British Columbia found that 11% of the richest 1% of Canadians are doctors. Nicole Fortin, David A. Green, Thomas Lemieux, Kevin Milligan, and W. Craig Riddell, "Canadian Inequality: Recent Developments and Policy Options," *Canadian Public Policy* 38 (2) (2012): 121–145.

33 According to BC Budget 2012, the RRSP deduction costs BC $459 million.

Much new revenue could be raised if BC were to liberate itself from federal tax policy choices that undermine progressivity and our fiscal capacity. There are two ways to deal with this. One option is for BC to refuse to match federal tax credits (as we are doing with the public transit tax credit or the textbook amount), or to introduce our own (lower) provincial caps to deductions such as the RRSP deduction.

Alternatively, BC could adopt a minimum tax, which limits the kind of tax deductions that can be claimed or the amounts that can be claimed in certain deductions for high-income individuals. A minimum tax can be designed to kick in at a certain high income threshold for total income assessed, for example $100,000, $200,000 or $500,000, to ensure that high income individuals pay a minimum effective tax rate as a share of their income. Without minimum tax provisions, certain high income individuals can take advantage of so many tax breaks that their effective tax rate becomes lower than that of many middle income families.

Would this increase the administrative burden of the provincial income tax system? Unlikely. In an era when many individuals and all accountants use software to prepare income tax returns, calculating one's minimum after excluding certain deductions (such as the capital gains exclusion), or lowering the allowable deductions amounts (such as reducing the RRSP deduction ceiling), can be easily built into the software and calculated with the click of a button. Broadening the income base in this way could result in a few hundred million dollars more for the provincial treasury.

GET RID OF MSP PREMIUMS

The MSP premium is BC's most regressive tax, charging a flat dollar amount per person or family. Households with $50,000 of income and those with $500,000 of income pay the same amount, now $1,596 per year for a family of three or more.

As noted earlier, the MSP premium is BC's most regressive tax, charging a flat dollar amount per person or family. Households with $50,000 of income and those with $500,000 of income pay the same amount, now $1,596 per year for a family of three or more, an amount that is inconsequential for upper-income families, but a significant expenditure for modest-income ones. MSP premiums represent 3% of income for the family earning $50,000 but only 0.3% of income for a family earning $500,000.

And adding insult to injury, many people with jobs that offer benefit plans (who are more likely to be upper-income) have their MSP premiums paid by their employers, while lower-income people in precarious work without benefits are left having to pay MSP premiums themselves.

Currently, BC raises about $2 billion per year from MSP premiums, and this is projected to increase to $2.2 billion in 2013/14. However, it is possible to scrap this regressive tax in a revenue-neutral way by replacing the lost income through the more progressive income tax system. There are many ways this can be achieved. One option (noted above) would be to increase the tax rates in all five income tax brackets by 20% (making them 6.07%, 9.24%, 12.6%, 14.75%, and 17.64% respectively) and add two new tax brackets at income levels of $150,000 and $200,000. Such a transformation of the income tax system would raise just over $2.2 billion, equivalent to the lost MSP income, but the distribution of this $2.2 billion in taxes would be much more progressive.

For example, an individual earning $50,000 would see their income taxes increase by a maximum of $574 (depending on deductions and credits claimed), but they would no longer be paying an MSP bill of $798. In contrast, someone making $500,000 will also no longer pay the MSP bill of $798, but their income tax will have increased by $27,548 (see Appendix 2 for more details).

Notably, the CCPA/Environics poll found that 61% of British Columbians were willing to pay more income tax if it allowed for the elimination of MSP premiums.

PROPERTY TAX OPTIONS

BC's property taxes tend to be lower than in most provinces, particularly when the generous home owner grant is factored in.[34] This is arguably a misguided policy choice, given that households (particularly wealthier ones) cannot avoid property taxes, whereas, using various (legal) loopholes as noted above, they can substantially reduce their net income for tax purposes and end up paying little in income taxes. For this reason, SFU Public Policy Professor Rhys Kesselman proposes that BC increase its property taxes on higher-value homes.[35] In particular, Kesselman recommends an annual property surtax, progressively applied, beginning with a 0.5% tax rate on values in excess of $750,000, then 1% on value above $1.25 million, and 1.5% on value in excess of $2 million. He suggests that a similar progressively increasing property tax could also be applied to passenger vehicles, which would generate new revenues, particularly from expensive/luxury cars. The same escalating tax could also be levied on other luxury items, such as boats/yachts.

BC's property taxes tend to be lower than in most provinces. This is arguably a misguided policy choice, given that households (particularly wealthier ones) cannot avoid property taxes, whereas, using various (legal) loopholes as noted above, they can substantially reduce their net income for tax purposes.

The property tax home-owner grant represents foregone income to the province of approximately $800 million (the province gives back nearly 40% of the total raised in BC property taxes), yet it goes to many upper-income households that do not need it. Kesselman is right to suggest that our public resources could be much more fairly and effectively used to help British Columbians who need assistance covering their shelter costs by transforming the grant into an income-tested credit that focused on low and modest-income renters and home-owners.

Home-owners already receive preferential treatment in the tax code as capital gains tax is not applied to the sale of primary residences, and restructuring the home-owners grant in this way could be an equitable means of raising additional revenues. In the absence of an inheritance tax (Canada is one of few industrialized countries that does not have an inheritance tax), various creative approaches for property taxation can also help reduce wealth inequality.

Corporate Tax Options

INCREASE CORPORATE INCOME TAXES

BC's corporate income tax rate has been cut from 16.5% in 2001 to only 10% today. This represents a loss in government revenues in excess of $1 billion annually (the exact amount varies depending on the level of corporate profits). BC's corporate income tax rate is now the lowest in the country, on par with Alberta and New Brunswick.[36] The federal corporate income tax rate has similarly been cut steeply, from 28% in the year 2000 to 15% in 2012.

In Budget 2012, the BC government announced a one percentage point increase in the corporate income tax rate beginning in 2014, from 10% to 11%, to assist with balancing the budget. The increase would come into effect only if the budget is not already balanced by then. Using estimates from the BC Ministry of Finance on the cost of the corporate tax cuts bundled with the carbon tax, we estimate that a one percentage point increase in the corporate income tax

34 See *BC Budget and Fiscal Plan 2012/13 to 2014/15*, pp. 129-130.

35 J. Rhys Kesselman, "A prescription for what ails BC's economy," *The Vancouver Sun*, September 15, 2012.

36 See *BC Budget and Fiscal Plan 2012/13 to 2014/15*, p. 128.

would raise between $172 and $209 million in 2014.[37] The BC business community supported the proposed tax increase and did not warn of any dire consequences for the economy, recognizing that at 11% the BC corporate tax rate remains very competitive.

If the BC corporate income tax rate were returned to the rate that existed in 2008 (12%), the province would stand to regain between $340 and $418 million a year. If corporate income taxes were raised to 13.5% (2005 level), BC would likely raise between $600 and $730 million in new revenues.

BROADEN THE CORPORATE INCOME TAX BASE

As with personal income taxes, the corporate tax system is beset with a maze of tax expenditures, including tax credits, deductions in the computation of income, the ability to defer tax to future years, and various tax exemptions. Consequently, *effective* corporate tax rates are often much lower than the statutory rates just mentioned above. For example, an analysis of corporate income taxes prepared for the BC Federation of Labour found that between 2001 and 2010, BC's corporate income tax revenues represented on average only 8% of corporate pre-tax profits, and the BC Budget projects even further declines.[38]

If the BC corporate income tax rate were returned to the rate that existed in 2008 (12%), the province would stand to regain between $340 and $418 million a year. If corporate income taxes were raised to 13.5% (2005 level), BC would likely raise between $600 and $730 million in new revenues.

If these corporate tax expenditures were scaled back, the province could increase corporate tax revenues without any changes to the statutory rates themselves. Rethinking many of these tax expenditures could also result in a more equitable and less complex tax regime for many companies. Moreover, some existing tax credits and subsidies are supporting industries that, in the era of climate change, it no longer makes sense to preferentially support, such as mining, and the oil and gas sector. BC's tax code should support our climate strategy, not counter it.

Some specific BC corporate tax deductions, credits and subsidies that merit reconsideration include:[39]

- Various fuel tax exemptions, which represent an annual tax expenditure of over $20 million.
- The mining exploration tax credit, representing a tax expenditure of $25 million.
- Various natural gas drilling royalty credits, which represent $200–$300 million a year in forgone revenues.[40]
- Meals and entertainment deductions that provide a tax subsidy for luxury restaurant meals and items such as box seats for the Vancouver Canucks.

In addition, as is the case with personal income taxes, BC's corporate income taxes are assessed upon net income as calculated on federal tax returns. As a result, once again, BC's revenues are undercut due to a host of tax deductions and credits in the *federal* tax code.

37 In BC Budget 2012, the Ministry of Finance estimates that the corporate income tax cut (from 12% to 10%) cost BC $381 million in 2011/12 (Table 1, p. 66) and increasing the tax to 11% would reduce the cost to $209 million in 2014/15 (Table 2, p. 68), saving over $172 million (depending on their projection of profit growth since 2011). Thus, we can conclude that the cost of a single percentage point reduction in the corporate income tax rate is between $172 million and $209 million.

38 BC Federation of Labour, *Failed Policies: Shifting Responsibility to Average Families, Part 1: Corporate Income Taxes* (2011).

39 For a full listing of BC tax expenditures, see *BC Budget and Fiscal Plan 2012/13 to 2014/15*, pp. 122-127.

40 *BC Budget and Fiscal Plan 2012/13 to 2014/15*, p. 134.

Notably, Alberta and Quebec have both chosen to break from the federal tax regime — they require corporations in their provinces to file provincial income tax separately, allowing those provinces the freedom to choose for themselves which deductions and credits have merit and are in keeping with provincial policy goals. BC should consider adopting this approach.[41]

RESOURCE ROYALTIES: RAISE THE RATES AND BROADEN THE BASE

The BC treasury should be collecting more rents and royalties from key public resources — our forests, natural gas, and water.

First, there is a huge amount of timber logged in the province that still generates the lowest stumpage fee of just 25 cents per cubic meter (meaning, essentially, 25 cents for a telephone pole). This minimum rate has been in place for decades, and it is time for it to be raised. Doubling this would raise at least an additional $6 million. But arguably, a minimum rate of $1 would be more appropriate. If this higher rate is applied to all such wood logged last year — fully 35% of the total log harvest — it would add at least $18 million more to provincial revenues. And, if a minimum dollar rate was applied to all logs with stumpage rates of between 25 cents and 50 cents per cubic metre, at least another $7.5 million in revenues would be realized. Additional stumpage revenue could be directed toward a revitalized reforestation effort, so that our forests are renewed in the wake of the beetle attack. Longer term, it is high time for a full review or commission to evaluate our stumpage regime, and ensure that appropriate royalty fees are being paid by the forestry industry.

BC needs a thorough review of its resource royalties for forestry, water usage, and natural gas. Arguably, the natural gas sector receives more in subsidies (credits, subsidized hydro power, and state-provided infrastructure) than it provides in royalties.

Second, water rental fees are too low. Virtually all the funds currently raised come from water used in the production of hydroelectricity. Perversely, industrial water users (such as the natural gas fracking industry, which quite literally removes water from the hydrological cycle forever because the water is rendered so toxic) pay very, very little for its usage. Currently, a fracking company in BC would pay the equivalent of about $2.75 per Olympic swimming pool's worth of water used.[42] In contrast, under water rental fees in Quebec, a similar charge would be in the range of $175. Again, a full review of water fees is in order, and clearly, much new revenue could and should be collected.

Finally, BC needs a thorough review of natural gas royalties. Arguably, the sector receives more in subsidies (credits, subsidized hydro power, and state-provided infrastructure) than it provides in royalties.[43] The effective royalty rate itself in BC, based on a combination of volume and market price, seems to run at about 10–11%,[44] a rate that seems remarkably low given that, unlike forestry, this is a finite non-renewable fossil fuel. And just as forestry wood waste left on the ground is not subject to stumpage, leaked or vented natural gas also escapes royalty charges, an omission that, if corrected, would broaden the revenue base (as well as encourage more efficient production).

41 Ontario also collected its own corporate income taxes until recently, when the province negotiated a tax collection agreement with the CRA, submitting to the federal government's definition of "taxable income" as of the 2009 tax year.

42 See Ben Parfitt, *Fracking up our Water, Hydro Power and Climate: BC's Reckless Pursuit of Shale Gas* (Vancouver: CCPA–BC, 2011).

43 See Marc Lee and John Calvert, *Clean Electricity, Conservation, Climate Change in BC* (Vancouver: CCPA–BC, 2012).

44 See *BC Budget and Fiscal Plan 2012/13 to 2014/15*, p. 134.

A full royalties review would carefully examine how other jurisdictions, in Canada and abroad, tax their non-renewable resources and develop recommendations for changes that would allow BC to maximize the economic rents collected from the use of our fossil fuels and ensure that our resource development is better aligned with the public interest.

Other Tax and Revenue Options

BC'S CARBON TAX

In July 2012, BC's carbon tax increased to $30 per tonne of CO_2, equivalent to about seven cents on a liter of gas. This was the last scheduled increase to the carbon tax, which had been increasing by $5 per tonne per year since its introduction in July 2008 (at $10 per tonne).

A $50 carbon tax would raise about $2.2 billion in total, doubling what the carbon tax currently raises, if it is expanded to cover the industries currently exempt (which alone would raise about $125 million at today's rate of $30/tonne). A related issue pertains to the fossil fuels we export, and the greenhouse gases embedded in what we import. Currently, these traded goods are not subject to BC's carbon tax.

CCPA research has shown that the existing carbon tax is regressive: lower-income households are paying more as a share of their income than higher income households. This is due to shortcomings in the design of the low-income carbon tax credit, which gets clawed back too quickly after a very low income threshold, making it of little help for modest income families hit hard by the tax.[45]

However, our reports have also shown how this regressive impact can be fixed through some relatively straightforward reforms. CCPA Senior Economist Marc Lee has modeled a progressive carbon tax regime that would see BC's carbon tax increase to $200 a tonne by the year 2020, along with a substantially enhanced lower-income credit that would fully offset the cost of the tax for the bottom half of BC households. Lee also models broadening the carbon tax to cover certain process emissions that are currently exempt from the tax, in the oil and gas, aluminum and concrete industries. Lee also recommends that the province dispense with the carbon tax's "revenue-neutrality" requirement, which sees all money raised by the carbon tax returned in the form of various tax cuts and credit, two-thirds of which currently go toward corporate income tax cuts. Instead, he recommends that half the carbon tax revenues are used for an expanded lower-income credit, and half for investments in climate action measures (such as public transit and building retrofits).

While a $200 carbon tax is a longer-term goal, a more modest interim option for the next four years would see the province continue its annual increases of $5 per tonne, taking the current carbon tax to $50 per tonne over the next four years (equivalent to 12 cents per litre of gasoline, compared to today's seven cents).[46] A $50 carbon tax would raise about $2.2 billion in total, doubling what the carbon tax currently raises, if it is expanded to cover the industries currently exempt (which alone would raise about $125 million at today's rate of $30/tonne).

If, as Lee proposes, the province assigned half this income to an expanded carbon tax credit, $1.1 billion would be available for this purpose (substantially more than the $188 million that is currently directed toward the low-income carbon credit). With this much in additional revenue, the credit could be refocused to improve the fairness of the tax. Currently, the credit goes only to very low-income households and individuals, while an enhanced credit could be extended

45 Marc Lee, *Fair and Effective Carbon Pricing: Lessons from BC* (Vancouver: CCPA–BC, 2011).

46 Marc Lee, *Building a Fair and Effective Carbon Tax to Meet BC's Greenhouse Gas Targets: Submission to the BC Carbon Tax Review* (Vancouver: CCPA–BC, 2012).

more broadly to the bottom 80 percent of households, fully compensating the bottom half for the carbon tax they pay and making them net beneficiaries of the tax.[47] Some of the credit could also be used to redress regressive rural impacts, or for business tax credits for businesses making green/climate action investments.

The other $1.1 billion raised would be available to ramp up the province's climate actions.[48]

A related issue pertains to the fossil fuels we export, and the greenhouse gases embedded in what we import. Currently, these traded goods are not subject to BC's carbon tax, placing some BC manufacturers at a competitive disadvantage. BC's coal and natural gas exports are combusted in other jurisdictions, and thus are not counted in the province's greenhouse gas emissions inventory. But, as the CCPA's Marc Lee has noted, "such exported emissions are double BC's own domestic emissions from burning fossil fuels."[49] There is no reason for these embodied carbon emissions to be exempt from the carbon tax. Similarly, embodied emissions in imports should face a carbon excise tax (under the PST system) to level the playing field for BC producers who pay the carbon tax. Taxing this imported and exported carbon could potentially raise billions more in revenue.

REGULATING AND TAXING MARIJUANA

Finally, it is worth including in a list of potential new revenue sources the proposal to end the prohibition of marijuana so that its distribution can be regulated and taxed. Most recently, advocacy for this policy has come from Stop the Violence BC (STVBC), an organization whose call for ending cannabis prohibition has been endorsed by a notable collection of former mayors, former provincial attorneys general, public health professionals and law enforcement leaders.

While their principal arguments relate to how prohibition fuels organized crime and gang violence, and drives up costs in the criminal justice system, they also note the potential for new tax revenues. According to a recent study by a coalition of University of BC and Simon Fraser University researchers, legalizing marijuana in BC could generate $2.5 billion in government tax and licensing revenues over the next five years or about $500 million per year.[50]

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In November 2012, STVBC released an Angus Reid poll showing strong majority support in favour of its position; 75% of British Columbians support the regulation and taxation of cannabis.[51]

Recent developments in the US provide an additional boost to this proposal. Two states, Colorado and Washington, have legalized marijuana for recreational use after ballot initiatives received support from a majority of voters in the two states in the 2012 US elections.

47 Such a credit is modeled on the Canada Child Tax Benefit, which is also an income-tested benefit scaled back as family income increases, but has a long phase-out "tail" so that about 80% of households with children receive some amount of the CCTB.

48 For more on modeling a $50 per tonne carbon tax and expanded low-income credit, see Marc Lee, *Building a Fair and Effective Carbon Tax to Meet BC's Greenhouse Gas Targets,* supra note 46.

49 Marc Lee, *Building a Fair and Effective Carbon Tax to Meet BC's Greenhouse Gas Targets*, supra note 46.

50 The study's findings refute the speculation that since BC's marijuana industry is largely for export, there would be little revenue from regulating the domestic market. Dan Werb, Bohdan Nosyk, Thomas Kerr, Benedikt Fischer, Julio Montaner and Evan Wood, "Estimating the Economic value of British Columbia's Domestic Cannabis Market: Implications for Provincial Cannabis Policy," *International Journal of Drug Policy* 23(6) (2012): 436-441.

51 For more on their poll, see the Stop the Violence media release "Public Opinion Reaches Tipping Point" (November 1, 2012) at http://stoptheviolencebc.org/2012/10/31/public-opinion-reaches-tipping-point/

PART 4

Responding to the Critics

THERE ARE SOME, OF COURSE, WHO WOULD CLAIM that most if not all of the revenue options and tax increases discussed above are ill-advised — that they would harm the economy and job creation, or discourage investment, work effort, and entrepreneurship, or encourage the wealthy and businesses to shelter their income from tax or move it out of BC. Consequently, they argue, the tax options above would not increase revenues to the degree we model. Here we offer a few brief responses:

Standard economic models indicate that if revenues raised are spent on public programs and capital projects (meeting pressing human and environmental needs), there is a net benefit with respect to GDP and job creation.

ARGUMENT 1: *Increasing taxes would reduce household spending capacity and present a drag on the economy similar to cuts in government spending.*

Response:

- If a government were to increase taxes without reinvesting these new revenues in the province (for example, if the money were used to pay government debt[52]), that would indeed be the result. But that is not what we are proposing. Rather, we argue that the government should raise revenues to spend on vital public programs and infrastructure to green our economy, and improve British Columbians' education, health, and quality of life. Standard economic models indicate that if revenues raised are spent on public programs and capital projects (meeting pressing human and environmental needs), there is a net benefit with respect to GDP and job creation (i.e., the stimulative effect of extra government spending exceeds the fiscal drag caused by the tax increase).[53]
- Raising taxes on upper-income households would have little impact on the real economy as it is taxing money currently saved (via purchasing financial assets or real estate) and putting it to use building public infrastructure and services (creating employment as well as providing better services).

52 Government debt is a problem when debt-carrying costs become very high, which is when debt becomes very large as a share of the economy. BC's provincial debt is low as a share of our economy and our debt servicing costs are very affordable (the silver lining of the slow recovery is the record low interest rates). At this stage, public funds can generate a much higher return when invested in programs such as early childhood education than by paying down our debt.

53 See, for example, Gerry Horne, *2004 British Columbia Provincial Economic Multipliers and How to Use Them* (Victoria: BC Stats, 2008).

- Taxation and income transfers that partially redistribute income and reduce the concentration of income at the top have additional positive effects on the economy. Wealthy people tend to (and can afford to) save a larger proportion of their income, invest it overseas, or spend it abroad. These uses of money represent "leakages" from the BC economy and reduce provincial aggregate demand. Conversely, lower-income people tend to spend all their income in the local economy, which is why increasing their incomes through redistribution in the tax and transfer system provides a net economic stimulus locally.

- Leading economists are now in agreement that too much income inequality is bad for an economy. Recently, the IMF, the Bank of Canada, and the Conference Board of Canada have all published research reports showing that inequality can diminish economic growth and increase financial volatility, leading to economic instability.[54] Thus, reforming the tax system to modestly redistribute more income can be positive for the economy.

ARGUMENT 2: *If BC raises its corporate and personal taxes it would chase away investment. Higher taxes would result in capital flight and wealthy people would move away from the province, reducing tax revenue instead of increasing it.*

Taxation and income transfers that partially redistribute income and reduce the concentration of income at the top have additional positive effects on the economy. Leading economists are now in agreement that too much income inequality is bad for an economy.

Response:

- There is plenty of room for BC to raise both personal and corporate taxes. While some corporations and individuals would no doubt complain loudly, and some would threaten to move, there is little evidence that reasonable tax increases would bring significant negative consequences for the province. Ultimately, BC is a highly desirable place to live, work and invest, with a mild climate and rich natural environment, and many are prepared to pay a tax premium for that privilege. In addition, there is virtually no actual evidence that tax increases lead to significant outmigration.[55]

- As documented earlier in the report, BC's personal income taxes are currently among the lowest in Canada (even for the highest income earners) and our corporate taxes are the lowest in the country. BC has room to move its personal and corporate tax rates to at least match the Canadian average, and the economic "price" of such tax changes is likely to be negligible. There is nothing radical in aspiring to be average when it comes to taxation levels.

- The global accounting firm KPMG produces a biennial report on the cost of doing business in large cities and major industrialized countries entitled *Competitive Alternatives*. These reports consistently find Canada, and cities in BC in particular, to be among the least expensive industrialized jurisdictions in which to do business.[56] In part this is because businesses look at more than taxes; they consider a host of factors including

54 For more on this point, see Conference Board of Canada, "Do government taxes and transfers help to reduce inequality?" at www.conferenceboard.ca/hcp/hot-topics/canInequality.aspx#anchor11 and Julian Beltrame, "Bank of Canada calls for control of free markets, less income disparity" Global News (The Canadian Press), March 12, 2013, www.globalnews.ca/money/bank+of+canada+calls+for+control+of+free+markets+less+income+disparity/6442599162/story.html

55 A recent report debunks the tax flight myth with a review of the US evidence: Robert Tannenwald, Jon Shure and Nicholas Johnson, *Tax Flight is a Myth: Higher State Taxes Bring More Revenue, Not More Migration* (Washington, DC: Center on Budget and Policy Priorities, 2011).

56 This has been a consistent finding in every edition of the report since it was first published in 1996. See KPMG *Competitive Alternatives*, various years.

the price of electricity, land, access to markets, the skills and training of the workforce, etc. More importantly, Canada offers significant cost advantages for business relative to the US, our closest and most direct competitor. Notably, many of these advantages are the direct result of public investments funded through taxes, such as our public health care system, public pensions and unemployment insurance/parental leave.

- In a special supplement to its 2012 report, KPMG examined business taxes in particular, assessing the general tax "competitiveness" of 55 major cities in 14 countries. In the country rankings, Canada was found to have the second lowest corporate taxes after India. And when the 55 cities were ranked, Vancouver was found to have the second lowest taxes after Chennai, India.[57] Clearly, BC has room to increase corporate taxes without significant consequence to its "competitiveness."

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- While a few corporations and individuals would carry through on their threats and leave, good public policy should not be made based on accommodating a small minority of individuals or businesses that lack a basic commitment to the province and the quality of life of its citizens. Their investments, if they are such a high flight risk, hardly contribute to a sustainable, robust economy for BC. If on balance the province can still raise more revenues and put that money to good use, then it is worth doing, and the net economic and employment impact will be positive.

ARGUMENT 3: *If we raise taxes, people would simply increase their efforts to avoid paying them, and thus revenue increases would be minimal.*

Response:

- The tax code is complex, and the preferential tax treatment of certain sources of income encourages people to engage in "creative" means of understating their income or sheltering it from taxes to minimize their tax liability. But this is hardly a reason not to pursue needed tax increases that serve the public interest. Instead of dismissing tax reform proposals, those who fear tax avoidance and evasion should focus their efforts on tackling these counterproductive behaviours. People using loopholes are using the tax system that's put in front of them, and would willingly do the right thing in a better system. If our tax system allows for too much income to be legally sheltered from tax, then we need to take a closer look at the various tax credits and deductions and end unfair tax preferences (building on some of our proposals presented earlier in the report). If individuals are engaging in legal tax avoidance, which is to say reducing their tax liability through actions that fall within the letter of the law, for example, by hiding their income in tax havens, then we need our governments to tighten tax loopholes and crack down on tax havens.[58] And if people are illegally evading their taxes, we need to beef up audits and enforcement.

57 KPMG, *Competitive Alternatives 2012 Edition – Special Report: Focus on Tax* (2012). Vancouver has been among the top four since the supplement report on tax was first published in 2008.

58 Canadians for Tax Fairness currently has a campaign underway aimed at tackling tax havens: http://tackletaxhavens.ca/

PART 5

Conclusion

BC OUGHT TO HAVE A MORE STEEPLY PROGRESSIVE TAX REGIME, with more tax brackets at upper-income levels. Such a policy would have the dual benefit of raising additional revenues for needed programs and tackling income inequality, which is higher in BC than in the rest of the country. It is only fair to ask those who have benefitted the most from BC's recent economic growth to contribute a little more to the common pool, especially when their taxes are lower than in the rest of the country.

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There is no shortage of options for raising new revenues for needed services and infrastructure. In this report we have presented a few options, along with estimates of the provincial revenues they would raise, and some examples of programs and infrastructure investment that these additional revenues could fund.

We are not recommending that the province adopt all of the options we present. Rather, we have highlighted the broad range of tax policy options available.

For most of us, our BC provincial income taxes are remarkably low, given what we receive in public services. The scope of unmet social and environmental needs in our province means we all need to pitch in a little more to strengthen our communities and build a province we can all be proud of.

Ultimately, as the CCPA/Environics poll results demonstrate, most British Columbians are prepared to pay a little more of their income in taxes, provided those new revenues are directed toward concrete improvements of the public services they value, toward shared societal goals (such as the elimination of poverty and homelessness), and provided increases are proposed under the right conditions—of transparency, participation and fairness.

It is time for a thoughtful, democratic conversation about taxes. The idea that we should debate whether taxes are 'good' or 'bad' is old. The questions we need to answer now are: What are the things we want to pay for together, and how can we raise the money needed in a way that ensures everyone pays their fair share?

Current provincial income tax payable by province

Table A1: Interprovincial Comparisons of Current Provincial Income Tax Payable, 2012 (dollars)

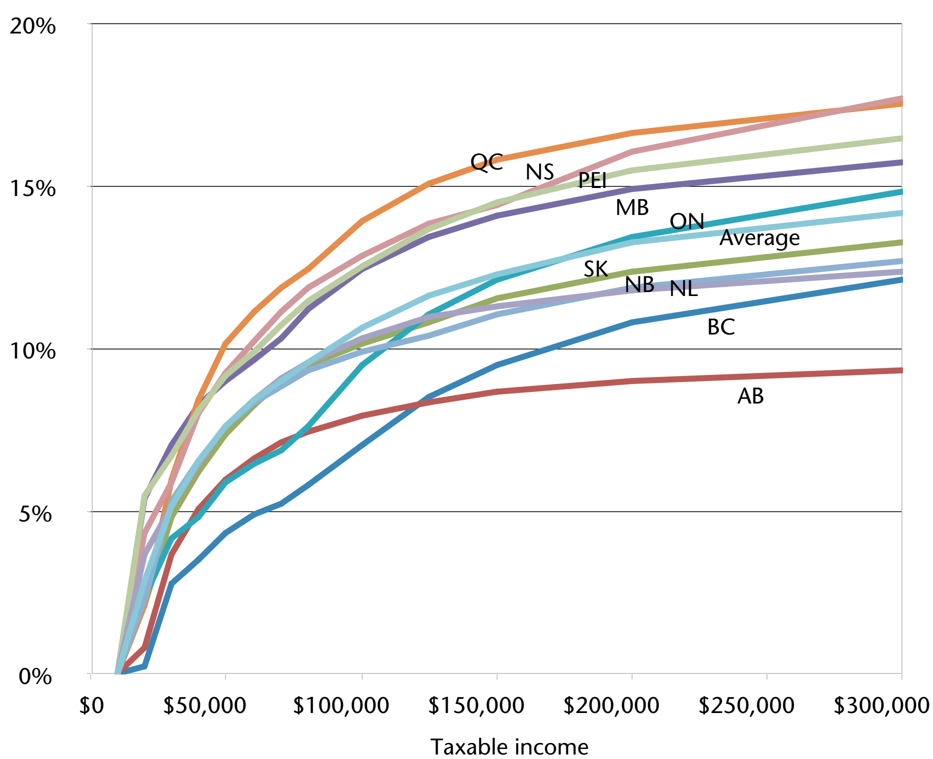
Taxable income	BC	AB	SK	MB	ON	QC	NB	NS	PEI	NL
10,000	0	0	0	0	0	0	0	0	0	0
20,000	41	154	426	1,071	475	416	453	859	1,089	730
30,000	833	1,086	1,452	2,107	1,246	1,785	1,601	1,753	2,002	1,532
40,000	1,400	2,018	2,477	3,289	1,907	3,372	2,626	3,189	3,236	2,591
50,000	2,139	2,958	3,669	4,499	2,942	5,047	3,781	4,631	4,557	3,795
60,000	2,909	3,957	4,969	5,773	3,856	6,684	4,990	6,139	5,937	5,045
70,000	3,679	4,957	6,269	7,188	4,771	8,321	6,200	7,806	7,492	6,328
80,000	4,616	5,957	7,569	8,928	6,058	9,958	7,421	9,473	9,162	7,658
100,000	6,985	7,957	10,169	12,408	9,444	13,885	9,901	12,865	12,502	10,318
125,000	10,583	10,457	13,515	16,758	13,797	18,812	13,017	17,240	17,094	13,643
150,000	14,258	12,957	17,265	21,108	18,149	23,653	16,592	21,615	21,687	16,968
200,000	21,608	17,957	24,765	29,808	26,854	33,266	23,742	32,115	30,872	23,618
300,000	36,308	27,957	39,765	47,208	44,413	52,481	38,042	53,115	49,242	36,918
500,000	65,708	47,957	69,765	82,008	79,233	90,911	66,642	95,115	85,982	63,518
1,000,000	139,208	97,957	144,765	169,008	174,081*	186,986	138,142	200,115	177,832	130,018

Effective Tax Rate (Provincial Income Tax as a Percentage of Taxable Income)

	BC	AB	SK	MB	ON	QC	NB	NS	PEI	NL
10,000	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
20,000	0.2%	0.8%	2.1%	5.4%	2.4%	2.1%	2.3%	4.3%	5.4%	3.6%
30,000	2.8%	3.6%	4.8%	7.0%	4.2%	6.0%	5.3%	5.8%	6.7%	5.1%
40,000	3.5%	5.0%	6.2%	8.2%	4.8%	8.4%	6.6%	8.0%	8.1%	6.5%
50,000	4.3%	5.9%	7.3%	9.0%	5.9%	10.1%	7.6%	9.3%	9.1%	7.6%
60,000	4.8%	6.6%	8.3%	9.6%	6.4%	11.1%	8.3%	10.2%	9.9%	8.4%
70,000	5.3%	7.1%	9.0%	10.3%	6.8%	11.9%	8.9%	11.2%	10.7%	9.0%
80,000	5.8%	7.4%	9.5%	11.2%	7.6%	12.4%	9.3%	11.8%	11.5%	9.6%
100,000	7.0%	8.0%	10.2%	12.4%	9.4%	13.9%	9.9%	12.9%	12.5%	10.3%
125,000	8.5%	8.4%	10.8%	13.4%	11.0%	15.0%	10.4%	13.8%	13.7%	10.9%
150,000	9.5%	8.6%	11.5%	14.1%	12.1%	15.8%	11.1%	14.4%	14.5%	11.3%
200,000	10.8%	9.0%	12.4%	14.9%	13.4%	16.6%	11.9%	16.1%	15.4%	11.8%
300,000	12.1%	9.3%	13.3%	15.7%	14.8%	17.5%	12.7%	17.7%	16.4%	12.3%
500,000	13.1%	9.6%	14.0%	16.4%	15.8%	18.2%	13.3%	19.0%	17.2%	12.7%
1,000,000	13.9%	9.8%	14.5%	16.9%	17.4%*	18.7%	13.8%	20.0%	17.8%	13.0%

Notes: Calculated for single individual with wage income only (most income from investments is taxed at lower rates). No deductions or credits except the basic personal amount, CPP/QPP contributions and EI premiums. Similar to 2012 BC Budget Table A4 (amounts up to income of $150,000 can be verified there). *Ontario's new tax bracket for income over $500,000 was phased over two years, so provincial tax payable at taxable income of $1,000,000 will be higher in 2013.

Figure A1: Provincial Income Tax as Percentage of Taxable Income, 2012



Notes: Calculated for single individual with wage income only (most income from investments is taxed at lower rates). No deductions or credits other than the basic personal amount, CPP/QPP contributions and EI premiums). "Average" shows the average of all provinces' effective personal income tax rates (including BC) at each income level. MSP premiums are not included, which means that modest-income British Columbians' tax bill is in the middle of the pack. Based on data in Table A1 on page 40.

Impact of Modelled Tax Increases on Tax Payable and Overall Effective Tax Rates

Tables A2 and A3 illustrate the impacts our modeled income tax rate increases would have on the income tax payable and the *effective* tax rate of British Columbians (that is, income tax payable as a share of taxable income). Proposed tax increases are calculated for a single individual with wage income only (most income from investments is taxed at lower rates). We assume no deductions or credits except the basic personal amount, CPP/QPP contributions and EI premiums.

Explanations of each scenario we modelled in this report are as follows:

Scenario 1: New tax bracket at $150,000+ with rate of 18%.

Scenario 2: Two new tax brackets: 18% at $150,000 to $200,000, and 21% over $200,000.

Scenario 3: Increase rates in the top two brackets (14.7% and 17%, respectively), and two new tax rates as in Scenario 2, but with higher rates of 20% and 22%.

Scenario 4: Increase rates in the top three brackets (12.29%, 14.7%, 17%), and two new tax rates at higher incomes as in Scenario 3.

Scenario 5: Current tax rates with modified Ontario surtaxes to get the same top marginal tax rate of 49.53%: 20% on provincial tax over $4,213, and 19.65% over $5,392.

Scenario 6: Current tax rates with modified Ontario surtaxes to kick in at a higher income level (top marginal tax rate remains at 49.53%): 20% on provincial tax over $6,000, and 19.65% over $8,000.

Scenario 7: Increase top bracket rate from 14.7% to 17%.

Scenario 8: Increase top bracket rate from 14.7% to 17%, and two new upper-income brackets (20% on income $150,000–$200,000, and 22% on income over $200,000).

Scenario 9: Introduce new top bracket at $200,000 with rate of 22%.

Scenario 10: Introduce new top bracket at $250,000 with rate of 22%.

Scenario 11: Start the third tax bracket at $60,000 (instead of $74,028). This way, about 20% of tax filers will fall into the top three brackets.

Scenario 12: Start third bracket at $60,000 instead of $74,028 and increase the rates in the top three brackets (12.29%, 14.7%, 17%). Two new tax brackets: 20% at $150,000 to $200,000 and 22% over $200,000.

Scenario 13: Increase each tax rate by 10% (5.57%, 8.47%, 11.55%, 13.52%, 16.17%).

Scenario 14: Increase each tax rate by 20% (6.07%, 9.24%, 12.60%, 14.75%, 17.64%).

Scenario 15: Increase each tax rate by about 20% (6.07%, 9.24%, 12.6%, 14.75%, 17.64%). New tax bracket for incomes over $150,000 with rate of 20%.

Scenario 16: Increase each tax rate by about 20% (6.07%, 9.24%, 12.6%, 14.75%, 17.64%). Plus add two new tax brackets: 20% on income of $150,000 to $200,000, and 22% over $200,000.

Table A2: Proposed Increase in Provincial Income Tax Payable

Taxable income	In dollar terms, by scenario									
	1	2	3	4	5	6	7	8	9	10
>60,000										
65,000										
70,000										
80,000				107	81					
90,000			121	317	380					
100,000			362	558	867	197				
125,000			940	1,136	2,294	1,424	501	501		
150,000			1,515	1,711	3,751	2,881	1,076	1,076		
200,000	1,650	1,650	4,165	4,361	6,665	5,795	2,226	3,726		
300,000	4,950	7,950	11,465	11,661	12,494	11,624	4,526	11,026	7,300	3,650
500,000	11,550	20,550	26,065	26,261	24,151	23,281	9,126	25,626	21,900	18,250
1,000,000	28,050	52,050	62,565	62,761	53,294	52,424	20,626	62,126	58,400	54,750
Provincial revenue	$ million									
	$400	$700	$1,020	$1,080	$1,025	$850	$375	$930	$725	$625

Taxable income	In percentage terms, by scenario									
	1	2	3	4	5	6	7	8	9	10
>60,000										
65,000										
70,000										
80,000				0.13%	0.10%					
90,000			0.13%	0.35%	0.42%					
100,000			0.36%	0.56%	0.87%	0.20%				
125,000			0.75%	0.91%	1.84%	1.14%	0.40%	0.40%		
150,000			1.01%	1.14%	2.50%	1.92%	0.72%	0.72%		
200,000	0.83%	0.83%	2.08%	2.18%	3.33%	2.90%	1.11%	1.86%		
300,000	1.65%	2.65%	3.82%	3.89%	4.16%	3.87%	1.51%	3.68%	2.43%	1.22%
500,000	2.31%	4.11%	5.21%	5.25%	4.83%	4.66%	1.83%	5.13%	4.38%	3.65%
1,000,000	2.81%	5.21%	6.26%	6.28%	5.33%	5.24%	2.06%	6.21%	5.84%	5.48%

Table A3: Proposed Increase in Provincial Income Tax Payable

Taxable income	In dollar terms, by scenario					
	Scenario 11	Scenario 12	Scenario 13	Scenario 14	Scenario 15	Scenario 16
$20,000			$102	$202	$202	$202
$25,000			$128	$253	$253	$253
$30,000			$153	$303	$303	$303
$40,000			$212	$420	$420	$420
$50,000			$289	$574	$574	$574
$60,000			$366	$728	$728	$728
$65,000	140	230	$404	$805	$805	$805
$70,000	280	459	$443	$882	$882	$882
$80,000	393	751	$536	$1,069	$1,069	$1,069
$90,000	393	961	$651	$1,297	$1,297	$1,297
$100,000	393	1,202	$774	$1,543	$1,543	$1,543
$125,000	393	1,780	$1,133	$2,263	$2,263	$2,263
$150,000	393	2,355	$1,501	$2,998	$2,998	$2,998
$200,000	393	5,005	$2,236	$4,468	$5,648	$5,648
$300,000	393	12,305	$3,706	$7,408	$10,948	$12,948
$500,000	393	26,905	$6,646	$13,288	$21,548	$27,548
$1,000,000	393	63,405	$13,996	$27,988	$48,048	$64,048
Provincial revenue	$ million					
	$200	$1,400	$890	$1,790	$2,075	$2,275

Taxable income	In percentage terms, by scenario					
	Scenario 11	Scenario 12	Scenario 13	Scenario 14	Scenario 15	Scenario 16
$20,000			0.51%	1.01%	1.01%	1.01%
$25,000			0.51%	1.01%	1.01%	1.01%
$30,000			0.51%	1.01%	1.01%	1.01%
$40,000			0.53%	1.05%	1.05%	1.05%
$50,000			0.58%	1.15%	1.15%	1.15%
$60,000			0.61%	1.21%	1.21%	1.21%
$65,000	0.22%	0.35%	0.62%	1.24%	1.24%	1.24%
$70,000	0.40%	0.66%	0.63%	1.26%	1.26%	1.26%
$80,000	0.49%	0.94%	0.67%	1.34%	1.34%	1.34%
$90,000	0.44%	1.07%	0.72%	1.44%	1.44%	1.44%
$100,000	0.39%	1.20%	0.77%	1.54%	1.54%	1.54%
$125,000	0.31%	1.42%	0.91%	1.81%	1.81%	1.81%
$150,000	0.26%	1.57%	1.00%	2.00%	2.00%	2.00%
$200,000	0.20%	2.50%	1.12%	2.23%	2.82%	2.82%
$300,000	0.13%	4.10%	1.24%	2.47%	3.65%	4.32%
$500,000	0.08%	5.38%	1.33%	2.66%	4.31%	5.51%
$1,000,000	0.04%	6.34%	1.40%	2.80%	4.80%	6.40%

Technical Appendix

This paper use Statistics Canada's Social Planning and Simulation Database and Model (SPSD/M) to model changes to the BC provincial income tax system and estimate their revenue impact in 2012.

The SPSD/M contains a detailed database of 100,000 representative individuals in 40,000 families, drawn from tax, Census and survey data sources. This is the same database used by governments in Canada when they analyze the impact of proposed tax changes. SPSD/M version 18.0 is used for this paper.

There are data discrepancies between the SPSD/M and the BC budget: the total amounts of provincial income taxes paid by individuals in the SPSD/M ($7.035 billion) do not match the provincial income tax revenues projected in the BC budget ($6.614 billion as of the 2012 First Quarterly Report). Some of that is due to the fact that the SPSD/M estimates are based on calendar years while the provincial budget reports tax revenues on an April to March fiscal year basis. To correct for the SPSD/M's overestimation of provincial taxes reported, we express our estimates of revenues generated from each tax scenario as a percentage of the total income tax bill and then use the aggregate income tax revenue amounts from the BC budget to arrive at a dollar estimate for the additional revenues generated by each tax scenario. The adjusted revenue estimates are rounded to the nearest $5 million.

Since the calculations were performed, the 2012 Second Quarterly Report has come out with a revised estimate for 2012/13 provincial income tax revenues ($6.897 billion), which is much closer to the SPSD/M forecast. As a result, the revenue estimates presented in this report are conservative estimates of what could be raised with various tax changes.

The SPSD/M is a static model and does not take into account any changes in taxpayers' behaviour in response to changes in taxes. However, for reasons outlined in Part 4, we believe such behavioural changes to be relatively minor. In their recent review of the literature, Diamond and Saez note that: "A number of studies have shown large and quick responses of reported incomes along the tax avoidance margin at the top of the distribution, but no compelling study to date has shown substantial responses along the real economic responses margin among top earners."[59]

It should be noted, however, that the modeling results presented here are meant to highlight the general effects of various tax changes and the level of magnitude of additional revenues that can be raised with each one. The exact size of revenues raised would depend on the specific parameters of a policy change as well as on the extent to which taxpayers would change their behaviour as a response to the tax changes.

59 Peter Diamond and Emmanuel Saez, "The Case for Progressive Tax: From Basic Research to Policy Recommendations," *Journal of Economic Perspectives* 25(4): 165-90 (2011).

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