Canadian Centre for Policy Alternatives | Ontario
January 2019

A New Revenue Tool

The case for a Greater Toronto and Hamilton Area sales tax

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ISBN 978-1-77125-408-3

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ACKNOWLEDGEMENTS

The authors would like to thank Luan Ngo, Chris Samuel and Jim Stanford for their thoughtful comments on an earlier version of this paper.

A New Revenue Tool: The case for a Greater Toronto and Hamilton Area sales tax

Introduction

This paper looks at how much revenue could be raised from a sales tax in the City of Toronto or in the Greater Toronto and Hamilton Area (GTHA). It provides an example of an enhancement to the sales tax credit to mitigate the impact on low-income households and estimates the distributional impact.

A New Municipal Sales Tax: Revenue Estimates

Table 1 shows the pre- and post-sales tax credit enhancement revenues for a 1 per cent and a 2 per cent municipal sales tax.

A 2 per cent sales tax in the City of Toronto would raise a billion dollars and a 1 per cent sales tax would raise half a billion dollars, if there were no change to the HST credit. A 2 per cent tax would result in a combined HST of 15 per cent, which would represent a 15 per cent increase on the current 13 per cent HST. A 2 per cent sales tax in the GTHA would raise $2.5 billion and a 1 per cent sales tax would raise more than $1.3 billon.

TABLE 1 Projected Revenues from a Toronto Sales Tax (2019 $mil)

	City of Toronto	GTHA
Total Revenue ($s millions)		
1 per cent	511	1,250
2 per cent	1,033	2,526
Net Revenue including the cost of an enhanced sales tax credit		
1 per cent	415	1,015
2 per cent	813	1,988

Source: Authors' calculations and SPSD/M

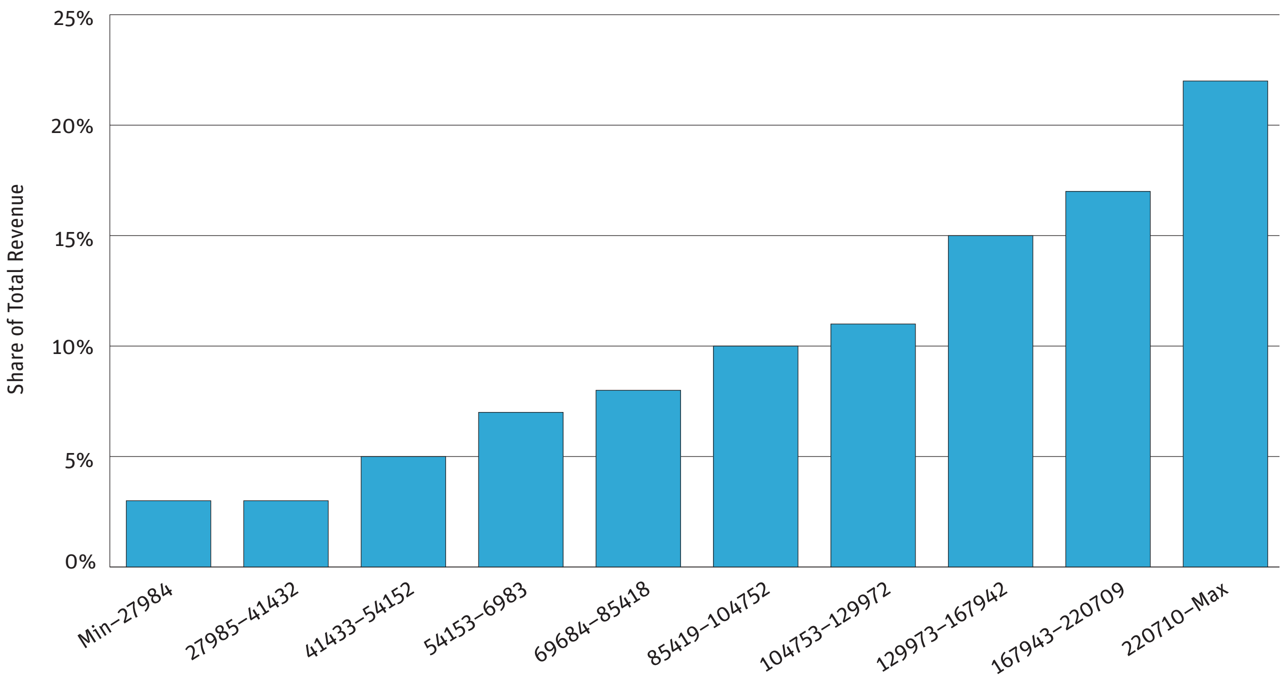
Distributional Impact of a Sales Tax Credit

To put the impact of this increase in context, a 2 per cent sales tax would amount to a six-cent increase in the cost of a coffee or a 30-cent increase in the cost of a movie. Everyone would benefit from the services that the tax could purchase. But because sales taxes have a bigger impact on low-income people, some of the revenues could be used to enhance the provincial sales tax credit in order to offset the impact of the increased tax for those with limited incomes.

To illustrate the potential impact of increasing the tax along with an enhanced tax credit, we have modelled a 25 per cent increase in the sales tax credit (rising from a maximum of $307 to $380 per person) for a 1 per cent increase in the sales tax and a 50 per cent increase in the sales tax credit (rising from $307 to $460) for a 2 per cent sales tax increase.

Figure 1 shows the projected distribution of net sales tax collected from a two per cent GTHA sales tax that includes an enhanced sales tax credit that would be fifty per cent higher than it is today. We look at 10 deciles of GTHA households divided by total pre-tax household income. It shows that the share of municipal sales tax revenue would climb steadily as you go up the household income spectrum. The first decile, the poorest 10 per cent of households, would pay 3 per cent of the total once they receive their enhanced sales tax credit. The richest 10 per cent of households (the 10th decile) would contribute 22 per cent of the total increase in sales tax revenue.

FIGURE 1 Who Pays for a Municipal sales tax in Toronto (By decile 2019)



Source SPSD/M and author's calculations

Implications for Implementing a Sales Tax

The City of Toronto is the poster child for the need for broader revenue-raising powers. The demands on city services and the need for investment in a wide range of areas exceed the capacity of property taxes to pay for them. The *City of Toronto Act*, in providing it with more revenue raising powers than other municipalities, is an acknowledgement of the city's unique needs and demands on its services but has yet to be drawn upon substantively.

A regional sales tax for the Greater Toronto and Hamilton Area (GTHA) would be a good solution to problems of underfunding.

A municipal sales tax would be a simple and effective way to raise revenue. Revenue from the tax would grow with the population and the economy. That money could be directed toward regional infrastructure projects.

Concerns have been raised that a municipal value-added tax would result in administrative complexities or border issues, but neither issue is problematic enough to offset the potential benefits. From an administrative perspective, extending the HST to municipalities would raise a number of issues associated with geographic allocation of input credits, revenues and place of supply.[1] However, Toronto's population is greater than that of six out of 10 provinces and its economy drives much of Canadian economic activity, so it should not be impossible.

Similarly, concerns about border issues — that businesses or consumers might go elsewhere to escape a sales tax — can be addressed as well. A city could set the rate at a low level and a regional sales tax would mean everyone buys in.

A regional sales tax would be beneficial from a tax design, compliance, and revenue-raising perspective. But even without regional agreement, the City of Toronto could go ahead with a municipal sales tax on its own.

Conclusion

There is widespread agreement that municipalities in the Toronto region need to increase their revenue-generating capacity in order to keep up with a growing population, service and infrastructure demands. Toronto's problems are particularly acute.

A municipal sales tax would be a powerful complement to property taxes and could offset expected future shortfalls in Toronto's Land Transfer Tax. The revenue-generating power of a regional sales tax is compelling: each percentage point could yield up to half a billion in new revenue for the City of Toronto or $1.3 billion for the GTHA.

Working through the HST credit system, an easily administered sales tax credit would mean low-income households would have their tax increase offset, redressing the regressive character of a sales tax. In fact, the public service improvements that a sales tax could allow municipalities to provide could be progressive in nature: everyone would benefit, but especially those who are low-income.

Methodology

This analysis is based on Statistics Canada's Social Policy Simulation Database Model (SPSD/M) 26.0. The assumptions and calculations underlying the simulation results were prepared by David Macdonald and the responsibility for the use and interpretation of these data is entirely that of the authors.

1 For further discussion of these issues see Bird, Richard. *The GST/HST: Creating an Integrated Sales tax in a federal Country SPP Research Papers Volume 5 Issue 12 March 2012*

We used SPSD/M to construct these revenue estimates and distributional impacts. SPSD/M does not provide for analysis/estimates for the City of Toronto directly. The most local geography available is CMAs in Ontario with more than 500,000 residents, which includes the GTA, Ottawa, Hamilton, and the Kitchener-Waterloo-Cambridge CMAs. All results are for CMAs in Ontario with more than 500,000 residents, but scaled down to match the population of the City of Toronto and the Toronto and Hamilton CMAs for the GTHA estimate. The income distribution in the GTA and the GTHA will not exactly match the income distribution of all Ontario CMAs.

We used households rather than families as the unit of analysis, as that is how the retail sales tax is calculated in SPSD/M. Households include all people living together with a common entrance. This can include extended families or unrelated roommates. Deciles were constructed using pre-tax combined household income. All projections are for the 2019 tax year.

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