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August 13, 2009

Tax Harmonization Could Create More Discord than Harmony

Minister Selinger is seriously considering the federal government's offer of a lump-sum payment for Manitoba to blend its sales tax with the GST, creating a new Harmonized Sales Tax (HST). Apparently, he worries that Manitoba will lose out if does not follow those provinces that have adopted this policy.

But sales-tax harmonization must be scrutinized carefully: it is complicated, and there are oft-cited assumptions that may not survive the light of day.

There is little debate about the effect on business: it wins in spades. Determining the net effect on ordinary people is more difficult. Advocates of harmonization, such as the B.C. government, which just closed a deal with Ottawa to switch to a HST, claim that the savings businesses realize will be passed on to consumers in the form of lower prices. The Winnipeg Free Press reports that Nova Scotians paid $84M more in tax the first year harmonization was implemented, and The Ontario Chamber of Commerce estimates that consumers will have to pay out an additional $905M to pay for the new HST. Will prices come down an equal amount?

How much would the change cost Manitobans? The Winnipeg Free Press estimates that an HST would increase sales tax revenue by $160M a year and argues that this could translate into a viable means of replenishing beleaguered municipal coffers. While it is true that municipalities have not received sufficient financial support from provincial or federal governments, increasing consumption taxes - amongst the most regressive of all taxes – is not the way to go. It is also not certain that either the province or Ottawa would agree to hand over money to municipalities.

In B.C., essential items such as children's clothing, car and booster seats and diapers that were not subject to the PST will be subject to the new HST, thereby increasing their cost 7%. The B.C. government dealt with this inequity by offering point-of-sale rebates, but there is a long list of items that will not receive these rebates. The list includes: safety helmets, first-aid kits, smoke detectors, energy-conservation equipment, funeral services, non-prescription medication, vitamins and dietary supplements, bicycles, school supplies (except books) and home-care services.

The B.C. government had made policy decisions regarding the exemption of these items from the PST to encourage British Columbians to purchase them, thereby fostering a safer, greener and more equitable society. Now that the PST is glued to the GST, B.C. can no longer unilaterally

CCPA
CANADIAN CENTRE
for POLICY ALTERNATIVES
MANITOBA OFFICE

309 - 323 Portage Avenue
Winnipeg, MB R3B 2C1
T 204.927.3200 F 204.927.3201
ccpamb@policyalternatives.ca
www.policyalternatives.ca

decide to exempt tax from products it feels perform a valuable social function.

Minister Selinger needs to think very carefully about giving away the province's ability to set its own sales-tax policy. It is surely not difficult to imagine that a more progressive NDP government could have policy differences with its more conservative federal counterpart.

On another note, why would a Conservative government, determined to decentralize Canada and strengthen economic and social regionalism, promote a blended tax that would download regional responsibility to Ottawa? The answer may lie in its even stronger desire to help Canadian business.

While strengthening business in itself may be worthwhile, doing so at the expense of consumers and marginalized Canadians should never be a policy goal. What then should we make of Mr. Flaherty's claim that decreasing red tape, taxes and expenses for companies will allow businesses to invest more, thereby providing more jobs for Canadians?

Writing before B.C. and Ontario harmonized their sales tax, policy analyst Erin Weir wondered if removing billions of dollars from business tax inputs was the best way to stimulate investment. He found that exemptions applied to those provincial sales taxes on the most common form of capital investment, namely machinery and equipment. Finance Canada estimated that these exemptions lowered Canada's marginal effective tax rate by 6.5 percent. Comparing that percentage to the US, Weir found that state sales taxes on capital investment had fewer exceptions, making their marginal effective tax rate higher than Canadian provinces'.

Weir estimates that only one quarter of the gains to business through harmonization would potentially encourage investment. He cites measures such as accelerated depreciation and/or investment tax credits as being more effective at stimulating investment.

One could argue in favour of making consumers bear the brunt of harmonization if there were a proven net gain through job creation and gains in environmental, health and safety policy. But the B.C. experience shows us that provincial policy can be hijacked by less-progressive federal policy. Weir's research at least questions the assumption that savings to businesses will result in meaningful investment. Furthermore, the cash paid to entice provinces to switch could perhaps be better spent on investing in Canada's social infrastructure.

We hope Minister Selinger will also consider the legacy of free trade in Canada. Advocates assured us that all Canadians would benefit from free trade because it would increase investment. Since its inception, wages have remained stagnant, growing corporate profits have been paid to shareholders rather than invested, more of Canada's resources and wealth have been taken over by foreign interests and our sovereignty has been diminished. Sales-tax harmonization could well strengthen that unhappy legacy by enriching business at the expense of consumers and eroding Manitoba's ability to implement meaningful tax policy.

Lynne Fernandez is a political economist with the Canadian Centre for Policy Alternatives, MB.

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