Submission to the House of Commons Standing Committee on Finance, Pre-Budget Consultation

By Seth Klein and Marc Lee
November 1999

Good afternoon, and thank you Mr. Chairman and committee members for this opportunity to once again appear before the finance committee. I'm happy to be here with Marc Lee this year, our Centre's new economist, who has been doing some excellent work on the issues of taxes and productivity.

We are happy to take this chance to once again highlight some of the ideas in the Alternative Federal Budget, and to share some thoughts on the fiscal debates you are following.

According to Finance Minister Martin, Canada's economic "fundamentals" have never been better. Whose fundamentals? Unemployment and underemployment still plague us, poverty has risen, economic inequality is growing, unemployment insurance and welfare have been cut, municipalities have declared homelessness a national emergency, medicare is in crisis, universities and colleges face severe underfunding and student debt is soaring, and the environment has virtually dropped off the political radar.

1999 is the 10th anniversary of the all party federal resolution calling for the elimination of child poverty by the year 2000. Needless to say, our chances don't look good. Tomorrow, in cities and towns across Canada, vigils will be held to mark the 10th anniversary of the Commons' resolution.

Not only have we failed to eliminate child poverty, but it has gotten worse. We use StatsCan's LICO as a poverty measure. We can argue about that, but the point is that the trends are clear, and they are going up. The child poverty rate went up right after the Commons' resolution, as the recession hit (deeper and longer than necessary, had the Bank of Canada not been so fanatical in its war on inflation). The child poverty rate dipped down slightly in 1994, but since the 1995 federal budget, it has gone back up (at least until 1997, the last year for which we have data).

Also, in these past ten years, we have seen homelessness escalate, and food banks proliferate.

We do not believe it overstates the case to say that to even be talking about tax cuts that disproportionately benefit upper income earners, when child poverty remains near 20% and homelessness is a national emergency is, quite simply, a moral outrage. Something is just not right here. We are a rich country; richer than we were when we took better care of one another. The tone of the debate suggests that something is dreadfully wrong with our priorities.

Putting the surplus back to work

We estimate a federal budget surplus next year of almost $12 billion. There can be no more excuses for failing to address the social, economic and environmental deficits that plague our communities. The polls consistently tell us Canadians are more concerned with social re-investment than with debt reduction or tax cuts, and Canadians are right. Most people understand that we need government to correct for the failures of the market, such as the lack of affordable housing and child care.

It is not enough to set targets for balancing the budget and lowering the debt. Minister Martin set, and then significantly beat, his targets for deficit reduction (at a considerable economic and social cost). Now he is talking about setting targets for tax reductions. What we need are clear targets for lowering unemployment, poverty and homelessness, and a determination to meet these social targets with as much determination as was shown in the campaign to eliminate the deficit.

So, how can that be done?

double federal transfer payments to the provinces for health, education and welfare over the next two years, and invest in new public services, like public home care, thereby restoring some 100,000 public sector jobs;

heeding the call of the Campaign 2000 advocates, who are calling for increases of $2 billion per year as an investment in Canada's children, for the next 5 years, in the form of increases in the Child Tax Benefit (with guarantees that this benefit will not be clawed back from the poorest of the poor -- those on social assistance), a national child care program, and new spending on early childhood education and social housing;

create a National Investment Fund to finance economic development in hard-pressed regions, financed by small but compulsory deposits by the private charter banks;

institute a Community Reinvestment Act that will require private banks and other financial institutions to reinvest a share of their assets in the communities where they do business;

increase spending on our social, environmental and physical infrastructure (such as social housing, child care spaces, parks, municipal services, energy conservation projects and environmental clean-ups);

assist in the redistribution of working time (it's crazy that some are working themselves silly while others are jobless), by banning compulsory overtime and reducing the statutory working week; and

restore EI benefits and coverage, and as the Throne Speech suggested, increase the time available for paid parental leave.

It's not enough to simply re-invest in existing public programs. We need new public programs that address the challenges and difficulties of modern life — programs like public home and community care and public pharmacare (recognizing that health care is increasingly moving outside the walls of the hospital or doctor's office), and public child care (recognizing that most parents, whether by choice or necessity, work outside the home).

Much as the tax cut campaigners would have us believe otherwise, healthy families are more than our after-tax incomes. We need more than an increase in our disposable income. We also need help providing our children with quality care and education (from early childhood right through to post-secondary) and time to spend with our families, help looking after our parents in their old age, help finding work when the market fails to provide adequate employment at a decent wage, and help finding homes when the market fails to provide sufficient, affordable and decent housing. In short, most of us depend, in some way or another, on healthy public programs.

Productivity

While tax cuts (again) have been advocated to boost Canada's productivity performance, there is good reason to believe that they will fail to deliver. The link between taxes on one hand and investment and growth on the other is inconclusive at best. In fact, the highest productivity growth rates over the 1990s are in high-tax nations like Norway and Denmark. In Canada and the US, top marginal tax rates in the 1950s were in the 90% range, and were correlated with high productivity growth and high real GDP growth.

Where the federal government can make a difference is not by standing on the sidelines, but through increased public investment in areas where the private sector has little incentive to invest in on its own. There has been a significant decline in public investment in recent years due to cutbacks. Current public investments are only sufficient to offset the depreciation of existing public capital.

Public investments -- in areas such as infrastructure, R&D, mass transit, health care and education -- contribute to sustained productivity increases and often facilitate or complement private sector investments. However, they require that governments act with a longer-term time horizon in mind; for example, the benefits of early childhood development may not be apparent to the economy (or the treasury) for several decades.

Fair tax reform

All the above ideas could be paid for out of the growing federal surplus. But that's not to suggest the tax system should remain unchanged. The tax system is grossly unfair and lacks progressivity. In fact, when all federal and provincial taxes are considered, Canada already has a "flat tax" over the entire income range.

Across-the-board tax cuts are not what we need. The federal surplus is largely the product of some painful and unnecessary spending cuts — cuts that have hurt the poor, the unemployed and students the hardest. To now use the surplus for a tax cut that would disproportionately benefit the wealthy is Robin Hood in reverse, and just plain wrong.

Now, more than ever, with the market producing a growing gap between the haves and have-nots, we need a progressive tax system that will mitigate this inequality. We need tax changes that will lower the taxes paid by low and middle-income earners, while increasing the taxes of those earning over about $100,000 (who are generally more astute at claiming various deductions). And we need changes that will better meet society's environmental goals.

As the CLC submission clearly showed, not everyone's disposable income has gone down in the 1990's by the same amount. A review of the StatsCan data indicates that since 1989, while families in the top 2 quintiles (those with family incomes over about $50,000) saw their disposable incomes fall by about 4.5%, the bottom two quintiles (those with family incomes under about $35,000) saw their disposable incomes fall by about 8.5%. Between 1993 and '97, disposable incomes have gone up, for all but the bottom quintile (those with average incomes of about $16,000). That is because their market income is up only slightly, their government transfer income is down by almost the same amount, and their taxes are up. Bracket creep is disproportionately hitting these people, as are government cuts. They have been dealt a double whammy, and it is they who deserve tax relief and increased social spending.

A few ideas:

tax capital gains at the same rate as income (a dollar earned is a dollar earned—surely investment income does not merit special tax status over hard-earned labour income);

re-establish two upper-income tax brackets, for those earning over $100,000 and $150,000 (this would emulate the US, which has two additional federal income-tax brackets);

institute an inheritance tax, at the same rate as the US, on transfers of wealth over $1 million (this would raise about $3 billion);

broaden the personal and corporate income tax base by closing various loopholes like the meals and entertainment deduction and the political lobbying deduction;

put a cap on the deductibility of corporate executive salaries, set at 10 times the average wage (surely that's reasonable);

bring in a minimum corporate income tax, so corporations can't stack their deductions and eliminate their taxable income;

apply the GST to brokerage fees and commissions (why treat these services any different than a haircut for the average wage earner?); and establish new "green tax" measures, such as a tax on carbon emissions, while eliminating subsidies like the special tax treatment afforded oil and gas production.

But on the other side of the ledger:

increase GST tax credit for adults, and disability tax credits;

significantly increase the child tax benefit by $2,000 per child per year, and ensure this benefit goes to all low and modest-income families (the welfare as well as the working poor);

increase the basic personal exemption; and

index tax brackets to inflation, thereby ending the "bracket creep" that disproportionately hits low and middle income earners.

Ultimately, we are more than individual consumers. Our government should remind its citizens why we pay taxes — they are the price we pay for a civilized society, the price we pay for goods and services we have chosen to provide for one another collectively, and they are an expression of our commitment to care for one another and to pursue some of our aspirations as citizens together.