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The Great BC Tax Cut Giveaway

By Marc Lee

In the late-1990s, BC was ground zero for Canadian "tax rage." Alleged high taxes became a scapegoat for any difficulties that the province was facing (rather than financial chaos in important export markets on the other side of the Pacific). Lower taxes, it was claimed, would improve economic growth, make BC more competitive, and keep talented individuals and corporations from fleeing the province to less tax-burdensome climes.

At the same time, most British Columbians support more funding for schools and universities, a better health care system and a cleaner environment. Somewhere amidst the hyper-focus on tax cuts it was forgotten that taxes pay for services that people value.

By giving a large portion of the tax cut pie to high income earners, the Liberal's tax cuts leave a hole in the budget that cannot be filled by the modest stimulus the tax cuts will give to the economy. Big tax cuts have to be accounted for somewhere: either through larger deficits, spending cuts, or the privatization of public assets. When this other shoe drops, and it must, the real cost of tax cuts to BC's fiscal situation will become apparent.

Anatomy of a Tax Cut

On their first full day in office, the Liberal government announced the largest tax cut in Canadian history. The tax cuts lived up to their promise of being dramatic, but the most surprising element in the tax cut package was that it went far beyond campaign rhetoric that the cuts would be focussed on low and middle income earners. While everyone across the political spectrum understood that the Liberals' tax cuts would target the bottom two tax brackets, to almost universal surprise the biggest breaks went to the top brackets.

Table 1 shows the value of BC's tax cuts for different income levels, based on data from the BC Ministry of Finance. While the tax cuts were spun as benefitting all equally, a deeper look suggests that those with higher incomes received a much larger

Table 1: BC Tax Cuts 2002

Gross Earnings	BC Income Tax before Tax Cut		Tax Cut in 2002	BC Income Tax after Tax Cut		Tax cut as a Percent of Income
	(dollars)	(percent of income)	(dollars)	(dollars)	(percent of income)	
$20,000	$843	4.2%	$236	$607	3.0%	1.2%
$30,000	$1,536	5.1%	$430	$1,106	3.7%	1.4%
$40,000	$2,429	6.1%	$644	$1,785	4.5%	1.6%
$50,000	$3,559	7.1%	$904	$2,655	5.3%	1.8%
$60,000	$4,642	7.7%	$1,155	$3,487	5.8%	1.9%
$80,000	$7,517	9.4%	$1,947	$5,570	7.0%	2.4%
$100,000	$10,989	11.0%	$2,857	$8,132	8.1%	2.9%
$150,000	$20,603	13.7%	$5,297	$15,306	10.2%	3.5%
$200,000	$30,453	15.2%	$7,797	$22,656	11.3%	3.9%

Source: BC Ministry of Finance and Corporate Relations.

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proportionate benefit relative to their income. At the $20,000 income level, the value of the fully phased-in tax cut is a mere $236, or 1.2% of income. As income rises so does the value of the tax cut, in both straight dollar terms and as a percentage of income. By $200,000 of income, the tax cut amounts to about $7,800, or 3.9% of income.

This is consistent with the government's claim of an across-the-board 25% tax reduction only because those with higher incomes pay relatively more in taxes as a share of income—the effect of a progressive tax system. By giving the well-off a larger break as a percentage of income, the tax cuts make BC's tax structure more regressive, and hence contribute to a worsening picture in BC in terms of income inequality.

The distribution of the tax cuts looks even worse when we consider how the total tax cut pie has been sliced (Table 2). The total tax savings of those earning less than $30,000 per year—48.8% of taxpayers—amount to $180.5 million in 2002, or about 13.4% of the tax cut pie. Those earning between $30,000 and $60,000—38.3% of taxpayers—will receive about $456.5 million in 2002, or 33.9% of the total tax cut.

The big surprise is at the high end: 13% of taxpayers making more than $60,000 will receive 52.8% of the total tax cut in 2002. Closing in on the top of the income ladder, the 1.1% of taxpayers earning more than $150,000 will receive a whopping 20% of the total tax cut. Given the government's own claim about not knowing the full state of provincial finances, a massive tax cut that gives such a large share to high income earners can only be considered fiscally irresponsible.

The tax cut also reveals lopsided priorities. When fully phased in next year, it will give the approximately 50,000 people in BC with incomes over $100,000 a total savings of about $370 million—an amount that could, for example, easily settle the current disputes with the BC Nurses' Union and the Health Sciences Association.

It is unfortunate that many British Columbians have gladly accepted a few hundred dollars in their pockets while the province's wealthy have made out like bandits. These tax cuts are not a free ride. According to Ministry of Finance bureaucrats, the tax cut creates a big hole in the 2001-02 Budget, estimated at $1.2 billion out of a $24 billion budget. With the tax cuts a given, the prospect of either a large deficit, large spending cuts or privatization of public assets is daunting. The overall fiscal situation may worsen more if the government moves on to much-demanded tax cuts for the corporate sector, including lower corporate income tax rates and elimination of the corporate capital tax.

Table 2: The Tax Cut Pie

Income Interval	Percentage of BC Taxpayers	Total Tax Savings in 2002 (millions of dollars)	Share of Tax Cut Pie (%)
$1-$30,000	48.8%	$181	13.4%
$30,000-$60,000	38.3%	$457	33.9%
$60,000-$80,000	7.8%	$237	17.6%
$80,000-$100,000	2.5%	$101	7.5%
$100,000-$150,000	1.6%	$104	7.7%
$150,000+	1.1%	$269	20.0%
Total	100.0%	$1,348	100.0%

Note: Figures have been calculated based on 1998 tax data (most recent year). Percentages may not sum to exactly 100% due to rounding. Income intervals are based on gross income before deductions.
Source: Canada Customs and Revenue Agency, Tax Statistics on Individuals, British Columbia, Table 2A

The Elusive Economic Stimulus

During the election campaign, the Liberals continued to soft-sell their tax cut plans by claiming that tax cuts would pay for themselves. That is, the tax cuts (to low and middle income earners) would stimulate so much economic growth that the taxes on this new income would offset the value of the initial tax cut. And this would mean that there would be no pain felt in terms of cuts to health care and education.

While such claims are generally regarded as dubious economics, it was certainly good politics for an opposition determined to win the government. But now that the election is over and the tax cuts have been delivered, the government is quietly backing off this claim in order to deal with economic reality.

The tax cuts will provide a stimulus to the economy. For 2001, they represent new money injected into the economy because they are essentially deficit-financed (because of some accounting changes this year that benefit the government's bottom line, this point may not be obvious at first glance). However, the overall impact will likely be rather modest. First, because they are so tilted towards upper-income earners—who are more

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An Investment Strategy for BC's Resource Sector

By Dale Marshall

BC's resource sector needs a bold and comprehensive investment strategy to reverse the lack of investment that has plagued the province since the early 1990s. Forest companies, for example, have invested just enough to counter the depreciation of their aging machinery. Opportunities to become more efficient and productive in pulp and to move up the value chain in solid wood have been foregone, leaving the industry in an uncompetitive and unstable position.

The new BC government has promised to cut taxes, regulations and resource rents, but such concessions should not be a blank cheque. If the premise behind the cuts is to get investment in BC, then they should be tied to ironclad commitments from resource companies to cease their capital strike and spend money on their BC operations.

The focus of an investment strategy should be to adopt new environmentally-friendly technologies and move up the value chain, thereby providing resource-dependent communities with both economic stability and environmental sustainability. The provincial government can play a role in encouraging and facilitating investment—from many places and in different forms—to move the resource sector towards a more viable *and* responsible position. This strategy should challenge BC's resource corporations to enter into a new social contract with British Columbians by working cooperatively with the government that represents them.

But a new approach also involves looking for alternatives to investment from the large corporate sector. Communities themselves, co-operatives, workers, the small business sector, First Nations bands, and public finances can all be a source of investment capital. Such sources are less likely to compromise the long-term ecological integrity of BC's natural systems or the health of the people of the province. Ultimately, the more options a government has to choose from with respect to managing its resources, the more bargaining power it has with those wanting a piece of public resources.

The following policy ideas are a mix of "carrots" and "sticks" that would go a long way toward generating new investment in BC's resource sector.

In order to increase investment in value-added wood products, the provincial government should:

- ban the export of raw logs from Crown land;
- provide tax credits to forest companies investing in value-added production, with the revenue coming from increased stumpage rates; and
- make more wood available to small firms wanting to manufacture value-added products by reforming the Small Business Forest Enterprise Program and establishing more log yards.

Pulp mills can be encouraged to meet Zero-AOX regulations (eliminating chlorinated toxins from their effluent) and become closed-loop by:

- providing low- or zero-interest loans to pulp producers wanting to invest in closed-loop technology; and
- extending the deadline on the Zero-AOX Law (with a firm end date), but implementing a tax shift policy that increases the cost of AOX emissions, with revenues used to give tax credits to companies investing in compliance.

For reasons of social justice and putting an end to uncertainty in BC, the provincial and federal governments should:

- negotiate interim agreements with First Nations people and, as part of treaty settlements, provide them with resources to develop forestry plans and market ecologically-friendly forest products.

In fisheries, the two levels of government should work together to:

- implement a progressive royalties system in all fisheries, with the revenue being used to diversify fishing economies and develop and market locally-based, sustainable fish products; and
- mandate a future ban on open net fish farms and—in the interim—implement a tax shift policy that increases fees for open pen licenses and grants tax credits for the purchase of closed containment technology.

In order to generate a more sustained flow of capital from non-renewable resources, the provincial government should:

- establish a trust fund by pooling a portion of resource royalties and taxes from oil, gas, coal and other mining operations, and use the capital for economic development projects within the province; and
- amend the *Mines Act* so that companies developing a non-renewable resource must pay a community transition bond, to be used by the community and workers once the project is closed down.

Finally, a range of policy mechanisms can be used to generate investment that is not specific to one resource sector. These policies include:

- establishing a Provincial Resource Investment Bank to collect revenue from various resource activities and BC investors, and extend favourable financing to investment projects evaluated through a transparent, competitive bidding process;

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Recent Indicators

	Unemployment rate (%)				Average Weekly Earnings		
	June 2001	May 2001	April 2001	June 2000	May 2001	April 2001	May 2000
BC	7.0	6.8	6.9	6.8	$649.78	$650.42	$635.75
Canada	7.0	7.0	7.0	6.6	$635.08	$634.96	$611.63

Note: Unemployment figures are seasonally adjusted.
Source: Statistics Canada

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likely to invest the proceeds in the financial markets, pay off personal debt or take a Hawaiian vacation.

Low and middle income earners are much more likely to spend the tax cut. A post tax cut poll by Ipsos-Reid found that 48% of those receiving a $100 tax cut would spend it, whereas only 18% of those receiving a $1000 tax cut would spend it, preferring instead to pay off debt or invest it. Even for those with a $100 tax cut, 26% said that they would pay off debt, pointing to the underlying fact of high personal debt levels at a wide variety of income levels. This suggests that much of the hoped-for economic stimulus will remain elusive.

A second aspect has to do with the nature of the government's fiscal situation in 2002. If balancing the budget quickly is deemed to be a high priority, then public services will need to be cut. This would draw money out of the economy, thereby offsetting the stimulative impact of the tax cuts (indeed, a "balanced budget" tax cut—where spending falls by the same amount as taxes are cut—would actually be a drag on economic growth).

An alternative path for the government would be to run deficits in the short-term while keeping the lid on spending, allowing growth in the economy to bring tax revenues back into line with the current expenditures. This would allow the Liberals to stick to their promise of not cutting health care and education (which together account for two-thirds of budgetary expenditures). Down the road, this could re-balance the budget within a few years. It would also mean that public expenditures would not keep up with population growth or inflation. In either case, the new tax cuts will push BC's social deficits further into the red.

Marc Lee is the BC Office's research economist. For a more detailed look at BC's fiscal situation in light of the tax cuts, see the CCPA's submission to the Fiscal Review Panel on the web at policyalternatives.ca (also available by calling the office).

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- passing enabling legislation for communities to develop economic development plans, and helping communities acquire the capacity to realize them;
- establishing performance requirements for companies receiving government grants or subsidies, with penalties (a requirement to pay back the grant or subsidy with interest) for companies that fail to meet those requirements; and
- implementing policies that facilitate and encourage the development of employee share ownership plans in BC companies.

This list is not exhaustive. These and other policy ideas are elaborated on in *Re-capturing the Wealth: Investment Solutions for Jobs and Environmental Sustainability in BC's Resource Sector.* All are hopeful and realizable policies that together form a compelling investment strategy to reinvigorate BC's resource sector.

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