

Personal Taxes in British Columbia

The tax cut is the political panacea of the day, hailed by the media as “good for what ails you.” Like its predecessors — debt reduction, deregulation, free trade and tight monetary policies — the call for tax cuts promises much. As one might expect, politicians of all stripes, eager to win favour with the voters, are tripping over themselves to be associated with the idea. At a time of eco-

The Tax is Always Cheaper on the Other Side

It is commonly reported that BC has the highest taxes in Canada. Such statements are largely based on the top marginal income tax rate. In BC, the top rate was 54.2% in 1998, indeed highest in the country. In 1999, this rate fell to 52.7%, below Newfoundland’s top rate of 53.3%, and is further scheduled to drop to 49.9% by 2001.

Unfortunately, the debate on high taxes begins and ends with the marginal tax rate, which is the rate paid on the last dollar of income. The marginal tax rate rises as income rises, reflecting progressivity — the idea that those who make more should pay a higher percentage of their income in taxes. In BC, only income in excess of about \$80,000 gets taxed at the top rate. Interestingly, only 4% of BC taxpayers make enough money to pay the top marginal rate, while most taxpayers do not even come close.

A deeper look at the income tax system beyond the marginal rate tells a different story about taxes

Marginal and Average Income Taxes, 1998

	Top Marginal Income Tax Rate (%)	Federal and Provincial Income Tax as a % of Income					
		\$50,000 Income		\$75,000 Income		\$100,000 Income	
		Single	Family	Single	Family	Single	Family
BC	54.2	27.0	15.7	34.6	22.9	39.3	27.3
AB	45.6	26.4	15.5	33.0	22.4	36.1	26.6
SASK	51.6	29.9	17.6	37.2	25.6	40.8	30.2
MAN	50.1	29.9	16.7	36.8	25.0	40.1	29.8
ON	50.3	25.6	14.8	33.2	21.8	37.5	25.9
PQ	52.5	32.4	17.0	39.5	27.3	42.8	32.1
NB	50.6	29.0	17.0	35.8	24.6	39.2	29.1
NS	49.7	28.2	15.8	35.0	24.0	38.5	28.4
PEI	50.3	28.6	16.8	35.9	24.3	39.5	28.9
NFLD	53.3	30.3	17.9	37.8	25.7	41.7	30.4

Notes: “Single” is an unattached individual with no dependents

“Family” is a two income family of four

Source: Canadian Tax Foundation

nomic slowdown, a simple message that promises cash in hand while rebooting the economy is a compelling one.

There are good reasons to be skeptical about the ability of the tax cut to deliver. First, the proposition that taxes are too high in BC is based only on the top marginal tax rate, rather than a look at average taxes paid. Second, in a balanced budget framework, reductions in taxes must be matched by cuts in publicly-funded services, such as health care, education and welfare. Finally, the economic benefits of the tax cut are largely overstated, particularly when aimed at those that need it least.

in BC. Total federal and provincial income tax for those making between \$20,000 and \$75,000 per year is less only in Alberta and Ontario, but more in every other province. At the \$50,000 income level, the total in-

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come tax bill amounts to 27% of income for a single taxpayer with no dependents, and 15.7% for a two-income family of four. At \$75,000, this rises to 34.6% for the individual and 22.9% for the family.

Only well above \$100,000 a year do income taxes in BC become high relative to other provinces. Even at the immodest sum of \$100,000 per year in income, combined federal and provincial income taxes are only 39.3% of income for the individual and 27.3% for the family, comparable to other provinces. This suggests that preoccupation with marginal tax rates can be very deceptive.

When all taxes are considered — income, sales, property and payroll taxes, plus health care premiums — the differences are smaller still. When these are factored into the equation, BC is the second lowest tax jurisdiction in the country, again for all but the very wealthiest residents. Even a well-off family of four, with an income of \$90,000, would pay only \$830 less tax in Alberta than BC — hardly enough to justify the cost of the move.

By international standards, taxes in BC

And some US states, like California, actually have higher taxes than BC, except on the wealthiest.

The Full Costs of a Tax Cut

Not surprisingly, most people would like lower taxes and lower public debt. But most people also want better health care, quality education, a clean environment and good roads, among other things. Public policy is about reconciling these conflicting choices. Canadians have traditionally chosen to support programs that increase the fairness and equity of our society. Before succumbing to tax cut euphoria, British Columbians should think deeply about the price they are willing to pay.

The biggest expenditure items in the BC budget are health, education and social assistance, which together account for almost 80% of total provincial spending. What's left goes to a myriad of public services, such as law enforcement, infrastructure and environmental protection. So the appropriate question for tax cutters is: which publicly-funded services can you do without?

In terms of economic impacts, the tax

economic growth. This is borne out by statistical models by Informetrica and the Conference Board of Canada, which address the role played by government expenditures through wages paid to public employees, purchases of goods and services from business, and transfer payments to both individuals and businesses.

Part of the reason why tax cuts do not provide the bang for the buck is due to leakages. While much of a tax cut windfall may be spent, some of it will be saved, so the benefit of increased disposable incomes is not fully realized. And given the record high levels of personal debt in Canada, the proceeds of a tax cut may simply go toward paying down credit card balances. Of the part that is actually spent on goods and services, a sizable portion flows out of the province to pay for imports from the rest of Canada, the US, or the rest of the world.

These leakages are much smaller for direct government expenditures on employment and for consumer spending by low income households. Tax cuts at the high end of the income spectrum have less economic impact, as the beneficiaries least need the boost in income. If there are to be more tax cuts, they should be aimed at low income British Columbians. A tax cut for low income earners would increase purchases of goods and services, rather than be invested in the stock market or offshore. This would have a much greater stimulative impact when there is slack in the economy, and it would enhance the progressivity of the tax system.

At a time when income inequality is worsening, the tax system has a fundamental role to play in ensuring more equitable outcomes. The 1999 Alternative Federal Budget outlines a large number of areas where federal tax reform can work to increase the fairness of the system, all within a revenue-neutral framework. Provincially, we should strive for the same. Like death, taxes may be inevitable, but they are the price we pay for a civilized society.

BC Government Expenditures, 1998-99		
	\$million	% of Total
Health	7,416	36%
Education	5,954	29%
Social Services	2,951	14%
Protection of Persons and Property	1,026	5%
Natural Resources and Economic Development	857	4%
Transportation	783	4%
Other	1,550	8%
Total	20,536	100%

Source: BC Budget 1998

are not excessive, either. BC's highest marginal tax rate is average for the European Union, and only slightly above the OECD average. While taxes in the US tend to be lower, the difference is not as large as many suggest when out-of-pocket costs like private health insurance (which can run US\$400-500 per month) are factored in.

cut versus services trade-off is not a neutral proposition. A tax cut would increase total disposable income, by putting money in people's pockets to spend, thereby increasing economic growth. But this is not the end of the story. Cuts to government spending more than offset any benefit derived from a tax cut, thereby diminishing

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Lowering Taxes Does Not Lead to Increased Government Revenues

by Seth Klein

[The following is excerpted from a new CCPA/Parkland report entitled *A Tale of Two Provinces: A Comparative Study of Economic and Social Conditions in British Columbia and Alberta*.]

Increasingly, British Columbians hear the win-win claim that lowering taxes would actually increase government revenues. Allegedly, individuals will work harder and businesses will increase their investment in response to lower taxes, and more individuals and businesses will be attracted to the province, thereby raising overall government revenues.

We have heard these claims before. Advocates, known as “supply-siders,” had their heyday during the Reagan administration of

the 1980s. But the evidence does not substantiate this view.

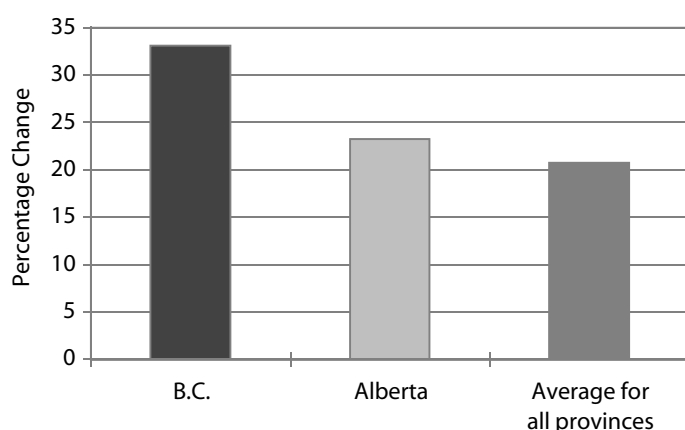
Ronald Reagan cut taxes in the U.S. just prior to the recession of the early 1980s. On the basis of a theoretical proposition known as the Laffer curve (dubbed “voodoo economics” by George Bush during the 1980 Republican primaries), the Reagan administration claimed tax cuts would stimulate growth and increase government revenues. In fact, government revenues fell and U.S. federal deficits and debt grew to record high levels. MIT economist Paul Krugman, who calls the Laffer curve “crude and silly”, notes that gross investment relative to GDP actually fell after the Reagan tax cuts. The tax cuts also acted as Robin Hood in reverse: by extending the largest tax breaks to the wealthiest citizens, the tax cuts exacerbated inequality.

Recent experience in Alberta and BC also defies the proposition that cutting taxes leads to greater government revenues. As the accompanying chart shows, overall income tax revenues have been growing in both provinces since 1992-93 (revenues were down in both provinces that year, as the recession cut into incomes and corporate profits). According to neo-conservative logic, we would expect to see income tax revenues in Alberta growing at a faster rate than in BC, given that tax cuts have been deeper in Alberta. But this has not been the case. Even with Alberta’s deeper tax cuts, faster economic growth, and strong growth in corporate profits, both personal and corporate income tax revenues in Alberta, adjusted for population growth, increased at a slower pace than in BC during the four years between 1992-93 and 1996-97.

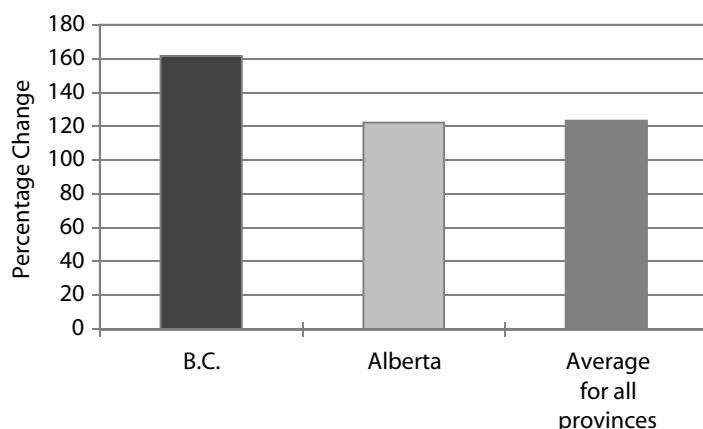
Overall provincial revenues actually declined in Alberta in 1995-96. The Alberta government predicted in its 1998 Budget that tax cuts would offset revenue growth, and estimated that overall revenues for 1998-99 would fall by almost \$2 billion due to declining oil prices, their lowest level since 1993-94. So much for tax cuts producing increased revenues in Alberta this year.

These data make clear that tax cuts do not increase government revenues. Revenues may increase *despite* a tax cut, but not *because* of a tax cut. Ultimately, tax revenues in BC and Alberta have more to do with factors such as population growth, where we are in the business cycle, and international demand and prices for our major commodity exports. If taxes are cut during a downward point in the business cycle, revenues may decrease (as happened to Alberta in the mid-1980s). In

Change in Revenues from Personal Income taxes, 1992/93-1996/97



Change in Revenues from Corporate Income Tax, 1992/93-1996/97



Source: Calculated from Statistics Canada data, Public Accounts, Financial Management System.

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general, revenues increase along with population and economic growth. The question is: will revenues increase sufficiently to keep pace with the needs of a growing society and the commensurate rise in demand for public services? The evidence indicates that tax cuts only decrease what revenues might otherwise be, undercutting the money available to fund health care, education, welfare,

and other public services.

In fact, the OECD recently released a report warning against the competitive lowering of taxes across nations, given the impact this would have on government services. The competitive lowering of taxes serves corporations and the wealthy very well, but is not in society's best interest.

Recent Indicators

	Unemployment Rate			Average Weekly Earnings		Inflation Rate 1998
	Nov-98	Dec-98	Jan-99	Oct-98	Increase over prev. yr.	
Canada	8.00%	8.00%	7.80%	\$609	2.00%	0.90%
BC	7.90%	8.20%	8.10%	\$624	1.50%	0.30%

Source: BC Stats, Statistics Canada

Changes in Total Employment (seasonally adjusted)

	Total Employment (thousands)			Growth Rate (%)	
	Dec-89	Dec-97	Dec-98	Past Year	Since Dec/89
Canada	13,149	14,115	14,562	3.2	10.8
BC	1,545	1,837	1,895	3.1	22.6
AB	1,270	1,482	1,532	3.4	20.6
SASK	453	479	481	0.3	6.3
MAN	509	543	554	2.0	8.7
ON	5,270	5,494	5,707	3.9	8.3
PQ	3,163	3,302	3,398	2.9	7.4
NB	298	323	336	4.1	12.7
NS	382	398	402	1.1	5.1
PEI	54	61	60	-1.0	11.7
NFLD	204	196	199	1.6	-2.1

Notes: Numbers may not add due to rounding.
 "Since Dec. 1989" measures Dec/'89 to Dec/98.
 "Past year" measures Dec/97 to Dec/98.

Source: Statistics Canada

Percentage of unemployed people eligible for Unemployment Insurance

	1989	1997
Canada	74%	36%
BC	66%	34%
Vancouver	63%	26%
Victoria	51%	25%
Southern Interior BC	60%	44%
Southern Coastal BC	57%	35%
Northern BC	62%	36%

1997 net outflow of UI premiums from BC (except Lower Mainland): \$1.8 billion
 Source: Canadian Labour Congress, *Left out in the Cold*, January 1999

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