Canadian Taxpayers Federation

2016-17 Federal Pre Budget Brief

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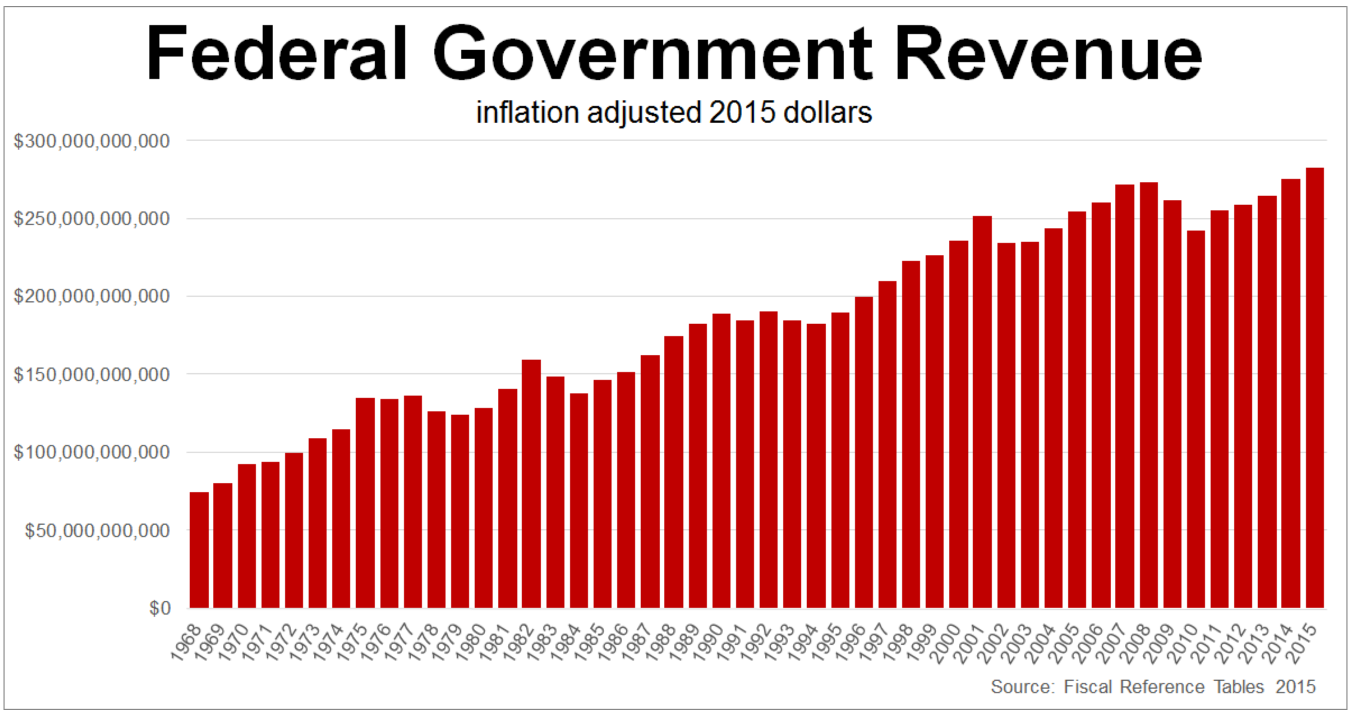
Introduction

For the 2016-17 budget, Canada has a new federal government for the first time in a decade. The new government, while rightly grappling with the new economic reality faced by many Canadians, must nonetheless resist the temptation to act imprudently. The historical record is clear, going back nearly half a century: plunging the federal budget into deficit has never been a short-term or inexpensive exercise. Small deficits have inevitably turned into larger ones, and debt and interest payments have risen. Since 1990 alone, Canadians have spent **$1.3 trillion** of their tax revenues servicing the federal debt. The opportunity cost of this money cannot be captured by reference to the debt-to-GDP ratio alone.

While it is true that government can be a force for good, it is equally true that well-intentioned governments can, with the wrong policies, end up doing more harm than good. The limitations of government must be respected. We believe our recommendations strike a balance between the government's need to act, while recognizing these limitations.

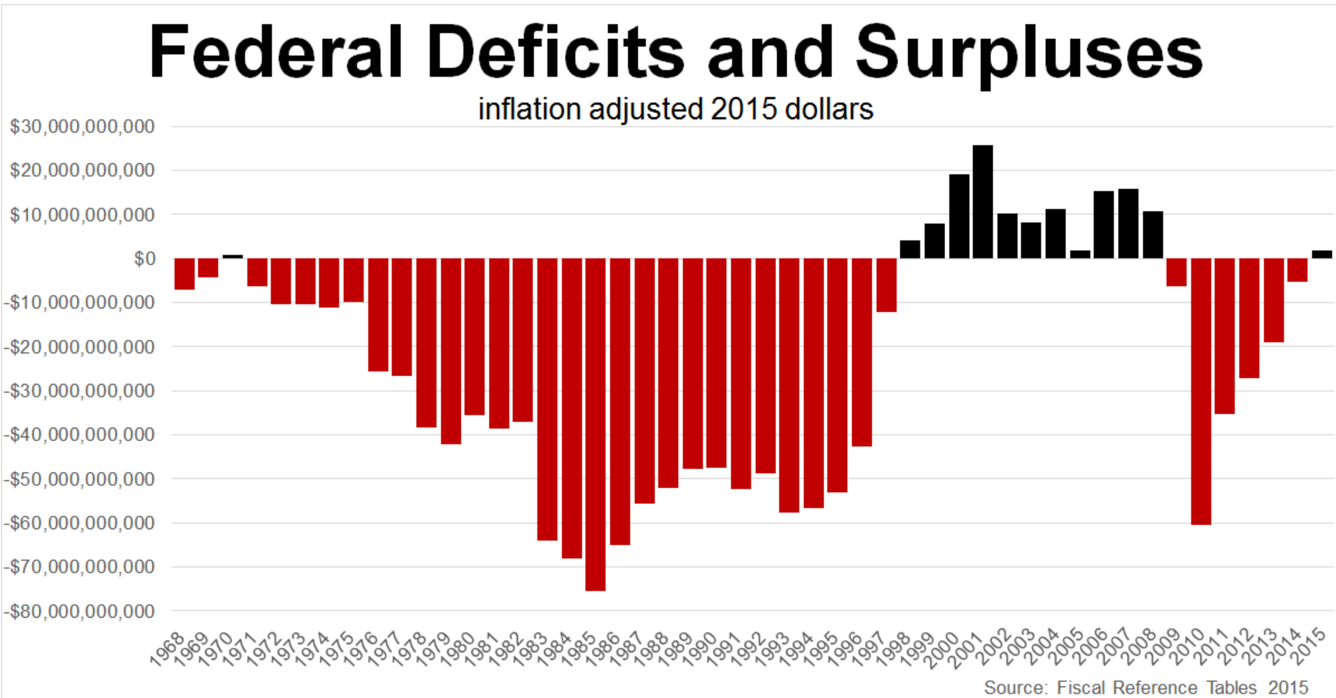


Contrary to what some commentators have asserted, the federal government does not face a shortage of revenues; rather, revenues are at all-time highs.

Perhaps the biggest challenge for the new government is to **control spending**, and ensure the best value for tax dollars spent. Most Canadians would be justified in asking precisely what they have been getting for an additional $50 billion in annual federal spending since 2005-06. Clearly, there remain opportunities to seek out further savings, reallocate inefficient spending, and simplify the tax code.

Recommendation #1: Balance the Budget

Balanced budgets are rarely seen creatures at the federal level. Since 1968, the federal government has run a deficit in 35 out of 48 years. The empirical fact is that historically, deficits have tended to grow and persist, rather than represent short-term cyclical undertakings.



The new government should not repeat – for almost identical reasons and in an identical way – the 2009 mistake of their immediate predecessors. Indeed, many current cabinet ministers were rightly critical of the Harper government's record on deficits and debt, and as recently as April 2015 argued that a Liberal government would balance the books[1].

The government has made major investments in infrastructure a central component of its policy program, and no one can deny the importance of infrastructure to Canada's long-term economic interest, but this truism cannot be used to wish away fiscal constraints. Projects must be prioritized and hard decisions must be made. Governments which succumb to the temptation to say "yes" to every request for public dollars inevitably find themselves in a difficult position very quickly. In this respect we encourage the new government to take a page from their federal predecessors of the 1990s, and not their provincial brethren at Queen's Park.

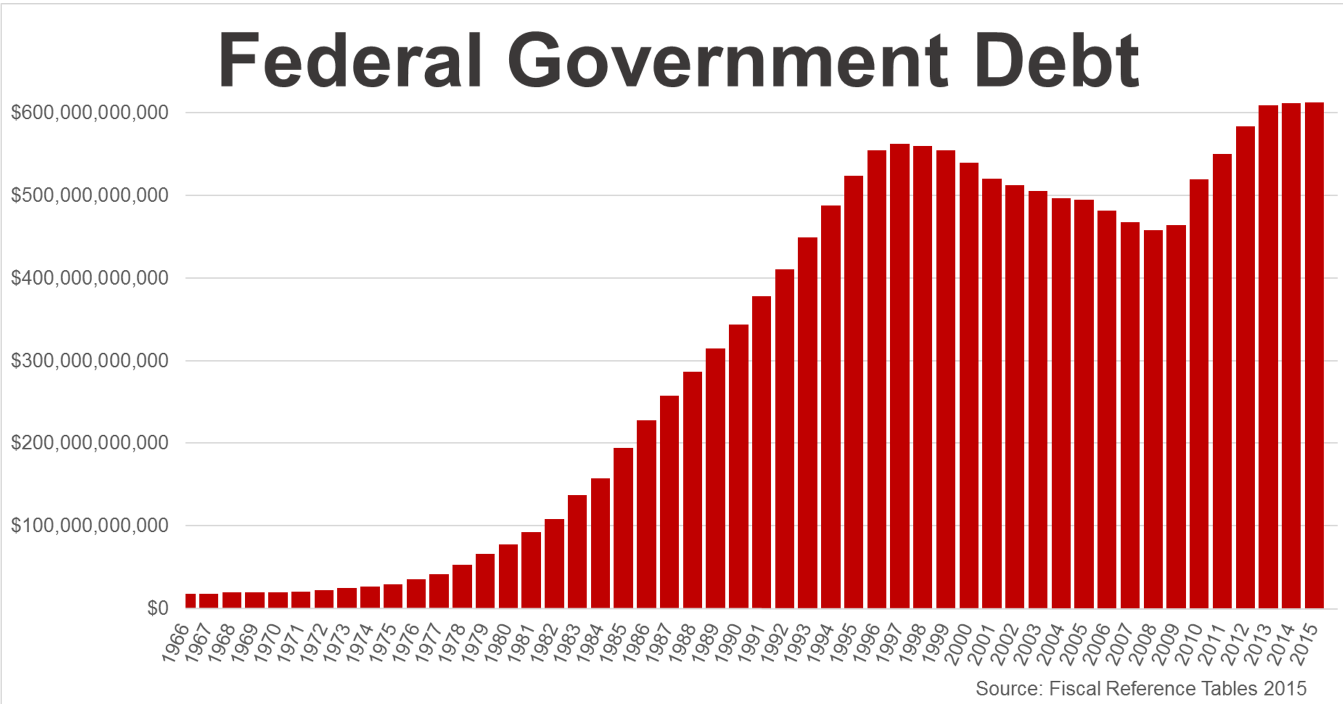
[1] Scott Brison, April 23, 2015 – Hansard
http://www.parl.gc.ca/HousePublications/Publication.aspx?Language=E&Mode=1&Parl=41&Ses=2&DocId=7934159

Furthermore, it would be ill-advised to attempt to leverage this proposed deficit infrastructure spending as "stimulus" for reasons identified by Université de Laval economist Stephen Gordon, who observed that government spending (a demand response) cannot offset the effects of changes in oil prices (a supply shock)[2]. University of British Columbia economist Kevin Milligan also identified several reasons that attempts to stimulate the economy though increased government spending would be ineffective, in particular that the theoretical impact of stimulus spending is greatly reduced in small, open economies with flexible exchange rates, such as Canada's[3].

Indeed, a 2010 study by the Fraser Institute found that the 2009 Harper government stimulus package had next to no economic impact, and that the subsequent economic recovery was primarily driven by private sector business investment and increased exports[4].

[2] http://www.nationalpost.com/m/search/blog.html?b=news.nationalpost.com/full-comment/stephen-gordon-the-government-stimulate-these-problems-away&q=Stephen%20gordon&o=8
[3] http://www.macleans.ca/economy/economicanalysis/why-a-big-stimulus-plan-isnt-the-fix-to-what-ails-canada/
[4] http://www.fraserinstitute.org/sites/default/files/did-government-stimulus-fuel-economic-growth.pdf

Recommendation #2: Create a legislated debt reduction schedule or a budget line item



While we believe the government should not run a deficit and add to our federal debt, if it does so, it is essential that a concrete plan be formulated to return to balance and begin to pay down our federal debt over the long term. Our federal debt is a perpetual fiscal hangover that continues to drain public dollars to this day.

Federal debt servicing will cost Canadians $26 billion in 2015-16: more than the government spent on National Defence. Much is made of the low debt-to-GDP ratio and there is no question Canada is relatively well placed compared to some of our G7 peers[5]; but focusing on the ratio alone masks the opportunity cost ($1.3 trillion since 1990[6]). Indeed, if the federal government were debt free, the entire 2015 Liberal platform could be implemented for 2016-17 with a $16 billion surplus to spare rather than a proposed $10 billion deficit[7].

Debt repayment must be treated as a priority, to be considered at the same stage as other spending priorities.

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[5] http://blog.euromonitor.com/2015/08/lessons-for-g7-economies-from-japans-super-high-public-debt-to-gdp-ratio.html
[6] http://www.taxpayer.com/media/DebtServicing1990to2015.png
[7] https://www.liberal.ca/files/2015/10/New-plan-for-a-strong-middle-class.pdf

Recommendation #3: End "tax-on-tax"

Some taxation is generally accepted by the public as a necessary evil. But the notion of charging a tax *on top* of another tax strikes many as double-dipping and a stealth attempt by governments to bilk taxpayers. The CTF has long called for an end to this practice.

Gasoline is a classic example of this dubious practice: GST or HST is applied to the full pump price, after federal and provincial per-litre taxes. Consequently, in addition to the actual market value of gasoline, government taxes the tax added onto its price. In 2015, federal and provincial governments collected $1.3 billion in GST on gasoline and diesel sales taxes just from this tax-on-tax[8]. Alcohol, tobacco and aviation fuel are just a few other examples of this taxation-by-stealth.

Gas Tax-On-Tax

Province/City	Tax-On-Tax Per Litre		Tax-on-Tax Collected		
	Federal	Provincial	Federal	Provincial	Total
Newfoundland	$0.01	$0.02	$9,381,140	$15,009,823	$24,390,963
PEI	$0.01	$0.02	$2,192,060	$3,945,708	$6,137,768
Nova Scotia	$0.01	$0.03	$14,759,572	$29,519,144	$44,278,716
New Brunswick	$0.01	$0.02	$14,077,458	$22,523,933	$36,601,391
Quebec outside of Montreal	$0.01	$0.03	$61,523,155	$116,893,994	$178,417,149
Montreal	$0.02	$0.03	$70,068,900	$133,130,911	$203,199,811
Ontario	$0.01	$0.02	$228,800,320	$366,080,512	$594,880,832
Manitoba	$0.01	$0.00	$19,852,008	$0	$19,852,008
Saskatchewan	$0.01	$0.00	$25,032,106	$0	$25,032,106
Alberta	$0.01	$0.00	$76,785,378	$0	$76,785,378
BC outside of Vancouver and Victoria	$0.02	$0.00	$25,002,780	$0	$25,002,780
Vancouver	$0.02	$0.00	$47,297,833	$0	$47,297,833
Victoria	$0.02	$0.00	$5,583,847	$0	$5,583,847
Canada	$0.01	$0.02	**$600,356,556**	**$687,104,024**	**$1,287,460,581**

[8] http://www.taxpayer.com/media/GTHD-Report-2015.pdf p12

Recommendation #4: Reduce the political party donation tax credit

Canada's federal political party donation tax credit is extremely generous – much more so than charitable donations, including such worthy organizations such as the Canadian Cancer Society, the Salvation Army and the Canadian Red Cross.

While donating to political parties is an act of civic engagement and should be encouraged, it should not be at the expense of charitable donations and other causes less favoured; political parties should be required to compete for donations on a level playing field with charities. The CTF recommends that the government harmonize the tax-deductibility of political parties downward to match the deductibility for charities.

Tax Credits from Donations

Donation	Federal Political Party		Registered Charity	
$200	$150	75%	$30	15%
$500	$350	70%	$117	23%
$1,000	$558	56%	$262	26%
$1,500	$650	43%	$407	27%

Recommendation #5: Resist any demands for new sugar or fat taxes

In recent years, well-meaning groups such as health advocacy organizations have been pressing governments worldwide to implement new "sugar" or "fat" taxes on the premise that taxing them will reduce their consumption and improve public health. The track record of these taxes in the jurisdictions which have implemented them suggest they don't achieve this objective.

A prominent example is Denmark, which in 2011 was the one of the first countries in the world to bring in a fat tax, and the first to abolish it thirteen months later.[9] No wonder: it was a fiscal disaster, driving hundreds of thousands of Danes across the German border for cheaper groceries and costing hundreds of jobs, according to Jens Klarskov, CEO of *Dansk Erhverv* (the Danish Chamber of Commerce).

As the Fraser Institute has pointed out, Canadian customs tariffs already add $3.6 billion in consumer costs to nearly everything we buy here.[10] Throwing on another tax would just further grow that price gap.

The argument for fat and sugar taxes revolves around higher prices limiting consumption and thus curbing obesity. But reducing sales is not the same as reducing caloric intake; one conundrum is that obesity rates continue to rise even through sugar consumption has dropped in Australia, Canada, and the United Kingdom[11].

9 http://translate.google.com/translate?sl=auto&tl=en&js=n&prev=_t&hl=en&ie=UTF-8&layout=2&eotf=1&u=http%3A%2F%2Fwww.skm.dk%2Fpublic%2Fdokumenter%2Fpresse%2FFaktaark_afgiftsogkonkurrencepakke.pdf&act=url

10 http://www.huffingtonpost.ca/mark-milke/canada-tariff-imported-goods_b_2707650.html

11 http://www.theglobeandmail.com/report-on-business/rob-commentary/what-canada-can-learn-from-mexicos-sugar-tax-its-no-panacea-for-obesity/article28233833/

Recommendation #6: Pass a *Truth in Budgeting Act*

Between budgets, governments do not provide costing for the legislation they introduce. The CTF thinks this needs to change.

The CTF recommends the government pass a *Truth in Budgeting Act*, which would require MPs and ministers to cost-out the bills they introduce in the House. Any piece of new legislation would legally require a cost estimate, compliant with government accounting standards. Both the implementation (year one) and ongoing (annual) cost would be calculated, added to the legislation's preamble, and made public.

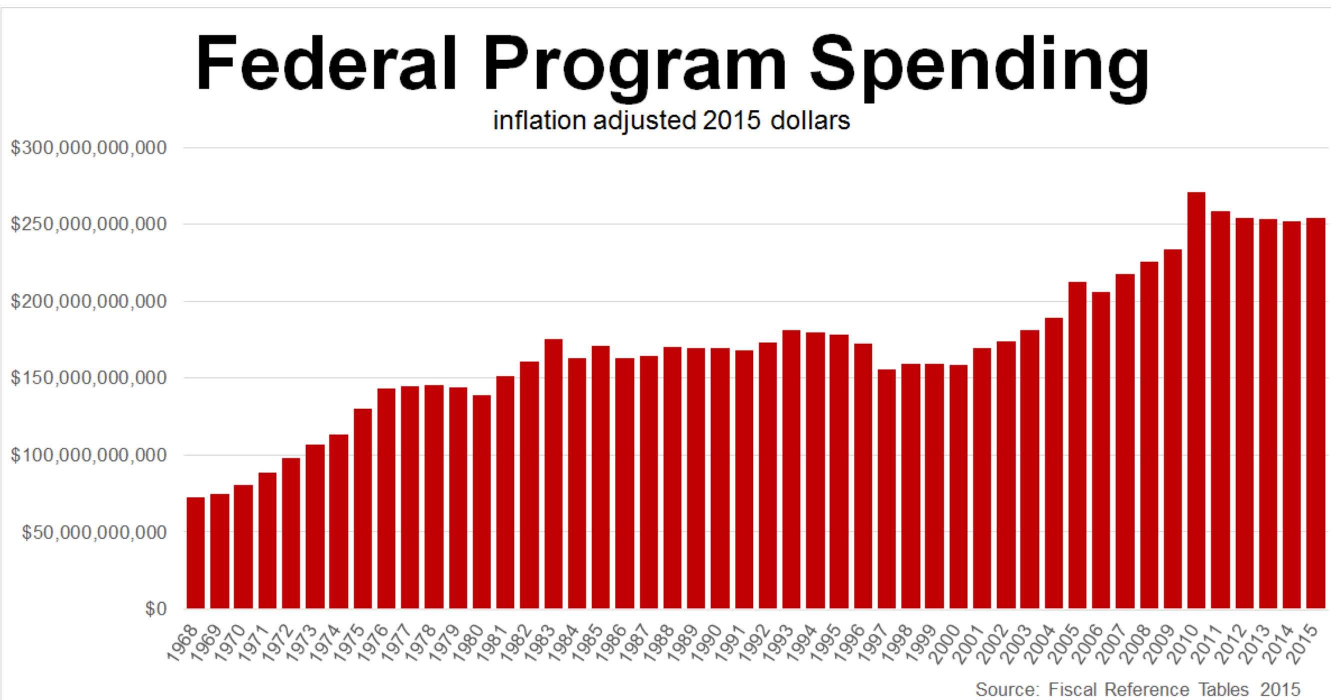
We are encouraged by the new governments' commitment to these principles as part of their election platform[12].

[12] https://www.liberal.ca/files/2015/10/New-plan-for-a-strong-middle-class.pdf p31

Recommendation #7: A core review to identify $15 billion in waste by 2017-18

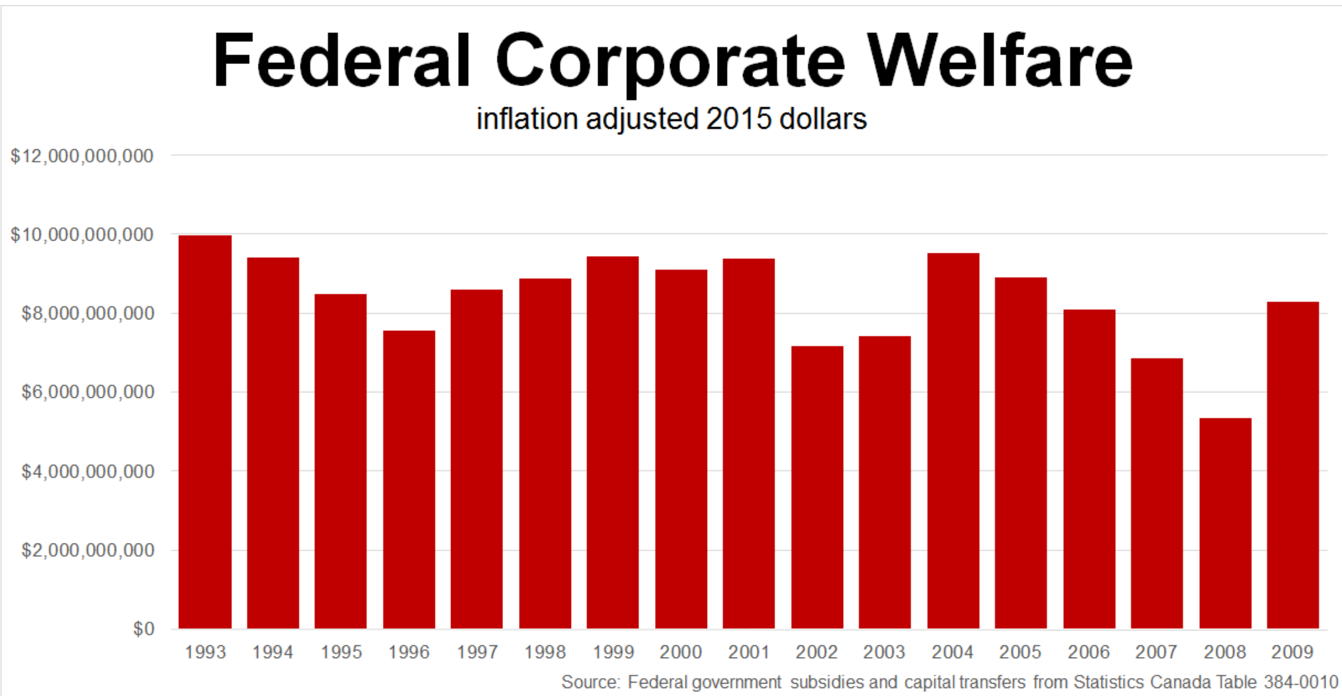
The CTF proposes that the government commit to a core review over the next 12 months, with the results made public in advance of the 2017-18 budget. A target should be to identify the least efficient/most wasteful 5% (or $15 billion) of all program expenditures.

Program spending is currently near all-time real dollar highs, having ballooned by more than 23% since 2005-06, the final year of the last Liberal government, when spending was $205.6 billion; under the Conservatives, program spending had risen to $253.8 billion by 2014-15. Canadians need confidence that this money is being used efficiently; if not, it should be reallocated and/or returned to Canadians in the form of tax relief.



Recommendation #8: Put an end to corporate welfare and regional development

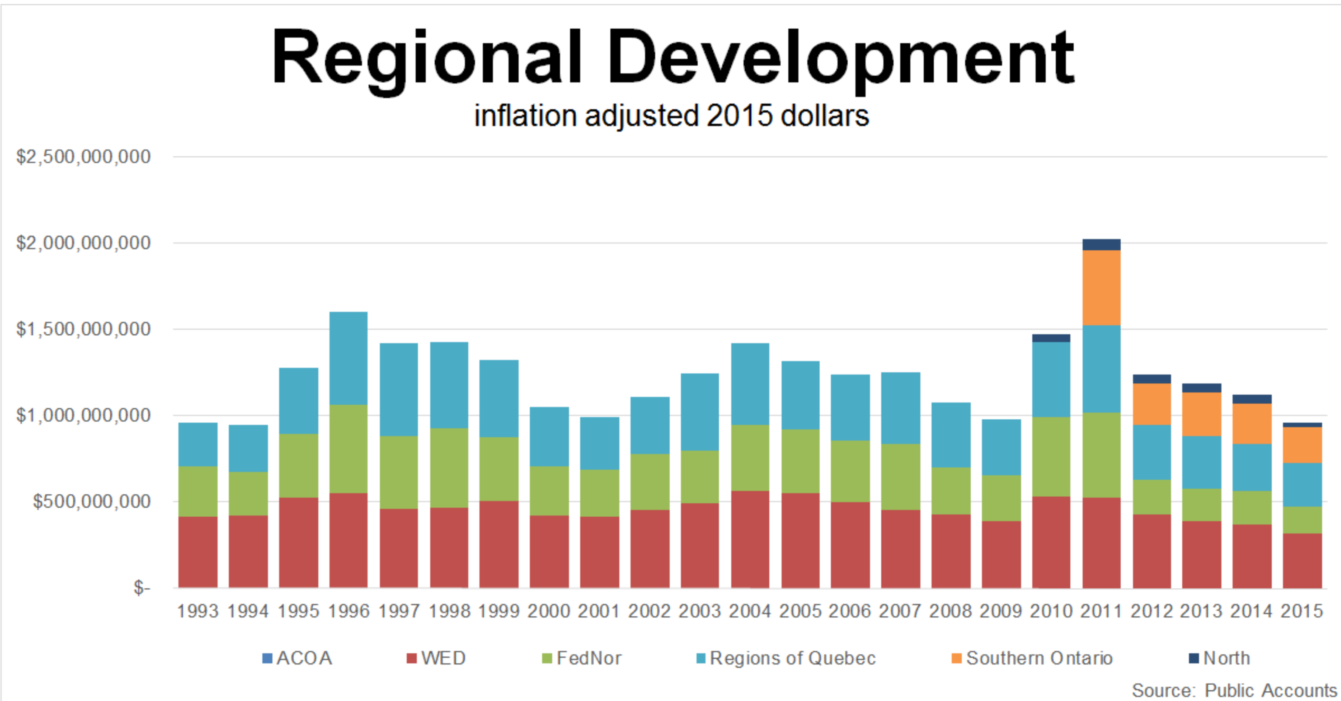
There is no getting around it: corporate welfare is bad. It is politically-driven and flies in the face of generally accepted economic theory and sound business practices. It creates perverse incentives for private sector businesses both to take inappropriate risks (on the assumption the government will come to their rescue) and attempt to squeeze more public dollars from governments (by threatening to move their operations elsewhere).



In some cases, major corporations such as Pratt & Whitney, Bombardier, General Motors and Chrysler have pocketed billions of taxpayer dollars – while still reducing their workforces. Indeed, one bailout inevitably sets the stage for the next, as we are seeing with Bombardier's current request for money, which Quebec has justified on the grounds that General Motors and Chrysler were previously bailed out.

Canadians who have lost jobs or businesses, but not received special bailouts from government rightly ask: why should these companies get special treatment?

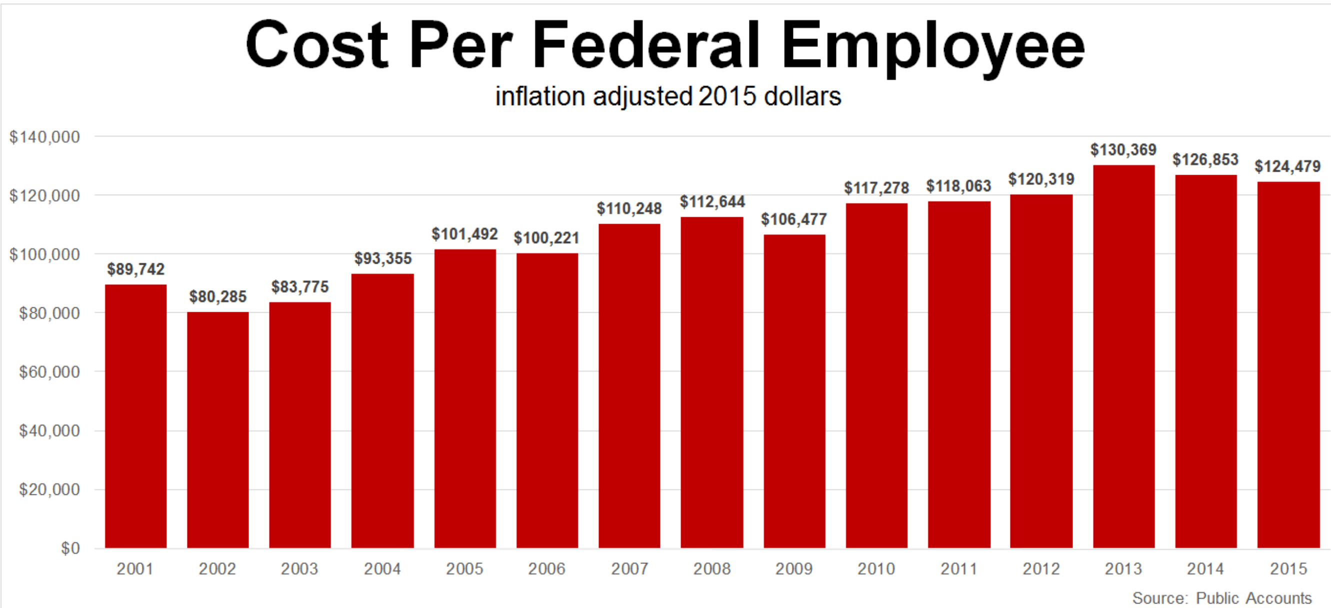
Regional development shares similar features to corporate welfare, in that is creates perverse incentives, with outcomes that do not match policy objectives. Governments have a role in assisting economically disadvantages regions of the country, but pouring in billions of dollars in dubious project funding is simply wasteful.



The CTF recommends that the government should begin phasing out these wasteful practice by:

- reducing total spending each year
- moving away from unconditional grants and towards loans
- creating tougher conditions for the acceptance of any public funds. In the case of corporate welfare, this should include waiving any rights to confidentiality of repayment terms
- broadening Access to Information laws to allow third parties to better scrutinize subsidy recipients
- for corporate welfare, negotiating provisions in any new trade agreements that bind our trading partners to similar restrictions on subsidizing private business

Recommendation #9: Control public sector pay and benefits



There is a natural tension between the interests of public sector unions and the interests of Canadian taxpayers at large: the former group wants to get as much as possible for its members; the latter group is the one paying for it, and needs confidence they are getting value for money. Public sector workers deserve fair treatment – but fair doesn't mean the government should be overly generous. It is important that the government be as hard-nosed an advocate for taxpayers at the bargaining table as union leaders are for their membership.

Public sector salaries are just one piece of the puzzle. Pensions are another. While direct comparisons are difficult to make for the federal public sector[13], the vast majority of federal government employees with pensions have generous defined-benefit plans, which are increasingly rare in the private sector, precisely because they are far more expensive to employers.

The CTF recommends that the government:

- use private sector benchmarks in negotiating with public sector unions
- increase the transparency surrounding the total compensation to public sector workers, in order to facilitate comparisons with private sector compensation levels

[13] https://www.fraserinstitute.org/sites/default/files/comparing-government-and-private-sector-compensation-in-canada.pdf see Appendix B

Recommendation #10: Rethinking Employment Insurance: A Model for the Future

Canada's Employment Insurance system is a major pillar of Canada's social safety net. Yet upon closer inspection it is in effect a patchwork of complex rules that apply unevenly across the country, treating workers dramatically differently depending on their occupation or where they live.

The CTF believes that it is time to rethink the entire Employment Insurance model, and published a 2013 report[14] making suggestions for a revamped EI system that will help end chronic unemployment, reduce perverse incentives and treat all workers fairly.

The current EI system effectively functions as a massive regional wealth transfer, and stands in stark contrast to its original intention of being a way to temporarily assist Canada's most vulnerable.

The CTF proposes a revised system built around a new concept: the Employment Insurance Savings Account (EISA). Working Canadians would continue to pay EI premiums – only into a personal EISA account, which could be drawn on if they (or their spouse or other family member) loses a job. Remaining funds could then be invested in a Registered Retirement Savings Plan (RRSP)-eligible investment vehicle. Upon retirement, any outstanding EISA balance could be transferred into an RRSP, and rolled into a Retirement Income Fund (RIF), Tax-Free Savings Account (TFSA) or Pooled Registered Pension Plan (PRPP) – significantly increasing retirement savings, another key benefit.

[14] http://www.taxpayer.com/media/EI%20ReportCTFNov2013.pdf