CANADIANS FOR TAX FAIRNESS
CANADIENS POUR UNE FISCALITÉ ÉQUITABLE

Taxes are Key to Reducing Inequality

Presentation to Carleton University IPE Conference*:*
Political Economy: Old Challenges, New Responses
March 20 and 21, 2017

by Dennis Howlett, Canadians for Tax Fairness

1. Why We Need to Reduce Inequality

The tax system is a powerful tool for redistributing wealth and reducing inequality.

Closing the gap between rich and poor is not only a moral and ethical imperative; it is key to improving population health and quality of life for everyone (rich or poor) and, if that was not reason enough, it is also vital to restoring a healthy balance to a market-based economy.

The market does not do very well at sending signals about what should be produced unless those with lower incomes have sufficient resources to create the effective demand for goods and services that meet their basic needs. When wealth becomes too strongly concentrated in the hands of a few, consumer demand weakens, with disastrous consequences for job creation and economic growth.

In the past, concentration of wealth may have facilitated capital formation, which when invested in productive capacity created jobs and boosted the economy. But increasingly wealth is not being put towards long-term productive investment but into speculative investments that don't have any redeeming qualities and actually make our economy much more susceptible to bubbles and crashes.

Finally, as Linda McQuaig and Neil Brooks made clear in **The Trouble with Billionaires**[i], wealth concentration also under-mines democracy by enabling those with great wealth to influence government policies in ways that benefit themselves to the disadvantage of the majority.

So it's clear that we need to reduce inequality. But how is the best way to do this?

2. Taxing the Rich

The tax system can be used both to address the excess income and wealth at the top end as well as redistributing resources to the bottom. We have to tackle inequality at both ends of the problem.
The existing tax system in Canada does help to redistribute income to some extent.

Income taxes are progressive and the federal Liberal government has made them a little more progressive by adding a new top marginal rate of 33% to income over $200,000 last year. Several provincial governments have also raised income taxes on the richest taxpayers.

But other taxes, such as value added taxes and property taxes are regressive. That is why income taxes need to be progressive in order to counter-balance regressive taxes.

Progressive income taxes, though, are not enough to do the job especially when there are two big gaping holes that undermine the progressivity of the tax system:

- The huge number of tax loopholes (or tax expenditures) that allow the wealthy to avoid paying anything close to the top marginal rate on much of their income.
- The lack of any real tax on wealth (as opposed to income).

Unfair and ineffective tax expenditures, what we call tax loopholes, riddle our tax system and bleed the government of revenue that could otherwise have been raised and used to fund government programs.

David Macdonald from the Canadian Centre for Policy Alternatives recently published a study of the distributional analysis of tax expenditures that found of the 64 tax expenditures where distributional data was available, only five were relatively progressive. The other 59, costing over $100 billion, were regressive. The five most regressive loopholes provide 99% of their benefit to upper half of income earners.[ii]

Finance Minister Morneau has said he plans to close a number of tax expenditures in the upcoming Federal Budget. The Finance Department thinks there is about $3 billion in savings that could be realized. The **Alternative Federal Budget 2017**[iii], which I helped write, has identified over $16 billion in unfair and ineffective tax loopholes that should be closed. We will see on Wednesday how far the government goes in its stated commitment to make taxes fairer.

Income inequality in Canada is bad enough. But the disparity in wealth is an even bigger challenge. Canada does not tax wealth. The IMF has estimated Canada could generate $12 billion annually from a tax of just 1% on the net wealth of the top 10% of households. The **Alternative Federal Budget 2017** proposes that the federal government get a start on taxing wealth by introducing a minimum inheritance tax of 45% on estates valued above $5 million, similar to the estate tax in the U.S., which would net an estimated $2 billion annually in new revenues.[iv]

Canadian tax system is also able to transfer benefits to low income Canadians in a very efficient way and has been successful in reducing poverty, especially for seniors and more recently for families with children. But we still have high levels of poverty in Canada, which undermines population health and creates barriers for people to contribute to society to their maximum potential. Here are some ways they could be improved to do a much better job of reducing income inequality at the bottom end.

3. Reducing Child Poverty

The new and improved Canada Child Benefit which replaces the Canada Child Tax Benefit and the Universal Child Care Benefit, promises to do a much better job of reducing child poverty. An additional

$4.5 billion was budgeted so that now it provides a benefit of up to $6,400 per year for each child under the age of 6, and up to $5,400 per year for each child aged 6 to 17. The increased level of support and the targeting of additional benefits to low income families while maintaining the universal basis of the program is a significant improvement on the previous versions of child and family benefit programs.

A major short-coming of the changes introduced in July of 2016, however, is that there is no automatic indexing of the benefit to inflation. This will result in a significant decline in the real value of the benefit over time. The former CCTB/NCBS system was indexed and indexing should be restored to prevent the weakening of its anti-poverty impact over time. Another issue that needs to be addressed is the low take up rate of the CCB among certain groups, particularly on reserves among First Nations people, where 60% of children live in poverty.

The experience of growing up poor has long-lasting and costly health impacts, even if those individuals escape poverty in later years. Campaign 2000 estimates that 1.3 million children lived in poverty (Low Income Measure, After Tax) in Canada in 2014.[v] While the new and improved CCB is estimated to reduce the number of children living poverty by 300,000 by 2017, that would still leave a million children living in poverty. We can't stop now, as we have some ways to go yet if we are to eliminate child poverty. The government should commit to reducing child poverty by 50% over the next 5 years. While a combination of measures including a national housing strategy and a national child care program could contribute to achieving this goal, annual increases of **$1 billion** to the CCB could do a lot of the heavy lifting.

4. Reducing Seniors Poverty

Old Age Security and the Guaranteed Income Supplement together with public and private pensions and individual savings helped reduce poverty among Canadian seniors to a low of 3.9 per cent in 1995 (using the Low Income Measure, After Tax). However, since then we have been losing ground and poverty rates have risen to about 11 per cent as more Canadians are retiring without adequate company pensions or retirement savings.[vi] Less than 40 per cent of Canadians are now covered by workplace pensions, and employers have been reducing benefit levels. Only 30 per cent of Canadians who are eligible to do so contribute to RRSPs. While enhancements of the Canada Pension Plan by increasing income replacement rate to one third of earnings will help address this challenge to some extent in the next 7 years, greater reliance on public support will be unavoidable in the next few years.

The 10% increase to the Guaranteed Income Supplement top-up benefit for lowest income single seniors that was announced in the 2016 Federal Budget will cost about $670 million and remove about 85,000 single seniors from poverty. This is a good start but over 600,000 seniors are still left living under the poverty line.

Increasing the GIS top-up benefit is a good way to direct funds to those most in need. There should be annual increases similar to the **$670 million** made last year but for senior couples as well so as not to increase the gap between what an single senior and an individual senior who is in an economic family receives, with the goal of completely eliminating poverty among seniors in the next 5 years.

5. Reducing Working Age Poverty

While some progress has been made in reducing poverty rates among seniors and families with children, relatively little has been done to address poverty experienced by working age adults.

More than 12 per cent of working-age Canadians live in relative poverty. Canada ranks 20th out of 31 developed countries.[vii] Provincial minimum wages and social assistance rates fall far below the poverty line. While child and senior poverty has been the focus of government anti-poverty initiatives in recent years, very little attention has been given to addressing working age poverty.

The federal government has some tools available that could be used to tackle this problem.
A very cost effective and efficient way to deliver benefits to many low income Canadians would be to boost the GST/HST credit. Benefits could be targeted to those most in need by using a top up benefit, similar to that used by the previous Conservative government when it increased GIS rates for seniors. The GST/HST benefit now costs about $4 billion. We recommend doubling this amount for an additional expenditure of **$4 billion** a year.

6. Reducing Poverty for Working Poor

The Working Income Tax Benefit, introduced in 2007 and strengthened in 2009, provides a supplement to the working poor to off-set the loss of benefits resulting from going off social assistance as well as the increased costs associated with working, such as transit. It is a refundable tax credit that provides up to $1,015 a year for single persons and about $1,844 per couple, depending on the province. The credit is slightly more for those with a disability. About 1.5 million individuals received this benefit in 2013 at a cost to the government of just over $1 billion a year. This benefit has provided a positive incentive for people to move off welfare and into the workforce, but it does not do enough to help working poor families who have never been on social assistance.

The maximum benefits should be doubled over 4 years, and the program should extend its reach higher up the income ladder so that it becomes a major income support for Canadians who work but remain poor. This would cost an additional **$250 million** a year.[viii]

Raising minimum wages so that a single person working full time would have an income above the poverty line would be an important complement to this program – one that would not require any government expenditure and that could actually increase tax revenue. While the federal minimum wage covers less than 10% of the workforce, reinstating a federal minimum wage at $15 an hour could help to establish a national benchmark that could encourage other jurisdictions to also ensure their minimum wages are a living wage.

7. How to Pay for Boosting Poverty Reduction Measures

The enhancements to the various existing benefit programs we have suggested total about **$6 billion** a year. This could be funded by simply redirecting some of the $14 billion the government spends subsidizing RRSP savings, and $23 billion it spends subsidizing Registered Pension Plans which primarily benefit middle and upper income Canadians. Lowering the annual RRSP contribution limit to

$20,000 could save **$2 billion** a year while still providing a retirement savings option for most middle and lower income Canadians. A life time limit of $50,000 for Tax Free Savings Accounts would save a modest **$100 million** a year initially, but would increase to billions of dollars in future years. Closing tax loopholes such as the stock option deduction could save **$800 million** a year. Limiting the Capital Gains Deduction by increasing the inclusion rate from 50% to 75% or setting it at 100% with an inflation adjustment could save up to **$10 billion** a year. These are just a few of the **$16 billion** in unfair and ineffective tax expenditures that we have identified in our Pre-Budget Consultation Submission to the Finance Committee.[ix] Closing these loopholes would not only save more than enough to cover the additional anti-poverty measures we suggest, they would also help to reduce inequality by reducing government subsidies to the very rich. And there would be funds left over to invest in a national child care program and a national social housing program that would also help reduce poverty while boosting employment and the economy as a whole.

8. Reducing poverty would also lead to savings on health costs, criminal justice and increased tax revenue

Increased tax revenue resulting from increased labour force participation rates would also help to offset the costs of poverty reduction expenditures. And there would be many other savings that could be realized in government expenditures on health and criminal justice, just to name a few. While an up-front investment in poverty reduction is required, there would be big returns on that investment in many ways including a healthier society, economic growth and increased tax revenue.

9. Fair Tax policies easier to implement than Basic Income

There are risks inherent in replacing all existing social assistance programs with a basic income as some people living in poverty could end up in a worst situation.[x] The full savings from replacing other social benefit programs such as welfare and disability benefits could not be realized without federal-provincial agreements. Without replacing many of these existing benefit programs, there would not be the funds needed to set Basic Income rates at adequate levels. For this reason, we would be very cautious about seeing the Basic Income as the solution to poverty and income inequality in Canada.

We think it would be possible to achieve ambitious poverty reduction targets by significantly augmenting many of the efficient and cost effective delivery mechanisms that already exist in the federal tax and social transfer system. This would be much easier to implement and could help to augment the inadequate levels of support provided by almost all provincial and territorial welfare programs.

---

[i] McQuaid, Linda and Brooks, Neil, **The Trouble with Billionaires: How the Super-Rich Hijacked the World and How We Can Take It Back**, Toronto: Penguin Books, 2010.

[ii] For details see Macdonald, David, Out of the Shadows: Shining a light on Canada's unequal distribution of federal tax expenditures, Ottawa: Canadian Centre for Policy Alternatives, 2016. https://www.policyalternatives.ca/loopholes

[iii] https://www.policyalternatives.ca/sites/default/files/uploads/publications/National%20Office/2017/03/AFB2017_Main_Document.pdf

[iv] Canadian Centre for Policy Alternatives, **High Stakes, Clear Choices: Alternative Federal Budget 2017**, p. 33.

[v] http://campaign2000.ca/wp-content/uploads/2016/03/2015-Campaign2000-Report-Card-Final-English.pdf

[vi] https://d3n8a8pro7vhmx.cloudfront.net/broadbent/pages/4904/attachments/original/1455216659/An_Analysis_of_the_Economic_Circumstances_of_Canadian_Seniors.pdf?1455216659

[vii] https://data.oecd.org/inequality/poverty-rate.htm 2013

[viii] http://www.caledoninst.org/Publications/PDF/1001ENG.pdf
[ix] http://www.taxfairness.ca/sites/taxfairness.ca/files/pdf/c4tf_brief_to_fina_for_2017_pre-budget_consult.pdf
[x] https://www.policyalternatives.ca/sites/default/files/uploads/publications/National%20Office/2016/10/Policymakers_Guide_to_Basic_Income.pdf