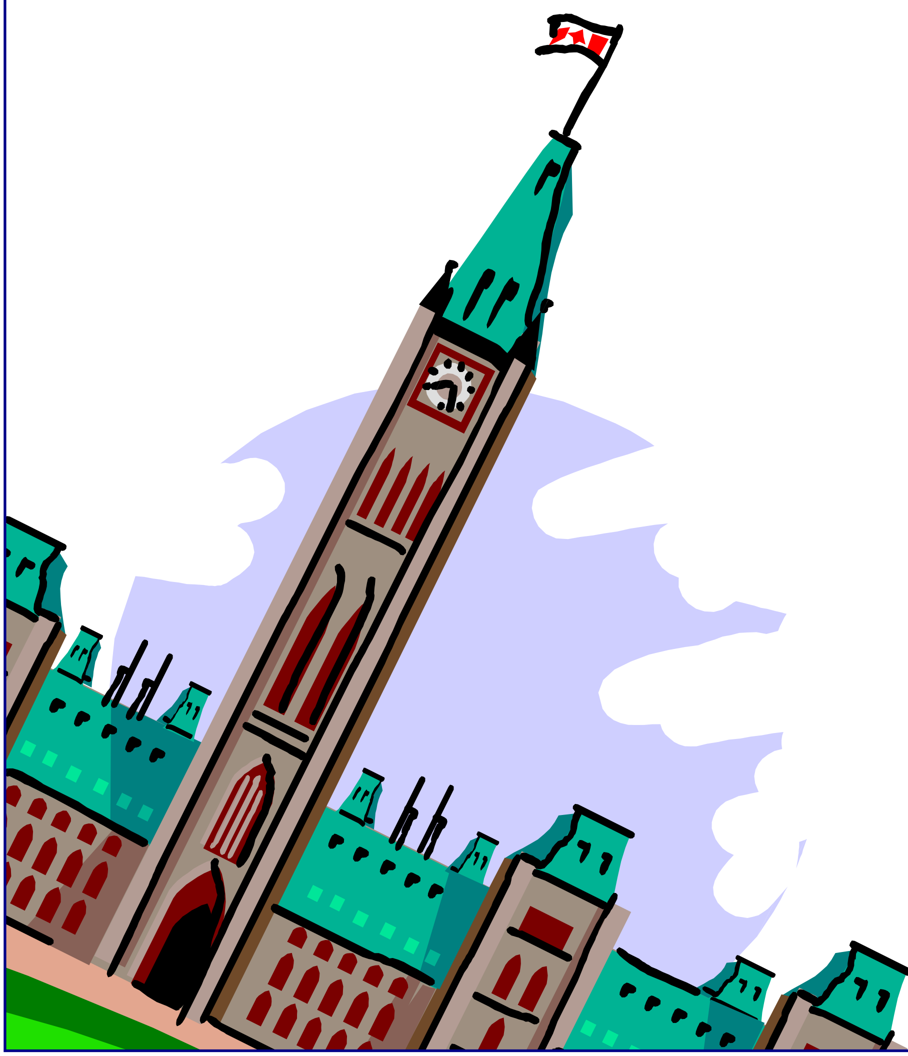
CANADIAN Taxpayers FEDERATION

Fighting for taxpayers

Tax Relief for All Canadians

2005-06 Pre-Budget Submission Before the
House of Commons Standing Committee on Finance

November 2004



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About the Canadian Taxpayers Federation

The Canadian Taxpayers Federation (CTF) is a federally incorporated, non-profit and non-partisan, advocacy organization dedicated to lower taxes, less waste and more accountable government. The CTF was founded in Saskatchewan in 1990 when the Association of Saskatchewan Taxpayers and the Resolution One Association of Alberta joined forces to create a national taxpayers organization. Today, the CTF has over 65,000 supporters nation-wide.

The CTF maintains a federal office in Ottawa and offices in the five provincial capitals of British Columbia, Alberta, Saskatchewan, Manitoba and Ontario. In addition, the CTF has a Centre for Aboriginal Policy Change in Calgary dedicated to monitor, research and provide alternatives to current aboriginal policy and court decisions. Provincial offices and the Centre conduct research and advocacy activities specific to their provinces or issues in addition to acting as regional organizers of Canada-wide initiatives.

CTF offices field hundreds of media interviews each month, hold press conferences and issue regular news releases, commentaries and publications to advocate the common interest of taxpayers. The CTF's flagship publication, *The Taxpayer* magazine, is published six times a year. An issues and action update called *TaxAction* is produced each month. CTF offices also send out weekly *Let's Talk Taxes* commentaries to more than 800 media outlets and personalities nationally.

CTF representatives speak at functions, make presentations to government, meet with politicians, and organize petition drives, events and campaigns to mobilize citizens to effect public policy change.

All CTF staff and board directors are prohibited from holding a membership in any political party. The CTF is independent of any institutional affiliations. Contributions to the CTF are not tax deductible.

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CANADIAN TAXPAYERS FEDERATION
PRE-BUDGET SUBMISSION

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Recommendations

1) **The federal government's fiscal strategy must be built on three pillars: (1) tax relief combined with fair and competitive taxation; (2) legislated debt reduction; and (3) controlling the growth of spending by redefining the role of government and ensuring program initiatives are warranted and achieving positive and measurable public policy outcomes.**

2) **The Basic Personal Exemption and Spousal Exemption should each be increased to $10,000 over two years and to $15,000 within five years, and subsequently remain indexed for inflation.**

3) **The federal government should introduce a per child tax credit or exemption rather than subsidize institutional day care.**

4) **The federal government should redress inequities in the payroll tax regime – such as employer overpayments – by harmonizing the employer Employment Insurance premiums with those of employees.**

5) **The federal government should institute a legislated debt retirement schedule with an annual payment of 5 per cent of total revenues collected.**

6) **The federal government should limit expenditure growth to a maximum annual amount of inflation and population growth combined.**

7) **The federal government should end all Corporate Welfare programs including TPC and those delivered by Regional Development Agencies. It should instead focus on reducing business taxes to promote economic competitiveness.**

8) **The federal government should adopt the Canadian Taxpayers Federation's *Municipal Roadway Trust* as the most expedient way to return gas tax revenues back to roads in Canadian cities – both large and small – thereby allowing municipalities to then reallocate existing roadway budgets to other infrastructure priorities.**

Introduction

A number of issues, primarily political but some economic, have emerged to make this year's pre-budget submission period unique. While the 2005/06 Budget presents an opportunity to improve the fortunes of Canadians, it also poses a legislative danger to the government:

- For the first time in a generation, no single political party in Parliament can command a majority. Canadians, in their wisdom, elected a minority government on June 28, 2004, and in doing so they denied any one party the ability to pass bills – including a budget – without first consulting with opposition members. While Prime Minister Paul Martin has the authority to govern, by dint of having the most seats in the House of Commons, he does not have a mandate to pass legislation freely.
- The last time a budget was tabled in a minority Parliament, not only was the government defeated in the House of Commons, but voters opted to change the government in the subsequent general election. This should serve as an additional reminder to government MPs, the Minister of Finance and the Prime Minister of the need to win multipartisan support and find a middle ground acceptable to Parliament and Canadians.
- Internationally, our rising dollar has put additional pressure on Canadian manufacturers who compete in foreign markets; and the re-election of President George W. Bush means the tax burden in the United States will continue to go down. The government of Canada will need to act if we hope to remain competitive with our largest trading partner.
- At home, public confidence in the federal government has deteriorated as a result of the sponsorship scandal, as reported by the Auditor General of Canada, and other spending and administrative scandals too numerous to outline here.
- On a positive note, the Canadian economy is healthy and the outlook is positive. Yet our high standard of living is falling behind other nations and our unemployment rate remains stuck at 7.1 per cent. We can do better, but improvements will only come with changes to Canada's regulatory and tax regime – something that is overdue.

In this minority Parliament, it is imperative for members of the House of Commons Standing Committee on Finance to underscore the importance of their work and recommendations with the Martin Administration. Because Canadians were not informed of the rising surplus prior to the last election, they were left out of the debate over how it should be used. Parliamentarians, therefore, have an important duty to ensure the wishes of taxpayers are reflected in the pre-budget process and the budget bill.

It is being increasingly acknowleddged that multi-year surpluses are the result of a structural level of over-taxation levied on Canadians by Ottawa. Finance Minister Ralph Goodale recently forecast the budgetary surplus will be $8.9-billon this year. Last month, he reported the 2003/04 surplus was $9.1-billion, and two years ago (2002/03) the surplus was $7-billion. Government spending restraint is not the cause of today's big surplus announcement – program spending has grown by 6 per cent a year since 2000. Rather, it is a structural over-taxation that has Ottawa swimming in cash. It exists because Ottawa continues to over-tax Canadians and will do so again this year, next year and in the years ahead.

Deeply troubling is the spending agenda undertaken by Mr. Martin and his refusal to reduce the taxes paid by Canadians and businesses, large and small. When the last budget was tabled, the government attempted to portray itself as fiscally responsible by telling Canadians it was holding program spending growth to 3.1 per cent in 2004/05. Yet the recent Economic and Fiscal Update revealed program spending will, in fact, grow by 6.5 per cent this year – more than a two-fold increase. Increasing spending at such a pace is simply not responsible or sustainable.

Meanwhile Canada's competitiveness is slipping. Our tax burden is the highest of the three North American Free Trade Agreement nations and our tax gap vis-à-vis the U.S. is growing. According to the Organization for Economic Co-operation and Development, the U.S. tax burden – calculated by measuring tax revenues as a percentage of gross domestic product (GDP) – dropped in 2003 from 26.4 per cent to 25.4 per cent whereas Canada's position was unchanged at 33.9 per cent. While Mexico's tax burden increased, it remained the lowest at 19.5 per cent.

For eight years, the Canadian Taxpayers Federation (CTF) has consistently advocated that the federal government build Canada's fiscal framework on three key pillars, and once again these proposals underpin the basis of our submission.

RECOMMENDATION #1

THE GOVERNMENT'S FISCAL STRATEGY MUST BE BUILT ON THREE PILLARS:

- **TAX RELIEF COMBINED WITH FAIR AND COMPETITIVE TAXATION;**
- **LEGISLATED DEBT REDUCTION; AND**
- **CONTROLLING THE GROWTH OF SPENDING BY REDEFINING THE ROLE OF GOVERNMENT AND ENSURING PROGRAM INITIATIVES ARE WARRANTED AND ACHIEVING POSITIVE AND MEASURABLE PUBLIC POLICY OUTCOMES.**

The CTF urges the government to heed the recommenadations in the pages that follow in the interest of Canada's short-term and long-term fiscal health.

Canadian Taxpayers Federation Supporter Survey

Each year, the CTF conducts a comprehensive national survey of its supporters. The CTF is a supporter-driven and supporter-financed organization, dedicated to lower taxes, less waste, and more accountable government. The recommendations contained in this pre-budget submission accurately reflect the priorities outlined by our supporters.

Canada's Economic Prospects

Economic forecasts prepared by major financial institutions show the prospects for the coming few years are positive. Over the next two years, our economy's growth rates will converge with those of the United States. The following chart illustrates three key measures of Canada's economy: GDP growth, inflation, and employment growth. Projections are based on the average of the most recent data from the following banks: RBC, BMO, Scotiabank, Laurentian Bank, and TD Economics.

Year	Real GDP Growth	CPI / Inflation	Employment Growth
2003	1.9%	2.8%	2.2%
2004 F	2.9%	1.8%	1.7%
2005 F	3.4%	2.0%	1.7%
2006 F	3.5%	1.4%	1.1%

Despite rising energy costs, prospects for inflation remain low, which should leave Canadians with less deterioration in their income over the next few years. Our economic fundamentals are good and this is reflected in growing government revenues. In 2005/06, Ottawa will collect $4.4-billion more than was predicted in last fall's budget update. And according to the TD Bank's forecasts, federal revenues will be up 23 per cent to $240-billion in 2009, while November's Economic and Fiscal Update puts revenue figures as high as $242-billion in that year.

Growing employment is another factor contributing to increased government tax revenues. Yet the trend is for slower employment growth over the next three years, and by 2006 overall employment will increase to 16.6 million. Since 1997, Canada's economy has added more than 2.2 million jobs (see chart below). Positive employment growth has allowed family incomes to rise along with family spending, which has contributed to increased federal personal income tax and Goods and Services Tax revenues.

Employment Growth 1997 to 2004

	1997	1998	1999	2000	2001	2002	2003	2004 Q
Canadian employment (thousands)	13,774	14,140	14,531	14,910	15,077	15,401	15,746	15,963
Cumulative growth in employment	n/a	2.7%	5.5%	8.2%	9.5%	11.8%	14.3%	15.9%

Q denotes the most recent quarterly employment results

Source: Statistics Canada

According to Statistics Canada, family income and spending grew substantially between 1997 and 2002. Average after-tax family incomes increased by 33 per cent to $60,500 in 2002. On the other side of the ledger, average family spending increased by 20 per cent, rising to $48,060. This is in sharp contrast to the period between 1990 and 1997 when incomes either fell or experienced no real increase. Between 1997 and 2002, Canada's 14 million families boosted GST revenues by $566-million. And over the same period, families increased total government tax revenues by an impressive $28-billion.

Federal Government Spending

Prime Minister Martin's government has increased spending this year by 6.5 per cent and plans to increase spending next year by another 5.7 per cent. Although these increases might appear modest, they remain out of line with population growth and inflation; and are not sustainable over the middle- and long-term. Canada's population will grow by 0.6 per cent this year and by the same amount the following year, whereas inflation is projected to be 1.6 per cent this year, and 2.0 per cent next year. The federal government's spending will exceed combined population and inflation growth, which totals 2.2 per cent this year and 2.4 per cent in 2005, by a magnitude of 70 per cent. This means the real size of the federal government is growing faster than is necessary to provide the same bundle of goods and services to Canadians. Regrettably, increased government spending has not been isolated to 2004.

Growth in Program Spending since Budget was Balanced in 1997/98

	1997-1998	1998-1999	1999-2000	2000-2001	2001-2002	2002-2003	2003-2004	2004-2005
Program spending ($-million)	106,864	109,995	109,583	118,694	125,018	133,593	141,355	150,488
Year-over-year growth	n/a	2.9%	-0.4%	8.3%	5.3%	6.9%	5.8%	6.5%
Cumulative growth	n/a	2.9%	2.5%	11.1%	17.0%	25.0%	32.3%	40.8%

Source: Fiscal Reference Tables 2004 and Budget 2004 – plus new spending initiatives

In the two years that followed balancing the books, the federal government kept program spending in check, but it has since risen rapidly. As of this year, the cumulative increase since 1997/98 is in excess of 40 per cent. When planned spending over the next five years is factored in, by 2009/10 spending will have increased by 75 per cent to $187-billion. If the government had budgeted more responsibly since 2001 and kept spending in line with population and inflation growth, program spending in 2009/10 would be a more modest $153-billion.

Over-Spending

It may be axiomatic that governments always tend toward over-spending. It is said that when confronted with growing costs, onetime minister-of-everything C. D. Howe quipped, "What's a million dollars?" To put that figure into perspective, it takes 183 average Canadian income taxpayers to get a million tax dollars. And if we update Mr. Howe's figure to reflect the times by asking how many taxpayers are required to bring in a billion dollars, we discover it takes a city with the population of St. John's. And what's $1-billion to the federal government? It is a mere one half of a percent of total federal government spending.

Size of Government

There is too little debate around the question of what is the right size of government. Very few Canadian opinion leaders see the need to control the rate of spending increases, while some believe government must continually expand and be all things to all people. Taxpayers know intuitively that any increase in the size of government will mean more money coming directly out of their pockets.

An important measure of government size is the number of employees it has on an annual basis. The following chart shows all federal government employment, by person – not in full-time-equivalents.

Growth in Federal Government Employment Since 1999

	1999	2000	2001	2002	2003 Q	2004 Q
Total employment (thousands)	421,519	429,019	437,822	447,743	456,187	458,213
Cumulative growth of employment	n/a	1.8%	3.9%	6.2%	8.2%	8.7%
Total wages ($-million)	19,472	22,822	22,201	23,265	23,907	n/a
Average wage	$46,195	$53,195	$50,708	$51,961	$52,406	n/a
Cumulative growth in average wages	n/a	15.2%	9.8%	12.5%	13.4%	n/a

Q denotes the most recent quarterly employment results

Source: Statistics Canada, Public Sector Employment

After reaching a low mark for government employment in 1999, Ottawa began to increase the number of federal employees from 2000 onwards. As of 2004, federal government employment was up 8.7 per cent over 1999 levels. Over the same period, growing government employment has also increased the cost of the payroll by more than $4.5-billion. And it is not simply a case of too many employees working in government. On average, government employees earn 20 per cent more than the average Canadian. Since 1999, government employees have enjoyed more than a 13 per cent increase in their average income. Indeed, average government employees are part of the 27 per cent of Canadian taxpayers who earn more than $50,000 per year.

Another popular measure of the size of government is relative to our economy. Between 1962 and 1997, Canadian governments spent more money than they could afford, piled up budgetary deficits, and increased the national debt from $14.8-billion to $562.9-billion. Since 1962, interest and service charges on the debt has cost taxpayers almost **$1-trillion**. This figure will continue to increase until the debt is eliminated.

If we examine program spending, less annual deficits, we find that over the last 40 years government program spending has accounted for an average 12 per cent of GDP. So today, when some say the size of government is too small relative to the size of the economy they are vastly overstating their case by neglecting to account for the presence of debts and deficits. It is inaccurate to compare today's balanced books with previous years of reckless deficit spending, without taking into account the size of those deficits.

Spending as a percentage of GDP is an interesting signpost, but not the best measurement when setting spending objectives. One thing is certain, between 1970 and 1976 program spending as a percentage of GDP exceeded 13 per cent in each of those years. Although Canada's monster deficits did not appear for another decade, the six year period in the early seventies of Big Government relative to our economy set the stage for ballooning debt in the 1980s and 1990s. Any move that would see federal government spending exceed 12 per cent of GDP is likely to produce similar results down the road.

When trying to determine the size of government, revenue is a better measurement. Once again if we discount revenues collected by the 18 per cent chewed up by interest servicing charges, between 1962 and 2003 revenues were on average 12 per cent of GDP. The figure dipped below the 12 per cent mark in the early 1990s and has exceeded 12 per cent every year since the budget was balanced – where it is projected to remain over the next two years.

Ottawa's Structural Over-Taxation of Canadians

Structural over-taxation occurs when a government consistently collects more revenues than it needs to meet its funding commitments. Given the previous thirty years of preoccupation with deficit spending, wrapping our minds around the notion that the federal government has too much money is a novel concept. In the last six years, government revenues have exceeded spending requirements by 5.7 per cent on average. This margin is well beyond a comfortable 2 per cent contingency reserve and means Ottawa is over-taxing Canadians.

The simplest and best remedy for structural over-taxation is broadly based tax cuts. Opting to target or gerrymander tax cuts is inherently unfair to those not fortunate enough to meet government criteria.

The level of taxes paid by Canadians and the resulting delivery of services – or lack thereof – continues to be an issue of great concern for CTF supporters. Indeed, it is this value for money proposition that continues to yield calls for greater tax relief, especially in light of the spate of scandals that have plagued the government over the past 24 months, from gun registry cost overruns to criminal investigations stemming from the sponsorship program.

The CTF commends the federal government for embarking on a five year tax reduction program beginning with the Febrary 2000 Budget, and strengthened by the October 2000 Budget Update. But today, the time for a new round of tax cuts is upon us.

The Positive Impact of the 2000-2004 Tax Cuts

In 2000, then-Finance Minister Paul Martin rolled out the largest tax cut in Canadian history. Government MPs distort the actual size of this tax reduction plan as a $100.5-billion tax cut. In actual fact, $20.7-billion of this amount included the ending of bracket creep, which did not lower taxes, but simply indexed brackets to inflation; and a $28-billion hike in Canada Pension Plan premiums is also not included. In addition, almost $6-billion in Canada Child Tax Benefit payments are incorrectly identified as tax relief, instead of being classified as a government expenditure. The real five year tax cut, once fully implemented by the end of 2004, amounts to $46-billion. While welcome news to taxpayers, it is a far cry from the $100-billion "as advertised."

Today, a Canadian earning $55,000 is taxed $1,396 less. This is a substantial improvement, and it should be noted that reducing taxes has "cost" the federal treasury in foregone revenue far less than estimated. Because of the stimulative effects of lower taxes, between 2000 and 2004, Ottawa's revenues declined not by $100-billion or even $46-billion, but by only $18-billion. In fact, total revenues today are $4-billion *higher* than they were in 2000; and government revenues today – after cutting taxes – are higher today than what Ottawa had estimated they would be *had taxes <u>not</u> been reduced*. (Before accounting for the foregone revenue resulting from the tax reductions between 2000 and 2004, total revenues for 2004/05 were predicted to be $193-billion in the 2000 Economic and Fiscal Update. Yet in the 2004 Economic and Fiscal Update it was reported revenues will be $194-billion this year.)

If we look at Canada's economic performance between 2000 and 2004, the virtues of lower taxes become all the more apparent. The following chart compares five measures of Canada's economic growth relative to other advanced economies.

Select Measures of Economic Growth 1999 to 2004

	1999-2000	2000-2001	2001-2002	2002-2003	2003-2004	2004-2005	Cumulative
Real GDP growth							
Advanced economies	3.5%	3.9%	1.2%	1.6%	2.1%	3.6%	12.4%
Canada	5.5%	5.2%	1.8%	3.4%	2.0%	2.9%	15.3%
Growth in consumer spending							
Advanced economies	4.0%	3.7%	2.3%	2.3%	2.1%	2.7%	13.1%
Canada	3.8%	4.0%	2.7%	3.4%	3.1%	3.2%	16.4%
Growth in fixed asset formation							
Advanced economies	5.5%	5.3%	-0.9%	-2.0%	2.5%	5.7%	10.6%
Canada	7.3%	4.7%	4.1%	2.4%	4.9%	6.0%	22.1%
Growth in employment							
Advanced economies	1.4%	2.1%	0.7%	0.3%	0.6%	0.9%	4.6%
Canada	2.8%	2.6%	1.1%	2.2%	2.2%	1.8%	9.9%
Growth in per capita GDP							
Advanced economies	2.9%	3.3%	0.6%	1.0%	1.6%	3.1%	9.6%
Canada	4.7%	4.3%	0.7%	2.3%	1.1%	2.2%	10.6%

Source: OECD World Economic Outlook, September 2004

The conclusion: Canada's economy outpaced the growth of other advanced economies in the world throughout the government's five year tax reduction plan. Reducing taxes helped grow the economy, fuel job creation, and put money into the pockets of hardworking Canadians.

But looking ahead we are beginning to stall vis-à-vis our competitors – making the need for further tax relief measures to sustain our economic growth all the more necessary. According to the Organization for Economic Co-operation and Development, our personal income tax burden remains amongst the highest of the G-7 nations. In fact, this standing has not changed in almost a decade. According to the Fraser Institute, taxation by Canadian governments at all levels accounts for 48.8 per cent of total household income (Tax Freedom Day, 2004).

Our overall tax burden is still far too high, saps productivity, deters wealth creation, and remains a visible competitive disadvantage for us versus the United States. The question that logically follows is, how do we rectify this situation?

Principles of Taxation

- The tax system should be simple. Government accountability is enhanced when citizens understand their tax system. Complexity is the adversary of accountability.
- The tax burden should be low, since dollars multiply more rapidly in private hands than in government pockets. High tax rates retard wealth creation by discouraging risk-taking, saving, and investment.
- The tax system should be flatter. This is important because simplicity is enhanced with fewer tax brackets. As long as the government retains a generous basic personal exemption the tax system will remain fair.
- The purpose of the tax system should be to calculate and collect taxes in the fairest, lowest and most efficient way possible for the operations of government.
- The tax system should generate revenues necessary to cover the cost of essential government programs and services, no more, no less.
- The tax system should not be used as an instrument of social policy, designed as a means to political ends. Taxes are a vehicle for raising revenues.
- The tax system should promote economic prosperity and enhance Canada's competitive position internationally.
- A tax system that is simple, low, flat and fair will:
    1. Promote the incentive to work, save and invest.
    2. Increase disposable incomes and reduce personal debt levels.
    3. Generate better economic prosperity for all citizens.

Personal Income Taxes

2004 CTF Supporter Survey Questionnaire

Question: If federal taxes were to be cut, which ONE tax would you give the highest priority to reducing?

	2004	2003
Personal income tax	41 %	42 %
GST & sales taxes	32 %	32 %
Gas taxes	13 %	8 %
Payroll taxes & levies	6 %	6 %
Business / corporate income tax	5 %	5 %
Customs & excise taxes	1 %	1 %
Undecided / no answer	3 %	7 %

Personal income tax relief has consistently remained a top priority for CTF supporters over the past six years. In response, a concerted focus was placed on advocacy efforts to re-index the tax system to inflation – thereby ending bracket creep – combined with an equal effort to call for lower rates of taxation across all income tax brackets.

While progress has occurred in reducing income taxes, much work remains to be done. Reliance on federal income taxes as a percentage of total revenues remains too great. Moreover, the modesty of federal income tax relief becomes self-evident when federal income taxes are expressed as a percent of GDP.

Fiscal Year	Personal Income Taxes (PIT) $-million	Total Federal Revenues Collected $-million	PIT as % of Federal Revenues	Annual GDP $-million	Federal PIT as % of GDP
1993-1994	50.0	116.0	43.1%	724.2	6.9%
1994-1994	55.3	122.5	45.2%	767.2	7.2%
1995-1996	58.8	131.4	44.8%	806.8	7.3%
1996-1997	62.6	140.9	44.4%	838.7	7.5%
1997-1998	69.6	152.1	45.8%	884.6	7.9%
1998-1999	72.2	156.1	46.2%	914.7	7.9%
1999-2000	79.1	166.1	47.6%	982.1	8.1%
2000-2001	85.9	182.7	47.0%	1,075.3	8.0%
2001-2002	79.5	171.7	46.3%	1,107.1	7.2%
2002-2003	81.7	177.8	45.9%	1,154.6	7.1%
2003-2004	84.9	186.2	45.6%	1,214.2	7.0%
2004-2005	89.3	194.0	46.0%	1,289.5	6.9%
2005-2006	95.1	199.9	47.5%	1,357.8	7.0%
2006-2007	101.6	209.7	48.5%	1,425.7	7.1%
2007-2008	108.7	220.3	49.3%	1,492.7	7.3%
2008-2009	116.3	231.2	50.3%	1,562.9	7.4%
2009-2010	124.1	242.3	51.2%	1,636.4	7.6%

* 1997-1998 to 2003-2004 figures taken from Fiscal Reference Tables, October 2004
* 2004-2005 to 2009-2010 figures taken from Economic and Fiscal Update, November 16, 2004

The Basic Personal Exemption & Spousal Exemption

A new opportunity to provide Canadians with broad-based tax relief has arrived: It is time to dramatically raise both the basic personal exemption (BPE) – which is the amount an individual earns before paying federal income taxes or, to be technical, the exemption that is multiplied by the lowest tax rate of 16 per cent to yield a non-refundable tax credit – and the spousal exemption, which stand at $8,012 and $6,784 respectively, to $15,000 over the next five years.

While the BPE has been indexed to inflation since 2000, it is far below the amount it would have been if it were indexed to inflation since 1986. If the BPE were indexed for inflation since the imposition of the income tax in 1917, it would now exceed $20,000. Higher BPEs are provided for in the provincial tax regimes in Alberta, British Columbia and Saskatchewan.

A low BPE and spousal exemption means Ottawa taxes people even at the bottom of the income scale. Why should the BPE be set at $15,000? It is approximately the amount earned in a year by a minimum wage worker. It is worth asking why government taxes people struggling to make ends meet or just entering the workforce, particularly when much of the tax paid by these workers is recycled back to them in the form of GST refundable credits, Canada Child Tax Benefit payments and other income-based benefit schemes. It would be far better if people were permitted to keep more of their hard-earned money to provide for themselves and their families, free of meddling bureaucrats.

By setting both the BPE and spousal exemption at $15,000, individuals earning $15,000 or less and families with incomes below $30,000 will no longer pay any federal income tax. All other taxpayers will save $1,100 a year; and the tax bill of a dual-income family will fall by $2,200 and that of single-income families by $2,400.

Raising the spousal exemption to match the basic personal exemption will correct a current bias against single income families and improve tax fairness. Our tax system penalizes any family that opts to have one member stay at home. Without dwelling on the clear downgrading of work in the home that this implies, it is particularly unfair to those low-income families struggling to make ends meet as it can push parents into the workforce when they have a young family at home who needs them.

Raising the BPE and spousal exemption over a five year period will result in foregone revenues of $4.5-billion next year, and rise to $28.5-billion in 2009. Such a change will remove 1.8 million Canadians from the tax rolls and also benefit the remaining 13.8 million taxpayers.

Over 82 per cent of Canada's 22.3 million tax filers earn $50,000 or less and 97 per cent make less than $100,000. It is worth repeating that raising the BPE is a tax cut for all Canadians, albeit one that provides the greatest benefits to low- and middle-income earners. And spread over five years, it is relatively effortless for Ottawa to allocate the rising surplus and government savings to raise the two exemptions. And if a selection of tax credits were phased out over five years, the actual cost could be much lower. Assuming 1/5 of the GST credits and Age Credits were eliminated, then the foregone revenue would be less. However, if the actual cost to government in lost revenues matched the pattern set with the 2000 tax cuts, then lost revenue would again be lower than anticipated.

RECOMMENDATION #2

THE BASIC PERSONAL EXEMPTION AND SPOUSAL EXEMPTION SHOULD EACH BE:

- **INCREASED TO $10,000 OVER TWO YEARS AND TO $15,000 WITHIN FIVE YEARS (ACCORDING TO THE FOLLOWING SCHEDULE), AND SUBSEQUENTLY REMAIN INDEXED TO INFLATION.**

2005	**$ 9,000**
2006	**$ 10,000**
2007	**$ 11,500**
2008	**$ 13,000**
2009	**$ 15,000**

Adopting the above schedule would be fair to all taxpayers by providing tax relief across all income brackets. Efforts to help Canadian families would be achieved by providing sustained tax relief for low-income parents as opposed to fostering government dependency on income redistribution efforts. This CTF proposal has received editorial acclaim in the ***Vancouver Sun, Montreal Gazette,*** and ***Calgary Sun***.

A Wrongheaded Approach to Child Care

The Speech from the Throne announced the federal government's intention to implement a national child care program. The centrepiece of this strategy is likely to include a national version of Quebec's so-called $7.00 per day child care system.

Yet the Quebec program is not the success story told by its proponents. The provincial government has reformed the costly system by raising co-payments from $5/day to $7/day. When the program was introduced in 1997, Quebecers were told it would cost $250-million to administer each year. In 2002, it cost $1.2-billion. Moreover, it has many of the same problems Canadians have come to associate with Canada's health care system: Waiting lists that vary from community to community; a one-size approach to raising children; and rising demand for a program politicians say is "free." Most damning is the program bias towards warehousing children rather than providing families the option of raising children at home with a parent.

A better approach to enhancing child care for all Canadian families would be to offer a child tax deduction. Public policy bias on this issue must be neutral as it is parents who are best able to decide what type of child care arrangement most suits their family. For families with children there is no question child care and development are important and costly propositions. But it is not the role of government to create one system – institutionalized care – that penalizes another – namely helping a parent remain at home. Rather than reward or encourage the use of child care outside of the household for some, Canadians families should have the option to decide for themselves how best to raise their children.

RECOMMENDATION #3

THE FEDERAL GOVERNMENT SHOULD INTRODUCE A PER CHILD TAX CREDIT OR EXEMPTION RATHER THAN SUBSIDIZE INSTITUTIONAL DAY CARE.

Payroll Taxes

Despite government claims to the contrary, the total payroll tax burden faced by Canadian workers, as indicated below, and employers continues to rise.

Payroll Taxes Paid by a $41,000 Employee (1996-2005)

Calendar Year	EI Rate per $100 of Earnings	Total EI Taxes Paid	CPP Rate per $100 of Earnings	Total CPP Taxes Paid	Total Payroll Taxes Paid
1996	2.95 %	$ 1,150.50	2.80 %	$ 893.20	**$ 2,043.70**
1997	2.90 %	1,131.00	3.00 %	969.00	**2,100.00**
1998	2.70 %	1,053.00	3.20 %	1,068.80	**2,121.80**
1999	2.55 %	994.50	3.50 %	1,186.50	**2,181.00**
2000	2.40 %	936.00	3.90 %	1,329.90	**2,265.90**
2001	2.25 %	877.50	4.30 %	1,496.40	**2,373.90**
2002	2.20 %	858.00	4.70 %	1,673.20	**2,532.20**
2003	2.10 %	819.00	4.95 %	1,801.80	**2,620.80**
2004	1.98 %	772.20	4.95 %	1,831.50	**2,603.70**
2005*	1.95 %	752.70	4.95 %	1,881.64	**2,634.34**

* Denotes anticipated reduction in EI premium in 2005

Compared to 10 years ago, Canadian workers now pay $590.64 more in combined payroll taxes while employers have been burdened with an extra $442.44 during this same period.

As infuriating as high payroll taxes are, the most insidious aspect of the payroll tax burden is the estimated $750-million in annual overpayments of Canada Pension Plan (CPP) and Employment Insurance (EI) premiums now paid by employers to the federal government.

As Canadian Press (January 26, 2001) reported:

> The overpayments occur because the government collects the contributions on the first $39,000 of income and, for many people, that amount is reached in less than a full year. It is not uncommon, for instance, for an employee to notice their paycheque has suddenly increased in June or July when the maximum is reached. If an employee changes jobs after they have contributed the maximum, or if their company is merged or sold to become a new legal entity, they must start paying the premiums all over again. So must the employers, who are required to match their employees' contributions to CPP on a dollar per dollar basis and pay $1.40 for every dollar contributed to EI.

RECOMMENDATION #4

THE FEDERAL GOVERNMENT SHOULD REDRESS INEQUITIES IN THE PAYROLL TAX REGINE – SUCH AS EMPLOYER OVERPAYMENTS – BY HARMONIZING THE EMPLOYER EMPLOYMENT INSURANCE PREMIUMS WITH THOSE OF EMPLOYEES.

Eliminating the National Debt

The $61.4-billion of debt paid down over the last seven years is a bright spot in the federal government's finances. The Prime Minister has set a goal of reducing our debt-to-GDP ratio to 25 per cent within ten years. Although to some this seems a big undertaking, it is easily attainable without a change in current policy. If the economy grows at a nominal rate of less than 4 per cent per year and the government simply applied its contingency reserves against the debt at year's end, the target will be met.

The federal government must go further however, by shifting from its record of debt elimination by accident to debt elimination by design. It can do this by retaining the practice of budgeting a contingency reserve and continuing to direct all annual surpluses to debt repayment. In addition, Ottawa should add a mandated debt repayment line-item in each budget. The CTF first advocated such a policy in 1997, one year ahead of the budget being balanced. Today, we recommend a phased-in line item worth 5 per cent of revenues, which would begin next year at 1 per cent of revenues. That would guarantee a debt repayment of $2-billion next year, rising to $11-billion in 2010/11. In addition to this measure, the federal government must also begin the sale and divestiture of Crown assets. These sales, along with recent sale of Ottawa's stake in Petro-Canada, must be used entirely to reduce the federal government's debt. These assets were acquired in times of budget deficits and therefore they ought to be used to bring down the debt. This measure would reduce the debt by an average of $705-million in each of the next five years.

Proposed Debt Elimination Measures (2005 – 2010)

($-million)	2005-2006	2006-2007	2007-2008	2008-2009	2009-2010	2010-2011
Debt retirement schedule	2,004	4,130	6,400	8,847	11,362	11,883
Sale of Crown assets (debt elimination)	705	705	705	705	705	705
Net Debt Elimination:	2,709	4,835	7,105	9,552	12,067	12,588

Source: CTF calculations based on TD Economics' revenue forecasts

With debt interest payments still consuming $37.6-billion or almost 18 cents of each tax dollar – the federal government's single largest expenditure – debt retirement must remain a top priority. To abdicate responsibility for reducing Canada's $501.5-billion debt is to continue the fiscal crime of intergenerational tax evasion against future generations of taxpayers.

Not only will debt elimination ensure future generations are not saddled paying for yesterday's program expenditures, debt elimination also increases available resources. By reducing the national debt by $61-billion, the federal government will save approximately $4.0-billion this year on debt interest payments it is no longer required to make.

RECOMMENDATION #5

THE FEDERAL GOVERNMENT SHOULD INSTITUTE A LEGISLATED DEBT RETIRMEMENT SCHEDULE WITH AN ANNUAL PAYMENT OF 5 PER CENT OF TOTAL REVENUES COLLECTED.

Growth in Federal Expenditures

It is important to note the government's record of surplus budgets is largely the result of robust economic growth in Canada's two "have" provinces – Alberta and Ontario – and from the continued over-taxation of Canadian workers and employers through the EI surplus which now estimated at $46-billion given the notional surplus which exists in the EI Account.

While expenditures were reduced in the 1995 budget to address Canada's fiscal crisis, the growth of program spending since the federal books were balanced in 1998 has continued unabated, as the chart below demonstrates.

Fiscal Year *	Total Revenues $-billion	Program Spending $-billion	Year over Year Percentage Change	Spending Percentage Change since 1997/98	Cumulative Spending Increase since 1997/98 $-billion
1997-1998	152.1	106.9	n/a	n/a	n/a
1998-1999	156.1	110.0	2.9%	2.9%	3.1
1999-2000	166.1	109.6	-0.4%	2.5%	2.7
2000-2001	182.7	118.7	8.3%	11.1%	11.8
2001-2002	171.7	125.0	5.3%	17.0%	18.2
2002-2003	177.8	133.6	6.9%	25.0%	26.7
2003-2004	186.2	141.4	5.8%	32.3%	34.5
2004-2005	194.0	150.5	6.5%	40.8%	43.6
2005-2006	199.9	159.1	5.7%	48.8%	52.2
2006-2007	209.7	166.8	4.9%	56.1%	60.0
2007-2008	220.3	173.9	4.2%	62.7%	67.0
2008-2009	231.2	180.2	3.6%	68.6%	73.3
2009-2010	242.3	186.7	3.6%	74.7%	79.9

*1997-1998 to 2003-2004 figures taken from Fiscal Reference Tables, October 2004
* 2004-2005 to 2009-2010 figures taken from Economic and Fiscal Update, November 16, 2004

From 1997/98 through to 2005/06, federal spending is projected to increase by $52-billion, which represents a 49 per cent spending increase over eight years. This is **almost double** the combined rate of inflation and population growth over this same period. As a consequence, the number of federal public servants on the public payroll is also increasing and the reduction trends of the mid-1990s are now a distant memory.

RECOMMENDATION #6

THE FEDERAL GOVERNMENT SHOULD LIMIT EXPENDITURE GROWTH TO A MAXIMUM ANNUAL AMOUNT OF INFLATION AND POPULATION GROWTH COMBINED.

Corporate Welfare – Failed 19th Century Industrial Policy

Despite overwhelming international evidence pointing to the folly of industrial subsidies, the federal government continues its economically destructive policy of picking market winners and losers through a variety of direct industrial assistance and regional development schemes principally under the auspices of Industry Canada and Human Resources Development Canada.

In six successive reports analyzing over $50-billion in government assistance to industry – using data obtained through *Access to Information* – over the past six-years the CTF has found:

- Some $2.15-billion distributed through the Defence Industry Productivity Program was distributed in grants, contributions and loans between 1970 and 1995 with less than 20 per cent repaid;

- Almost 50 per cent of $11.2-billion in assistance distributed by Industry Canada from 1982 to 1997 was earmarked for 75 of Canada's largest and most profitable corporations;

- The Atlantic Canada Opportunities Agency (ACOA) wrote off an astounding 34 per cent ($200-million) of its $591-million loan portfolio between 1990 and 1999;

- Western Economic Diversification recouped a paltry 3.4 per cent of its $134-million conditionally repayable loan portfolio between 1987 and 2000; and

- Technology Partnerships Canada (TPC) – the government's flagship industrial assistance program – has collected less than 3 per cent of $1.6-billion in loan agreements signed since 1996. TPC officials have forecast their **best case** repayment scenario as less than one-third ($2.13-billion) of a planned $6.4-billion in loans through to the year 2020.

The CTF has consistently maintained that lowering personal and business taxation levels and fostering an internationally competitive regulatory framework – facilitated by adopting an aggressive anti-subsidy stance at the WTO and other multilateral organizations – are two of the key elements needed to promote economic growth and raising the real incomes of citizens.

The CTF has long opposed business subsidies and corporate welfare, as they are inherently unfair and make for bad public policy. By phasing out such programs over five years, spending reductions of $500-million to $4-billion could be realized.

RECOMMENDATION #7

THE FEDERAL GOVERNMENT SHOULD END ALL CORPORATE WELFARE PROGRAMS INCLUDING TPC AND THOSE DELIVERED BY REGIONAL DEVELOPMENT AGENCIES. IT SHOULD INSTEAD FOCUS ON REDUCING BUSINESS TAXES TO PROMOTE ECONOMIC COMPETITIVENESS.

Gas Taxes for Cities – The *Municipal Roadway Trust*

The future of Canada's urban regions – large and small – has become a topical public policy issue for all orders of government; federal, provincial and municipal. According to Statistics Canada, 80 per cent of Canadians live in cities of 10,000 people or more and over 60 per cent of Canadians live in Canada's six largest metropolitan areas.

Current economic competitiveness literature points to cities as the generators of economic growth in the 21st century. Canadian municipal leaders have raised valid concerns with respect to their ability to compete on the world stage vis-à-vis their

American, European and Asian counterparts. One key area where Canadian cities fall behind their competitor urban regions is in the construction and maintenance of modern infrastructure (roads, transit, airports, etc.).

Last year the federal government collected $5.3-billion in gas and excise tax revenues but only returned a paltry 2.5 per cent or $135-million in the form of transfers for provincial roadway development.

Even if all infrastructure funding mechanisms are added in, since 1994 the federal government has returned less than 10 per cent of its tax haul at the pumps to Canada's cities.

In its 6th annual Gas Tax Honesty Day report (May 20, 2003), the CTF again proposed a ***Municipal Roadway Trust*** program (first advocated in 2002) that would devote $2.2-billion of gas tax revenues – 50 per cent of total collections – annually for three years to municipalities to draw upon for roadway expenditures. This would allow cities to redirect portions of their current "works" budgets to other priorities such as transit and waterworks initiatives.

Accountability would be maintained with annual reports from municipalities, verifiable by the Auditor General of Canada. This model, endorsed by the ***National Post***, provides immediate cash for urban regions and provides federal accountability for federal tax dollars. Annual oversight, and penalties if appropriate, would ensure that municipal governments build real infrastructure instead of the recent abuses experienced in tri-partite infrastructure programs – bocce ball courts, canoe museums and riverfront fountains, for example.

Year 1 – Gas Tax Distributions to Major Municipalities

City	Halifax	Montreal	Ottawa	Toronto	Winnipeg	Regina	Calgary	Edmonton	Vancouver	Victoria
Percentage of federal GDP	0.9%	8.9%	3.2%	15.6%	1.9%	0.6%	3.6%	3.2%	5.5%	0.8%
Portion of ½ federal fuel tax ($-million)	18.3	223.8	78.4	383.1	44.8	13.5	103.3	91.0	135.1	18.9

RECOMMENDATION #8

THE FEDERAL GOVERNMENT SHOULD ADOPT THE CTF'S *MUNICIPAL ROADWAY TRUST* AS THE MOST EXPEDIENT WAY TO RETURN GAS TAX REVENUES BACK TO ROADS IN CANADIAN CITIES – BOTH LARGE AND SMALL – THEREBY ALLOWING MUNICIPALITIES TO THEN REALLOCATE EXISTING ROADWAY BUDGETS TO OTHER INFRASTRUCTURE PRIORITIES.

Conclusion – Fiscal Impacts

Implementing these eight recommendations will ensure that the federal government pursues a responsible and sustainable fiscal strategy.

With strong leadership, the recommendations contained in this submission can be implemented within the current fiscal framework and allow the government to reduce taxes and plan for annual contingency reserves of $3-billion.

Underlying Balance of Government Initiatives and CTF Recommendations

($-million)	2005-2006	2006-2007	2007-2008	2008-2009	2009-2010	2010-2011
Revenue	197,604	206,103	214,168	222,562	230,441	240,876
Program Spending	160,628	166,801	172,639	178,383	183,873	190,974
Debt Charges	35,887	35,083	34,436	33,418	31,960	30,040
Total Spending	196,515	201,884	207,075	211,801	215,833	221,014
Surplus	1,089	4,219	7,093	10,762	14,608	19,863
Net Federal Debt	490,257	481,210	466,986	446,617	419,781	387,170

Source: Public Accounts, Budget Documents, Conference Board Estimates, TD Economics Estimates and CTF calculations

The combined impact of reduced taxation and spending, along with reallocation of more resources to debt elimination, will allow the federal government to continue to deliver surpluses in the coming years. The exercise of streamlining government will help to greatly improve existing and new policy initiatives. Over the last few years, Canadians have witnessed numerous examples of government waste. If the Martin Administration is serious about making the federal government less wasteful and more accountable, these savings will help that process. At the same time, they will enable the federal government to reduce its over-taxation of Canadians by delivering broadly based tax relief in the upcoming budget.

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