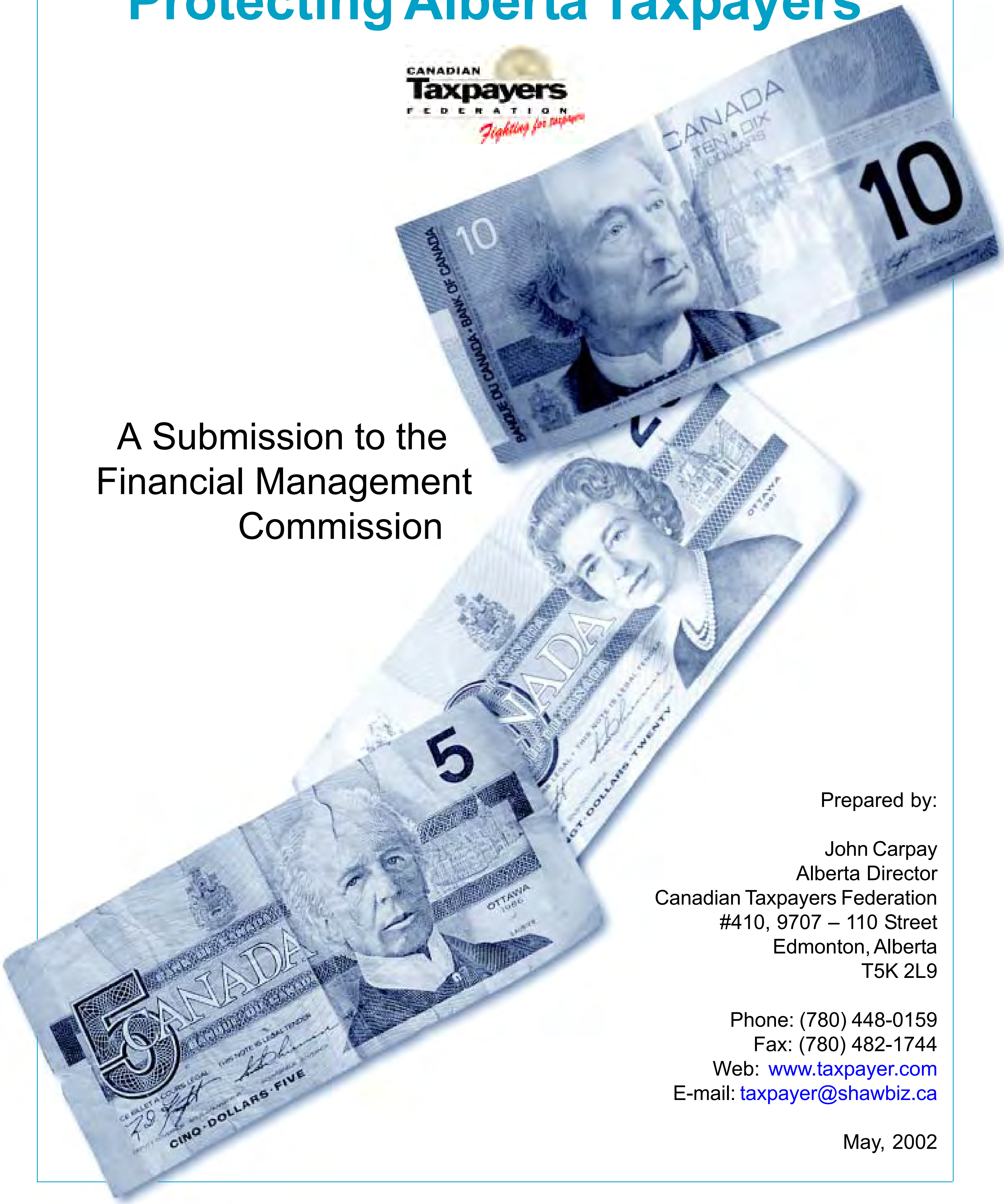
Protecting Alberta Taxpayers

CANADIAN Taxpayers FEDERATION
Fighting for taxpayers



A Submission to the Financial Management Commission

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May, 2002

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Executive Summary

- Alberta has a proud record of achievement since 1993: Canada's lowest provincial taxes, Canada's lowest debt-to-GDP ratio, and Canada's lowest unemployment rate.

- Alberta's success is the result of the *Deficit Elimination Act, Balanced Budget and Debt Retirement Act,* and now the *Fiscal Responsibility Act*. Legislation has empowered politicians to say "no" to the insatiable demands of groups and individuals who lobby aggressively, continuously and persistently for more spending.

- In spite of the *Fiscal Responsibility Act*, program spending is up 45% from just six years ago, in contrast to 12% population growth and 13% inflation. If program spending since 1996 had risen to keep pace with inflation and population growth, Alberta would be completely debt free today in 2002.

- The clearly stated preferences of Albertans for tax cuts over spending increases, expressed in two large-scale surveys in 1998 and 2000, have been ignored. The *Fiscal Responsibility Act* does not protect Albertans from roller coaster budgeting or from tax increases. It does not force legislators to prioritize spending, or to justify proposed tax increases.

- A law limiting the growth in government spending to the rate of inflation plus population growth has protected taxpayers in the state of Washington since 1995. Amending Alberta's *Fiscal Responsibility Act* to limit growth in program spending to inflation plus population growth would end roller coaster budgeting. It would empower elected representatives to prioritize spending and to resist pressure from special interest groups.

- The Heritage Fund should be built up so as to eliminate Alberta's personal income tax. If one half of oil and gas royalties are put into the Heritage Fund, and if growth in program spending is limited to inflation and population growth, income from the Heritage Fund will be able to replace what government takes from Albertans in personal income tax.

- A minister who exceeds his budget should lose a portion of his salary, as is done in B.C. with it *Balanced Budget and Ministerial Accountability Act*.

- The *Alberta Taxpayer Protection Act* should be amended to require a referendum on any and all proposed tax increases. The onus should be on politicians to justify a tax increase. Taxpayers should not have to justify why they are entitled to keep more of their own hard-earned money. In the same way, the *Municipal Government Act* should be amended to protect taxpayers from municipal tax increases.

Alberta's proud record of achievement

In spite of the tax increases introduced in Budget 2002-03, Alberta still remains the lowest-taxed province in Canada. It is no coincidence that the province with Canada's lowest tax burden also has Canada's lowest unemployment rate.

Adjusting for inflation and population growth, and excluding oil and gas royalties from the equation, Albertans in 2002 are paying less provincial tax, per person, than in 1992 or in 1997.

The Alberta government can take credit for having introduced a single rate of income tax, which was recommended by the Canadian Taxpayers Federation in the spring of 1998. Corporate income tax rates have also been reduced, which benefits all Albertans as consumers, employees and shareholders.

Alberta ranked first in the Fraser Institute's 2001 *Budget Performance Index*. In the sub-indexes for "Tax Rates and Revenue" and "Debt and Deficit," Alberta ranked ahead of the other nine provinces and the federal government.

According to the November 2001 report of the *Dominion Bond Rating Service* ("The Wind has Turned"), Alberta has the lowest debt-to-GDP ratio in Canada at 2.2%, down from 30.1% in 1993-94. By way of comparison, the province with the second-lowest debt-to-GDP ratio was British Columbia, where the ratio had steadily *increased* to 23.4%. Federally the ratio was 50.3%.

In 1994-95, Albertans paid $1.746 billion in debt servicing costs: $645 per capita. At $585 million in 2002-03, debt servicing costs today are $187 per capita. In real terms, this is only *one fourth* of what per capita debt servicing costs were eight years ago.

Legislation: the secret to Alberta's success

Since 1993, legislation has made it easier for MLAs and Ministers to resist pressure from the many groups, organizations and individuals who lobby aggressively and persistently for more spending. The *Deficit Elimination Act*, the *Balanced Budget and Debt Retirement Act*, and now the *Fiscal Responsibility Act* have empowered politicians to say "no" to spending demands which are virtually unlimited.

Critics of Alberta's existing spending control legislation have pointed out that it interferes with the political discretion of elected representatives. The critics are correct. That's the whole point. The balanced budget requirement and the debt repayment requirement of the *Fiscal Responsibility Act* "interfere" with the government's fiscal choices, and so they should. This kind of "interference" protects taxpayers.

In a perfect world, legislators would resist spending pressures and keep the budget balanced *without legislation*. In a perfect world, legislators would put three quarters of a surplus towards debt repayment *without legislation*. But in the real world, legislators need the help of legislation to say "no" to the special interest groups who lobby continuously for more spending.

Alberta's fiscal success is the result of legislation requiring the budget to be balanced, legislation requiring 75% of a surplus to go to debt repayment, and legislation establishing a timetable for debt elimination.

In the *Fiscal Responsibility Act*, Alberta has a solid legislative foundation on which to build.

Spending growth outpaces population growth and inflation

In spite of the *Fiscal Responsibility Act*, Alberta in 2001-02 spent more per person on government programs than any other province in Canada. In the Fraser Institute's 2001 *Budget Performance Index*, Alberta actually ranked *behind* the federal government, Ontario, B.C., Quebec, Nova Scotia, New Brunswick, and Newfoundland in the Spending Sub-Index.

2001-02 Government Program Spending (excluding debt servicing costs)

Province	2001-02 budget (in $ millions)	population (in millions)	per person spending
Aberta	19,998	3.064	$6,527
Prince Edward Island	861	0.139	$6,194
British Columbia	24,839	4.096	$6,064
Quebec	43,506	7.411	$5,870
New Brunswick	4,302	0.757	$5,683
Saskatchewan	5,748	1.016	$5,657
Newfoundland	3,008	0.534	$5,633
Manitoba	6,389	1.150	$5,556
Nova Scotia	4,418	0.943	$4,685
Ontario	54,156	11.874	$4,561
Total/Average	167,225	30.984	$5,397

Source: Provincial Budget Documents, 2001-02, and Statistics Canada for population figures
Source for Alberta government program spending: Alberta Finance, Third Quarter Fiscal Update

Alberta government program spending has gone up 45% in the past six years, from $12.768 billion in 1996-97 to $18.571 billion in 2002-03. In contrast, Alberta's population grew 12% and Alberta's Consumer Price Index rose 13%.

Albertans prefer tax cuts to spending increases

In response to the Alberta government's "Talk it up, Talk it out" survey in 1998, Albertans attributed the highest importance to paying down debt (74.8%), followed by reducing taxes (61.4%). Increasing priority spending ranked third (56.1%), followed by increasing savings in the Heritage Fund (19.2%).

In response to the Alberta government's "It's Your Money" survey in 2000, Albertans attributed the highest importance to tax cuts (73%), with more spending on programs a distant second (44%). Regarding the use of so-called one-time revenues, spending ranked *third* behind one-time tax rebates and savings.

Politicians often complain that voters want lower taxes *and* more spending on programs. If questions about lower taxes and more program spending are asked separately, it should come as no surprise that most people want both. What is significant about "Talk it up, Talk it out" and "It's your money" is that Albertans were expressly asked to *choose priorities* as between tax cuts, increased spending, debt repayment, and saving for the future. The preference of Albertans for tax cuts over spending increases, expressed in these surveys, is significant because Albertans were not asked about tax cuts in isolation from other priorities.

As indicated above, program spending is up 45%, compared to 12% population growth and 13% inflation.

If the opinions of the tens of thousands of Albertans who completed these surveys are to be taken seriously, the right balance between debt repayment, tax cuts and spending increases has *not* been struck.

In spite of the *Fiscal Responsibility Act*, the tax cuts enjoyed by Albertans have been *small* when compared to the massive increases in spending. The fiscal preferences of Albertans have been substantially ignored, in spite of the Fiscal Responsibility Act.

Why Alberta's "roller coaster" budgeting hurts taxpayers

Per capita program spending (in 2002 constant dollars) went from a high of $8,611 (first budget under Premier Don Getty) to a low of $5,311 (1996-97) to another high of $6,651 (2001-02) and now down again to $5,941 (2002-03).

This "roller coaster" budgeting is bad for taxpayers, because short-term and long-term planning is difficult (if not impossible) in the absence of steady, reliable funding. Funding instability does not promote prudent spending decisions.

If an individual earns $45,000 one year, $60,000 the next, and $30,000 the year after that, it will be difficult for him to make prudent decisions about spending, saving and investing. The same principle applies to government programs. This is especially true for transportation and infrastructure. When necessary repairs and maintenance are neglected, fixing the problem costs taxpayers far more in the long run.

The *Fiscal Responsibility Act* has not, and cannot, put an end to Alberta's "roller coaster" budgeting.

Alberta could have been debt-free already

If spending on government programs since 1996 had risen steadily each year with inflation and population growth, Alberta would be debt-free today. Taxpayers would have paid billions of dollars *less* in debt servicing costs. Taxpayers today would be keeping more of their hard-earned money, enjoying the freedom of choosing how to save, spend, invest or give to charity as they see fit.

Year	Program Spending Per person (constant 2001 $)	Population (millions)	Total annual savings (in $ millions) if spending control legislation had been implemented in 1996
1996-97	$5,212	2.781	0
1997-98	$5,455	2.837	$689
1998-99	$5,465	2.907	$735
1999-00	$5,954	2.959	$2,196
2000-01	$6,250	2.997	$3,111
2001-02	$6,527	3.064	$4,029

Total spending reductions from 1996-97 to 2000-01: $10,760 million
Alberta's accumulated debt at March 31, 2002: $ 6,015 million

As the chart above shows, if legislation had limited growth in government spending to inflation and population increases, Alberta could have committed an additional $10.76 billion towards debt repayment in the years 1996-97 through to 2001-02. This is more than the $6.015 billion remaining debt as of March 31, 2002.

A failure to focus on priorities

A spending increase of 45% (in contrast to 13% inflation and 12% population growth) reflects a failure to prioritize spending on what is most important.

The Alberta government should ask the following questions about every government ministry, program, and project: is it really necessary for government to perform this task? Is it impossible for individuals, families, charities, faith-based groups, other voluntary associations, and the private sector to accomplish the goal? Is this program or project so important that it justifies taking money away from a young family? Only when the answers to these three questions are "yes," "yes," and "yes" should the government take money from the taxpayers who have earned it.

Spending on government programs should be subject to "sunset" laws, by which the program automatically expires after five years (or a shorter or longer time period as may be appropriate). As the program approaches its legislated expiry, MLAs should measure the program's results, ask the same three questions listed above, and then vote to renew, alter, replace or discontinue the program.

The *Fiscal Responsibility Act* does not require the government to ask these questions, or force legislators to focus spending on priorities. The door is always open to spending increases which far outpace inflation and population growth. This results in tax increases, as was demonstrated by Budget 2002-03.

Further, the *Fiscal Responsibility Act* does not ensure that Alberta keeps its advantage over other jurisdictions. This, too, was demonstrated by the failure of Budget 2002-03 to proceed fully with scheduled cuts to corporate income tax. In a global economy, in which technology enables businesses to relocate more easily than ever before, it is important for Alberta to keep its Advantage, not only in relation to other provinces, but in relation to jurisdictions around the world.

A summary of the shortcomings of the *Fiscal Responsibility Act*

The *Fiscal Responsibility Act* has not prevented a 45% increase in spending on government programs, far in excess of inflation and population growth. *The Fiscal Responsibility Act* did not prevent Alberta from spending more per person on government programs in 2001-02 than any province in Canada. The *Fiscal Responsibility Act* did not protect Alberta taxpayers from the tax increases introduced in Budget 2002-03, in spite of an unequivocal pre-election promise that the only way taxes would go was "down."

The *Fiscal Responsibility Act* did not facilitate or enable Alberta to proceed fully with scheduled cuts to corporate income tax, thereby diminishing its advantage.

When projected revenues from oil and gas exceed their historic average, the *Fiscal Responsibility Act* does not prevent government from taking the portion which exceeds the historic average and budgeting it for spending rather than for debt repayment and tax cuts.

The *Fiscal Responsibility Act* allows the clearly expressed fiscal preferences of Albertans for tax cuts over spending increases to be ignored. The agendas of spending advocates continue to be imposed on the majority of Albertans who prefer to keep more of their own hard-earned money.

The *Fiscal Responsibility Act* has not given Alberta the debt freedom which it could have achieved already, if program spending since 1996 had increased only to keep pace with inflation and population growth.

The *Fiscal Responsibility Act* does not protect Alberta taxpayers from the ills of "roller coaster" budgeting.

The *Fiscal Responsibility Act* does not force legislators to focus spending on priorities. Rather, it allows spending to increase at a rate far in excess of inflation and population growth. The *Fiscal Responsibility Act* does not protect taxpayers from tax increases or from the spending increases which cause them.

The solution: spending control legislation

The shortcomings of the *Fiscal Responsibility Act* can be remedied by amending this legislation to limit the annual growth in spending on government programs to Alberta's annual inflation and annual population growth.

Currently, the *Fiscal Responsibility Act* already imposes spending limits on legislators by banning deficits, establishing a schedule for debt repayment, and requiring three quarters of a surplus to go towards debt repayment. These existing spending limits empower legislators to say "no" to spending demands which are inevitably unlimited. Current spending limits also have the effect of dampening the enthusiasm of spending advocates, because special interest groups already know ahead of time that the budget must be balanced, that debt must be repaid, and that three quarters of the surplus must go towards debt repayment.

The challenge is to build on the spending limits which the *Fiscal Responsibility Act* already provides, and to improve this legislation for the benefit and protection of Alberta taxpayers.

Spending control legislation works in Washington state

Chapter 43.135 of the *Revised Code of Washington* imposes a state expenditure limit on the General Fund, into which sales, business, property and other taxes are placed for state expenditures. This law indexes the maximum growth in government spending to a "fiscal growth factor" based on inflation and population growth. Since 1995, this law has allowed Washington taxpayers to keep billions of dollars more of their own hard-earned money.

The fiscal growth factor is applied to the previous state expenditure limit, and is used to set a new state expenditure limit for the upcoming budget. The fiscal growth factor also applies to fees and licences, unless the Legislature specifically votes for a larger increase.

The state expenditure limit may be exceeded upon declaration of an emergency for a period up to one budget cycle (twenty-four months) by a law approved by a two-thirds vote of each house of the Legislature and signed by the governor. The law must set forth the nature of the emergency. The definition of "emergency" is limited to natural disasters that require immediate government action to alleviate human suffering and provide humanitarian assistance. Any additional taxes imposed to deal with the emergency stay in place only until thirty days after the next general election, unless an extension is approved at that general election.

Revenues received in excess of the state expenditure limit are deposited into an Emergency Reserve Fund. Deposits are made at the end of each fiscal quarter, based on projected revenues and expenses. The Legislature may appropriate moneys from the Emergency Reserve Fund only with approval of at least two-thirds of the members of each house of the Legislature.

Source: Washington state web site at http://www.ofm.wa.gov

The benefits of spending control legislation for Alberta

Spending control legislation would put an end to the problems created by roller coaster` budgeting. Infrastructure, transportation, and other important programs would receive adequate, stable and reliable funding.

Spending control legislation would end the trend of the past six years towards larger government. MLAs and Ministers would be further empowered to resist pressure from special interest groups to increase spending at a rate faster than inflation and population growth.

Spending control legislation would force each ministry – and the Alberta government as a whole – to prioritize spending rather than look to taxpayers for more money.

Currently, planning the annual budget is made more difficult by the fact that there is little certainty as to how much money will be spent on programs the following year. Due to the fact that program spending can increase at a rate faster than inflation and population growth, there is little if any pressure to prioritize spending. <u>There is no legislated spending limit, therefore the door is always open to go after taxpayers for more of their money</u>.

In contrast, when everyone knows in advance how large (approximately) next year's budget will be, budget planning and spending decisions will be more prudent. When the players in the budget process (MLAs, Ministers, individuals and groups advocating more spending) know that spending increases are limited to inflation and population growth, they will be forced to choose priorities. Legislators will not be tempted to look to taxpayers for more money to finance an ever-growing government, because the door to this temptation will be closed and locked.

Spending control legislation will work in the same way that the *Deficit Elimination Act*, *Balanced Budget and Debt Retirement Act,* and *Fiscal Responsibility Act* have worked: by imposing limits which protect taxpayers.

Spending control legislation will ensure that Albertans' clearly expressed preferences for tax cuts over spending increases will be implemented rather than ignored. It will accelerate Alberta's progress towards debt freedom. It will protect Albertans from tax increases such as those imposed in Budget 2002-03. It will preserve the Alberta Advantage.

Ultimately, spending control legislation will allow Albertans to keep more of their own hard-earned money. This will ensure that Alberta's high rate of economic growth and job creation is sustained. Of even greater importance, spending control legislation will create room in the private, non-profit and voluntary sectors to empower voluntary associations: families, community groups, faith-based groups, and charities. This in turn will lead to a better and stronger civil society.

Use the Heritage Fund to eliminate personal income tax

In February of 2001 the Canadian Taxpayers Federation released a commissioned study which sets forth Alberta's potential for income tax freedom by 2015. Dr. Jean-Francois Wen of the University of Calgary Economics Department shows how the Heritage Fund can be built up with oil and gas revenues until it becomes large enough to provide a steady, reliable source of revenue to replace what the government takes from Albertans in personal income tax.

The goal of eliminating personal income tax cannot be achieved without spending control legislation. As a further example of the need for spending control legislation, after the massive spending increases in Budget 2001-02, the date for Alberta's income tax freedom had to be pushed back ten years, to 2025.

The study's target date for income tax elimination is based on historic averages for oil prices, and increases in government spending that keep pace with, but do not exceed, population growth and inflation. Available from www.taxpayer.com/studies/Alberta and from the CTF's Edmonton office, the study demonstrates that eliminating provincial income tax is both desirable and possible. But achieving goals requires setting goals. In the same way that Alberta has established a timetable for complete debt freedom, spending control legislation can incorporate a timetable for achieving freedom from income tax.

Impose financial penalties on ministers who exceed their budgets

British Columbia's *Balanced Budget and Ministerial Accountability Act* promotes accountability by penalizing cabinet ministers if their ministries go over the spending limit set out in the budget. This *Act* imposes a 20% reduction on the $39,000 cabinet portion of a minister's salary ($45,000 for the Premier). The MLA portion of a minister's salary is not affected by this legislation. One half of this amount (20% of $39,000 or $45,000) is restored if the government's bottom line result meets or beats the deficit target for the year. The other half is restored to individual ministers if the actual spending in their ministry (including other appropriations under their responsibility) is less than or equal to the target set out in the main *Estimates* for that year.

Alberta should pass similar legislation. In light of the Alberta government's tendency to spend more than what was budgeted for (the 2001-02 fiscal year is an exception), the current practice of positive encouragement obviously isn't working. A minister who fails to keep her or his department's spending within the limit set out in the Annual Budget should have her or his salary reduced accordingly.

In the absence of real consequences, there is no accountability.

Strengthen the *Alberta Taxpayer Protection Act*

The *Alberta Taxpayer Protection Act* requires only that a referendum be held prior to the introduction of a provincial sales tax. All other new taxes and tax increases can be imposed without any restriction or restraint – even when this blatantly violates an unequivocal election promise.

Why limit this legislation to a general provincial sales tax? As taxpayers are the people who foot the bills, should they not be consulted on any and all tax increases?

Taxpayer protection legislation in Washington state requires voter approval for any tax increases or new taxes. This applies to expanding the base for a tax, or increasing the rate of any and all taxes, including sales and use taxes, property taxes, business and occupation taxes, and fuel taxes.

Section 10(1) of Manitoba's *Balanced Budget, Debt Repayment and Taxpayer Protection Act* provides that "the government shall not present to the Legislative Assembly a bill to increase the rate of any tax … unless the government first puts the question of the advisability of proceeding with such a bill to the voters of Manitoba in a referendum, and a majority of the persons who vote in the referendum authorize the government to proceed with the changes."

Section 10(2) dispenses with the referendum requirement where changes to federal tax laws affect provincial revenues and where a proposed change is designed to restructure the tax burden and does not result in an increase in revenue.

If drafted as it has been in Manitoba, taxpayer protection legislation will never stand in the way of reforming and improving the tax system – as long as the changes do not result in a tax increase.

The recent increase in health care premiums – which are a tax no different from personal income tax, corporate income tax, taxes on liquor, tobacco, fuel and hotel rooms, etc. – should have been put to Albertans in a referendum. A referendum protects taxpayers from those who lobby aggressively, persistently and continually for more spending. A referendum forces politicians to justify why taxpayers ought to relinquish more of their hard-earned money. A referendum places the onus on politicians to demonstrate that they have cut not only wasteful spending, but spending in low priority areas. A referendum forces politicians to ask the three tough questions referred to above ("**A failure to focus on priorities**").

The *Alberta Taxpayer Protection Act* should be amended to require the consent of Alberta taxpayers in a province-wide referendum for any tax *increase*, regardless of its form.

Put taxpayer protection into the *Municipal Government Act*

In the same way at the municipal level, citizens should also have the right to veto tax hikes and new program spending with a petition signed by two thirds of the affected ratepayers. Municipal tax increases, spending on major capital projects, and significant borrowing should go to a municipal referendum for taxpayer approval. The government should amend Alberta's *Municipal Government Act* accordingly.