Brief to House of Commons Finance Committee

Re: Study of Income Inequality in Canada
from: Dennis Howlett, Canadians for Tax Fairness

Use the tax system to help reduce poverty and inequality

The tax system is a key tool for redistributing wealth. Closing the gap between rich and poor is not only a moral and ethical imperative, it is also critical to restoring a healthy balance to a market-based economy. The market does not work very well to send signals on what should be produced if there is not some correlation between the effective demand of the members of society and their need to ensure that their basic needs are met. At the same time when wealth becomes so concentrated in the hands of a few, there is weak consumer demand with disastrous consequences in terms of jobs and economic growth.

Canada is growing more unequal. Social and economic disparities threaten democracy itself as those with the most wealth are able to influence political decision-making, and do so to protect and strengthen their own interests. The wealthiest, who can afford to pay a fair share of our public service costs, enjoy a tax system skewed in their favour.

A more progressive tax system can help to narrow the growing gap between rich and poor and boost the economy by stimulating consumer spending by middle and lower income Canadians. Higher tax rates on higher income brackets should be restored.

But restoring higher income tax rates for higher incomes alone will not ensure the rich pay a fairer share. Most very rich people don't pay anything close to the highest marginal rate on their income because they find all kinds of ways – both legal and illegal- to avoid paying taxes.

One of the most unfair things about our tax system is that income from investments is taxed at a much lower rate. And the really rich get most of their income from investments. Over 2/3 of the capital gains exemptions goes to tax filers making over $100,000 a year. This cost the government over $11 billion in 2007.

Governments need to adopt the principle articulated by the Carter Commission on taxation 50 years ago that, “a buck is a buck,” regardless of how you earn it.

Tax breaks that disproportionately benefit the rich, such as the very high limit on RRSP contributions, and the Stock Option Deduction need to be curtailed. The Stock Option

Deduction, for example, saw 90% of the benefit going to the less than 1% of tax filers with incomes of over $250,000.

Canada is one of the few countries that does not have an inheritance or estate tax. This means that wealth is passed on from generation to generation and gets more and more concentrated in the hands of a few. It is proposed that this tax be only applied only to amounts in excess of $5 million. This means that inheritances of cottages or other property that has been held in the family for decades would not be affected. Family farms would also be able to be passed on to following generations without facing a tax penalty.

The Alternative Federal Budget 2012 estimates this could raise $1.5 billion a year.

The tax system can help to take away an unfair share of resources from the rich, but it can also be used to give some of these resources to support the poor.

The tax and transfer system has worked to moderate the growing gap between rich and poor. Between 1981 and 2010, the market income inequality as measured by the Gini coefficient increased by 19.4 per cent. But this was partially offset by transfers and taxes so that after transfers and tax are taken into account inequality increased by only 13.5 per cent. It is still a high number, but it could have been much worse.

But our tax and transfer system could be doing a much better job. According to a recent study by the Centre for the Study of Living Standards, "If Canada's redistributive effort were to be raised to the OECD average, nearly two thirds of the increase in after-tax inequality that has take place in Canada since 1981 would be eliminated. Equally, if the level of redistributive effort that was in place in Canada in 1994, the year where redistribution was greatest, had still been in place in 2010, one half of the rise in after-tax inequality between 1981 and 2010 would be reduced. Canada thus has much room to increase its redistributive effort. What is needed is political will."[1]

The Canadian tax system has had several programs that have been very successful in helping to reduce poverty. For children there are the Canadian Child Tax Benefit and National Benefit Supplement and Child Disability Benefit. In many provinces and territories the federal and provincial/territorial efforts have been combined in the National Child Benefit to which the Federal Government has contributed just over $10 billion a year. Currently the maximum annual benefit is $3,485 for first child to families with net incomes below $24,183 in 2011. The National Child Benefit is a universal program that provides a benefit even to those families who have incomes below the level

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Centre for the Study of Living Standards, **The Impact of Redistribution on Income Inequality in Canada and the Provinces**, 1981-2010, September 2012. http://www.csls.ca/reports/csls2012-08.pdf where they have to pay taxes. It delivers more support to families that need more help but almost 90% of families with children get some portion of the benefit.

The National Child Benefit has been largely responsible for reducing the incidence of low income among families with children from 17.6% when it was introduced in 1998 to 10.5% in 2005. Child poverty could practically be eliminated if this benefit were increased to a maximum of $5,400 per child. This would cost just over $5 billion. This may seem like a lot but it could be partly offset by eliminating the Universal Child Care Benefit which costs about $2.5 billion a year.

The Working Income Tax Benefit is a program introduced in 2007 and improved in 2009 that provides a supplement to the working poor to offset the loss of benefits that results from going off social assistance and the increased costs associated with working such as transit. It is a refundable tax credit that provides up to about $1000 a year for single persons and about $1750 per couple depending on the province they live in and slightly more for those with a disability. Although it has helped to provide a positive incentive for people to move off welfare and into the workforce, it does not do enough to help working poor families who have never been on social assistance. The maximum benefits should be raised 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. Raising minimum wages so that a single person working full time would have an above the poverty line income is an important complementary measure that would not require any government expenditure and could actually increase tax revenue.

The Old Age Security and Guaranteed Income Supplement has helped to greatly reduce seniors' poverty in Canada to less than 5%. Instead of cutting back on these successful programs, benefits should be increased with the goal of eliminating poverty among seniors all together. Strengthening public pension and improving the Old Age Security/Guaranteed Income Supplement programs is becoming more important now as more and more Canadians workers are reaching retirement age finding without robust company pensions or private RRSP savings to rely on. Less than 40% of Canadians are now covered by workplace pensions and employers have been reducing the level of benefits. Only 30% of Canadians who are eligible to do so contribute to RRSP savings and many of those that have retirement savings have seen them shrink as a result of the global economic recession in 2008.[2]

A small part of the $29 billion the government now spends in tax breaks for RRSPs and company pensions which mainly benefits wealthier Canadians, which is greater than the total cost of the OAS, could be used to increase the OAS/GIS benefit for single

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Monica Townson, CCPA Policy Brief: A Stronger Foundation, Pension Reform and Old Age Security, November 2009.

seniors to at least the poverty line and keep the retirement age at 65. These government programs could be complemented by improvements to the Canada Pension Plan to strengthen our old age security system. A doubling of the replacement rate from 25% of covered earnings to 50% of average adjusted pensionable earnings as suggested by the Canadian Labour Congress could be achieved by a modest increase in employee and employer contributions, without any additional cost to the government.

We are pleased that the Finance Committee has undertaken this study on an important issue that affects our economic performance as well as social well being. We trust you will be able to make some strong recommendations for government action, particularly on how the tax system could contribute to reducing the income gap.