Why Alberta Needs a Sales Tax

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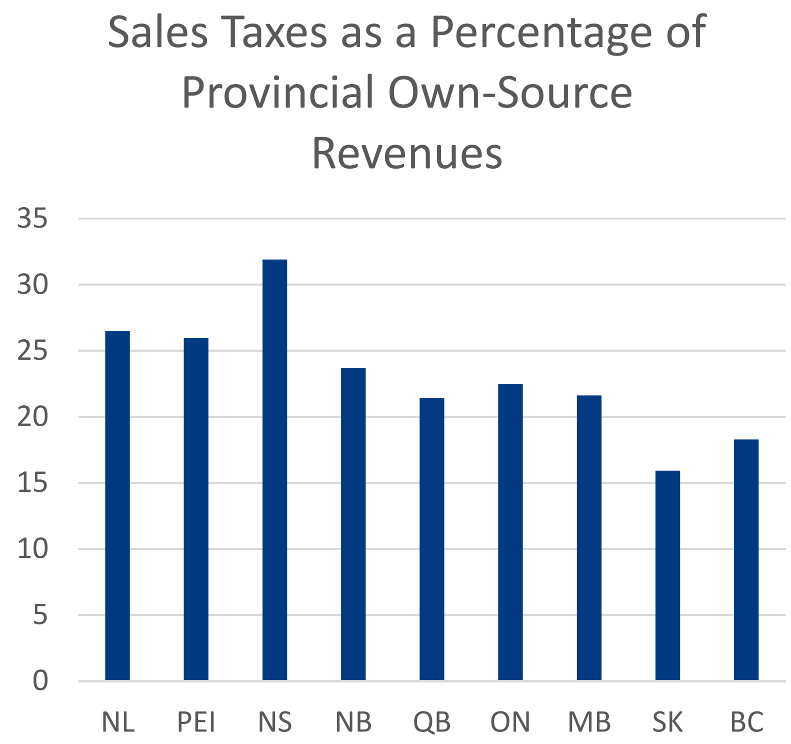
ALBERTA NEEDS A SALES TAX

- To change the tax mix to increase consumption taxation and reduce taxes on income-generating activities.
  - Increase incentives to work, save, and invest resulting in faster economic growth and higher living standards for Albertans.
- To address the province's fiscal problem of excessive reliance on volatile resource revenues, and unsustainable deficits.
  - Some combination of revenue increases and expenditure restraints will be necessary to address the province's deficit-debt problem.

PROVINCIAL SALES

- Alberta is the only province that does not levy a sales tax.
- In the other provinces, sales taxes have provided on average 23 percent of their own-source revenues.
- In Alberta, non-renewable resource revenues have provided 28.6 percent of own-source revenues.
- Alberta has largely used its non-renewable resource revenues to avoid levying a sales tax.



WHY ADOPT A SALES TAX?

- Non-renewable resource revenues are volatile and may decline over time because of resource depletion, technological change, and environmental concerns.
- General sales taxes, especially value-added sales taxes such as the GST, are ***less costly*** sources of tax revenue than personal or corporate income taxes.
- The impact of a sales tax on low income individuals and families can be offset through refundable tax credits.

ECONOMIC COST OF TAXATION

- Taxes reduce incentives to work, save, invest, and undertake risky projects and innovations.
- The loss of private sector income-generating opportunities as a result of taxation is the economic cost of taxation, in addition to the administration and compliance costs in collecting taxes.
- The marginal cost of public funds (MCF) is the economic loss incurred in raising an additional dollar of tax revenue from a particular tax.

THE MARGINAL COST OF PUBLIC FUNDS FOR MAJOR PROVINCIAL TAXES

	Corporate Income Tax	Personal Income Tax	Provincial Sales Tax
BC	5.69	3.88	---
AB	4.72	1.77	
SK	***	2.32	1.53
MB	4.70	2.42	1.41
ON	5.29	6.77	---
QB	3.46	3.05	1.69
NB	***	2.51	1.59
PEI	***	2.41	2.44
NS	***	3.09	1.62
NL	***	3.81	1.82

Note: *** indicates that a tax rate increase would reduce the long-run total tax revenues. --- indicates that the MCF could not be computed because the own semi-elasticity could not be estimated. Source: Dahlby and Ferede (forthcoming).

THE MARGINAL COST OF PUBLIC FUNDS

- Raising tax revenues through corporate income taxes is the highest cost source of tax revenues (except in Ontario).
- SK, NB, NS, PEI, and NL are on the “wrong side” of the Laffer curves for corporate income tax revenues.
- Provincial sales taxes are the lowest cost source of tax revenues for the provincial governments (except in PEI).
- There is an economic gain in shifting the tax mix away from corporate income taxes and raising an equivalent amount of revenue from a sales tax increase.

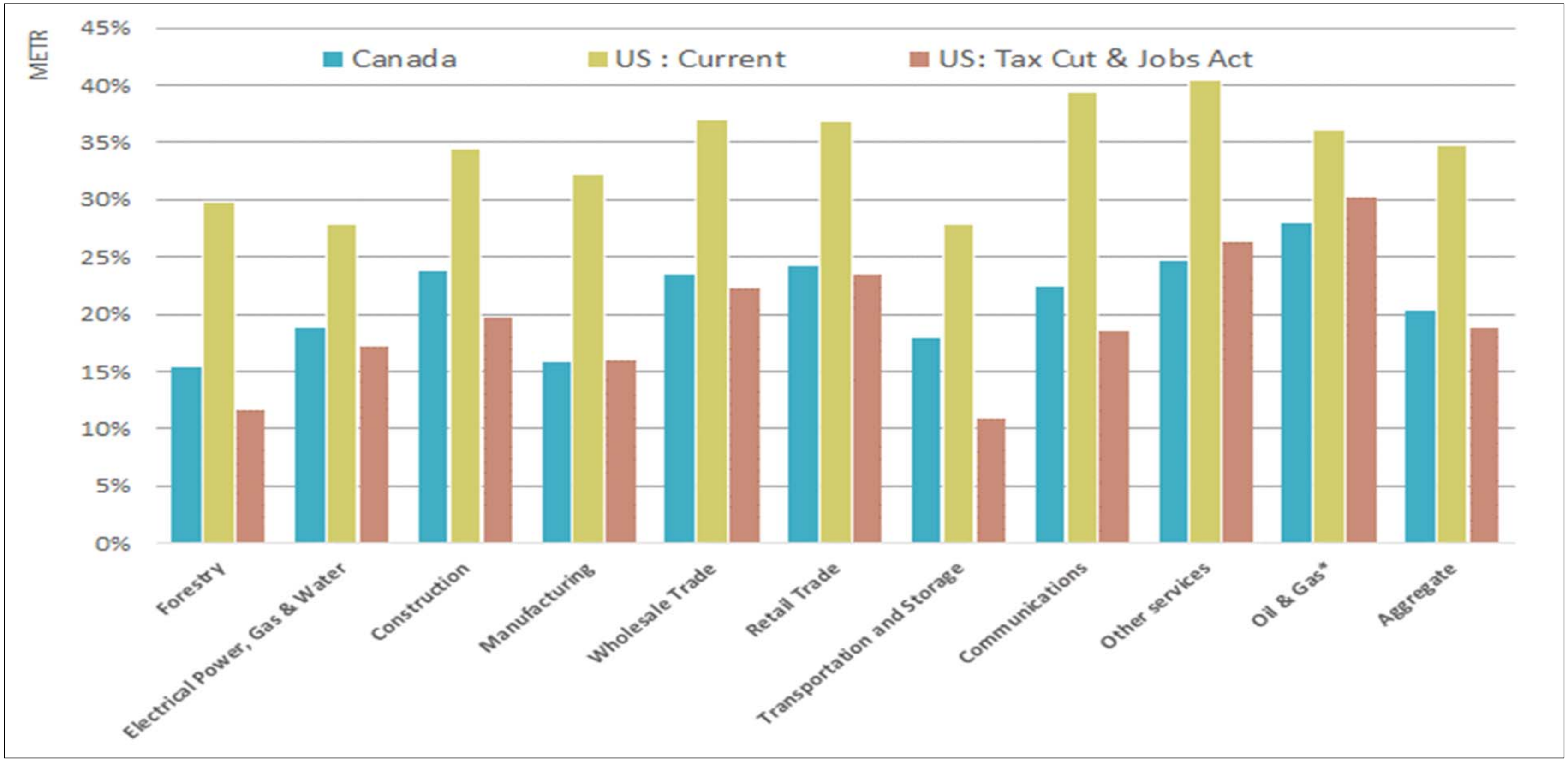
THE GAINS FROM SHIFTING THE TAX MIX FROM CIT TO AN HST

- Ferede and Dahlby (2012) fund that a one percentage point reduction in the provincial corporate marginal tax rate is associated with a 0.34 percentage point increase in the ratio of private investment to GDP and 0.1 to 0.2 percentage point increase in a province's annual growth rate.
- A reduction in the corporate tax rate by increasing investment in machinery and equipment would increase in labour productivity, resulting in higher wages and salaries for Alberta workers.
- McKenzie and Ferede (2017) found that a $1 reduction in provincial corporate income taxation would increase wages and salaries by between $1.52 in Alberta to $3.85 in Prince Edward Island.

US TAX REFORM

- The need to improve the competitiveness of our tax system is now more urgent with the US tax reforms that have lowered the US statutory tax rate to 21 percent and introduced other measures to lower the marginal effective tax rate on investment in the US.
- The lower statutory tax rate and restrictions on interest deduction in the US will increase incentives for US multinationals to shift profits to the US through transfer pricing and to increase interest deductions in the countries where they operate through borrowing by subsidiaries.

EFFECTS OF US TAX CUTS ON MARGINAL EFFECTIVE TAX RATES ON INVESTMENT (METR)



Source: Bazel, Mintz and Thompson (forthcoming).

CONSUMPTION TAX

- Our current tax system is a hybrid of income and consumption taxation because of the tax treatment of savings (RRSPs, TFSAs) and tax treatment of housing and other consumer durables. Sales tax is just another form of consumption taxation.
- The impact of a sales tax on low income individuals and families can be offset through refundable tax credits.

IS A SALES TAX FAIR?

- Most desire a progressive tax system that imposes a higher rate on those with a higher *standard of living*.
- Consumption is a better measure of an individual's standard of living than current income.
- Consumption out of inherited wealth, or offshore income not reported to tax authorities, is subject to sales taxes, but not income taxes.
- Under an income tax, individuals, such as hockey players, who earn large amounts of income early in their careers pay more than those with a steady (but equivalent in present value terms) earnings.
- Increased reliance on sales taxation can shift some of the burden to older generations who have benefited from previous periods of buoyant economic growth.

ADDRESSING THE PROVINCE’S FISCAL GAP

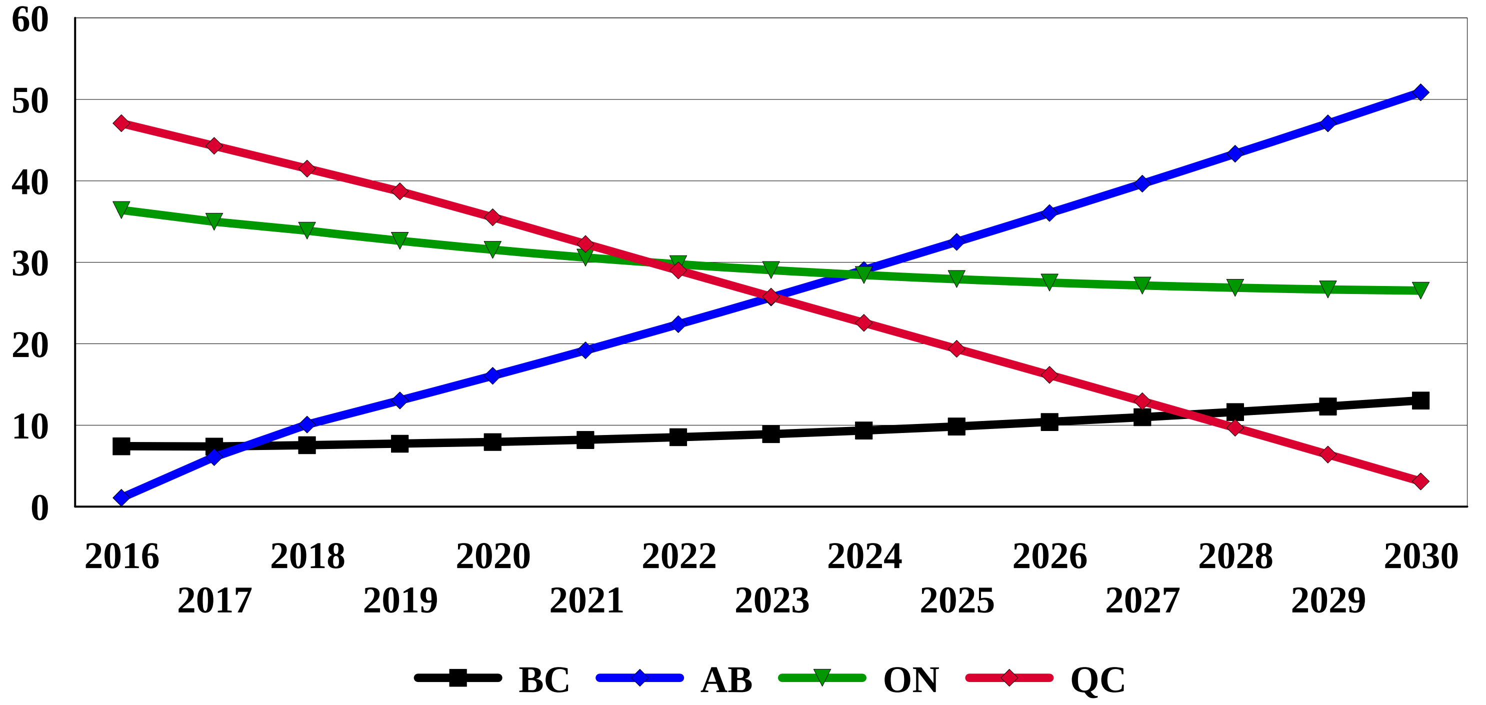
- In 2017-18, the budgetary deficit is forecast to be $10.3 billion and the province’s net debt will increase by $12.8 billion.
- The Parliamentary Budget Officer (2017) has *projected* the future deficits and debts of the provincial governments *based on current revenue and expenditure trends*.
- Alberta’s debt is project to continue to grow relative to GDP and the current fiscal situation of the province is therefore *unsustainable*.

THE PBO (2017) FISCAL SUSTAINABILITY REPORT

- "Current fiscal policy in Alberta is not sustainable over the long term. PBO estimates that permanent tax increases or spending reductions amounting to 4.6 per cent of provincial GDP ***($14.1 billion in current dollars)*** would be required to achieve fiscal sustainability.
- This is equivalent to a ***permanent 25 per cent increase in the tax burden*** (including federal transfers) or a ***20 per cent reduction in program spending.*** Health care spending is the key fiscal pressure in our projection, increasing by 2.5 percentage points of GDP over 2020 to 2091." p.72 (emphasis added)

PROJECTED NET FINANCIAL LIABILITIES OF FOUR CANADIAN PROVINCES

Net Financial Liabilities as a Percentage of GDP



Source: PBO (2017)

A FISCAL ADJUSTMENT IN ALBERTA

- Some combination of revenue increases and expenditure restraints are necessary to address the province’s deficit-debt problem.
- In the 1990s, the Klein government reduced spending by 20 percent across the board.
- Are Albertan’s prepared to see major service cuts in health, education, social services and public infrastructure?

REVENUE ENHANCEMENTS

- Are Albertan's prepared to see major tax increases?
- A higher corporate income tax rate and a higher top personal income rate would likely generate some additional revenues, but at the cost of reduced investment and slower wage and salary growth.
- Higher tuition fees and user fees for provincially funded services, such as highways and roads, could be levied.
- Higher provincial and municipal property taxes could be levied and a land transfer tax could be introduced.
- The Province could levy a sales tax.

AN 8 PER CENT HST IN ALBERTA

- An 8% provincial sales tax levied on top of the federal 5% GST would raise a substantial amount of revenue.
- Based on Basel and Mintz (2013) an 8% HST:
  - Would raise roughly $8.4 billion for the provincial government.
  - About $800 million would be attributed to non-residents (tourists).
  - Provincial HST Credit of $1 billion for low income individuals.
  - Net revenue of $7.4 billion, roughly 50% of the fiscal adjustment required for a sustainable fiscal policy.

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