

# How Progressive is Canada's Tax System?

**A** fair tax system is a progressive tax system, where people with higher incomes pay a greater share of their income in taxes. Growing evidence demonstrates that “fair is smart, that progressive taxes, where those who benefit most pay the greatest share, make good economic sense.”<sup>16</sup>

Fairness and equity in the distribution of federal and provincial taxes are pressing issues today given the recent growth of income inequality in Canada, and the associated increase in the concentration of income and wealth.<sup>17</sup>

The continuing trend of tax cuts for high-income individuals and corporations has disproportionately benefited a select few at a high cost to our nation's economic and social well-being. Canada needs a fair tax system that ensures sufficient federal revenue and creates a vibrant economy that benefits all people.

## Canada's Tax System<sup>18</sup>

- Canada's tax system is comprised of a variety of measures and programs ranging from personal income tax and local property taxes to payroll premiums to commodity taxes such as the GST/HST. And each has a distinct impact on individuals and families at the top, middle, and bottom of the income ladder.
- Personal income taxes can be relatively progressive if higher tax rates are applied as individuals earn higher amounts of income. At the same time, many sources of income for high earners such as investment income from stock options or capital gains are taxed

more lightly than income from wages and salaries, undermining the progressivity of the system.

- Higher income Canadians are also able to access generous tax deductions like RRSP contributions and other tax expenditures that greatly lower their effective tax rates – that is the amount of total income paid in taxes.<sup>19</sup>

And “other taxes in the Canadian tax mix, such as sales taxes, are actually regressive, which is to say that lower income families pay a higher effective tax rate than those with higher incomes.”<sup>20</sup>



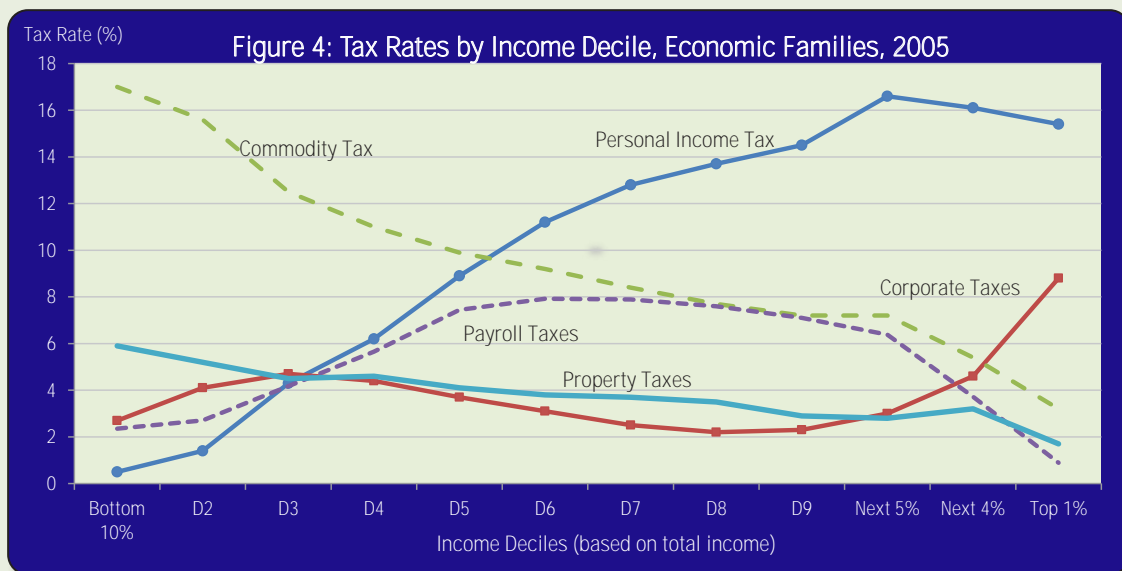
## Tax Terms

- A **progressive tax system** is where people with higher incomes pay a greater share of their income in taxes.
- The opposite of a progressive tax is a **regressive tax**, where the share of income paid in tax decreases as income rises. Sales taxes, for example, are largely understood as regressive since low income households end up spending a larger share of their income on taxes because

most of their income is spent on goods and services, while higher income households have the funds to save and invest.

- A **proportional tax** is one where everyone is required to pay an equal proportion of their income in tax such as a flat tax. This type of tax is also highly regressive as a 10% tax, for example, represents a much heavier burden for low as compared to high income households.

**A sales tax (or “commodity tax”) is regressive because lower income families pay a higher effective tax rate than those with higher incomes**



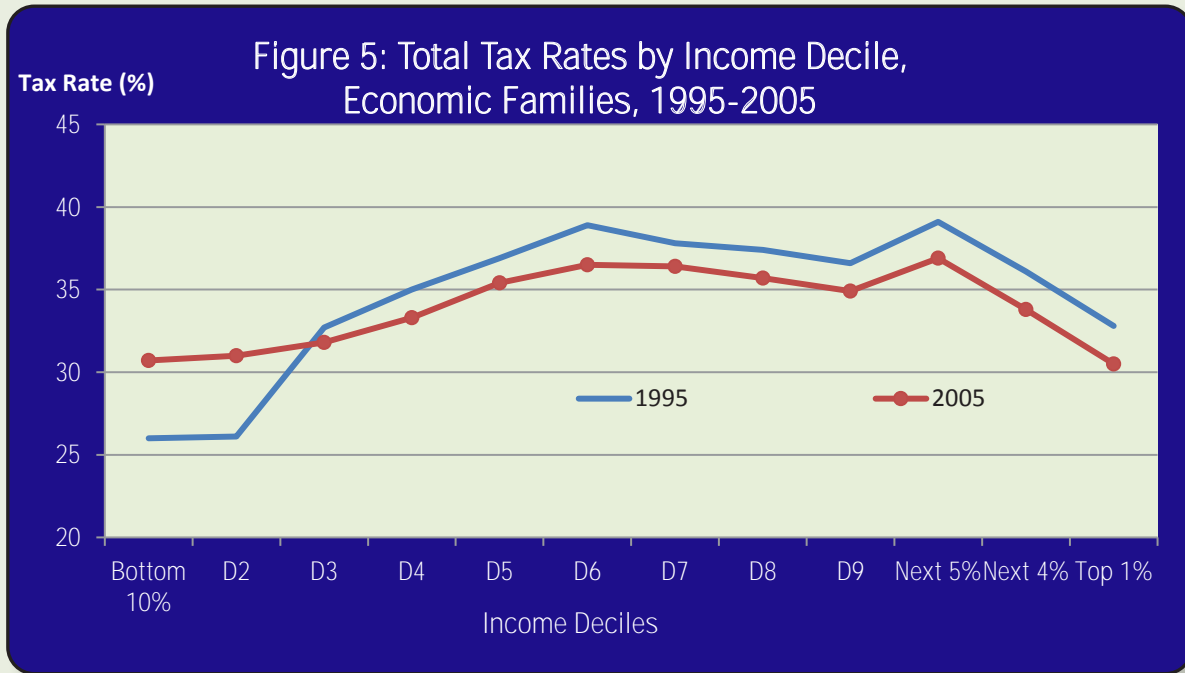
Source: Marc Lee (2007), *Eroding Tax Fairness*. Canadian Centre for Policy Alternatives.

## The wealthy have benefited the most from two decades of tax cuts

- Changes introduced through the 1990-2005 period reduced rates for top income earners considerably, while rates for bottom income earners actually increased as a result of changes in consumption, payroll and property taxes and other provincial taxes and fees.<sup>21</sup>
- In 2005, total rates of tax paid ranged from 30.7% for individuals in the bottom 10%, to 36.5% for those in the middle, to 30.5% for the top 1% of families. The richest 1% of Canadians actually paid a lower rate than the poorest 10% of Canadians.<sup>22</sup>

- The OECD corroborates these findings, concluding that tax cuts in Canada between 2000 and 2006 mainly benefited high income groups at the expense of low and modest income earners.<sup>23</sup>
- Tax changes since 2006 have continued to disproportionately benefit the wealthy, particularly single earner families with children and senior couples with substantial pension incomes.<sup>24</sup>

**Canada's overall tax rate is now an inverted u-shape, progressive from the bottom to the middle of the income distribution but regressive thereafter**



Source: Marc Lee (2007), *Eroding Tax Fairness*. Canadian Centre for Policy Alternatives

<sup>16</sup> Alex Himelfarb (2015), "Why We Hate Taxes – And Why We Shouldn't," Alex's Blog, January 3, 2015. <https://afhimelfarb.wordpress.com/2015/01/03/why-we-hate-taxes-and-why-we-shouldnt/>  
<sup>17</sup> OECD (2011), "Country Note: Canada." *Divided We Stand: Why Inequality Keeps Rising*. <http://www.oecd.org/canada/49177689.pdf>. Income inequality among working-age persons has been rising in Canada, particularly since the mid-1990s. The rise in inequality has been largely due to widening disparities in labour earnings between high and low-paid workers, but also to less redistribution. The tax-benefit system now offsets less than 40% of market inequality, compared to more than 70% prior to the mid-1990s.

<sup>18</sup> This section is based on Marc Lee's report: Marc Lee (2007), *Eroding Tax Fairness: Tax Incidence in Canada, 1990-2005*. Canadian Centre for Policy Alternatives. [https://www.policyalternatives.ca/sites/default/files/uploads/publications/National\\_Office\\_Pubs/2007/Eroding\\_Tax\\_Fairness\\_web.pdf](https://www.policyalternatives.ca/sites/default/files/uploads/publications/National_Office_Pubs/2007/Eroding_Tax_Fairness_web.pdf)

<sup>19</sup> An individual's effective tax rate is calculated by dividing total tax paid by taxable income.

<sup>20</sup> Marc Lee and Iglia Ivanova (2013), *Fairness by Design: A Framework for Tax Reform in Canada*. Canadian Centre for Policy Alternatives, p. 19. [https://www.policyalternatives.ca/sites/default/files/uploads/publications/National%20Office/2013/02/Fairness\\_By\\_Design\\_A\\_Framework\\_For\\_Tax\\_Reform\\_In\\_Canada\\_0.pdf](https://www.policyalternatives.ca/sites/default/files/uploads/publications/National%20Office/2013/02/Fairness_By_Design_A_Framework_For_Tax_Reform_In_Canada_0.pdf)

<sup>21</sup> Marc Lee (2007).

<sup>22</sup> *Ibid.*, p. 17.

<sup>23</sup> OECD (2008), *Taxing Wages 2007*. Cited in Eric Beauchene (2008), "Canada's wealthy benefit most from tax cuts, OECD finds." *Canwest News Service*, March 24, 2008. <http://www.vivelecanada.ca/article/235929770-canadas-wealthy-benefit-most-from-tax-cuts-oecd-finds>

<sup>24</sup> Kevin Milligan (2009), "What have four Conservative budgets done to personal income taxes?" Prepared for the John Deutsch Institute conference on the 2009 Federal Budget, Kingston, May 7-8, 2009. <http://faculty.arts.ubc.ca/kmilligan/research/papers/Milligan-Budget-2009.pdf>