A SHERRY COOPER BUDGET

Brian K. MacLean

Budget 2000 may provide large percentage tax cuts to low- and middle-income Canadians, but the truly big bucks go to big corporations and high-income individuals. Since 1995, the federal books have been balanced largely on the backs of social programs. Yet now that the deficit is gone, Mr. Martin has made only a token attempt to restore the cuts in social spending. Instead, with income tax cuts that axiomatically deliver more dollars to those with higher incomes, Mr. Martin has launched a second stage in the dismantling of the Canadian welfare state. Rather than what it purports to be, a budget aimed at the interests of low- and middle-income Canadians, the budget is a tribute to the effectiveness of Canada's business lobby..

Le budget 2000 prévoit peut-être, en termes de pourcentage, d'importantes réductions d'impôts en faveur des Canadiens à revenu faible ou moyen. Mais les vrais bénéficiaires de l'exercice demeurent les grandes entreprises, ainsi que les particuliers jouissant de revenus élevés. Depuis 1995, l'équilibre budgétaire du gouvernement fédéral s'est réalisé en bonne partie aux dépens des programmes sociaux. Or, maintenant qu'il est atteint, M. Martin a très peu fait pour véritablement rétablir le financement des programmes sociaux. En accordant des réductions d'impôts qui profitent surtout aux plus riches, M. Martin a plutôt lancé la deuxième phase du processus de démantèlement de l'État providence canadien. En vérité, son dernier budget, qui prétend servir les intérêts des Canadiens à revenu faible ou moyen, constitue un tribut à l'implacable « lobbying » du milieu canadien des affaires.

If a man can be judged by the company he keeps, then evidence on who praises a federal budget may provide hints for judging it. In the case of Finance Minister Paul Martin's 2000 federal budget, high marks were awarded by Sherry Cooper. Readers who follow coverage of the Canadian economy in newspapers and on television will know that Ms. Cooper is chief economist with Nesbitt Burns, a Bank of Montreal affiliate.

Ms. Cooper, described recently in the *Globe and Mail* as "one of the government's harshest and most vocal critics in recent years," was moved by the budget to pen a glowing column in the *National Post*. In "How Martin's new budget changed my mind," Ms. Cooper praised Mr. Martin with a generosity not seen since the release of his watershed 1995 budget, with its deep cuts in program spending (see p. 24).

In understanding the character and origins of the 2000 federal budget, two questions are particularly revealing. First, what makes the budget so attractive to Ms. Cooper? Second, what role has this vocal government critic and her allies played in making such a budget possible?

Although Ms. Cooper is officially chief economist for Nesbitt Burns, in reality she functions as a communications officer for what the financial newspapers call the "business lobby." If reporters from Canada's leading newspapers want to get the big business take on any breaking news, Ms. Cooper is just a local phone call away. If the TV networks seek her opinion, she is ready to join their shows through Nesbitt Burns' private remote camera, with the brokerage's trading floor as a backdrop.

Given that Ms. Cooper represents the business lobby and "high net-worth individuals," why is she lavishing praise on a budget described by the finance minister and much of the news media as being for low- and middle-income Canadians?

The *Budget Plan* does an excellent job of concealing certain facts from the general public. For example, in the budget documents, tax savings are repeatedly expressed as a percentage of income. Consider how this mode of expression can be used to transform a typical taxpayer case provided in the *Globe and Mail* on Feb. 29. For a married couple with one income of $20,000, the tax savings are calculated as $73 by two tax practitioners with Ernst & Young.

The married couple gets an addition to pre-tax income of 0.37 per cent, by my calculation.

You might view the high-income couple as winners by a ratio of over two to one. Or you might view it in dollar terms as the Department of Finance giving a kitchen radio to the low-income couple while awarding the high-income couple a 27-inch surround-sound TV with a satellite dish and six months of complimentary programming. Finance would prefer that you regard the $73 as a sold 8.5 per cent savings of previously-owed federal income taxes ($860 according to Ernst & Young) and the $1,173 as a mere 3.4 per cent savings (relative to $34,078 in federal income taxes), showing that “Low, middle incomes benefit most.” According to Finance’s favoured mode of expressing tax reductions, the taxpayer who previously paid one cent in federal income taxes and now pays zero has experienced savings of 100 per cent, the maximum possible. She should be eyeing with glee the shiny penny that, on her next purchase, she can now apply to the GST — the highly regressive GST upon which Finance will increasingly rely as a revenue source.

To be fair, Finance may have learned this technique of presenting tax savings from Monte Solberg, the Reform finance critic, who has used it to sell his flat tax ideas. But you can be sure that if either Finance or Mr. Solberg decided to raise taxes one cent for someone paying zero taxes, they would not be consistent and portray it as an infinitely large percentage increase over the zero taxes previously paid. The mode of expression produces nonsense in both directions, but for misleading low- and middle-income Canadians, it is only useful for selling tax cuts, nor tax increases.

To take another example, the budget refers to reducing “corporate tax rates to 21 per cent from 28 per cent for businesses in the highest taxed sectors, such as high-technology services, to make these businesses more internationally competitive.” How much this corporate tax giveaway is going to cost the Department of Finance is never once stated clearly.

In the *Budget Plan* the value of corporate tax relief in fiscal year 2000-01 (which runs to the end of March 2001) is variously presented as $5 million (p. 20), $60 million (p. 203), minus $65 million (p. 22 and p. 156) or minus $100 million (p. 84), depending upon whether previously announced measures are considered, whether the numbers are rounded, and other factors. The numbers are small in part because the cut scheduled for January 20001 is only one percentage point of the seven planned, but also because it will only be in operation for the last three months of the 2000-01 fiscal year. If you dig a little deeper, the budget indicates that if the cuts were back-ended, the cumulative cost to Finance by 2004-2005 would be a minimum of $4 billion. If the reduction to 21 per cent occurred in the last two years rather than in the final year the cumulative cost would be $5.5 billion. Although the budget does not document the following scenario, if the reduction to 21 per cent were implemented in 2002-2003, the cumulative cost apparently would be about $9 billion.

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Every time corporate tax cuts are mentioned in the budget, they are justified as a special measure to promote high-tech firms and make Canada internationally competitive. But no examples of the intended beneficiaries of these tax cuts are provided. They presumably include names like Royal Bank, Bank of Montreal, Toronto Dominion, CIBC, Scotiabank, and maybe even Nesbitt Burns, which picks up the tab for Sherry Cooper’s media appearances. Major beneficiaries also include retailers like Walmart, phone companies like Sprint, fast-food purveyors like McDonalds, hoteliers like Holiday Inn, and car rental chains like National. But citizens reading the budget see none of these names mentioned.

Consider what that means. At a minimum, the federal government is proposing to provide $4 billion in tax relief to large corporations over the coming years. The rationale for this massive giveaway is limited to a few vague budget sentences about aiding high-tech service sector firms and increasing Canada’s international tax competitiveness. But the beneficiaries are not listed. The project proposal for these tax expenditures could be scribbled on a postcard. And no criteria are provided for judging their success, for there is no political need to do so. Even though the giveaway is several times the $1 billion in improperly documented HRDC funding, the harsh and vocal critics of government spending love it. The handout to corporations is 80,000 to 180,000 times the $50,000 allocated by HRDC to the much-ridiculed Wiarton Willie groundhog festival. But I have yet to see one newspaper editorial criticising either the corporate tax giveaway or the questionable way in which it has been slipped through.

My two examples illustrate why Ms. Cooper was moved to proclaim: “While there is much yet to be done, the seeds have been sown for a

dramatic shift in Canadian tax policy. We have embarked on a grand experiment." With his budget, Mr. Martin delivered on practically all business lobby requests. On the taxation side, he reduced tax rates for large corporations and for "small" businesses, began eliminating the high income surtax, lowered the inclusion rate for capital gains taxation, provided more favourable treatment of stock options, and increased the foreign content limit for RRSP contributions. On the expenditure side, Mr. Martin has returned only dimes and quarters to a social programs piggybank that he has raided for loonies since 1995. Annex 3 of the *Budget Plan* nicely summarizes the situation: "Federal program spending is expected to fall to 12.2 per cent of GDP in 1999-2000 ... This represents a 5.3-percentage-point drop from its peak in 1992-93. Likewise, provincial-territorial program spending is expected to decline to 16.0 per cent of GDP in 1999-2000, down from 20.1 per cent in 1992-93." The budget even shows that Canada's total government program spending has fallen below that of Japan, even though Canada lacks Japan's generous company-provided housing and other company welfare measures. As a percentage of GDP, Canadian federal programme spending is projected to decline to 11.6 per cent in 2001-02, the lowest ratio in over 50 years, indicating this is not simply programme demand declining as the economy moves to a business cycle peak.

As the Canadian Labour Congress put it, "Mr. Martin chose to do the minimum in terms of shoring up social programs, while delivering most of the tax cut program demanded by Bay Street ... In the final analysis, Mr. Martin's 'balanced approach' hid a major long-term tilt to the right." The wording may come from the opposite side of the class divide, but the substance of the assessment is remarkably similar to Ms. Cooper's.

An historic budget like the one brought down Feb. 28 warrants discussion not just of its character — of who benefits from which tax and expenditure changes — but also of its origins. It needs to be situated in the broader sweep of the country's economic history.

The 2000 budget marks a milestone in the dismantling of the Canadian welfare state that was begun with Mr. Martin's 1995 budget. That budget marked the beginning of a deficit reduction crusade that was carried out mainly through cutbacks in government spending, especially social programme funding. By fiscal year 1999-2000, the federal government found itself awash in actual and projected surpluses, at least partly because of solid economic growth made possible by our piggybacking on the booming US economy. But rather than place his primary post-deficit emphasis on the restoration of social programme funding, Mr. Martin leaned in favour of tax cuts.

Future historians and political scientists will no doubt portray these milestone budgets as the product of complex economic and political processes. They should not overlook the role of the business lobby in influencing federal budgets — a role the lobby itself might concede, since it is such a public relations success story.

For the first half of the 1990s, the business lobby's campaign to transform the welfare state focused shrewdly on the underground economy and "the debt wall." Part one of the argument was that the Canadian dollar would collapse — we would hit a debt wall — if Ottawa failed to reign in government deficits. Part two was that deficits had to be controlled not by tax increases but by spending cuts. High taxes, it was claimed, were already driving economic activity underground. The campaign paid dividends in Mr. Martin's February 1995 budget, the budget that set in motion spending cuts designed to reduce the share of income spent on federal programmes back to 1950s levels.

Having got the spending cuts, business moved on to its second objective: to reduce the tax burden and to deprive governments of revenue that might allow rebuilding social programmes. Thus was born the "tax rage" campaign with its dire warnings of "brain drain."

Just as the debt wall scare required the underground economy argument to rule out the possibility of reducing deficits through tax increases, so the brain drain campaign required some justification for ruling out a concerted effort at rebuilding social programmes. How convenient then that, leading up to the 2000 federal budget, a scandal emerged about $1 billion of improperly documented HRDC spending that was cleverly transformed by the business lobby, the Reform Party, and their media allies into fodder for the campaign against government spending in general. Once again a one-two combination from the business lobby paid rich dividends at budget time.

In fact, none of the business lobby's major arguments stand up to scholarly scrutiny. The debt wall was typically illustrated with examples of currency collapse in countries with fixed

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exchange rates. The size of the underground economy was greatly exaggerated, when a temporary surge in underground transactions due to the GST was falsely attributed to the influence of supposedly high income taxes. The brain drain campaign relied mainly on anecdotes precisely because, as John Helliwell's article in the Sept. 1999 issue of *Policy Options* made clear, aggregate statistics provide nothing but contrary evidence. As for the HRDC scandal, it requires considerable ideological ingenuity to be twisted into evidence against spending on social programmes. The most natural interpretation is that job creation grants were paid for with a small fraction of the money "saved" by hacking away at the old unemployment insurance system. Highly visible job creation projects provided a convenient smokescreen behind which the Liberals allowed the real levers of job creation (monetary and fiscal policy) to be used for pleasing the business lobby, the biggest fans of zero inflation and barebones social programsme. That jobs grants became politicized should serve to highlight the non-politicized nature of spending on employment insurance, health, education and welfare.

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Not only that, business lobby arguments have failed to convince the general public. According to opinion polls, most Canadians still want to see the restoration of social programmes, especially health care and education. And only a tiny minority support tax cuts for the rich or for business.

But the success of the business lobby is best measured in terms of its influence over key politicians and Department of Finance officials and hence over budgets. If this influence is achieved, persuading either academics or ordinary Canadians becomes unnecessary. By this standard, the business lobby has scored a resounding success. Ms. Cooper is to be congratulated, but not by low- and middle-income taxpayers.

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Sherry Cooper's reaction to the budget I went into the budget lock-up on Monday like everyone else, prepared to be cynical about this year's budget. In an effort to get a head start, I drafted a preliminary assessment last Saturday, assuming I knew what was coming. I highlighted the missed opportunity and chastised the government once again for its refusal to recognize the importance and urgency of tax cuts. Sequestered in Ottawa's Congress Centre, I ploughed into the budget documents, yellow highlighter in hand.

Twenty minutes later, I deleted my original draft and started over. This time I congratulated Mr.Martin for a meaningful change in direction, the first step in a five-year plan to appreciably reduce the tax burden of all Canadians. There were three things that changed my mind: First, the surprise restoration of full indexation of the tax system for inflation; second, the reduction in capital gains tax rates; and third, the cut in corporate tax rates. Each on its own is not enough, not nearly enough. But introduced together, they give a strong signal of a directional change in policy. Mr. Martin stated repeatedly that the current tax-cut package is the minimum we can expect ...

The big winners in this year's budget are middle-class families with children, and that represents the majority of the population. The reduction in the middle tax bracket, the hike in the child tax credit and basic personal exemption and the increase in income thresholds all contribute to a significant reduction in the middle-class burden ... But more on the personal tax front is needed. Let us not forget that CPP premium hikes will wipe out more than $14-billion of the tax cut over the next five years, fully offsetting the positive effects of the Employment Insurance premium reductions. Still, we have seen little tax relief for higher-income Canadians — whose talent is so desperately needed in the new economy ...

The corporate tax cuts are only a beginning as well, but a welcome one ... The five-year phase-in of the business tax reduction is too slow. Our relatively high business tax burden encourages corporations to shift income and jobs to jurisdictions where the rates are much lower ... The capital gains tax cut was also a positive first step, taking our top capital gains tax rate down from roughly 36 per cent to 32 per cent (varying from province to province). This is not enough, however; the capital gains tax rate in the US is 20 per cent, and in Britain it is slated to go to a mere 10 per cent.

While there is much yet to be done, the seeds have been sown for a dramatic shift in Canadian tax policy. We have embarked on a grand experiment. We will see this year that tax revenues rise, not fall, despite the cuts. Budgetary surpluses will remain large and more aggressive action to reduce taxes and pay down the debt is in the cards.

Reprinted courtesy *National Post*, 1 March 2000