

# **Top-End Progressivity and Federal Tax Preferences in Canada: Estimates from Personal Income Tax Data**

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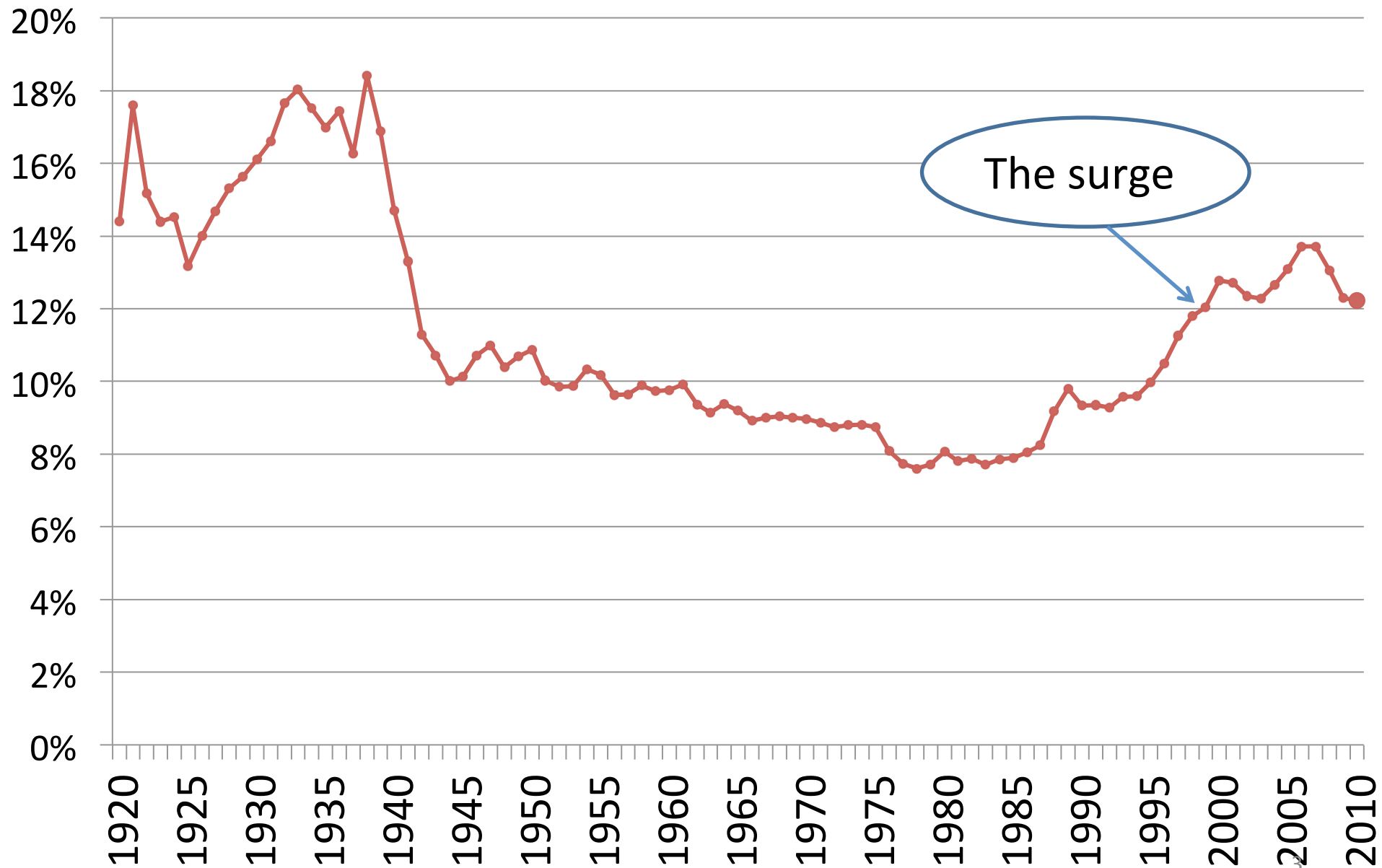
**Prepared for the IRPP-CSLRN conference  
Inequality in Canada: Driving Forces, Outcomes and Policy  
Ottawa, February 24-25, 2014**

All opinions expressed are those of the authors (oral presentation: Veall). Thanks to Julien Dicaire, Hung Pham, Mohammad Mashiur Rahman and Yue Xing for excellent research assistance and SSHRC for financial support.

## *Starting Point :*

- Much of the increase in income inequality in the last years is due to a surge in the income share of the top 1%, top 0.1% and top 0.01%

# Income Share of the Top 1%, Canada, 1920-2010



## ***Motivation (1) :***

1. How what the Dept. of Finance calls “tax expenditures” (tax credits, deductions, preferences) benefit top 1%, top 0.1%, top 0.01%
2. U.S.: Hang, Nunn, Toder and Williams (2012) and Brown, Gale and Looney (2012)

## ***Motivation (2) :***

3. Chris Ragan, *Globe and Mail online*, Feb. 11, 2014:  
“The Canadian income tax system is replete with billions of dollars of ‘tax expenditures’ ...While some of these are sensible, many others needlessly complicate the income tax system and increase the growing perception of unfairness. I challenge the government to commit to eliminating \$2-billion to \$3-billion of tax expenditures each year for the next three years. Once achieved, the stage would be set for a small overall reduction in tax rates.”

## *Motivation (3) :*

- In considering a tax expenditure, overall/top-end progressivity is one of the factors that matters as well as
  - Administrative ease
  - Economic efficiency: overall, purpose of measure, gov't revenue
- Related work: Department of Finance (2011): Gini ↓ with tax credits and ↑ with deductions
  - does not look at individual tax preferences

# *What we do :*

- Simple and rough, 2011
- Use Longitudinal Administrative Database (5 million records, aggregates): Canada Revenue Agency published data used as a check
- Allocate benefit of tax expenditures (from Dept. of Finance 2012 for 2011) across income categories
- Income = all individual filer current income, including K gains, gov't transfers
- Method: adjust usage by decile (and top 1%, 0.1%, 0.01%) for:
  - Nonrefundability (credits)
  - Different tax rates, including zero (deductions)

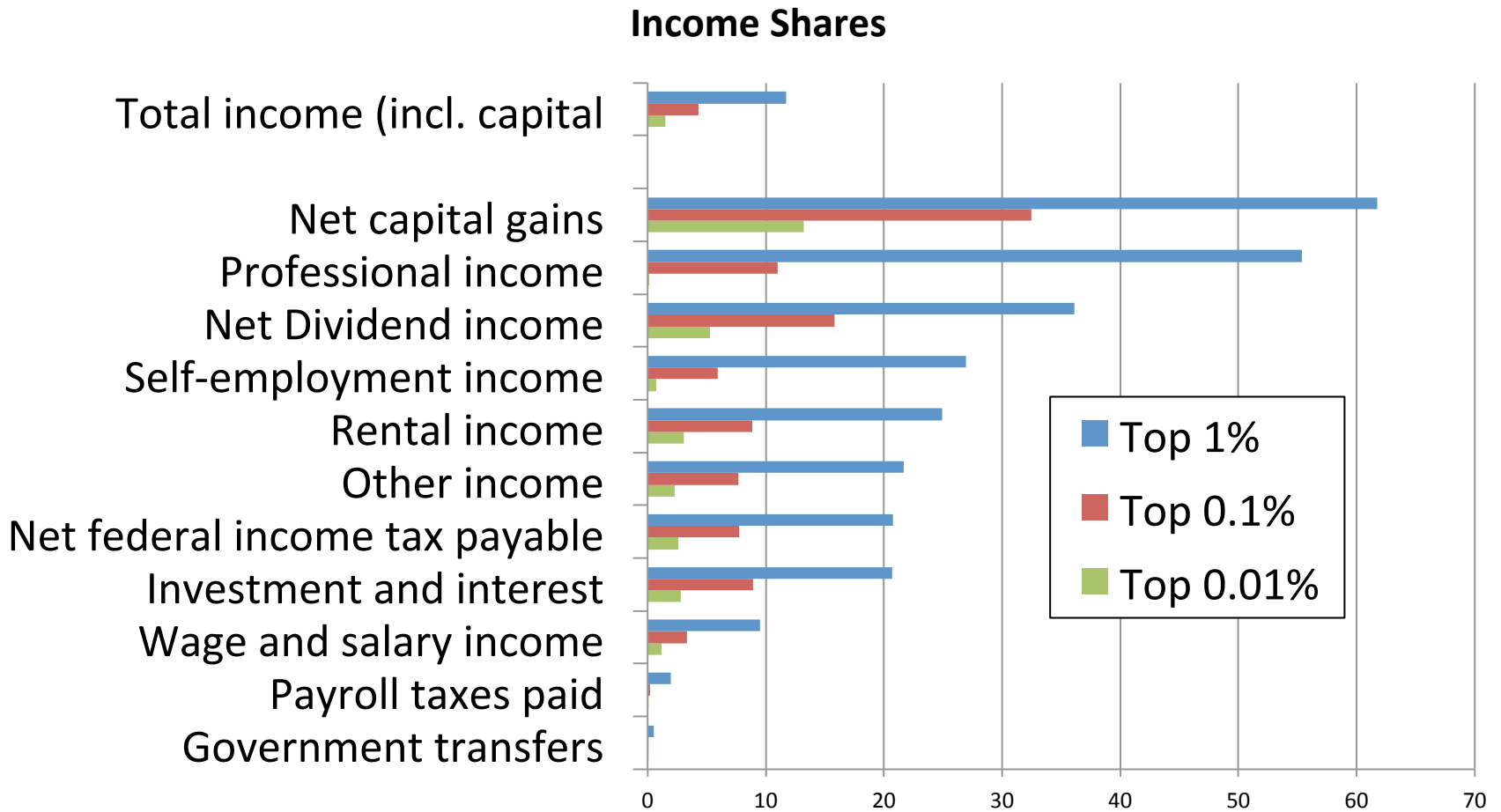
## ***Caveats :***

- No behaviour
- Tax rate calculated at average for decile (and top 1%, 0.1%, 0.01%)
- No behaviour
- Tax rate is marginal “first \$” rate
- **No behaviour**

*... but*

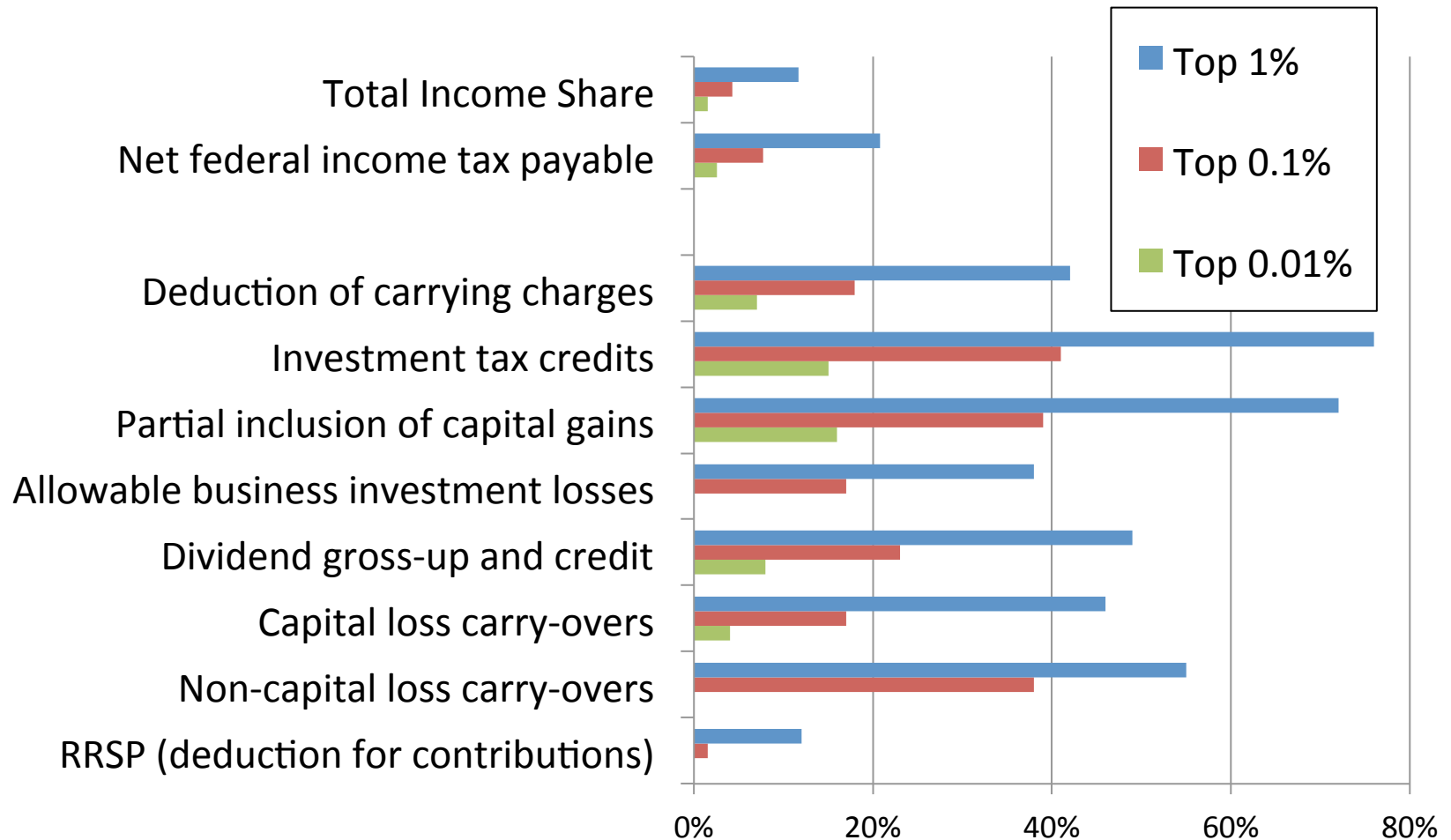


# Estimated share of selected income categories



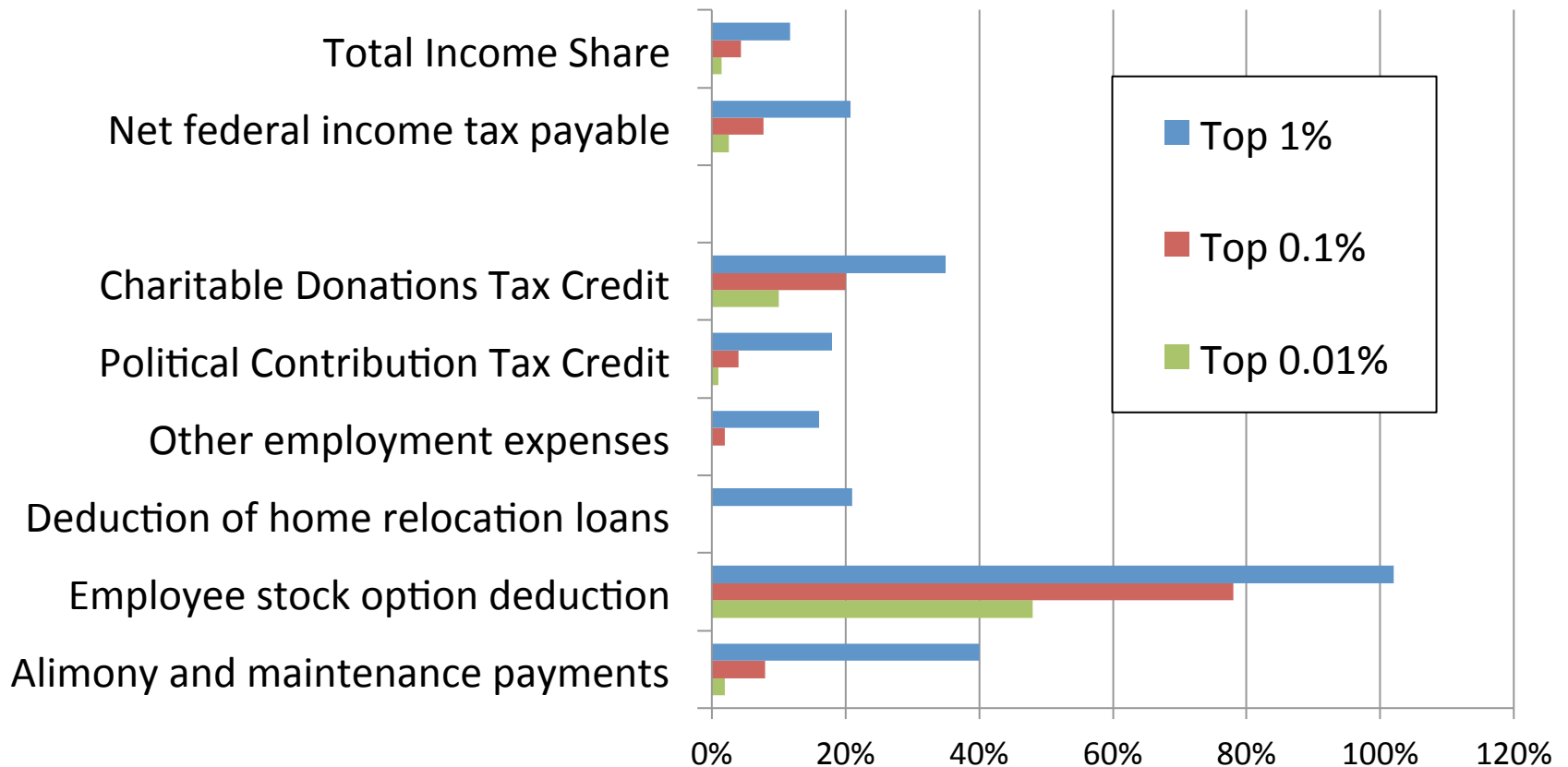
# Estimated Allocation of Benefits

## Items Related to Capital Income



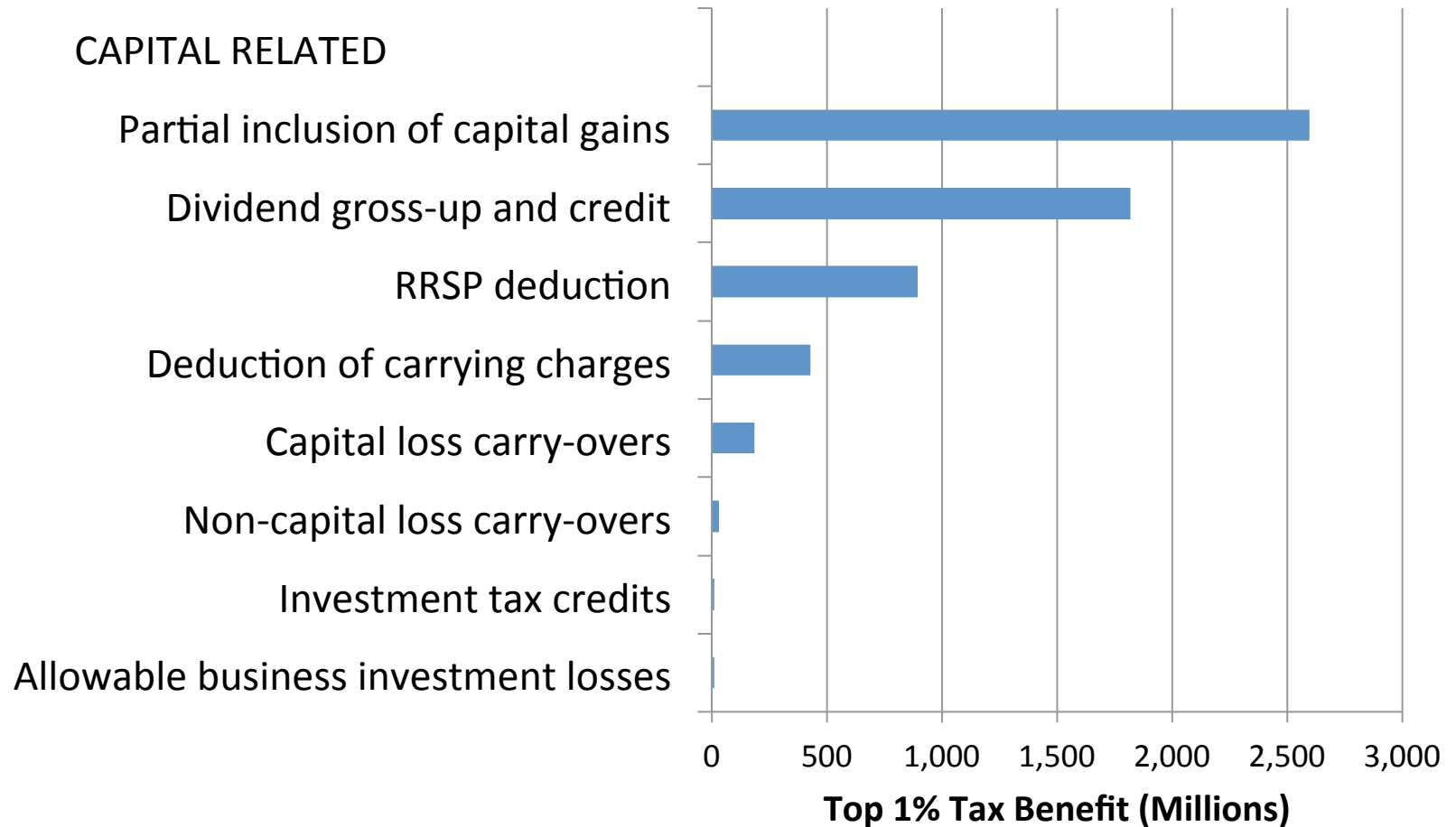
# Estimated Allocation of Benefits

Largely Not Related to Capital Income



# Estimated Benefits going to the Top

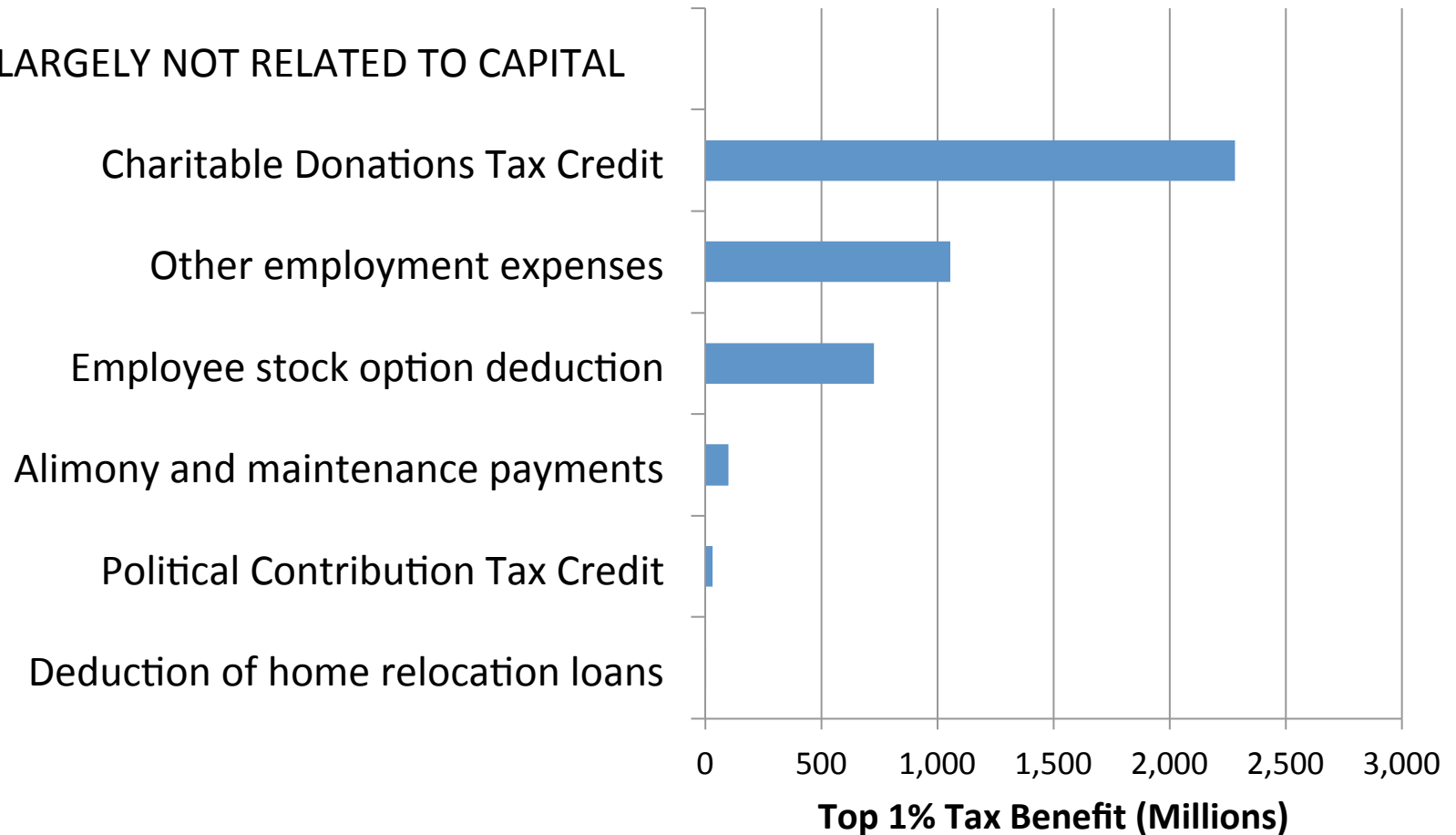
## 1%



# Estimated Benefits going to the Top

## 1%

LARGELY NOT RELATED TO CAPITAL



## *Other* :

- Labour Sponsored Venture Capital Corporations Credit (now discontinued)
- Tax-Free Savings Accounts
- Neither benefit top-end as much as RRSPs

## ***Tax measures we couldn't do :***

- Carry-forward of Education, Textbook and Tuition Tax Credits (2011 tax expenditure of \$535m)
- Non-taxation of veterans' disability pensions and support for dependents (\$140m)
- Partial Deduction of Meals and Expenses (\$180m)
- Registered Education Savings Plans (\$185m)
- Lifetime Capital Gains Exemption for Farming, Fishing Properties (\$330 million); for Small Business (\$560m)
- Flow-through share deductions (\$280m)
- Mineral Exploration Tax Credit (\$125m)

# *Conclusions (1) :*

- Thought experiment: suppose one were looking to chop federal personal income tax expenditures whose removal would
  - Improve top-end progressivity
  - Could be done with a “stroke of the pen” i.e. no new reporting requirements such as implicit rent on owner-occupied housing, or (arguably) employee benefits
  - Not affect capital income
- Not many (Focuses the debate? Role of trusts, CCPCs?)



## *Conclusions (2) :*

- In practice, almost all of the tax preferences in the Canadian personal income tax system that do not involve capital income or stock options increase rather than reduce progressivity at the very top end

***Thank you !***