Rethinking Fiscal Arrangements in Canada

Robin Boadway
Queen’s University

Queen’s International Institute on Social Policy Conference

Building Back Better:
Forging a Post-Pandemic Social Policy That Works for All

August 25 – September 10, 2020
Overview

• Issues with existing fiscal arrangements

• Fallout from the pandemic shock

• Policy options
Issues with Federal-Provincial Fiscal Arrangements Pre-Pandemic
Growing Vertical Fiscal Imbalance

• Provincial debt-GDP ratios relatively high
• Provincial social spending growing vis-à-vis federal transfers
• Demographic pressures on both expenditure and revenue sides
• Municipalities increasingly constrained
• Advantage of sizeable federal-provincial transfers:
  • Federal leadership in revenue-raising versus
  • Advantages of social program decentralization
  • But, danger of soft budget constraint
Continuing Horizontal Imbalance

• Sizeable fiscal capacity differences
  • Differences in provincial debt-GDP ratios, growth rates and demographic pressures
  • Pressures on natural resource provinces

• Shortcomings of equalization
  • Structural issues: GDP cap; resource revenues; carbon taxes; needs
  • Inadequate as insurer of risk to provincial revenues
  • CHT/CST more effective at equalizing “have” provinces down

• Fiscal competition pressures leading to protective measures
Inadequate Fiscal Stabilization

Provinces prone to idiosyncratic fiscal shocks
• Have limited self-insurance ability, with the arguable exception of resource revenues; resource provinces have not self-insured
• Federal government can pool risks across provinces and time, but
• Equalization program not very stabilizing: standard varies with shocks
• Fiscal Stabilization Program has inadequacies:
  • $60 per capita limit has not changed and is declining in real terms
  • Deductible on resource revenue is 50%; based on actual revenues
Coordination of Responsibility Issues

Federal-provincial harmonization done on a case-by-case basis

• Tax harmonization a success story, but incomplete
• Environment: diverse carbon pricing and regulation approaches
• Progress on internal common market: CFTA and bilateral agreements
• Capital market regulation a work-in-progress
• Social safety net/protection: lack of coordination between social insurance (EI), income security, tax transfers and social assistance
• Limited coordination among provinces in areas of provincial jurisdiction
Fallout from the Pandemic Shock
Fiscal and Economic Fallout

• Once-over increase in federal and provincial debt
• Increase in private indebtedness and bankruptcies
• Vulnerabilities of social protection exposed
  • Inadequacy of EI, income support for working poor and precariat
  • Long-term care, childcare
  • Public health preparedness
• Temporary job loss concentrated among low-wage, service sector workers and those unable to work from home
• High-income earners sheltered
Intergenerational Impact

Cost of pandemic uneven across generations

• Immediate costs to the young:
  • Loss of education opportunities
  • Disadvantages of delayed job market entry

• Capital income better protected than labour, favouring the well-off elderly

• Potential for current younger generations to suffer as pandemic debt paid down in future

• Older generations spared costs of financing debt
Policy Options for Fiscal Arrangements
Policy Options: Fiscal Reforms

• Spread cost of pandemic debt across generations
  • Pay debt off gradually to spread burden to future
  • Tax reform to spread costs to older generations: broaden income tax base, once-over Pigou wealth tax

• Reallocate debt from provinces to feds: once-over transfer

• Reform fiscal transfers
  • End cap on equalization
  • Tie growth of CHT/CST to provincial program expenditures
  • Enhance fiscal stabilization

• (Potential new spending power initiatives)?
  • Long-term care, childcare, pharmacare
Policy Options: Structural

• Reallocate expenditure responsibilities
  • Make social assistance federal
  • Create federal-provincial basic income guarantee

• Change vertical balance: increase in federal tax room & CHT/CST
  • Make provinces less vulnerable and preserve tax harmonization

• Tax reform to improve fairness & incentives to innovate and invest
  • Basic income guarantee, broaden capital income base
  • Reinstate inheritance tax
  • Reform CIT to encourage investment & reduce incentive for debt finance
Policy Options: Institutional

• Federal and provincial responsibilities are interdependent, but often conducted in silos
• Worth exploring institutional mechanisms for fostering coordination and harmonization
  • Expand Council of the Federation to include federal government?
  • Fiscal Council to monitor federal and provincial fiscal situations?
  • Grants Council to advise on federal-provincial transfers?