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e-brief

Watch Out for Hidden Taxes

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During the current election campaign, parties have taken quite different positions on tax policy: The New Democrats advocate tax increases, the Conservatives a tax cut and the Liberals want neither. In evaluating these positions, many Canadians may wonder how Canada's tax levels stack up against those of other industrialized nations. This e-brief compares total government tax levels among OECD countries, including Canada.

In making such comparisons, commentators often quote tax-to-GDP ratios, while ignoring such non-tax revenues raised by governments as oil and gas royalties, as well as user fees and profits of public enterprises. Unlike taxes, payments that are independent of any service or benefit provided to the public, non-tax revenues are usually a compulsory payment made by an individual or business for a specific public service; for example, drivers' license fees are non-tax revenues, while the new Ontario health premium is a tax.

Canadian governments raise a relatively large amount of revenue, $497 billion in 2003, close to 41 percent of national income, or $15,770 per capita. That was down a little from 2001 - the most recent year for OECD data comparisons - when Canadian government revenues reached a record 44.1 percent of GDP.

Canadian governments are neither high nor low tax collectors when only traditional taxes are considered (see the table below). Canada's tax-to-GDP ratio was 35.1 percent in 2001, the 18th highest for the 25 OECD countries. Canada's tax-to-GDP ratio is significantly higher than that of its largest trading partner, the United States, as well as that of the fastest growing economy among all countries, Ireland, and resource-based Australia. On the other hand, Canada's tax-to-GDP ratio is well below most European countries, including the United Kingdom.

However, this comparison masks a critical fact. Although governments in a lot of countries raise more revenue than Canada, very few use non-tax sources to the extent that Canada does. In 2001, all government revenues other than tax amounted to 9 percent of GDP in Canada, far outranking most other nations - only Sweden, Norway and the Slovak Republic collected more non-tax revenue as a share of GDP than Canada.

Compared to most OECD countries, then, Canadian governments rely on substantially more revenues derived from non-tax sources. The most important categories include resource revenues and profits from government enterprises and user fees, sales and fines which, taken together, accounted for more than 9 percent of GDP. When adding all other types of government revenues to tax revenues, Canada moves up to 14th among the 25 OECD countries and joins the ranks of an average European country; in fact, it has an even higher revenue-to-GDP ratio than the United Kingdom.

Part of the growth in non-tax revenues can be attributed to resource revenues, which have grown sharply due to oil-price shocks and increased provincial levies. However, Canadian governments have increasingly turned to other non-tax revenues to fund their activities.

Perhaps as a sign of the times, greater reliance on user fees is not surprising. Income taxes, the primary source of revenue, are highly distorting because they undermine incentives to work, invest and take on risk. User fees, which are payments for public services, are less distorting since Canadians contribute to the cost of specific services that are of benefit to them. Administrative fees, sales, fines and charges have increased 21- fold from 0.14 percent of GDP to 3.03 percent of GDP between 1975 and 2001.

However, Canadians have two concerns with user fees and other compulsory payments. For one thing, such fees are often raised by a monopolist - the government - without competitive pressure to keep the cost of public programs as cheap as possible. For another, some fees, such as student tuition costs, may be difficult for low-income Canadians to pay unless they are provided transfers or exemptions.

In 1966, after the introduction of most social programs in health care, public pensions, old age security and unemployment insurance, Canadian governments actually absorbed a smaller share of the economy, with tax and non-tax revenues at about 31 percent of GDP. This was similar to the United States, where the revenue-to-GDP ratio was 28 percent. However, since then, Canadian governments have grown faster and they now absorb almost 10 points more than the U.S.

So depending on the measure, Canada does look like a high tax collector when taking into account the substantial revenues that it raises from non-tax sources. Canadian governments do not have to tax as much to fund program services because they receive substantial resource and fee levies to pay for them.

Because Canadian governments still absorb over two-fifths of Canadian incomes to fund their programs, Canadians should ask them why they cannot reduce taxes and other levies to levels found in some dynamic economies like Ireland and Australia, which also have good social services, as well as those of our most important economic partner, the United States. And when politicians promise to raise, lower or keep taxes at their current levels, Canadians should remember that when it comes to raising revenue, governments are many-handed creatures - what they do not take in taxes they can take through several other means. They have done just that, with increasing zeal, over the past 30 years.

Table 1: *Government Sector Revenue, 2001*

	Total General Government Revenue	Total Tax Revenue	Difference
		% of GDP	
Sweden	61.7	51.4	10.3
Norway	58.3	43.3	15.0
Denmark	58.0	49.8	8.2
Finland	54.2	46.1	8.1
Austria	52.2	45.4	6.8
Slovak Republic[a]	51.4	34.9	16.5
France	50.9	45.0	5.9
Belgium	49.9	45.8	4.1
Netherlands	46.5	39.5	7.0
Italy	45.8	42.0	3.8
Greece	45.6	36.9	8.7
Germany	45.5	36.8	8.7
Luxembourg	45.4	40.7	4.7
Canada	**44.1**	**35.1**	**9.0**
Iceland	43.7	36.5	7.2
New Zealand[b]	43.4	35.5	7.9
Portugal	42.1	33.5	8.6
Czech Republic	41.5	38.4	3.1
United Kingdom	41.1	37.3	3.8
Spain	39.2	35.2	4.0
Australia[a]	36.4	31.5	4.9
Ireland	35.2	29.9	5.3
United States	34.7	28.9	5.8
Korea	32.3	27.2	5.1
Japan	31.9	27.3	4.6

Source: National Accounts of OECD Countries, Paris, 2003; and Revenue Statistics, 1965-2001, OECD, Paris, 2002.

a 2000.

b 1997.