Canadian Student Review

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SPRING 2021 QUARTERLY STUDENT MAGAZINE

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Dear Readers:

Spring is in the air, and we hope you are looking forward to an even more beautiful summer!

This issue features two of our student contributors. William Dunstan presents an interesting article on boutique tax credits and Brennan Sorge discusses the necessity for Canada to have a manufacturing sector. In addition to these two articles, this issue also highlights a recent infographic showing that Canada’s high tax rates are pushing many of its best and brightest innovators to leave for other countries. You’ll also find a video from the Fraser Institute’s Essential Austrian Economics series, “Interventionism.”

We’re also including a thought-provoking quote from Isabel Paterson, two exciting blog articles, and two more recordings from the Explore Public Policy Issues webinar series for your enjoyment.

If you or someone you know wishes to contribute content to the Canadian Student Review, please have them contact Daniela Castillo directly at Daniela.Castillo@fraserinstitute.org.

Regards,

Daniela and Ryan
BEWARE BOUTIQUE TAX CREDITS
WILLIAM DUNSTAN

A rule of thumb for crafting good tax policy is “lower the rates, broaden the base.” In other words, taxes should be as low as possible while applying to the widest range of economic activity as possible. So it’s disappointing that many “tax cuts” promoted by Canadian politicians in recent years are in fact targeted subsidies that actually do the opposite: shrink the base and raise the rates. Canadians should be wary of such boutique tax credits.

The term “boutique tax credit” refers to a tax expenditure—a subsidy delivered through the tax system in the form of deductions, credits, or other preferences—that targets a narrow group of people. Whether a particular tax expenditure fits this definition is a subjective judgment; however, there are several widely agreed upon Canadian examples of boutique credits. These include the Eligible Educator School Supply Tax Credit (EESSTC), through which educators receive a credit of up to $150 a year on out-of-pocket purchases of school supplies, and the former Public Transit Tax Credit (PTTC), which allowed regular public transit commuters to claim a 15 percent credit on transit expenses. There is also the former Children’s Fitness Tax Credit (CFTC), which offered parents up to $75 annually for enrolling their children in physical activity programs, along with various similar provincial credits that remain in place today.

Boutique credits unnecessarily complicate the tax system. This complexity raises costs for taxpayers by requiring them to spend more time completing their taxes, buy tax-filing software, or even hire tax professionals to ensure they don’t miss out on benefits. A 2014 Fraser Institute study found that use of at least one personal income tax expenditure, such as the PTTC or CFTC, increased taxpayers’ compliance costs by 20 percent on average (Speer et al., 2014). The administrative costs incurred when governments must process more complex files ultimately fall to taxpayers as well. Finally, tax complexity introduces intangible costs by reducing the tax system’s legitimacy in the eyes of the public. If people don’t understand the tax code, they are unlikely to perceive it as a fair system for raising revenue.

Boutique credits also tend to have regressive impacts. When the CFTC existed, Canadian parents in the lowest income quartile were half as likely to be aware that the credit existed and half as likely to have claimed the credit as those in the highest income quartile (Spence et al., 2010). This disparity is unsurprising considering that lower-income families are less able to afford organized physical activity programs or tax professionals who might alert them to the benefit. Of equal concern should be the lack of scrutiny applied to tax expenditures compared to that applied to direct spending programs through which these subsidies could alternatively be delivered. In 2015, the Office of the Auditor General of Canada concluded that insufficient information is provided on tax-based expenditures to support parliamentary oversight (OAG, 2015).
Given all these negatives, why do governments bother to craft such narrowly targeted tax expenditures? Boutique tax credits have two ostensible policy purposes: providing incentives for and rewarding desirable behaviour. Unfortunately, they are not very effective at either.

Most boutique tax credits are too small and obscure to influence behaviour. Rivers and Plumptre (2018) suggest that the PTTC was ineffective at reducing traffic congestion and greenhouse gas emissions, estimating that the credit increased public transit ridership by less than 1 percent. In line with similar studies, they estimate that public transit has a price elasticity of demand of -0.17, which in plain language means that lowering the cost of public transit does little to boost ridership.

According to a 2009 survey, only 55 percent of Canadian parents were aware of the CFTC in 2009, and just 26 percent claimed the credit for 2007 (Spence et al., 2010). The same survey found that fewer than one in six parents who claimed the CFTC believed that the credit had caused them to increase their children's participation in organized physical activity. These figures reveal another inefficiency of boutique credits: lots of people receive money for purchases they would have made anyway.

But perhaps it is alright that these tax expenditures do little to change taxpayers' behaviour. Some might argue that these expenditures should aim to merely reward individuals who make the “right, responsible choices.” The problem, though, with using boutique tax credits to reward good behaviour is that governments must define who is eligible, and these definitions inevitably exclude worthy individuals. Children can get as much exercise playing at the park with friends as they get playing little league. Yet nowhere in Canada can parents claim a tax credit for taking their kids to the park. Teachers who plan lessons while off work enrich their classrooms as much as those who buy school supplies out-of-pocket, but only the latter are eligible for the EESSTC. These arbitrary exclusions are inherent to boutique tax credits; no tax authority is capable of monitoring how often kids go the park much less what teachers think about during their idle time. Notwithstanding these practical barriers,
why should government strive to offer preferential tax treatment to those who make “good” personal choices? Just because something is nice to do doesn’t mean that the state should reward this behaviour.

A more cynical perspective is that boutique tax credits are purely political tools. Targeted tax expenditures can appeal to particular segments of the voting public without eliciting a negative reaction from those who are ineligible—few people will oppose “tax cuts” that promise to get kids outside and moving! Add in the aforementioned lack of parliamentary oversight and it becomes clear why politicians might favour boutique credits despite their practical shortcomings.

Whether a given tax expenditure is a simple vote-buyer or a sincere attempt at good policy, Canadians should be wary of promises to reward and encourage “good” choices via the tax system. Boutique credits deserve greater scrutiny for both their effectiveness and legitimacy as policy instruments. And if governments do choose to subsidize desirable behaviour, Canadians should demand that these subsidies be delivered through direct spending programs that can be subjected to adequate parliamentary oversight and that are designed to influence marginal decision-making without becoming a give-away to folks who already engage in these activities.

William Dunstan is a Public Affairs and Policy Management student at Carleton University. He has a passion for the power of markets to improve people’s lives and for developing policy that allows this to occur.

REFERENCES


ESSENTIAL AUSTRIAN ECONOMICS: INTERVENTIONISM

THIS VIDEO FROM THE ESSENTIAL AUSTRIAN SERIES, UNCOVERS THE UNINTENDED CONSEQUENCES THAT POLICY INTERVENTIONS CAN HAVE ON THE MARKET.
MANUFACTURING IN CANADA
BRENNAN SORGE

Over the past year, the COVID crisis has highlighted a variety of economic challenges. One of the most public and pressing has been the vulnerability of long and interdependent global supply chains, especially for essential health care products. In the early days of the pandemic, Canada experienced a lack of supply in personal protective equipment, beginning with masks. More recently, problems have affected the supply of vaccines for the country.

Canada relies on imports to secure these products, putting the supply chain under the partial authority of foreign governments. Over the past year we’ve seen firsthand that during a crisis many foreign governments are more than willing to reduce or even cancel exports of essential goods like masks and vaccines (Ballingall, 2021, January 26). Understandably, we are now hearing calls to improve domestic manufacturing and tighten Canada’s supply lines.

If Canada really does wants to build a stronger domestic manufacturing system, it will need to take a new approach. Some of the largest manufacturing powers, countries like China and India, rely on their vast, low-cost labour force, often further supported by lax pollution standards (World Population Review, 2021). Canada will never be able to compete on the basis of low-cost labour, or accept pollution standards that would risk public health and foul the environment. The traditional response to this problem would be for Canada to impose tariffs and introduce subsidies to protect Canadian industry. However, such tactics would result in the public paying more to cover the higher import costs and the added expenses of state subsidized industry. That outcome is far from a solution. If Canada wants to build its domestic industry successfully, it will need to find different advantages it can leverage to compete effectively.

There are a few strategies that Canada could use to improve domestic manufacturing. To counteract our competitors’ low-cost labour advantage, we can encourage the alternative of automated manufacturing. This approach would have a number of advantages. Automated manufacturing will produce fewer jobs than traditional manufacturing, but these jobs will likely require higher skills and involve designing equipment and software, or maintaining and servicing equipment that is already in use. Most importantly, automated manufacturing can increase productivity, which would enable Canada to compete with foreign manufacturers.

Actively encouraging the adoption and use of these technologies will require some policy changes.

First, Canada needs to be more hospitable to manufacturing in the first place. Currently, regulatory costs on business can reach well into the thousands of dollars per employee (Cruz, 2021, January 25). Beyond just the monetary aspect, delays to projects, and hours spent on regulatory compliance rather than productive work all carry costs. Building up Canadian manufacturing would certainly be easier if these costs were lessened. In order to do so, government needs a strategy to reduce both the cost of regulation, and the time it takes for approvals to be reached.

Canada also has a few advantages it can leverage to build a strong domestic manufacturing industry. Manufacturers need reliable access to raw materials,
which Canada has in abundance. With regulatory changes in place, Canadian resource industries may become more vibrant as well, which would be a strong aid to domestic manufacturing (Aliakbari and Yunis, 2021). Canada is also highly sought after by immigrants, which is a major benefit in cutting-edge industries like automated manufacturing. It is essential that Canada change its immigration policies to encourage those with the skills needed to build this country’s manufacturing to move to Canada. The change should not be difficult given Canada’s skills-based immigration system.

Canada can also improve the way it treats investment. Building a robust domestic manufacturing industry will require substantial investment, which Canada has struggled to attract over the last few decades (Cross, 2017). To encourage investment, Canada could begin by adjusting business tax laws to promote domestic investment as an alternative to moving capital abroad. Countries like Ireland and Estonia already have similar systems that Canada could use as a model. Government could also work with financial institutions to ensure new and growing Canadian companies have access to capital markets.

Canada has real advantages that it could use in building its domestic manufacturing, including being resource rich and a global leader in attracting skilled immigrants. Our greatest disadvantage is our high labour costs, which can be mitigated with the use of automation technology. However, the advantages we have will require real policy change if they are to be used to their full potential.

**REFERENCES**


Brennan Sorge is currently an economics and business student at Thompson Rivers University. His interests centre on the effects of law and policy on the economy, and he hopes to act on these interests in further study of both economics and law.

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TAX REFORM SHOULD PLAY CRUCIAL ROLE IN COVID RECOVERY

ALEX WHALEN AND JAKE FUSS

While the COVID-19 pandemic continues, the focus will eventually turn more fulsomely to ensuring a robust economic recovery. Decisions about taxes will play a key role as governments grapple with large amounts of new debt from COVID-related spending. While the federal government may want to raise taxes as we emerge from the pandemic, it should be fully aware of the consequences of doing so.

Among the many taxes in Canada, business taxes, personal taxes, and capital taxes are especially important for economic growth. Among other things, these taxes affect incentives to invest, innovate, and start new businesses. They also affect Canada’s ability to attract foreign investment, top scientists, and other highly skilled professionals. Hence, these activities remain crucial to the growth of productivity and the incomes of Canadians.

Unfortunately, as noted in our new analysis, “Increasing Productivity Through Tax Reform” from the collection *Achieving the Four-Day Work Week: Essays on Improving Productivity Growth in Canada*, Canada’s current tax structure is out of step with comparable countries in many areas. With regard to business income taxes, Canada fared relatively well compared to its OECD peers as recently as 2017. However, its position has since deteriorated and Canada now has the 10th highest corporate tax rate (out of the 36 OECD countries). For capital gains taxes, Canada currently ranks below average and risks being among the highest-taxed countries if rumoured government changes to the tax are implemented.

Worse yet, Canada has the seventh-highest top combined (federal and provincial) personal income tax rate in the OECD. Several provinces currently have top combined tax rates exceeding 50 percent, which is substantially higher than the majority of US states and most other OECD countries.
Not all taxes are created equal. Business, personal, and capital taxes are the more productivity-damaging types of taxation when compared to consumption taxes such as the GST. In fact, Canada relies relatively more heavily on these more damaging forms of taxation than most other OECD countries.

Rather than simply raise taxes as a part of the recovery plan, Ottawa should consider structural reforms of the tax system. Specifically, it should make Canada’s tax rates more competitive for investment in physical and human capital with other countries and US states.

Finally, several recent public opinion surveys have highlighted an appetite among Canadians for a four-day workweek. If government reduced high marginal tax rates and shifted more of the tax burden towards consumption rather than production, it would promote productivity growth and higher wages, which in turn would enable Canadians (over time) to achieve a four-day workweek. Indeed, research has found that a four-day workweek would be economically feasible if governments pursue policies that improve productivity growth (i.e., policies that encourage investment, entrepreneurship, and innovation). Getting Canada’s tax structure right is key to creating the conditions for this opportunity.

As Canada works toward an economic recovery from COVID, crucial decisions will be made on tax policy. To attract investment, people, businesses—and potentially unlock a four-day workweek—the federal government must address Canada’s status as a high-tax jurisdiction. ◆

Read the blog post here.
Canada’s uncompetitive tax rates hinder investment, entrepreneurship, and innovation and make a four-day work week less likely.
FREEDOM IS DANGEROUS. POSSIBLY CRAWLING ON ALL FOURS MIGHT BE SAFER THAN STANDING UPRIGHT, BUT WE LIKE THE VIEW BETTER UP THERE

— ISABEL PATERSON
Recently, COVID-19 claimed another life—Rosine Chouinard-Chauveau, a 28-year-old actress in Montreal. However, her name will likely not be counted among COVID mortality numbers because she did not die from the virus. Rather, she died waiting for surgery for an undisclosed health issue.

According to a statement from Chouinard-Chauveau’s family, the surgery “could not take place on time due to the délestage in the health system to handle the pandemic.”

While many Canadians may be unfamiliar with the term, they’ll understand the concept. Délestage, in this context, refers to the cancelation or postponement of surgery and other medical treatments in anticipation of COVID caseloads. According to the Quebec government, an estimated 140,000 patients are waiting for surgery in the province, with nearly 44,000 having already waited more than six months.

To be clear, Quebec’s backlog is not unique to the province. In fact, across Canada, provincial health ministers made the difficult decision to cancel thousands of elective surgeries to ensure our scarce medical resources would be available for new COVID cases. The good news is provinces such as British Columbia have significantly reduced their COVID-related backlogs by increasing surgical capacity, partnering with private clinics and hiring new staff. However, despite the progress, BC’s government still reported 88,401 patients waiting for treatment in Nov 2020.

So what’s going on?

While COVID-19 has exacerbated challenges in the health care system, Canada has been rationing care for years. In fact, according to estimates published by the Fraser Institute, more than one million patients endured a median wait of 20.9 weeks for medically necessary elective care in 2019—long before COVID. Sadly, as families across the country know too well, these wait times can have serious consequences. Some patients may be in pain or unable to work while those less fortunate may experience a permanent deterioration of an otherwise treatable condition. And in the worst cases, patients may pay the ultimate price. A recent report suggests that at least 1,480 (and maybe as many as 3,841) surgeries were cancelled in 2018-19 because the patient died while waiting for care. And remember, that’s in the pre-COVID world.

Moreover, doctors across Canada increasingly indicate our current délestage approach to health care is extending beyond “elective” treatments (hip surgery, for example) to more critical areas such as cancer care and cardiovascular surgery where delays can be fatal. And when Canadians seek private alternatives within our borders, they run into provincial restrictions. In fact, Canada’s unique and restrictive approach to universal health care stands in stark contrast to other, arguably better-performing, universal health-care countries.

And just to be clear, today’s surgical backlogs (and other problems with Canada’s health care system) are not the result of inadequate funding. Canada ranks among the most expensive universal health care systems in the world yet has fewer physicians, beds, and diagnostic imaging scanners (such
as MRI machines and CT scanners) than comparable universal health care countries such as Switzerland, the Netherlands, Germany and Australia. And of course, we also have some of the longest wait times.

Our health care workers have done an incredible job during this pandemic, and in the absence of long-term data, health care officials had to make difficult choices in anticipation of COVID-19’s potential impact. But as the cost of these decisions adds up, and with new COVID-19 variants on the horizon, we may need to reassess the costs and benefits of our current approach to better optimize care for all Canadians—not just COVID patients. Or at least allow Canadians to access private alternatives. Not only would this help those specific patients, but it would also potentially reduce the strain on our overburdened public system.

Rosine Chouinard-Chauveau’s tragic story has shone a new light on an old problem; one that has been exacerbated, but not caused, by COVID-19. While it will take significant reform to address the routine rationing of care in our health care system, governments across Canada can no longer ignore the many non-COVID patients who’ve paid a heavy price since the pandemic began.

Bacchus Barua is Associate Director of the Fraser Institute’s Centre for Health Policy Studies. He completed his BA (Honours) in Economics at the University of Delhi (Ramjas College) and received an MA in Economics from Simon Fraser University. Bacchus has conducted research on a range of key health care topics including hospital performance, access to new pharmaceuticals, the impact of aging on health care expenditures, and international comparisons of health care systems. He also designed the Provincial Healthcare Index (2013) and is the lead author of The Effect of Wait Times on Mortality in Canada, and Waiting Your Turn: Wait Times for Health Care in Canada (2010–2014).
Enviropreneurs in Action
Holly Fretwell

Enviropreneurs, or environmental-entrepreneurs, are innovators who seek to do well (earn a profit) by doing good (enhancing the environment). This free market approach to environmentalism is based in property rights and demonstrates how we can live in a freer, cleaner, and more prosperous society. Holly Fretwell examines several case studies of enviropreneurs in action to show how markets improve environmental outcomes across the globe.

Link to Holly Fretwell Recording

Building a Sustainable and Resilient Indigenous Economy
Manny Jules

COVID-19 has revealed some difficult health, economic, and fiscal lessons for First Nations. Many have seen their public health outcomes worsen. Many First Nation economies declined more and most First Nation governments did not have the tax bases or fiscal powers to be resilient. Chief Commissioner of the First Nations Tax Commission Manny Jules presents a proposal for building a more sustainable and resilient First Nation economy supported by a competitive investment climate, more fiscal independence, and indigenous institutions and standards.

Link to Manny Jules Recording
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