

FISCAL POLICY

Let buck stop with provinces, C.D. Howe urges

Give them more say on taxes, spending

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Canada's fiscal imbalances would be resolved if Ottawa cut the GST and income tax, scaled back transfers to the provinces, and left the provinces more leeway to tax and spend, a study says.

"Under this approach, regional tastes gain more influence over how, and how much, provinces tax and spend," says the paper by Finn Poschmann and Stephen Tapp at the C.D. Howe Institute.

"And with the overall tax mix becoming economically smarter, Canadians' capacity to build their incomes and wealth would fare all the better."

Canadian taxpayers give the federal government about \$40-billion every year that goes toward cash transfers to the provinces, the study points out.

But the provinces are constantly complaining that the money is insufficient, or that it has been distributed unfairly. Plus, the provinces are facing higher health care and social program costs, prompting loud demands for more cash from Ottawa, the study says.

And since Ottawa is partly paying for many of the services provinces deliver, the public does not know who to turn to when something goes wrong. Complaints to a provincial government about health care, for example, are passed on to the federal government since it is responsible for funding. But Ottawa, in turn, blames the provinces for poor delivery of services.

"The voter has nowhere to turn in this endless loop," Mr. Poschmann said in an interview.

The best way to address the imbalances and designate accountability to the government that delivers services is for Ottawa to initiate a major rebalancing of taxation, he argues.

"The first mover is the federal government, which has plenty of room to lower taxes and to lower the GST," he said. "The federal government collects more money than it knows what to do with."

The tax cuts should be tied to either a freeze or even a rollback in the amount of money Ottawa transfers to the provinces. The federal government should reduce its role in health care and other social programs, and focus mainly on improving equalization transfers, to make sure all provinces have the wherewithal to deliver equally good social services, the C.D. Howe argues.

Mr. Poschmann concedes that no such changes would ever be floated during an election campaign. Conservative Leader Stephen Harper has proposed a cut in the goods and services tax, but stopped well

short of proposing a thorough tax reform, and would never dare breathe a word of cutting transfers to the provinces, he said.

But Mr. Poschmann does think that such reform will become imperative over the next decade or so. With the population aging, and demand on social services becoming more costly, tax reform will be an obvious goal, he said.

For the public, the result would be an unchanged level of taxation, with a more efficient and more accountable system for delivering social services and government programs, Mr. Poschmann said.

Such a plan may make sense from an economic point of view but would be very difficult to carry out on a political level, said David Perry, senior research associate at the Canadian Tax Foundation.

When the federal government cuts taxes, he said, it demands political credit for its moves -- whether or not the provinces are expected to pick up the slack. That would create friction with the provinces. And few governments want to be seen cutting funding for services, Mr. Perry added.

Still, he believes the C.D. Howe plan eventually will become a reality, "not as a deliberate policy, but as an evolution." As fiscal demands on the provinces grow, Ottawa's riches will appear excessive, and a rebalancing of taxes will become both a political and economic necessity, he said.
