

# The Tax You Really Pay

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The first question people ask about Canada's tax system is: how much tax do I *really* pay? Thirty years ago, average Canadians would have had a difficult time answering the question. In 1975, however, The Fraser Institute embarked on a project to find out how much tax, in all forms, Canadians pay to their respective federal, provincial, and local governments. In 1976, the Institute published *How Much Tax Do You Really Pay? Your Real Tax Guide*. It was a non-technical, do-it-yourself manual that enabled average Canadians to calculate the amount of tax they really paid. Last month, we released the thirteenth edition of that book, now entitled *Tax Facts*. Although the series has undergone many changes and now contains much more detail than the original publication, most of the core features remain. What follows are highlights from *Tax Facts 13*.

## The not-so-obvious taxes

Most Canadians would have little difficulty determining how much *income* tax they pay; a quick look at their income tax return or pay stub suffices. The amounts they pay of other prominent, direct taxes, such as Employment Insurance (EI), Canadian Pension Plan

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(CPP) premiums, and property taxes are also relatively easy to determine as they are either deducted from workers' pay cheques (EI and CPP) or assessed annually (property taxes). However,

most people are unaware that the direct taxes listed above account for less than half of their total tax bill.

A host of other taxes exist that are not as obvious to most Canadians. The first of these is sales taxes. While Canadians are painfully aware of sales taxes, calculating the amount they pay requires people to track all of their purchases of taxable goods and services. The second class of taxes of which Canadians are largely unaware are built into the price of goods and services. The most significant of these "hidden" taxes are import duties, excise taxes on tobacco and alcohol, amusement taxes, and gas taxes. Finally, most Canadians are unaware that they ultimately pay the employer's portion of payroll taxes such as EI and CPP premiums and other taxes levied on corporations. In other words, although businesses pay these taxes directly, the cost of business taxation is ultimately passed back to the employees on whose behalf they were paid.

In 2003, the average Canadian family earned an income of \$58,782 and paid total taxes equaling \$27,640. Of that total tax bill, income taxes accounted for only 32 percent, or \$8,887 (table 1). Sales taxes, social security taxes, and a host of other taxes accounted for the other two-thirds of the tax bill.

## The Canadian Consumer Tax Index

*Tax Facts 13* updates the Canadian Consumer Tax Index (CCTI) which tracks how the total tax burden of the average



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**Table 1: Tax Bill of the Average Canadian Family, 2003**

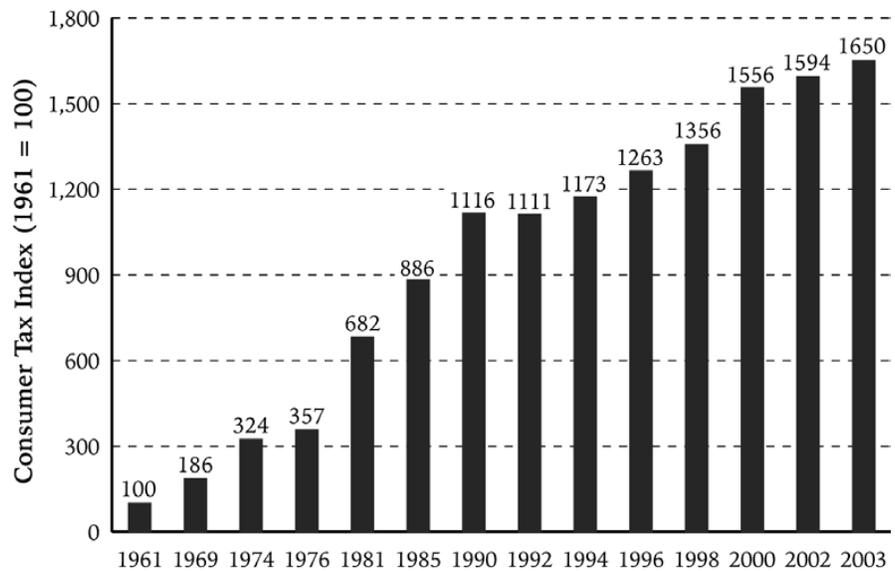
Total cash income	\$58,782
Taxes	
Income taxes	\$8,887
Sales taxes	4,507
Liquor, tobacco, amusement, and other excise taxes	1,772
Auto, fuel, and motor vehicle licence taxes	733
Social security, medical, and hospital taxes	5,659
Property taxes	2,375
Import duties	241
Profits tax	2,556
Natural resource taxes	333
Other taxes	578
<b>Total taxes</b>	<b>\$27,640</b>
Taxes as a percentage of total cash income	47.0%

Source: The Fraser Institute's Canadian Tax Simulator, 2003.

Canadian family has changed since 1961.<sup>1</sup> The value of the Canadian Consumer Tax Index for 2003 is 1,650, which indicates that the tax bill of the average Canadian family has increased by 1,550 percent since 1961 (see figure 1).

The dramatic increase in the CCTI from 1961 to 2003 was produced by the interaction of a number of factors. First, there was a dramatic increase in incomes over the period and, even with no change in tax rates, the family's tax bill would have increased substantially. In 1961, the average family had an income of \$5,000 compared to \$58,782 in 2003; this increase in family income alone would have produced a 1,076 percent increase in the tax bill from 1961 to 2003. The second contributing factor was an increase in the effective tax rate

**Figure 1: The Canadian Consumer Tax Index, 1961-2003**



Source: The Fraser Institute's Canadian Tax Simulator, 2003. Figure 4.1 from *Tax Facts 13*.

faced by the average family from 33.5 percent in 1961 to 47.0 percent in 2003.

To gauge the significance of the increase in the tax bill, contrast its evolution with other major expenditures of the average family. Figure 2 compares the total tax bill of the average family with spending on such basic needs as food, clothing, and shelter. It is clear from figure 2 that taxes have grown much more rapidly than any other single expenditure item. Taxes rose by 1,550 percent from 1961 to 2003. Meanwhile, expenditures on shelter increased by 936 percent, food by 460 percent, and clothing by 416 percent.

What benefits do families receive for their taxes? Did the average family's returns from government spending increase by as much as the tax bill? While it is relatively simple to calculate how the various governments spend a Canadian's tax dollar, doing this calculation does not answer the questions above. Whether or not our own per-

sonal benefits from government have increased relative to the rapidly increasing price we pay (taxes) is a question each of us can only answer for ourselves. For this reason, *Tax Facts* does not discuss the benefits that government spending creates.

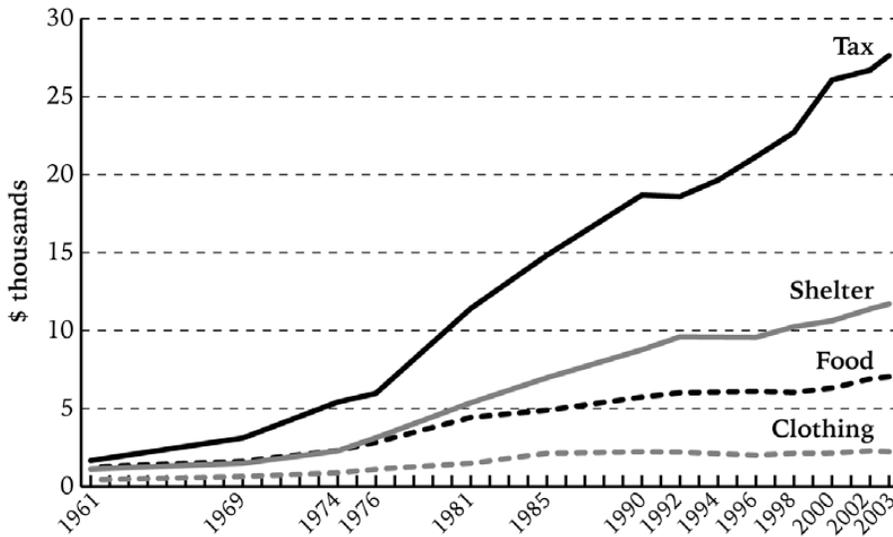
### The relative tax burden

The next thing Canadians want to know is how much tax other people are paying. That is, how fair is the tax system? Are some people paying more or less than others?

To answer that question, *Tax Facts* examines the relative income and tax position of Canadians. To that end, families are arranged from lowest to highest according to their income; 10 percent of the families with the lowest incomes make up the first of 10 income groups called deciles. The second income decile represents the next 10 percent of families, and so on. Finally,



**Figure 2: Taxes and Basic Expenditures\* of the Average Canadian Family, 1961- 2003**



\*All expenditure items include indirect taxes  
Source: Figure 4.4 from *Tax Facts 13*.

three broad income groups are created based on the income deciles. The lowest income group includes all of the families in the bottom three deciles; the middle income group includes the next four deciles; the upper group includes the top three deciles.

Table 2 shows the distribution of income and taxes for selected years. In 2003, the top 30 percent of families earned 59.0 percent of all income in Canada and paid 65.6 percent of all taxes. The bottom 30 percent earned 8.1 percent of all income and paid 4.3 percent of all taxes. Who belongs to the club of the top 30 percent of Canadian families? A family is included in the top 30 percent when its cash income exceeds \$73,016. The average family income in this group is \$122,882.

It is important to note that the figures presented in table 2 give only a snapshot of the number of Canadians who fall into various income groups at one time. Most families' incomes change over

time. Most young people start out in the low-income group and work up to the middle or high-income group. Given their initial lack of experience, their incomes start out low. Their incomes peak when they hit middle age, the prime earning years, and then begin to fall as they approach retirement. In other words, there is not a permanent underclass stuck in low income in Canada.

Statistics Canada's Survey of Labour and Income Dynamics has tracked just how much a family's income changes over time. Households in the survey were ranked based on their incomes and divided into five equal groups. The bottom group represents the 20 percent of families with the lowest incomes and the top group represents the 20 percent of families with the highest incomes. Over a five-year period, nearly 29 percent of all families moved up at least one group in earnings. More importantly, a total of 45 percent of those families in the bottom 40 percent of families (those in the bottom two groups) moved up at least

one group over the five-year period of the study.

### The rags-to-riches tax burden

The above discussion demonstrates how progressive our tax system is and how it imposes ever-increasing burdens on people as they earn more income. What about an individual who had started off in 1961 with meagre earnings and had worked his way up the ranks of income earners? What kind of message does our tax system send to this person? To answer these questions we created a hypothetical situation—a Canadian whose income grew from half of the average income in 1961 to double the average income in 2003.

This fictitious Canadian earned \$2,750 in 1961 and paid a total of \$960 in taxes. During the next 42 years his income grew steadily and at such a rate that by 2003 he was earning \$116,513 a year

**Table 2: Distribution of Income and Taxes**

Year	Income Groups		
	Lower 3 deciles (%)	Middle 4 deciles (%)	Upper 3 deciles (%)
<b>Decile distribution of income before tax (%)</b>			
1961	10.8%	35.6%	53.6%
1992	7.6%	31.7%	60.7%
2003	8.1%	32.9%	59.0%
<b>Decile distribution of taxes (%)</b>			
1961	8.7%	30.6%	60.9%
1992	3.9%	28.5%	67.6%
2003	4.3%	30.1%	65.6%

Source: The Fraser Institute's Canadian Tax Simulator, 2003.

(double the average 2003 income) and paid taxes amounting to \$61,083. While the income of our hypothetical person increased by 4,137 percent from 1961 to 2003, the amount of taxes he paid increased by an astonishing 6,263 percent.

## Conclusion

For all the money that Canadians pay to government, most know little about the Canadian tax system. *Tax Facts 13* was created to provide Canadians with basic knowledge about their taxation system. Within its pages is a simple tool that will help Canadians discover how much tax they really pay. It takes a few calculations, but arriving at the final result requires only a few minutes. Taxation is the most significant economic aspect of Canadian's lives. Can we afford not to know how much tax we really pay?

## Notes

<sup>1</sup>The CCTI does not track a particular family's tax burden from 1961, but rather the tax burden of a family that was average in each year.

## References

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