Analysis of the 2006 Federal Budget: A Disappointment for Ordinary Working Families

Introduction and Summary

Today's federal Budget falls short of what working families had in mind when they voted for this Parliament.

The Conservatives promised to govern in the interests of ordinary working families. But this is a Budget which stresses tax cuts and security issues over virtually all other priorities, and undercuts the ability of the federal government to make a positive difference in people's lives through social programs, over the long-term.

Essentially, the Conservatives have adopted the Liberal government's income tax cut, and added cuts to the GST and to business taxes. They clearly propose to leave most important areas of social spending to the provinces. Adding it all up, the Budget marks a significant retreat from the active leadership which is needed to create a more equal and caring Canada.

It is particularly frustrating that the new Conservative government has ignored the many voices calling for continuation of one of the key gains from the last minority Parliament - promises of a long-term investment to finally develop a national child care and early childhood education program.

Securing access to high quality, affordable, child care is the first priority of working families, and children, and working parents will be the losers from the decision to scrap this promising new program after this year.

The new Conservative child care plan will not create the kind of spaces we need, will not create enough spaces, and will not give the best start in life to many of our children. It will, therefore, not give working families the ability they seek to properly balance their employment and family responsibilities.

As expected, the Conservatives have introduced a $1,200 benefit for parents of children under age 6, taxable in the hands of the lower-earning spouse. They have slightly modified a flawed proposal by ensuring that refundable child tax and GST credits based on family income will not be reduced as a result. However, the maximum benefit will still go only to families with a stay-at-home parent, and working single parent and dual earner working families will get much less.

The huge federal government surplus of almost $18 billion in the coming fiscal year would have allowed the Conservatives to implement their major promises like reducing the GST while also continuing the key gains of the last Parliament for working people: child care; investment in education and training; and investment in the environment and community infrastructure.

While many of the gains from Bill C-48 - the NDP-Liberal budget deal of last year - are preserved through trust funds for the provinces to spend on higher education, affordable housing, environmental infrastructure and transit - these are only short-term measures. Over the longer-run, the government has set the stage for continuing spending cuts to match the revenues lost through their tax cuts.

Federal program spending will decrease as a percentage of GDP from 13.7% in 2004-05 to 13.0% in 2007-08. The government will not proceed with the $7 billion over five years in spending proposals announced in the Economic and Fiscal Update. The growth of program spending will be kept below the rate of growth in the economy.

Tax cuts plus some new spending initiatives are to be funded in part through an immediate cut to federal program spending by $1 billion this year, and another $1 billion next year. Details are unavailable but much of the impact will likely fall on support for civil society and advocacy organizations. A much more extensive process of program review has been launched to balance the books and, perhaps, increase transfers to the provinces, over the longer term.

On the spending side, the government has all but turned its back on the Kelowna Accord with aboriginal peoples, promising only modest funding for housing. And funding for implementation of a Kyoto implementation climate change plan has been withdrawn, with no details available on a promised alternative.

The new training agreements with the provinces announced in the 2005 Budget - which have been already translated into Labour Market Partnership Agreements with Ontario, Saskatchewan and Manitoba - are not funded in this Budget. We are left only with vague promises of consultations with the provinces on how to fund workplace skills training, literacy and immigrant settlement, notwithstanding the emergence of major skills shortages in many parts of our economy and major ongoing labour adjustment challenges.

One danger is that a softer economy would require even deeper cuts, since this Budget appears to contain only a modest surplus moving forward. Like the Liberals, the Conservatives will continue to pay down debt to the tune of $3 billion per year.

We are concerned that, looking forward, the federal government intends to leave too much to the provinces, and that this will widen regional disparities and weaken opportunities for working people. We have to be very careful that talk of a new partnership with the provinces does not translate into abdication of responsibility to set a broad national framework and a floor of services in important areas of shared responsibility, such as health, training and environmental infrastructure. (The CLC will respond later to the paper on fiscal relations released with the Budget.)

A Focus on Tax Cuts

The decision to go beyond the GST cut to announce further personal and corporate income tax cuts is troubling because it will significantly shrink the future fiscal capacity of the federal government. As a share of the economy, total federal revenues will fall from 16.4% of GDP in 2004-05 - the year before last year's Liberal income tax cuts - to 15.5% in 2007-08. That 0.9% of GDP sounds small but amounts to more than $10 billion in lost revenues each year. Cutting the GST by 1% reduces revenues by about $5 billion alone.

The centre-piece of this Budget is tax cuts. Originally, the Conservatives promised to cut the GST from 7% to 6% (and later to 5%), financed by ending the Liberal personal income tax cuts of November, 2005. (These were made retroactive to all of 2005, in the expectation that tax refund cheques would be arriving just in time for a planned 2006 election.)

In the event, the Conservatives have cut the GST by 1% effective July of this year, as promised, and have also preserved almost all of the Liberal tax cut. In a complicated set of changes, the basic personal income tax rate is to be raised from 15% to 15.5% (this is paid on income up to about $37,000 per year), and the basic personal exemption on which no tax is paid (now close to $9,000) will not increase by quite as much in the short-term as under the Liberal plan. But, the Budget introduces a new Employment Credit (worth 15% of $500 rising to $1,000 per year - or about $150) when fully phased-in.

The net result is that a bi-weekly pay cheque will fall very slightly for the rest of 2006, reflecting an increase of about $4 in federal income tax every two weeks compared to right now, or about $100 per year, with 2007 almost a wash. Cleverly from a political perspective, there are no further personal income tax cuts for high income earners as had been rumored, and this Budget is being sold as one providing tax cuts for ordinary working families. The government even promises to continue the Liberal promise to develop a new tax credit for the working poor. (Urban transit users will also benefit from a tax credit for transit passes, and there will be tax credits for children's sports fees plus small other tax measures for children with disabilities, students and others.)

Business tax cuts are much smaller than personal tax cuts, but small businesses get a rate cut, the minimum tax on the banks is cut, dividends received by corporations get more favorable tax treatment, the capital tax on large corporations is eliminated ahead of schedule, and, down the road, there will be cuts in the general corporate tax rate, from 21% to 19%, phased in from 2008. In this fiscal year, total business tax revenues will be reduced by about $1.4 billion. In essence the Conservatives have adopted and somewhat speeded-up the Liberal business tax-cut agenda which had been temporarily derailed by the NDP.

The CLC has long argued that across-the-board cuts to the corporate income tax rate are not the way to go, since much of the benefit will go to the already highly profitable bottom-line of the banks and energy companies. A better alternative would be to directly support job-creating new investments in machinery and equipment and in environmental upgrading. The Budget is almost irrelevant to the hard-pressed manufacturing sector, even as the dollar soars past the 90 cent mark.

Child Benefits and Child Care

As expected, the budget allocates $3.7 billion over two years for income support for parents. The Conservative's "Universal Child Care Benefit"(UCCB) will allocate $100 per month for each child under six, effective July 1, 2006. The income supplement will be taxable in the hands of the lower earning parent, but will not affect federal income-tested benefits. The Child Tax Benefit under-7 supplement will be eliminated.

The UCCB will not reduce the amount that can be claimed under the child care expense deduction. Neither will it reduce benefits that can be claimed under the Canada Child Tax Benefit or the goods and services tax benefit. The UCCB will cost $1.6 billion in 2006-07 and $2.1 billion in 2007-08.

With respect to child care, $650 million will be allocated to all provinces and territories on a per-capita basis this year. This slightly modifies the terms of the agreement, by including territories.

Next year the current agreement will be scrapped and just $250 million for new child care spaces will be allocated on the basis of grants or tax credits. This allows tax-exempt organizations to participate in the program.

Training and Better Jobs

When it comes to investment in more and better jobs, it is disappointing that federal funding for training and immigrant settlement programs will not be increased in line with the promises of a $3.5 billion investment over five years in the 2005 Economic Statement. This leaves the provinces to deal virtually alone with the challenges of workplace training, literacy, and skills upgrading for new immigrants.

However, the Conservatives have delivered on promises to support apprenticeship programs by providing a $2,000 per year credit to employers per apprentice hired (for the first two years), plus a $1,000 per year tax credit to apprentices who enroll in a Red Seal program. Many observers think the money would be better spent rewarding employers with employees who complete apprenticeship programs. There will also be a $500 tax deduction for tools. The government promises to consult on apprenticeship support, as well as on establishment of the promised new Agency to assess the credentials of new immigrants.

Modest but welcome promises are made to support restructuring of the hard-hit forest industry and to re-launch an older-worker adjustment program following further consultations.

Post Secondary Education

In the area of post-secondary education, the budget confirms a one-time allocation of $1 billion for infrastructure investment, as negotiated in the NDP-Liberal budget deal of 2005. Other than this, the Conservative budget eliminates all the improvements proposed by the Liberals last November to increase access to post-secondary education. This includes an additional $2.2 billion over five years for the Canada Student Loans Program, to increase grants, loans and debt management measures; $550 million to cover up to four years of undergraduate study for low-income students; and $210 million for graduate level scholarships. The Budget does, however, propose to expand eligibility for Canada Student Loans by reducing the expected parental contribution.

Essentially what this amounts to is increased debt loads for those choosing to study, and in the longer term, a Canadian workforce less equipped to compete in knowledge and innovation based fields.

Health Care

The government continues with funding allocations contained within the ten-year federal-provincial/territorial health care accord. The budget also allocates $460 million over two years for pandemic preparedness. Except for $52 million allocated annually to the Public Health Agency and Health Canada for cancer research and coordination among institutions, there is no new money added to health care. The Wait Times Guarantee has no money attached to it. Although this government positions itself as increasing accountability, there is no requirement that provinces must disclose the amount of public money spent in private health care.

Pensions and Retirement Security

On pensions, the government has followed through on its election promise to double the federal pension income tax credit to $2,000, which applies to income from RRSPs and employer pension plans but not CPP and Old Age Security benefits. Changes are also proposed to funding rules for defined benefit plans in the federal jurisdiction. These envisage making it easier for plan sponsors to address funding shortfalls, subject, in some cases, to agreement with plan members and retirees.

Among the options considered are approved letters of credit to cover solvency deficiencies (debt) in pension plans, and extending the current five-year payment schedule by an additional five years with the agreement of the federal regulator. Pension plans from crown corporations will be automatically eligible to extend payment of solvency deficiencies for an additional five years. All of these measures allow pension plan sponsors to forestall payment of debt, but they are pinned on the hope of steady increases in interest rates going forward. Nothing in this budget guarantees pensions will be fully-funded in the long run.

Lastly, on public pensions, the government will consider allocating a portion of any yearly surplus over $3 billion to the Canada and Quebec Pension Plans. The government promotes this as a measure to defray the cost of CPP/QPP contributions for younger Canadians, and to make both state pensions "economically competitive". What remains unaddressed with this announcement, however, are any measures to improve the quality of benefit levels provided by the CPP and QPP. Recent studies have confirmed that most elderly Canadians depend on public pensions as their primary source of income, but benefit levels remain below (or closely around) the poverty line.

Military Spending and Overseas Development Assistance

The Department of National Defence (DND) - and the arms industry - were big winners in this budget.

In 2004, DND had a budget of about $13 billion. On top of this base amount, the 2006 federal budget announces a $5.3 billion increase in annual military spending over five years, and this after the 2005 federal budget allocated had already added $12.8 billion to be spent over five years.

Where is this new DND money going? The government claims a variety of areas, from defending arctic sovereignty to preparing for natural pandemics. If DND's 2005 Defence Policy Statement is any guide, however, it will also go into Canada's growing support for the US military operations. DND's latest annual report indicates new recruits are urgently needed to focus on "failed and failing states", and to "root out security problems" before they attack Canadian targets.

On overseas development assistance, the Conservatives have pledged an additional $320 million for development aid (though this money is contingent on current levels of government surplus remaining constant). These funds will be targeted towards alleviating disasters caused by AIDS, polio, and financial crisis caused by natural disasters in countries with International Monetary Fund loans. While the $320 million is certainly welcome, it falls well short of the target set by the global Make Poverty History campaign (0.7% of the government budget).

Communities

The budget reduces the Permanent Residence Fee for new immigrants from $975 to $490 and provides minimal increases in funding for settlement, as well as establishing a new Agency to promote the recognition of foreign credentials.

While the November 2005 Kelowna Agreement promised $5.1 billion over five years for Aboriginal peoples, this budget allocates only $150 million in 2006-07 and $300 million in 2007-08. A further one-time payment of $300 million will be allocated to off-reserve housing. Another $300 million will be allocated to housing in the North. Both of these will be placed in a trust for the provinces and territories and allocated only if budget surpluses exceed $2 billion.

Urban and Environmental Infrastructure

The budget allocates some new money to existing federal infrastructure funds.

This includes the $1.3 billion in Public Transit Capital investments which was previously committed in Bill C-48. The budget also introduces a tax credit for the purchase of monthly public transit passes. This measure will cost $150 million in 2006-07 and $220 million in 2007-08.

Two new infrastructure programs include the Highways and Border Infrastructure Fund ($2.4 billion over five years), and the Canada

Pacific Gateway Initiative ($591 million over eight years) aimed at improving infrastructure for international trade.

New funding for existing programs includes the Canada Strategic Infrastructure Fund which provides for an additional $2 billion over four years starting in 2007. As well, the Municipal Rural Infrastructure Fund will receive $2.2 billion in additional funds over five years. The gas tax funding commitments previously allocated will be delivered upon. The budget allocates $7.1 billion over next four years under the New Deal for Cities and Communities agreements.

Affordable Housing

The budget provided $1.4 billion for affordable housing to be spent by the provinces over the next three years, down from the $1.6 billion announced as part of Bill C-48 last year. The one time funding is expected to assist in the development of 20,000-30,000 units. A $500 million housing retrofit program for low-income households program will not proceed.

Conclusion

In conclusion, this is very much a Conservative Budget. It sticks very closely to promises made in the election. The only big surprise is the extent to which Liberal income tax cuts were preserved. The scale of the tax cuts will make it impossible to make significant future social investments, particularly if the economy weakens. Spending cuts much deeper than those acknowledged in the Budget will likely be required to square the circle. The intent to devolve responsibility for social programs to the provinces is clear, as is the intent to ramp up the federal government’s security role.

For ordinary working families, the budget provides small tax cuts and a new child benefit for those with young children. This comes at the cost of what we have lost - a national child care and early learning program, and major new investments in training and environmental sustainability.

These choices will dominate political debate in the months ahead.

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