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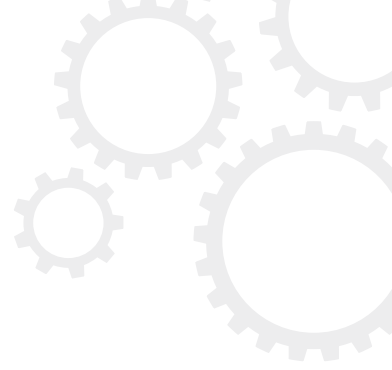
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# PAYING FOR THE RECOVERY WE WANT

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BY

Alex Himelfarb, Andrew Jackson,  
Katrina Miller, and Brian Topp



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## Introduction

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Within a few months, COVID-19 has imposed a global economic shock the like of which hasn't been seen since the Great Depression. The particular nature of this crisis, a pandemic with no certain end, sets it apart from other economic downturns. It forced an ultimatum: shut down the economy and most social activities in order to buy time and eventually manage the virus or suffer a much deeper and longer economic depression with a tragically high death count.

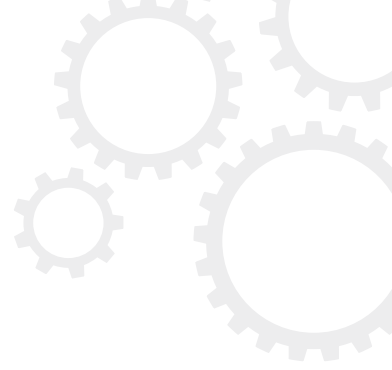
Canada's efforts to manage the COVID-19 pandemic has been steeped in a sense of solidarity with each other as we've undertaken great feats of public action: the Canada Emergency Response Benefit (CERB), widespread testing, and coordinated shutdown protocols are all proof of what we can achieve very quickly when we choose to do so.

And our efforts have brought us to a hopeful point. The curve of cases is flattening, and our health system has been able to handle the peaks we've experienced thus far. We are seeing a modest reopening in most parts of the country. But we must remember that the future path of this pandemic in Canada and worldwide is still uncertain, and thoughtful experts have warned us that it will continue to have a profound impact, both socially and economically, for at least the next couple of years.

While we won't know the full cost of the disease for quite a while, we do now know the economic cost of government action taken in the first few months of the pandemic. Finance Minister Bill Morneau's July economic update pegged the federal deficit at \$343 billion dollars.<sup>1</sup> Some deficit hawks have responded, predictably, that this is the time to start tightening the belt, a disastrous and completely unwarranted approach at this time—or at any time in the near future.

The economic update also told another story. Despite having the highest debt and deficit in a century, Canada's debt charges are the lowest they've been in the past 30 years.<sup>2</sup> The rock-bottom cost of debt means that at least for the next few years, government spending can be dictated by what people need in order to weather this storm and to rebuild smartly and justly to counteract two other calamities on our doorstep: inequality and climate change.

Pre-COVID, the world was just starting to come to terms with the extent of change that would be needed during the next decade to avoid widespread ecosystem collapse due to climate change. Indeed, the pandemic has provided a sobering appraisal of the deep cracks in our systems, from education and health to employment standards and income supports. We have been forced to face up to



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longstanding inequities and injustices that Indigenous people, women, Black people, and other racialized groups have borne for years. They have suffered some of the worst impacts of the virus.

A recent *Financial Times* editorial appraised the situation and surmised that “[a]s western leaders learnt in the Great Depression, and after the second world war, to demand collective sacrifice you must offer a social contract that benefits everyone.”<sup>3</sup> The piece went on to conclude: “[R]adical reforms—reversing the prevailing policy direction of the last four decades—will need to be put on the table. Governments will have to accept a more active role in the economy. They must see public services as investments rather than liabilities, and look for ways to make labour markets less insecure.”

The editorial constitutes a striking recognition from the halls of fiscal conservatism that

the Canadian government and governments around the world need a publicly led and funded social and economic transformation. The question is not whether we can afford it (as we cannot afford not to act) so much as how we will pay for it in a manner that is fair and equitable across social groups, regions, and generations.

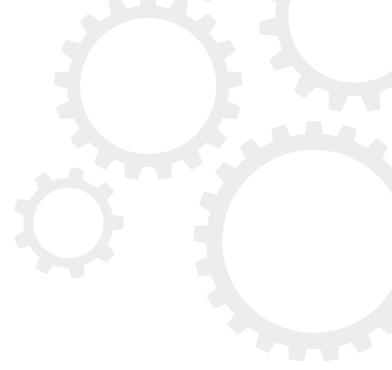
Continued deficit spending for the foreseeable future will be a necessity, and with interest rates for federal borrowing near zero, it is also good fiscal policy. Plenty of research has shown that bold investment now in core social supports such as health, education, and housing will reap long-term economic and social rewards. So, too, will investing in a low-carbon economy. Such investment relies on a simple truth: preventing problems is usually less expensive than fixing them.

But a transformation of this size also requires a permanent increase in public-

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sector supports and programs, and these cannot be funded indefinitely through deficit spending. Significant new sources of revenue are needed. Careful design of those revenue sources should reinforce our objective of creating a more equitable and sustainable society.

A well-balanced, well-designed, and fair tax system can support a society that is also well balanced, smart, and fair. Most Canadians endorse such an arrangement, but our current tax system misses the mark. Many of the decisions that federal and provincial governments in Canada and the governments of other industrialized democracies have made about public revenue over the past 30 years have not delivered on their promised benefits, though they have come with great costs.

Above all, since the 1980s we have managed to engineer an unprecedented transfer of wealth to a small minority that needed help the least while imposing austerity on the majority of the population. The result has been growing inequality and insecurity.

We have also paid huge opportunity costs by giving away the net value of our natural resources for free.

In some sense, these were two trillion-dollar thefts—from the majority of us to the rich and from all Canadians as collective owners of our resources to a relative handful of mostly foreign private shareholders.

To achieve what we need to achieve in these times, we will need to establish more balanced and sensible public revenue policies.

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## Stop Making the Same Mistakes

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Let's begin with a bit more about the road we've been on in recent times. First, our governments have used public revenue policy to implement a series of upward transfers of wealth to the most fortunate among us.

This choice was driven by a set of problematic assumptions: that our economy would do better if we got government out of the way and that tax cuts benefiting the rich would trickle down to the rest of us in the form of better jobs and higher wages. As we cut taxes, we heard with increasing frequency that we couldn't afford public spending to end poverty and homelessness or to achieve better health and education outcomes.

The result: wealth and income have become highly concentrated at the top. Economist Lars Osberg has shown that from the early 1980s, incomes in Canada rose much more rapidly than average for the top 1% while the living standards of the broad middle class stagnated. Today, the top 1% collect some 15% of all income, up from 8% in the early 1980s, and now own fully one-quarter of all wealth.<sup>4</sup>

The main driver of this dramatic increase in inequality is the expansion of profits for a concentrated group, based on increasingly insecure work and stagnated wages in the labour market.

Governments have exacerbated the problem by starving key income-support programs such as social assistance and Employment Insurance and by making the overall tax system more unfair. Since 1980, the tax rate on the top income bracket has dropped from 43%<sup>5</sup> to 33%,<sup>6</sup> and corporate taxes are down from 36%<sup>7</sup> to a staggeringly low 15%.<sup>8</sup> Tax breaks on income from investments have also become more generous over time.<sup>9</sup> All of these shifts in the system have overwhelmingly benefited the rich.

Economist Marc Lee has shown that while the effective tax rate is generally modestly progressive, the top 5% and, even worse, the top 1% pay lower taxes as a share of their income than do the broad middle class and the poor.<sup>10</sup>

These reforms have done much more than give the wealthy an unfair break. The Organisation for Economic Co-operation and Development (OECD) calculates that tax revenue in Canada fell from 34.7% of GDP in 2000 to 33.0% in 2019 (well below the OECD average of 34.3%).<sup>11</sup> That translates into lost annual tax revenues of *almost \$50 billion*.

Imagine how much better prepared we might have been for this pandemic if that annual \$50 billion had been invested in our health-care,



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long-term care, and income-support systems. Instead, we transferred significant sums to wealthy investors and corporations in the belief that these funds would create jobs through private investment in machinery, training, research and development, and economic diversification. There is little evidence that any of this occurred. Indeed, virtually every major assessment of Canadian economic performance over the past two decades and more has lamented our chronic weakness in business investment outside the resource sector. All kinds of tax and other incentives for businesses have failed to build a more technologically advanced and diverse economy, leaving us overly dependent upon extraction of raw materials, especially oil and gas.

Instead, the bulk of these savings from tax cuts have accumulated on private sector balance sheets as cash reserves<sup>12</sup>, funded the transfer of jobs and operations out of the country, and bank-rolled share buybacks and dividend payments that corporations could otherwise not have afforded.

We have also squandered our resource wealth, a painful and fateful mistake for a resource economy. The example of Norway haunts Canada. That country created a fiscal regime modelled on our own policies—arrangements set up during the 1970s by the Lougheed

and Blakeney governments in Alberta and Saskatchewan that astutely used public revenues gained from oil to invest in future economic health. And then the Norwegians stuck with them. As a result, Norway has converted three decades of natural resource development into over \$1.18 trillion in public investment capital—ample to fund Norway’s diversification away from fossil fuels and to a sustainable and prosperous full-employment economy. Canadians at both the federal and provincial levels instead listened to fiscal charlatans and decided, in effect, to throw our country’s natural resources away. In good part, the tax cuts outlined above were financed with one-time resource revenues—the classic mistake of buying groceries with the family silver.

After choosing to concentrate wealth in the hands of a tiny proportion of our citizens, finance the hollowing out of our economy, and squander the value of our natural resources, we then chose to try to make up for our inadequate tax revenues by imposing austerity on most of our citizens. Public services established under earlier, better policies have been squeezed for decades—notably, our public health care, income-support, and public education systems. We have denied ourselves the ability to make further progress, and now we are all paying for it as the COVID-induced recession has had more severe and



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even catastrophic consequences due to the lack of adequate social safety nets, health care, and public education.

Some of us have even paid with our lives. For example, Canada's choice to hand frail seniors over to deregulated private nursing homes led to conditions in our "system" of long-term care facilities that led to tragic suffering and death during the 2020 COVID-19 outbreak in Canada.

Regrettably, in the last three decades and to an unconscionable degree during the COVID-19 crisis, we have witnessed the many economic and social costs of the anemic public systems and growing inequality that now characterize Canadian society. A major paper published by the Broadbent Institute in 2012, "Towards a More Equal Canada,"<sup>13</sup> shows that extreme inequality lies behind the rise of many social ills, from health to crime.

Ultimately, extreme inequality lowers the equality of opportunity required for people to live healthy and prosperous lives. It also undermines democratic norms and values. Inequality produces a pervasive sense that the economic and social system is rigged, and this, in turn, fuels right-wing populism and racism and undermines the basis for social solidarity to deal with pressing issues (including the climate crisis).

Canada's economic performance and resilience have been hamstrung by rising inequality as stagnant wages and incomes reduce consumer spending and household debt goes up. Pre-pandemic household debt was an alarming \$1.78 for every dollar of disposable income. Some forecast it will rise to \$1.85 due to COVID-19.<sup>14</sup>

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## Affordable Choices for Rebuilding

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We do, however, have choices—affordable choices. Gross inequality, the hollowing out of the economy; and the gifting of our natural resources to wealthy corporations aren't immutable natural laws—and neither is austerity. These are simply the results of bad political decisions, made on the basis of arguments that have proven to be false.

The particular nature of the current COVID-19 crisis, a global pandemic with no end in sight, demands a vastly different response than solutions implemented during more recent recessions. Decision makers also need to take into account the way that policy choices leading up to and following the Great Recession of 2008–2009 created conditions that have made the costs of this crisis much higher than they would otherwise have been. Our strategy today must be based on understanding how vulnerable our world has become to crises like COVID-19 and the need to rebuild for resilience. The goal of the post-COVID recovery is not to return to the flawed “normal” of old but rather to transform Canada into a more socially equal, sustainable, and productive country that plays its part in a better world.

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**“Continued deficit spending for the foreseeable future will be a necessity, and with interest rates for federal borrowing near zero, it is also good fiscal policy.”**

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## Paying for a Fair Recovery: Macroeconomic Policy and Fair Taxes

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Since March 2020, the government of Canada has committed \$343 billion in various initiatives to prevent the COVID-19 quarantine from triggering a 1930s-style depression. The government was wise to do this, and their decisions have provided evidence that policy makers have understood that austerity makes economic shocks worse. But what now?

The government response to COVID-19 has, necessarily, resulted in a huge increase in government deficits and public debt, which will remain at high levels for some time. Spending increases were essential to deal with the impact of the virus on public services, especially health, and on workers who lost their jobs or much of their previous earnings. Many hard-hit sectors may not recover soon if at all, and governments across the country will have to provide assistance in both the short and long-term.

At some point, the federal government will need to outline both a continued response plan and a recovery plan. As we stated earlier and as many others across the political spectrum have argued, our society is in need of transformation, fuelled by robust public investment and a more active role for government in the economy.

It is also widely agreed that the increased public debt will be manageable in the short to

medium term as long as the Bank of Canada keeps interest rates at very low levels and continues to buy Government of Canada and provincial bonds to fund most of the new spending. For these reasons, it also makes the most sense for borrowing to happen at the federal level, especially to finance the response and recovery needs of Canada's municipalities, who are already facing a combined \$10–15 billion budget shortfall due to the pandemic.<sup>15</sup> As long as we use our national currency and borrow mainly from ourselves in Canadian dollars, we will not face a bondholders' revolt as forecast by some. The new debt will also shrink as a share of the economy if growth revives even modestly, and growth is likely not to revive if governments stop compensating the present fragility and low investments of the private sector.

However, if and when the economy returns to something like normal and household spending and business investment revive, too much continuing monetary stimulus will come at the risk of higher rates of inflation. While this is not an issue in the short to medium term, since there is a great deal of slack in the national and global economies, in the longer term, trade-offs will need to be made between desired goals. One lesson during the recovery from 2008 was that broad, stimulative monetary policy may just increase private debts, asset price inflation, and

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consumption, instead of resulting in public and private investments that would build a more productive economy and a fairer society. Stimulus spending must be engineered for clear outcomes if, for example, we want to give priority to green investments and affordable housing.

Fiscal austerity—that is, cutting government spending—is not the way to reduce higher public debt, either in human terms or in economic terms. Government spending in many areas is the best solution because it not only saves and creates jobs today but also boosts productivity and economic prosperity. Key examples include high-quality child care and health care, public infrastructure

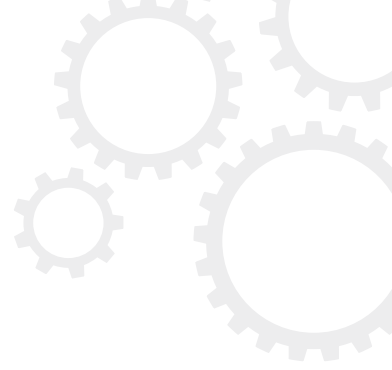
and education. There is every reason for governments to invest, especially at a time when interest rates are so low and business investment has been weak despite generous tax incentives.

All this said, we cannot expect stimulative monetary policy to do all of the work at a time when we want to make major investments in a clean economy while also improving our social programs and public services—from health care to income-support systems to affordable housing. In the medium and long terms, a sustained increase in tax revenues as a share of the economy will be needed to underpin a sustained increase in public spending.

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**“We need to create a tax system which can provide the foundation of an economy that serves the many rather than the powerful few.”**

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# Progressive Tax Reform

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Tax reform will also be essential to building the Canada we want. We need to create a tax system which can provide the foundation of an economy that serves the many rather than the powerful few, which ensures that those who have benefited most from earlier taxation structures pay the greatest share to build the Canada we want.

We propose five areas of focus to increase federal revenues:

## 1

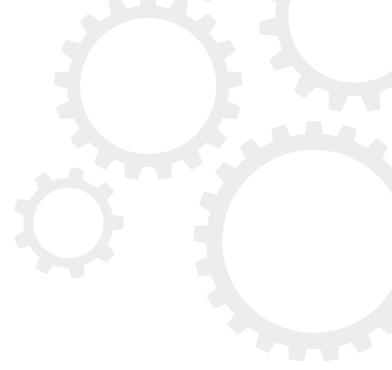
### **A graduated wealth tax should be applied to extreme wealth.**

The 0.1% of Canadian citizens who have accumulated the lion's share of income and wealth growth in Canada over the past 30 years should be educated so they understand that they have enough and it's time to share.

Wealth is actually a better way to assess ability to pay than income, which can vary greatly over time. Some argue that the wealthy already pay tax on their investment income, but this is often only a small proportion of the wealth that accumulates from year to year. Billionaires like David Thompson spend a very small part of their fortunes, leaving much of their annual wealth accumulation untaxed, and in Canada we do not even have an inheritance tax on

large fortunes. A recent Broadbent Institute report on wealth taxes has shown that even a modest wealth tax on all financial and non-financial assets can raise significant revenues while countering growing inequality.<sup>16</sup>

In the immediate short term, a wealth tax would allow the richest Canadians to make a contribution appropriate to their wealth toward repairing the damage that COVID-19 has done to public finances and toward implementing the necessary economic recovery plan. Those who speak for Canada's wealthiest often argue that sound public finance must be a key priority, so it makes sense that they contribute in proportion to their means. In the longer term, this measure will help begin to unwind the gross social and economic inequality that exists in Canada and allow governments to build a more equitable society. Many options have been presented for a wealth tax in Canada and the United States. The Parliamentary Budget Office recently estimated that a mere 1% tax on wealth over \$20 million would net approximately \$70 billion over 10 years, even with a realistic level of tax avoidance factored into the calculations.<sup>17</sup>



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## Progressive Tax Reform

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### 2

#### **Federal income taxes should be more progressive.**

While the Canadian tax-rate structure is moderately progressive over most of the income spectrum—taking a larger share of pre-tax income from the relatively well off—taxes on the top 1% or so are significantly lowered by the preferential treatment of certain types of income more prevalent among the wealthy. For example, only one-half of capital gains and stock options are liable to tax, while wages are 100% subject to tax. The dividend tax credit also lowers effective taxes for the very few Canadians who earn significant investment income outside pension plans and RRSPs.<sup>18</sup> These tax breaks should end. The top income tax rate in Canada is also lower than in many other jurisdictions. Income-tax reform should target increases at the top 1% (who have incomes above approximately \$250,000), with the possibility of the top end of that range, the 0.1%, (with annual incomes over half a million), paying a much higher rate. Tax avoidance by the very rich through the use of offshore tax shelters should also be countered—through much more intensive audits and stringent penalties and by ending tax agreements with countries used as tax havens.

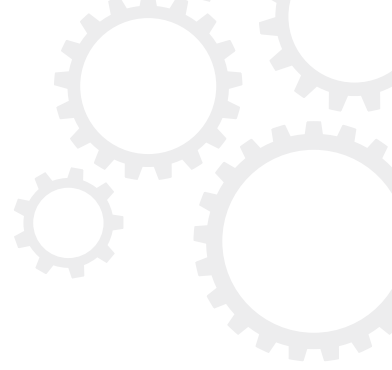
### 3

#### **End corporate welfare.**

Canada has a dismal track record when it comes to corporate welfare. But from now on, there can be no justification for public policy that allows for broad-brush tax concessions and other ways of giving money to privately owned corporations.

Since the 1980s, the corporate income tax rate has been steadily lowered, and corporate tax revenues have fallen as a share of all taxes in relation to GDP. While various federal governments and provincial governments have justified these lower tax rates as a means of boosting business investment, this investment rate has, in fact, fallen. Corporate tax cuts are actually irrelevant to most investment decisions, which are influenced largely by resource and intellectual endowments, public infrastructure, the skills of the available workforce and targeted tax credits and targeted subsidies such as those available for research and development. Corporate tax reform should eliminate broad tax cuts and shift the focus to more effective investment incentives.

After the pandemic has subsided or been reduced to much lower-risk levels, an excess-profits tax will need to be introduced in



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## Progressive Tax Reform

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recognition of the fact that while many at the bottom of the income scale paid a huge price as a result of the pandemic, some companies were making enormous profits during the crisis (and in some cases, because of the crisis).

In cases where Canadian governments do invest in private corporations, the public should always benefit from these public investments through public policy that requires the government to take equity or earn interest at rates that match the risk being assumed.

### 4

**As finances permit, revenues from resource development should be pooled in a sovereign wealth fund, to be invested in a green economic recovery.**

The government of Canada and the fossil-fuel-producing provinces (British Columbia, Alberta, Saskatchewan, and Newfoundland) may have missed their once-in-history opportunity to turn the petrochemical boom of the past 40 years into transformative capital. This may well stand as the single worst fiscal mistake governments have made in Canadian history, one that all Canadians will pay for—especially as we begin to take stock of the heavy environmental

deficits that the private beneficiaries of Canada’s resource giveaways hope to socialize. These costs include the expense of dealing with orphan wells and of land remediation. They are so enormous that they could dwarf the costs associated with the federal government’s present COVID-19 emergency program.

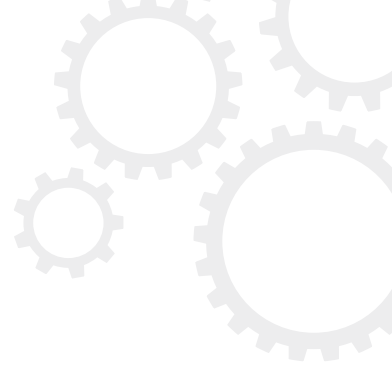
However, some revenues could be salvaged. The government of Canada, for example, could work to withdraw from its own fiscal addiction to one-time resource revenues and redirect them to a sovereign wealth fund that would invest only in sustainable economic diversification and decarbonization projects.

As their finances permit, provincial governments could undertake their own salvage efforts. Alberta, for example, could implement a provincial sales tax comparable to those of other provinces, balance its budget in one year, and begin to accumulate a provincial wealth fund.

### 5

**Increase consumption (sales) taxes and social-security premiums.**

Consumption taxes can be progressive if well designed (with compensating payments to citizens living on low incomes). That is



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## Progressive Tax Reform

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why most industrial democracies rely on them. However, in Canada, governments are extremely dependent on income taxes, which have been attacked and eroded, and resource revenues, which have been fecklessly wasted as we've described above.

For example, data from the OECD shows that Canadians pay much less of their income on sales taxes used to contribute to social-security programs than do citizens of European countries.<sup>19</sup>

While these taxes are often seen as regressive, even flat taxes benefit lower-income groups the most as long as the proceeds are spent on robust progressive universal and needs-based programs. In fact, under what has been called Canada's quiet bargain, the great majority of the citizens of this country receive much more

value from social-security programs and other public services than they pay for in the taxes that contribute to funding them.<sup>20</sup>

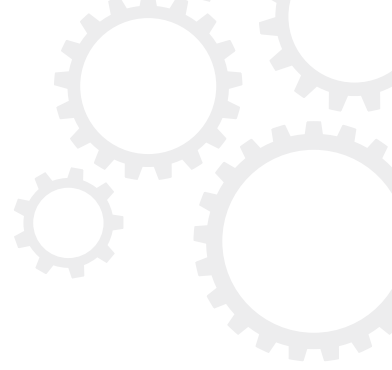
One clear example: carbon taxes and similar levies related to environmental damage should also form part of our governments' responses to the global climate crisis—to both incentivize behaviour and collectively invest in a future of proper care for the environment and for people affected by environmental pollution and the climate crisis.

Despite the quiet bargain, however, it would be unwise to raise consumption taxes during this time of economic recession. Though they are a necessary part of our fiscal tool kit, these taxes should be increased only in the context of fundamental tax reform.

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**“Plenty of research has shown that bold investment now in core social supports such as health, education, and housing will reap long-term economic and social rewards.”**

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## Conclusion

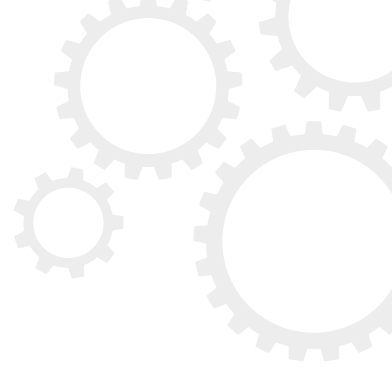
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Public policy should always start with a clear understanding of the desired outcomes.

Those who introduced austerity programs in response to the last global recession are already starting to propose that this approach be repeated. But such programs will only provide more “incentives” for those who need them least and more hardship and insecurity for everyone else. Most Canadians know from their lived experience that these policies have failed them and bear no relation to the kind of country they want to live in.

As Canadians, most of us are proud of the progress we’ve made together in creating some key elements of a fair and caring society: our public health and education systems are strongly supported and widely viewed as fundamental to our way of life. However, the pandemic and the twin crises of inequality and climate change that were already upon us pre-COVID have demonstrated with stark clarity that we have much more work to do.

We need to respond to the economic shock of the current crisis effectively and in a manner that benefits everyone. This will include planning for and preventing future crises related to climate change. We need to borrow and invest wisely and build a tax system that will establish and reinforce the foundation of an economy and a society that serve the many rather than the powerful few. We must also encourage behaviour that supports equality and sustainability and discourages behaviour that threatens those values. Finally, we must ensure that those who have benefited most from the way things were will pay the greatest share in building the Canada we want.



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## About the Authors

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### **Alex Himelfarb** **Broadbent, and Parkland Institute Fellow**

Alex Himelfarb is a former Clerk of the Privy Council and currently chairs or serves on numerous voluntary sector boards. He was also the Director of the Glendon School of Public and International Affairs, leading the Centre for Global Challenges. Dr. Himelfarb was a Professor of Sociology at the University of New Brunswick from 1972 to 1981. During this period, he undertook an Executive Interchange with the Department of Justice as Head of the Unified Family Court Project from 1979 to 1981. In 1981, he joined the Public Service with the Department of the Solicitor General of Canada. He has held a number of positions of increasing responsibility since that time, including Director General, Planning and Systems Group, Planning and Management Branch with the Department of the Solicitor General of Canada; Executive Director of the National Parole Board; Assistant Secretary to the Cabinet, Social Policy Development with the Privy Council Office; and Associate Secretary of the Treasury Board. While serving as Associate Secretary of the Treasury Board, he also headed the federal Task Force on the Social Union. In June 1999, Dr. Himelfarb became Deputy Minister of Canadian Heritage. He then served as Clerk of the Privy Council and Secretary to the Cabinet from May 2002 until March 2006 when he was nominated as Ambassador of Canada to the Italian Republic with concurrent accreditation to the Republic of Albania and the Republic of San Marino, and as High Commissioner for Canada to the Republic of Malta. Alex Himelfarb is a graduate of the University of Toronto where he obtained a Ph.D. in Sociology. He is an Atkinson Foundation Board member as well as a Fellow of the Broadbent and Parkland Institutes, respectively.

### **Andrew Jackson** **Senior Policy Advisor, Broadbent Institute**

Andrew Jackson is the Broadbent Institute's Senior Policy Advisor. In September, 2012 he retired from a long career as Chief Economist and Director of Social and Economic Policy with the Canadian Labour Congress. In 2011, he was awarded the Sefton Prize by the University of Toronto for his lifetime contributions to industrial relations. Educated at the University of British





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Columbia and the London School of Economics and Political Science, where he earned a B. Sc. and an M.Sc. in Economics, Andrew is the author of numerous articles and five books, including *Work and Labour in Canada: Critical Issues*, which is now in its second edition with Canadian Scholars Press.

### **Katrina Miller** **Program Director, Broadbent Institute**

Katrina Miller is the Program Director for the Broadbent Institute, driving the Institute's policy, campaign and communications work to build the progressive landscape in Canada.

She has over 20 years of experience as a communications and public policy strategist working with a wide array of labour, community, and other non-government organizations to promote progressive social policy. She seeks to share knowledge through training activists in communications tactics and facilitating campaign and strategic planning.

### **Brian Topp** **Partner, Guy, Topp & Company Public Affairs**

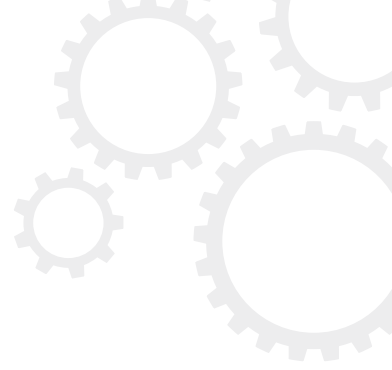
Brian Topp is a partner at Guy, Topp & Company Public Affairs; a fellow of the Public Policy Forum; and a Broadbent Institute Board member. He is also chair of the board of Creative Arts Savings and Credit union, co-chair of Film Ontario, and is a director of ROI Fund and Pinewood Toronto Studios. He served as deputy chief of staff to Premier Roy Romanow in the Government of Saskatchewan, and as national campaign director to federal NDP leader Jack Layton. He is the author of a book, *How We Almost Gave the Tories the Boot*, describing events around the 2008 "coalition crisis" in Parliament. He was born in Montreal and is a graduate of McGill University. Brian Topp recently completed a two-year stint as chief-of-staff to Alberta Premier Rachel Notley. During this period the Government of Alberta introduced a \$15 minimum wage; appointed a gender-balanced Cabinet; replaced a system of regressive flat taxes.

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