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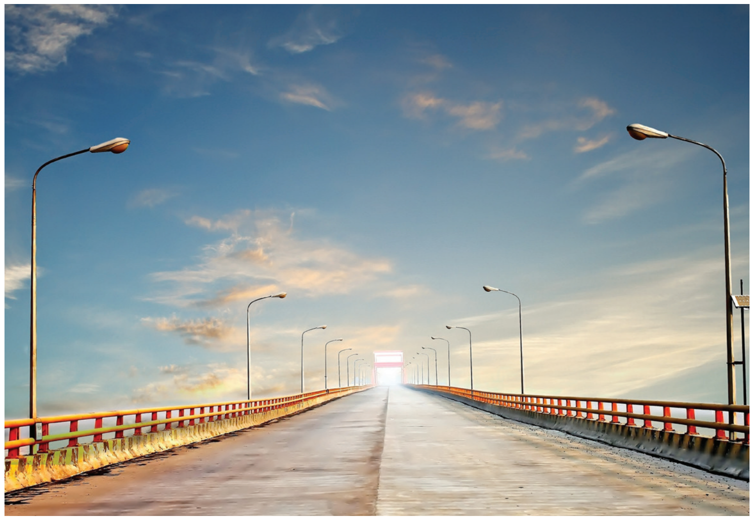

IT IS TIME TO INCREASE PROVINCIAL FUEL TAXES

DR. HARRY KITCHEN, TRENT UNIVERSITY

Many policy analysts and even the provincial government have suggested that increased taxes will be needed if the current deficit of $10.9 billion is to be eliminated and the province is to achieve a balanced budget within three years. Anticipating a tax increase, one might ask – "Which tax or taxes?" There is no clear answer, but there is likely to be more support for a tax linked to the user of a service (known as a "benefits-based tax"). Probably the easiest tax to raise is the provincial gasoline tax and the provincial diesel fuel tax. The Ontario government currently levies an excise tax of 14.7 cents per litre on gasoline and 14.3 cents per litre on diesel fuel. Both rates were set in 1992 and have not increased since then.

I. ARGUMENTS FOR INCREASING BOTH TAX RATES

There are several compelling reasons for increasing provincial fuel taxes, at least for the next five to seven years. It would generate much needed revenue for transportation infrastructure improvements and expansion. These tax rates were set 23 years ago, an unusually long time for holding a tax constant given that inflation has increased by more than 50% over that time. In real terms, the province is collecting far less today than it did in the 1990s – certainly not enough to cover expanded or improved transportation services. Increasing the tax now, when the price at the pump is lower than it has been for some time, would not push the price above levels that consumers and businesses faced in the recent past. Furthermore, this tax increase could be viewed as a crude form of a carbon tax (one that is, by the way, growing in popularity in a number of countries) and as such, it would be similar to the 6.67 cents per litre carbon tax on motor fuel and 7.67 cents per litre carbon tax on diesel fuel in British Columbia.

Government	Gasoline Tax (CAD ¢/L)	Government	Gasoline Tax (CAD ¢/L)
British Columbia	21.17	Manitoba	14.0
Québec	20.2	New Brunswick	13.6
Newfoundland & Labrador	16.5	PEI	13.1
Nova Scotia	15.5	Alberta	13.0
Saskatchewan	15.0	NT/NU	10.7
Ontario	14.7	Yukon	6.2

In essence, a tax hike on gasoline and diesel fuel would have a number of economic and environmental advantages for Ontario.

- It would impact total distance driven. Reducing unnecessary driving or engine idling would lead to less congestion and reduce overall environmental damage (costs);
- It would provide an incentive for switching to more fuel-efficient cars and public transit;
- It is a useful tool for curbing the costs of greenhouse gas emissions because emissions decrease as the amount of fuel burned decreases; and,
- It would assist in reducing urban sprawl – a recent Canadian study found that a 1% increase at the pump in the 12 largest Canadian metropolitan areas between 1986 and 2006 caused a 0.32% increase in population living in inner cities and a 1.28% reduction in low-density housing units.

Finally, if we turn to recent U.S. initiatives, seven states have increased or announced increases in their state fuel tax rates and other states are considering similar moves as a means of generating more revenue for roads and public transit.

II. SHOULD FUEL TAX REVENUES BE EARMARKED?

Yes. There are four main arguments to support earmarking:

1) It is consistent with the benefits-based principle of financing government services – those who use a service pay for it.

2) Earmarking facilitates long-term planning after establishing a dependable revenue stream.
3) It can prevent the political abuse of funds – there is more accountability and transparency when there is a link between the revenues from a tax and the service funded by the tax.
4) Most importantly, it boosts public support because people know where their tax dollars are spent.

III. REVENUE POTENTIAL[1]

If both taxes were increased in 2015 by an amount that reflects the inflationary increase from 1992 to 2014 (that is, to 23 cents per litre for motor fuel and to 22 cents per litre for diesel fuel) and then increased annually by an assumed rate of inflation of 2.5 percent per year until 2022, it is estimated that both taxes combined could generate additional provincial revenues of:

Revenue	Year
$1.7 billion	2016
$1.8 billion	2017
$1.9 billion	2018
$2.0 billion	2019
$2.1 billion	2020
$2.2 billion	2021
$2.4 billion	2022

IV. IS THIS A LONG-TERM SOLUTION?

No. A major advantage of increasing the provincial fuel taxes for the next five to seven years is that this change will generate much needed revenue. Beyond that time frame, however, tax revenue potential will fall as will the taxes' ability to impact road usage. As vehicles become more fuel-efficient, fuel tax revenues will drop. Other factors that will cause a reduction in fuel-tax revenues in the not-too-distant future include an increased reliance on electric and hybrid vehicles; the growth of younger adults living in highly urbanized areas who drive less; and an increase in the number of retiring Baby Boomers who will drive less than when they were younger. Of major importance here is the increase in more fuel-efficient, electricity-driven and hybrid vehicles that will lead to less revenue being generated without necessarily leading to a reduction in congestion – drivers of non-fuel cars will not have an incentive to economize on road usage because they will be getting a free ride compared to those with combustion engines. What will be needed in the long run, as has been noted by a growing number of policy analysts, is some form of road pricing and parking charges that apply to all vehicles.[2] Because of the length of time it will take to introduce and implement these new revenue tools, however, it makes sense to hike the provincial fuel tax to partially fill this revenue gap in the interim.

HARRY KITCHEN is Professor of Economics at Trent University. Over the past twenty years, he has completed more than 100 articles, reports, studies, and books on issues relating to local government expenditures, finance, structure and governance in Canada. In 2013, he was awarded a Queens Diamond Jubilee medal for policy analysis and research contributions to municipal finance, structure and governance in Canada.