

Chapter 4

Benefits from Public Services

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In a 1927 United States Supreme Court judgment, Justice Oliver Wendell Holmes famously declared, “taxes are what we pay for civilized society.”¹

While that is as true today as it was then, most of us have much less lofty reasons for paying the taxes that provide public services: we couldn’t get through a day without them. Every day, we consume, use, and benefit from public services of an astonishing variety without giving it a second thought—indeed, usually without giving it any thought at all. That variety, along with the differences in our personal circumstances means that each of our interactions with public services is different, but dependence on public services in our daily lives is common to all of us.

To demonstrate this point, I’m going to invite you now to stop reading and conduct a thought experiment. Think your way through your day, from when you got up in the morning until you went to bed at night (or the other way around if you are a shift worker), making a note of every time you used, consumed, or benefited from a public service.

Here are the results of mine:²

The alarm clock buzzed and I turned on the light. The electricity I used was distributed to my home by a public utility, and probably generated by a public utility. I used the toilet and flushed, the waste disappearing into my home’s plumbing system to be transported kilometres away and processed, all as a public service thanks to the taxes I pay. I brushed my teeth using water that came out of the tap when I turned the handle; water that was there because I paid my taxes. I walked out my front door and down a sidewalk that wouldn’t be there if my neighbours and I hadn’t paid our taxes. My children and I got into the car and drove down a street that wouldn’t be there if we hadn’t paid our taxes. I dropped off one of my children at the bus stop to go to school. To catch a bus that wouldn’t be there if we didn’t pay our taxes; to go to a school that wouldn’t

be there if we didn't pay our taxes. I managed to make it to my destination without incident, despite the fact that the roads were crowded with others doing exactly what I was doing, thanks to the traffic signals, rules of the road, and police officers that keep us safe. All paid for by taxes. Later that day, I picked up one of my daughters at school and drove her to an appointment with her doctor, the cost of which was covered by the taxes we all pay. At this point, my story becomes a bit repetitive, so I'll skip to my drive home, listening to a radio that wouldn't work if we didn't have a public regulatory system that restricted broadcasters to specific frequencies and making sure I caught the news on the CBC, Canada's public broadcaster. We sat down to dinner without a moment's thought to the safety of the food we were eating, thanks to a system of rules and regulations whose creation and enforcement was paid for through our taxes.

The variety and convenience of public services is obvious from our thought experiment. But the examples we encounter specifically each day barely scratch the surface. There's also the security provided by police, fire, and ambulance services not because of anything specific that they do for us on any specific day, but because they are there. Air quality regulation and enforcement without which life in many cities would be a living hell. The indirect benefits we receive because public services are available to others as well as ourselves, providing all of us with a better educated and healthier society.

It is also easy to miss the sheer scale of the public services enterprise. The millions of children who attend public elementary and secondary schools every day. The hundreds of thousands of teachers who meet these students every day to make the system work. The tens of thousands of Canadians who see a doctor or visit a hospital every day. The thousands of kilometres of sewers and water mains. The hundreds of thousands of kilometres of roads, streets, and highways, not to mention the system of public transportation. The millions of hectares of public parks.

Measuring the Benefit from Public Services

When we reflect on it, our day-to-day experience proves Justice Holmes' point. Life in the twenty-first century as we know it would not be possible without public services. Public services underpin our economy, make it possible for us to provide the essentials of human life to ourselves and our families, and enable us to participate in the economic, social, political, and cultural life of our communities.

Public services are pervasive. But are they a good deal? How important are public services to the lives of Canadians, compared to the goods and services we obtain directly in private markets? And in particular, given the constant and unrelenting attack on the taxes that pay for our public services from

conservatives, how does the value we receive from public services compare to the taxes we pay to provide them? In other words, from a macro perspective, how do public services measure up?

A number of studies have looked in some detail at these questions. The most recent of these, published by the Organisation for Economic and Co-operation Development (OECD) in January 2012, investigates the impact of in-kind direct services to households provided through the public sector in OECD-member countries (Verbist, Förster, & Vaalavuo, 2012). It estimates both the average value of these direct public services, per household, and the effect of these services on the distribution of resources among households.³ The study found that, on average across the OECD, these benefits increase average household disposable incomes by 29%, and that publicly provided resources have the effect of reducing household income inequality. Notably, the study found that the impact of public cash and in-kind benefits for reducing inequality increased in countries where average benefits rose between 2000 and 2007, and declined in countries where average benefits declined.

The OECD study estimates that, for Canada, expenditures on education, health care, early childhood education and care, social housing, and long-term care of the elderly alone have a value equivalent to 25% of disposable income in 2007. Including public pensions, cash transfers were equivalent to 14% of disposable income.

The power of these five categories of in-kind expenditures as a counterpoint to market income inequality is demonstrated by the study's estimates of the value of in-kind benefits as a percentage of disposable income, by income quintile.

By far the most important areas of in-kind benefit, both in aggregate and as influencers of the distribution of resources, are health care and education. Across the OECD, these five categories of public in-kind benefits are valued at

Table 4.1 In-kind benefits as a percent of disposable income in 27 OECD countries, 2007

Quintiles	1st Q	2nd Q	3rd Q	4th Q	5th Q	Total
Education	30.6%	18.5%	14.2%	10.4%	5.6%	11.8%
Health care	34.9%	22.2%	15.8%	11.8%	7.2%	13.9%
Social Housing	1.8%	0.7%	0.4%	0.2%	0.1%	0.4%
Early Childhood Education and Care	4.5%	3.0%	2.4%	1.5%	0.8%	1.8%
Elder Care	4%	1.9%	0.7%	0.4%	0.2%	0.9%
TOTAL	75.8%	46.4%	33.5%	24.3%	13.7%	28.8%

33.5% of the disposable income for the middle income quintile; nearly half the disposable income of households in the second quintile, and more than 75% the disposable income of households in the bottom quintile.

A similar study published in 2009 by the Canadian Centre for Policy Alternatives (CCPA) focused specifically on Canada (Mackenzie & Shillington, 2009). This study was broader in scope in two respects: it estimated the distribution of the value of all public services, not simply in-kind transfers, and it provided a breakdown of those benefits by category of public service, household type, and level of government providing the service.

Using data and analytical tools from Statistics Canada, the study authors estimated that in 2007 Canadians enjoyed an average \$15,000 benefit per capita from the public services that our taxes fund—roughly equivalent to the annual earnings of an individual working full time at the minimum wage.

Lower-income Canadians benefit more from personal transfer payments (most of which are income-related), but middle- and upper-income Canadians benefit fairly equally from all public services. The public services we use and benefit from change as we go through the life cycle. Seniors, for instance, benefit less directly from public education than they do from public health care—but when they were young parents raising children, the opposite was true.

The median Canadian household income (half live in households with incomes below that amount, and half live in households with incomes above it) was approximately \$66,000 in a 2.6-person household. That median household realized a \$41,000 benefit from public services, equivalent to roughly 63% of the household's private income.

The study authors found that more than two-thirds of Canadians benefit from public services worth more than 50% of their household's total earned income. The chart in Figure 4.1 shows the distribution of per capita benefits from public services, by income category.

The chart demonstrates the power of public services in redistributing resources. Although the per capita dollar value of services is relatively stable across all income ranges, benefit from public services declines as a share of household income as income increases.

The findings also revealed variations in both the level and distribution of benefits from public services, depending on family type.

The data show a per capita value of public services, ranging from \$13,332 for families with children to a maximum of \$25,386 for single seniors.

The composition of the benefit varies significantly by family type and life stage. Seniors tend to draw a substantial proportion of their benefit from income transfers and health care. For families with young children, naturally, education makes up the most significant share of benefit. For most other groups of Canadians, besides seniors, health care is the most significant service.

Figure 4.1 Household income in dollars (\$) per capita and percent (%) of household income benefits of public services would cost in Canada for 2006

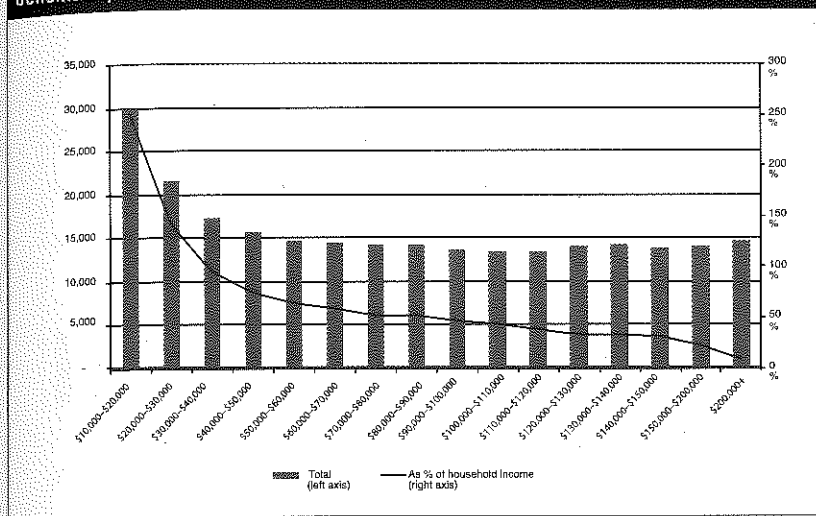


Table 4.2 Average and distribution of benefit from public services by family type

	% of Population	Per capita Benefit	% Education	% Health	% Transfers	% Other
Total	100%	16,527	16%	19%	21%	44%
Couples with Only Older Children	11%	14,758	17%	23%	7%	53%
Families with Children	41%	13,332	29%	15%	13%	43%
Lone Parents with Children	6%	20,416	28%	12%	24%	37%
Non-Senior Couple: No Children	15%	15,407	8%	25%	10%	57%
Other	2%	16,740	17%	17%	28%	38%
Senior Couple	12%	21,199	1%	21%	43%	34%
Single Senior	4%	25,386	0%	22%	50%	28%
Single Non-seniors	10%	21,929	10%	24%	9%	57%

The following three charts show the distribution of benefits from public services by income group for each of the three orders of government in Canada.

Figure 4.2 Per capita benefit from public spending by household income in Canada, 2006, federal government

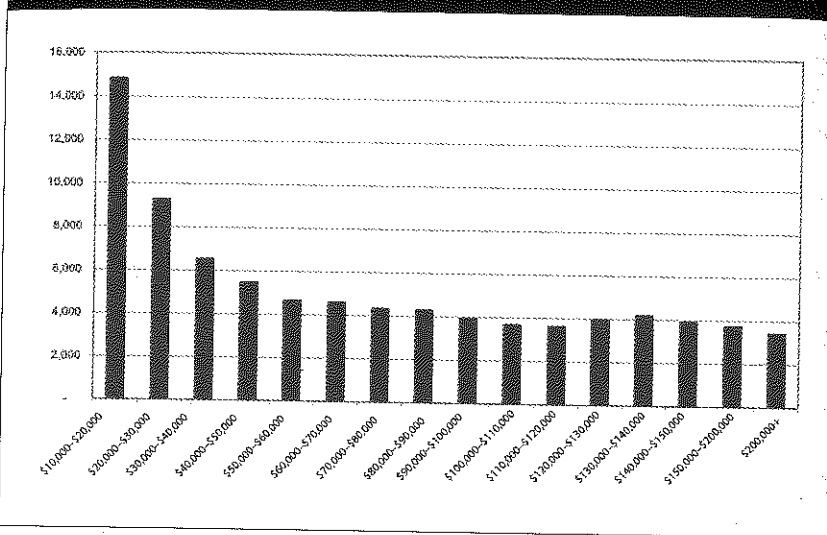


Figure 4.3 Per capita benefit from public spending by household income in Canada in 2006, provincial and territorial governments

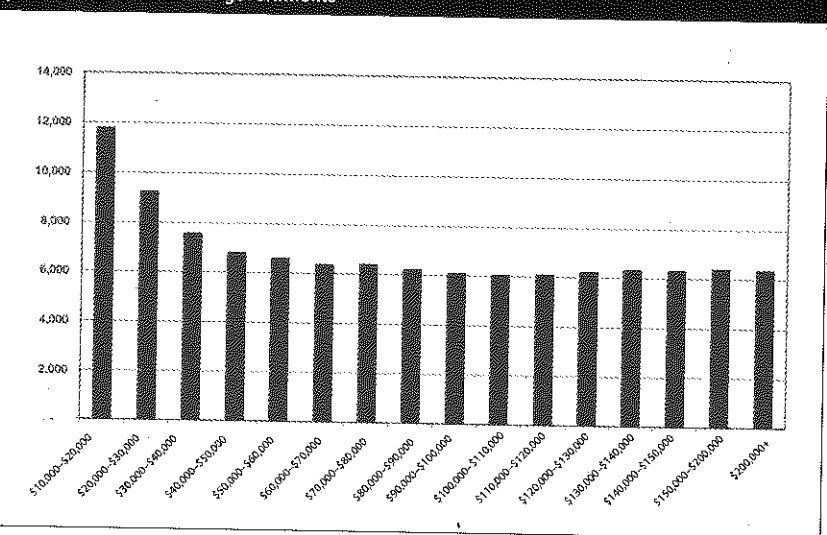
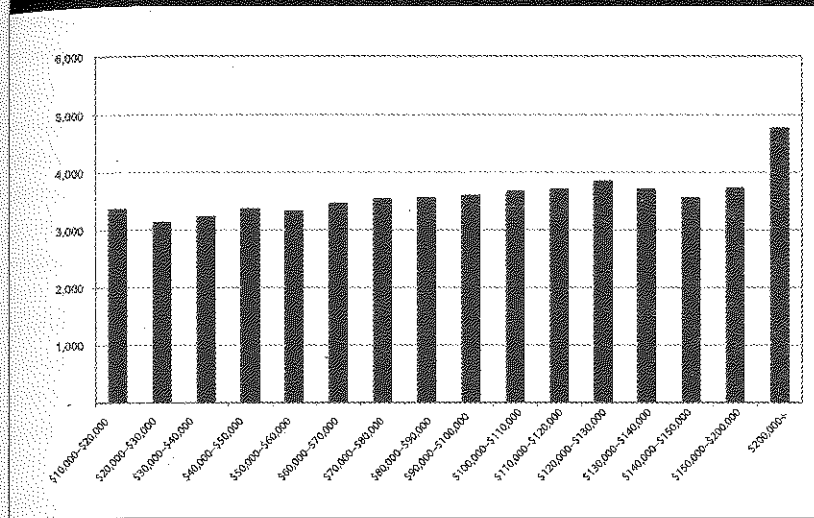


Figure 4.4 Per capita benefit from public spending by household income in Canada in 2006, local governments



While provincial governments are clearly the most important providers of public services in total, federal public services are more important when it comes to impact on income distribution. The value of local government services actually increases slightly in dollar terms as income increases, reflecting the importance of police and fire services in local services and the positive relationship between the value of those services and household income.

Public services account for a significant proportion of the living standard of most Canadians. The value we receive from public services, per capita, varies depending on income and family type, but within such a narrow range that public services deliver a virtually uniform value to all Canadians. In sum, public services amount to a demogrant—an entitlement based on citizenship.

This simple fact has profound implications for the way we think about public services in Canada and for the ongoing debate over taxes, tax cuts, and public expenditure restraint.

At a high level, the debate between taxes and public services cuts as a response to budgetary pressures is a metaphor for the tension between a citizenship democracy, represented by the democratic distribution of benefits from public services, and a dollar democracy, represented by the primacy given to the private economic interests of taxpayers; between citizenship and taxpayership. The data demonstrate that a dollar not spent on public services is not the same as a dollar raised through increased taxes. For the vast majority of Canadians, the loss in value from a dollar not spent on public services is significantly greater than the loss from an equivalent increase in taxes. Why? Because the benefit from public

services is distributed roughly equally among all Canadians, while revenue from taxation is not. Because taxation is, in aggregate, roughly proportional to income, and income is distributed unequally, the net value trade-off between taxes and public services is a virtual mirror image of the distribution of income in Canada.

This basic fact has not been lost on Canadians at the top of the income scale, whose economic interests are well served by a one-sided debate over the relative roles of tax increases and spending cuts in responding to budgetary pressures. The vast majority of Canadians, however, have been notably ill-served by it.

These findings also demonstrate the power of public investment as a redistributive offset to growing inequity in market incomes. Both the OECD and CCPA studies highlight the fact that public services account for a significant share of a middle-income household's living standard, a share that increases for moderate and lower-income households. This, in turn, challenges the way the debate over tax fairness has been framed in Canada, particularly by political progressives.

We don't levy taxes for the sake of levying taxes; we levy taxes to pay for public services. The implication of this is that what matters for the role of government in redistribution is the fiscal bargain—the relationship between taxation and benefit from public services—not just the impact of taxation in isolation.

Looking at the net impact of a policy change in the fiscal bargain casts a very different light on the debate over tax cuts and public spending in Canada. The CCPA study showed that the vast majority of Canadians would have been better off without the major tax cuts introduced in the 2000s, including cuts in consumption taxes and others considered to be regressive.⁴ In their analysis, the study authors estimate that 80% of Canadians would have been better off if, instead of cutting the GST, the Harper government had transferred the money to local governments to pay for more and better public services.

Compared to the broad-based income tax cuts implemented by provincial governments in the late 1990s and early 2000s, 80% of Canadians would have been better off if their provincial governments had spent the money on health care and education. And had the federal government invested in improved federal public services instead of cutting capital gains taxation by one-third in the early 2000s, 91% of Canadians would have been better off.

Of course, the advocates of tax cuts never present the real trade-off between taxation and the benefits from public services. The closest we came in Canada to a debate over this trade-off was when the Federation of Canadian Municipalities (FCM) advocated leaving the national GST rate at 7% and transferring the 2% the federal government was proposing to cut to local governments. And even in that instance, the FCM was unable to establish in the public mind the

relationship between funding for local governments as institutions and benefits to Canadian households.

In the absence of a way to make the benefits from public services visible to Canadians, the debate over tax cuts becomes a contest between a very concrete "saving" in taxes and an abstraction, a loss in fiscal capacity.

The tax cuts are made to sound like free money to middle-income Canadians. But when one factors in the value of the services that would have been provided from those foregone taxes, the cuts are anything but free. The data indicate that the tax cuts implemented in the last 15 years have had the net effect of reducing the living standards of most Canadians.⁵

The Challenge of Measuring Public Services

The results highlighted by these studies underline the economic importance of public services to the living standards of most Canadians. Yet even these data tend to understate both the value of public services to Canadian households and the net fiscal bargain. Measures of the value of public services developed from aggregate economic data, including all of the measures cited above, tend to understate significantly the value of public consumption relative to market consumption.

When we measure the value of privately produced goods and services, we do so using market prices, which at least theoretically reflect the amount that a willing buyer is prepared to pay a willing seller, and thus reflect the value to the buyer of the good or service.

With public services, measurement is not nearly that straightforward.

Most public services do not trade in a traditional market. And many services that are funded by market-like user fees provide benefits that do not flow exclusively to those who pay the fees. As a result, even if there is an equivalent price charged for a service, it often does not fully capture the benefit provided by that service. The underlying issue is that transactions involving private goods and services, consumption, use, and benefit have essentially the same meaning, but that is not generally true for public services.

We interact with some public services as consumers, consuming in the sense that our use of the service precludes its use by someone else. The interaction of parents and students with education is a good example. My son or daughter's attendance at our local school means that that place is not available to another's child. So is the relationship we have as patients with the health care system. The 15 minutes that I spend with my doctor during my checkup is 15 minutes not available to someone else. Generally, we choose to provide these services publicly because we are not prepared to leave it entirely to the market and the resources it makes available to individuals to determine their use. For example, we see access to education and health care as fundamental entitlements.

In some cases, we provide market-like goods and services publicly simply because it is more efficient to do so. We could, theoretically, require every property owner to put a light on their property near the street, but it is far more efficient to provide street lighting as a public service. For example, in some Canadian provinces, automobile insurance is provided publicly, because they have determined it is more efficient to do so.

Many other public services can be used without being consumed. For example, within limits, my use of a street or road does not preclude someone else from using it as well. We share the use of the street, just as we share the use of the water and sewer system with our neighbours. Similarly, the security provided by police, fire, and ambulance services or the armed forces is enjoyed by all, but consumed to exhaustion by no one.

Finally, we may benefit from public services which we neither use nor consume. For example, as noted above, we benefit from the health and education systems not only because we or our children use them but also because the fact that these services are generally available to everyone makes us all better off. We benefit individually when we use the health care system, but we also all benefit from the fact that people in our society generally are healthier as a result. A better-educated population is more productive and better able to engage in the social, political, and cultural life of the community.

Similarly, people who choose to use private transportation benefit from the public transportation system because it takes cars off the roads, reducing congestion. Users of private transportation who have experienced the effects of labour disputes or technical problems in the transit systems of large cities understand those benefits only too well.

These characteristics make the valuation of public services very difficult. In principle, an evaluation of public services should take into account all of the benefits that all of us receive. And in some cases, when decisions are being made about new projects or programs, analysts try to do just that. They attempt to measure benefits from public goods, services, and programs that cannot be captured in a price, or even a proxy for a price.

Generally, however, we don't try to measure the benefits from public services. Instead, we adopt the oversimplified convention that public services are valued at their cost. Even in cases where benefits have been estimated in deciding whether or not to go ahead with a project, from that point on, the value of the project is measured at its cost.

The value of government services in our gross domestic product, for example, is measured using the cost of providing those services.

Measuring the Value of Public Services at Cost: Implications

The fact that we measure the value of public services at their cost has significant implications. By definition, there is no measured economic gain from expenditures on a public service, so there is no economic basis for determining whether or not we have enough of any given service. This is a particular problem with shared-use services and services that deliver general social benefits to both non-users and users. For example, relying on users to pay for public transit will inevitably result in our having less public transit than we need, because the price users are prepared to pay does not reflect the benefit to the community at large of investments in transit.

Measuring public services at their cost distorts the decisions we make about establishing new public services or expanding existing ones, because it is difficult to identify and measure all of the benefits that flow from those investments. It is particularly a problem, however, during periods of "fiscal constraint," when governments are looking for ways to "save" money. Because the budget-makers value services at their cost, by definition expenditure on any public service can be reduced without any net cost to society.

A perfect indication of this problem arose in the debate in Ontario over spending cut recommendations in the report of former TD Bank vice-president Don Drummond. Among Drummond's recommendations was the elimination of the government's new early learning program—the extension of kindergarten programming to a full day, integrated with after-school child care.

Extensive studies have shown repeatedly that the benefits to society from early learning investments, both in the short and long term, significantly outweigh program costs. In the short term, the payoff comes in the form of greater labour force participation and increased productivity for parents of children in early learning programs.⁶ In the long term, the evidence of better educational outcomes for children participating in early learning programs is overwhelming. Indeed, in deciding to extend kindergarten to a full day, the Government of Ontario relied on studies that identified precisely those kinds of economic gains (Pascal, 2009).

In an accounting framework in which services are valued at their cost, however, early learning programs can be eliminated at no net cost, since the benefit foregone has the same value as the cost savings from eliminating the program. Drummond's acceptance of deficit reduction as an overriding goal tipped the balance in favour of eliminating the program. The evidence supporting a net benefit from these programs may have been critical in the adoption of the policy in the first place, but it played no role whatsoever in the recommendation for its elimination.

A similar problem underlies our chronic underinvestment in public infrastructure. Infrastructure investments are undertaken based on long-term net benefits. Often the decisions to make these investments are supported by cost-benefit studies that demonstrate a positive net return to society after all costs are taken into account. Once the investment is complete, however, those net benefits completely disappear from our accounting, which by definition indicates that we receive no net benefit. For example, a decision to invest in road widening or a higher-capacity bridge would have been based in part on the value of the time saved by road users benefiting from reduced congestion. However, in economic accounts, those benefits are not recognized. The ongoing value of the road-widening or bridge is measured only by its economic depreciation.

Again, the distortion in decision-making created by this accounting convention was evident in a recommendation from the Drummond Report to cancel or defer a substantial proportion of the Ontario Government's proposed infrastructure renewal program. Indeed, the entire Drummond review exercise was based on the premise that while tax increases are costly to households, cuts to public services can be made with no net cost.

This theme—cutting public services without reference to the benefits foregone as a result of those cuts—is not unique to Ontario. It is repeated in all three orders of government and in every part of the country.

In some instances, the consequences are immediately evident. Fees charged for services that used to be universally accessible; reduced hours or closures for public facilities; reduced entitlements to cash benefits. In other instances, it can take years, even decades, for the full impact to be felt. Toronto is paying the price today for the cancellation of transit investments by the Harris Government 15 years ago. Canadians who have suffered from the consequences of the 2008 depression have been doubly burdened by the deterioration of the social safety net through two decades of cuts to social housing, employment insurance, and social assistance programs.

Cost-based accounting for the output from public services also distorts the debate over public service productivity. Valuing services at their cost means that, under standard measures of productivity, public service productivity by definition cannot increase. Any improvement in public service operations will be reflected in lower costs, which in turn will be reflected in a lower measured value for the service.

The fact that conventionally measured public service productivity cannot increase by definition highlights the disingenuousness of conservatives who criticize the productivity of public service workers.

Conclusion

Public services are pervasive. They affect virtually every aspect of our lives. They contribute significantly to our standard of living. They act as a powerful counterweight to the tendency of market forces to produce economic outcomes that are increasingly inequitable. They democratize consumption. Yet these services are pervasive to such an extent that we take them for granted. They are invisible.

That invisibility is not benign. It distorts our perceptions of the choices that are open to us. It leads us to underinvest in public services that are critically important to our economic future. And it makes public services vulnerable to the seductive and self-serving claims of conservatives that we can balance budgets simply by reducing public spending and without consequences, that tax cuts can be implemented at no cost, that any gain from a tax cut, no matter how small, is “worth it.”

Conservatives have taken full advantage of the invisibility of public services. The idea that any tax cut is worth it has been used as a smokescreen to obscure the fact that while tax cuts go disproportionately to those with high incomes, the costs of the public expenditure restraint needed to pay for them are borne disproportionately by lower- and middle-income Canadians.

And until we start to pay attention to the value we receive from the public services we use, that will continue.

Notes

- 1 *Compañía General de Tabacos de Filipinas v. Collector of Internal Revenue*, [1927]. Interestingly, the popular version of that quote—“I like to pay taxes. With them I buy civilization”—is directly parallel to billionaire Warren Buffett's comparison of his and his secretary's tax rates. The quote is attributed to Mr. Justice Holmes in an anecdote drawn from a conversation between Holmes and his secretary, and was reported by soon-to-be Justice Felix Frankfurter in his 1938 book, *Mr. Justice Holmes and the Supreme Court*.
- 2 I told a variant of this story for the first time in a presentation to the Standing Committee on Finance and Economic Affairs of the Ontario Legislature in 2002. I had been making a pitch on behalf of the Ontario Alternative Budget project for increased investments in public services, when a Conservative member of the committee accused me of suggesting that we would be better off if the government had more of our money and we had less of it to use ourselves. I replied that I wasn't sure I would have put it that way myself, but that's exactly what I was saying. And then I proceeded to take her through my day. Her question time was up before I finished.
- 3 The study focused on cash transfers and in-kind transfers for health, education, housing, early childhood education, and care and long-term care for the elderly. The figures presented here do not include cash transfers, which on average across the OECD were measured at 23% of disposable income.
- 4 A regressive tax is not one that raises more revenue from lower-income households than it does from higher-income households; it is a tax that raises *proportionally* more revenue from lower-income households than from higher-income households—that is, a tax that amounts to a higher proportion of the income of lower-income households than of higher-income households. Thus a tax can be regressive and still provide the tax side of a fiscal bargain that results in a net transfer of resources from higher-income to lower-income households.

- 5 A 2011 study for Canada using a standard international method for comparing living standards conducted for the Centre for the Study of Living Standards found an average total benefit of 55% of household income and an average net benefit (after taxes) of 7% of household income (Sharpe, Murray, Evans, & Hazell, 2011, p. 24).
- 6 These were the findings of Fortin, Godbout, and St-Cerny in their working paper, *Impact of Quebec's universal low-fee childcare program on female labour force participation, domestic income and government budgets*. Their analysis concluded that the tax/transfer return to the federal and Quebec governments from Quebec's universal low-fee child care program significantly exceeded its cost.

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Chapter 5

Canadian Public Opinion on Taxes

Frank Graves

Introduction

The study of public opinion on taxes is one of the most frustrating and confusing areas for the analyst of public attitudes, fraught with apparently ambiguous results that easily lead to diametrically contradicting conclusions. Whether it is in the service of disingenuous manipulation, or a genuine attempt to understand and reveal more about society and political choice, this is an area where one can easily construct two completely and apparently irreconcilable pictures of what the public really thinks. The data also consistently reveal a gap between what Canadians say and how they vote. Simply put, taxes do better on surveys than they seem to do in politics.

The Variety of Public Meanings of Taxation

Before I talk about the most recent data on taxes, I should contextualize the discussion by considering several factors that can further complicate the already complicated matter of gauging the public's views on taxes.

Part of the apparent ambiguity in public opinion on taxation can be explained by the variety of taxes we are talking about and the ways in which questions concerning them are framed. Another challenge is the differences in vested interests, values, and ideologies of the respondents. And there is also the fact that the public outlook on taxes is in a state of some flux; both in attitudes to taxes themselves and in outlook on closely related issues such as inequality, the role of the state, and views of the Canadian economy in a changing global context. In the next section, I will examine some partial indicators of these issues, and then turn to the historical context and some speculations about the future of this debate.

Type of Tax

Not surprisingly, attitudes toward taxes vary by the type of tax in question. For example, a majority of Canadian adults (59%) believe that the various