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CESTNICK

TAX MATTERS

Young Canadians will foot the bill for higher debt

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I've given my share of bad gifts to my wife, Carolyn, in the past. I've learned that exercise gear is not a good gift idea unless she specifically asks for it. And so, the weights I bought her three years ago went over like a lead balloon, outdone by the air freshener I bought for her birthday five years ago, and the mother of them all: the Olay Pro-X anti-aging deep wrinkle treatment I gave her for Christmas last year. These were memorable occasions for me – for all the wrong reasons.

Just as Carolyn is likely concerned about our upcoming anniversary and the gifts that may await her, I'm concerned about a particular gift that our children are going to inherit. Not my children, in particular. I'm talking about all young Canadians. That gift is a lot of debt that will have serious implications for them.

The debt

The amount of federal debt in Canada has reached historic levels. According to research from the Fraser Institute, the amount of debt in Canada per person reached a record high of $48,764 in 2020 when the pandemic hit. But the research shows that the debt cannot be attributed entirely to the pandemic emergency spending. When COVID-related spending is excluded, the per-person debt would still have been at record highs of $42,380 in 2020. This is 43 per cent higher than personal debt levels at the peak of the Second World War and 13 per cent higher than in 2019 (even after adjusting all figures for inflation).

Then, in 2021, federal per-person debt reached a new record at $48,955. Without COVID-related spending in 2020 or 2021, the per-person federal debt would still have reached $41,340 in 2021. The fact is that the federal debt was already on an upward trajectory even without the pandemic, which only made the problem worse.

Today, the government's federal debt per person is $47,070, which is still more than 25 per cent higher than in 2019, prior to the pandemic.

The cost

The cost of this increase in federal debt will be significant for all Canadians, but especially for younger generations. The Fraser Institute calculated the increase in personal income taxes that Canadians will have to pay to keep pace with the interest costs on the federal debt over their lifetimes.

The study shows that 16-year-olds in Canada today will pay an additional $29,663 in personal income taxes over their lifetimes just to pay the interest on the federal debt accumulated to date. The age 16-to-25 cohort today will each pay at least $20,000 in additional personal income taxes to cover federal interest costs. That's right, these additional taxes won't even reduce the level of the debt but will cover the interest only.

Older Canadians will face a lower burden than younger folks. Your 16-year-old child or grandchild can expect to pay 12 times the amount that a 65-year-old will have to pay. Canadian taxpayers aged 16 to 80 will pay, on average, $10,498 in extra taxes to cover federal interest costs on today's federal debt.

It's worth noting that, since the Fraser Institute has done the math here, interest rates have risen. An increase in rates will only increase the burden that Canadians face when covering interest costs on the debt. In the very, very long-run, inflation will reduce the real burden of the federal debt, but the interest on the debt is an annual cost that Canadians – particularly our children and grandchildren – will have to pay for.

Frankly, mortgaging the future of our children doesn't sit well with many Canadians. This is why holding our government accountable for its spending is so important. And to reiterate, this upward trend in the federal debt is not simply a COVID-driven trend.

The prognosis

So, what exactly will the government do to increase the tax burden on Canadians? While I don't have a crystal ball, I suspect that there are two areas in particular that this government might focus on. The first is the tax rate on capital gains. This would be an easy change because capital gains are perceived as the income of the wealthy. And to remind those who might have forgotten, the capital gains inclusion rate, which is currently 50 per cent, was 75 per cent throughout most of the 1990s.

What about principal residences? Real estate represents the greatest store of wealth for many Canadians. And today, your principal residence can be exempt from tax most of the time. Starting next January, you'll have to own a property for at least 12 months to access the exemption. Our rules are still more generous than in the U.S., so we could see further changes down the road, such as a limit on the total exemption that can be claimed.

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