



Fiscal Impact Estimate of Bill C-463: *Discover Your Canada Act*

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www.pbo-dpb.gc.ca

Key Points of this Note:

- In September 2011 the Standing Committee on Finance (FINA) passed a motion that “[c]onsistent with the Parliamentary Budget Officer (PBO) mandate[...] the PBO automatically always provide the Committee, within 45 calendar days of a Private Members’ Business item’s appearance on the Private Members’ Business Order of Precedence, a detailed and comprehensive costing analysis of all such items.”
- This report fulfills that motion with respect to Bill C-463: *An Act to amend the Income Tax Act (travel expenses)*. The proposed legislative amendments would provide individuals with tax deductions for travel expenses of up to \$2,000 per year, effective January 1, 2017. Fares for air, rail and bus modes would be eligible, provided they are:
 - Purchased from a Canadian-based carrier;
 - Travel is not for business purposes; and,
 - Travel is within Canada, crossing at least three provincial/territorial boundaries.
- Financially, the proposed measure could be expected to increase spending on eligible travel by 9 to 11 percent, at a fiscal impact of \$90 to \$120 million in 2017.
 - The costs of Bill C-463 are assumed to be borne by reduced federal personal income tax revenues.
 - Secondary economic and fiscal benefits associated with this tax measure are acknowledged, but not quantified in this note.

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1. Introduction

The Parliamentary Budget Officer's (PBO's) legislative mandate includes the preparation of cost estimates for any issue under the jurisdiction of Parliament.¹ In September 2011, the House of Commons Standing Committee on Finance passed a motion requiring that the PBO prepare a cost estimate of all private members' bills (PMBs) within 45 calendar days of the item's appearance on the PMB Order of Precedence.

Bill C-463: *An Act to amend the Income Tax Act (travel expenses)* would provide that the costs of purchasing travel tickets be deductible from a taxpayers' income, conditional that:²

- i. Tickets are purchased from a Canadian-based air, train or bus carrier;
- ii. Expenses are incurred for non-business purposes; and,
- iii. Travel crosses three different provincial boundaries, at minimum.

The maximum amount of ticket expense eligible for the deduction is \$2,000 annually. Travel expenses relating to an eligible child of a taxpayer can also be deducted, to a maximum of \$2,000 annually, per child.³

Travel expenses are deductible at different rates for each mode of travel: 40 per cent deductible by air, 75 per cent by train, and 100 per cent by bus.

From a fiscal perspective, federal income tax deductibility is the only material consideration in this estimate.

2. Methodology

The approach used to cost Bill C-463 incorporates a dynamic analysis, as a behavioural response can be expected. This approach prepares an estimate of the overall impact on federal tax revenues by:

1. Identifying a baseline group of existing travelers that would benefit from the proposed tax measure;
2. Determining the expected behavioural impact in response to the tax measure;
3. Determining the level of anticipated benefits; and,
4. Determining the duration of these benefits.

Identifying the Eligible Subset of Travellers

In 2010, Canadians spent \$3.2 billion on domestic travel fares in air, bus, train, boat and other commercial modes.⁴ This spending constitutes, on average, approximately 0.22 per cent of GDP.⁵ Assuming these expenditures remain a constant share of GDP, travel expenses eligible for tax deduction under Bill C-463 can be estimated for when the Bill would come into force in 2017.⁶

Travel expenses are eligible for tax deductibility conditional on three criteria:

- i. *Tickets are purchased from a Canadian-based air, train or bus carrier*

⁴ Statistics Canada. Table 426-0017, 2006-10. <http://www5.statcan.gc.ca/cansim/a26?lang=eng&retrLang=eng&id=4260017&paSer=&pattern=&stByVal=1&p1=1&p2=-1&tabMode=dataTable&csid=>. Accessed December 2012.

⁵ PBO projections.

⁶ Travel expenses are defined within Bill C-463 as 'the cost of purchasing a ticket or tickets from a Canadian-based carrier for a trip or trips by airplane, train or bus within Canada where each trip is not related to a business purpose and requires crossing at least three provincial boundaries'.

http://www.parl.gc.ca/content/hoc/Bills/411/Private/C-463/C-463_1/C-463_1.PDF

¹ <http://laws-lois.justice.gc.ca/eng/acts/P-1/FullText.html?term=79.2>. Accessed September 2012.

² http://www.parl.gc.ca/content/hoc/Bills/411/Private/C-463/C-463_1/C-463_1.PDF. Accessed December 2012.

³ 'Child', as defined in *Income Tax Act*, s. 63.

Approximately 92 per cent of domestic travel fares are in the air, bus and train modes.⁷ For the purposes of this analysis, it is assumed that this share remains stable and that all domestic air, bus and rail travelers utilize a Canadian-based carrier.

ii. Travel is not for business purposes

Historically, 12 per cent of Canadian travel expenditures are for business purposes and this analysis assumes that this relationship remains constant into future years.⁸ As such, 88 per cent of domestic travel expenditures meet the non-business purpose criterion of Bill C-463.

iii. Travel is within Canada, and crosses at least three provincial/territorial boundaries

Bill C-463 requires that eligible travel expenses are incurred in domestic travel where at least three provincial boundaries are crossed. Accordingly, eligible origin-destination province pairs are set out in Figure 2-1.

A sample of air traveller origin-destination data indicates that, on average, 23 per cent of domestic trips cross at least three provincial boundaries.⁹ This share is assumed to be representative of current domestic travel patterns.

Canadian air travel data also shows that the average price of long-haul domestic travel is 57 per cent higher than that of short-haul travel.¹⁰ This pricing differential is assumed to reflect the cost differential for eligible travel relative to ineligible travel in all modes for Bill C-463.

As such, the dollar-weighted share of domestic travel in the air mode spanning at least three provincial boundaries is estimated at 31 per cent.¹¹

Figure 2-1

Eligible Origin-Destination Province/Territory Pairs

Origin	Eligible destinations
BC	QC, ON, PE, NS, NB, NL, NU
AB	QC, PE, NS, NB, NL
SK	PE, NS, NB, NL
MB	PE, NS, NL, YT
ON	BC, NS, NL, YT
QC	BC, AB, YT, NT
NB	BC, AB, SK, YT, NU, NT
PE	BC, AB, SK, MB, NT, YT, NU
NS	BC, AB, SK, MB, ON, NT, YT, NU
NL	BC, AB, SK, MB, ON, YT, NT, NU
YT	MB, ON, QC, NB, NS, PE, NL
NT	QC, NB, NS, PE, NL
NU	BC, NB, PE, NS, NL

Sources: Bill C-463, PBO calculation.

Reliable origin-destination data for the rail and bus modes was not located, so a range of estimates were generated. At the high end, rail and bus travel patterns are assumed to be identical to that of the air mode (*i.e.* 31 per cent of trips span at least three provincial borders on a dollar-weighted basis). At the low end, eligible domestic travel is estimated to be 8 per cent, or one-fourth the frequency of air travel.^{12, 13}

⁷ Statistics Canada. Table 426-0017.

<http://www5.statcan.gc.ca/cansim/a26?lang=eng&retrLang=eng&id=4260017&paSer=&pattern=&stByVal=1&p1=1&p2=-1&tabMode=dataTable&csid=>. Accessed December, 2012.

⁸ Statistics Canada, Table 401-0041.

<http://www5.statcan.gc.ca/cansim/a26?lang=eng&retrLang=eng&id=4010041&paSer=&pattern=&stByVal=1&p1=1&p2=-1&tabMode=dataTable&csid=>. Accessed December, 2012.

⁹ Statistics Canada, 1995-99. Sufficiently detailed Domestic Air Passenger Origin and Destination data was not located after 1999.

¹⁰ Statistics Canada, Table 401-0041.

<http://www5.statcan.gc.ca/cansim/a26?lang=eng&retrLang=eng&id=4010041&paSer=&pattern=&stByVal=1&p1=1&p2=37&tabMode=dataTable&csid=>. Accessed: December 2012

¹¹ Eligible travel is estimated to comprise 23% of travel volumes, but comprises 31.4% of the dollar value of travel, as an eligible ticket is estimated to be 57% more expensive than an ineligible ticket.

¹² Assumptions are based off data from the Canadian Travel Survey, 1997-2004.

¹³ Information provided by VIA Rail indicates that in 2012, 9.4 per cent of VIA passengers crossed three or more provincial boundaries (on a dollar-weighted basis). This is within the range used in this analysis.

Tax Deductibility

The net impact of a tax deduction is a function of the taxpayers' marginal federal personal income tax rate. For the purposes of this analysis, the marginal tax rate for the median Canadian traveller (22 per cent) was applied to all travelers when computing the value of the tax deduction in all modes.^{14,15}

The effective price impact at a 22 per cent marginal tax rate in each of the three eligible modes of transportation can be estimated, and is set out in Figure 2-2.

Figure 2-2
Effective Net Travel Expense Impact,
Bill C-463

Mode	Per cent deductible ¹⁶	After tax price reduction ¹⁷
Air	40%	-8.8%
Bus	100%	-22%
Train	75%	-16.5%

Source: PBO calculation.

Behavioural Effects

Based on existing literature examining the elasticity of demand for airline travel in developed economies, including Canada, it is expected that Canadians would adapt their travel behaviour in response to the measures proposed in Bill C-463.^{18,19,20}

It is generally observed that as the number of available travel mode alternatives increases and/or the time opportunity cost of travel decreases, consumers become more sensitive to price. Furthermore, narrow price impacts (e.g. a price change on one specific route) will result in greater consumer price sensitivity as compared to broader price impacts (e.g. a price change to all domestic routes).²¹

For the purposes of this analysis, the price elasticity for long-haul domestic travel is estimated to be -1.0. This index is based on a composite of empirical findings from existing literature. Illustratively, a one per cent decline in the price of travel is expected to result in a one per cent increase in the quantity of travel demanded.

This analysis assumes that tax measures will be fully reflected in consumer ticket prices and potential surplus is not captured through a pricing response by air, train or bus carriers. Should carriers respond to the measures proposed in Bill C-463 by increasing ticket prices on eligible routes, a corresponding decline in induced demand can be expected.

Should Bill C-463 be enacted, the PBO estimates that between \$900 million and \$1.1 billion per year (indexed to 2013 dollars) in travel expenses will be eligible for tax deduction. Of this spending, \$80 to \$110 million is expected to be directly induced due to Bill C-463 (Figure 2-3).

¹⁴ Statistics Canada, Social Policy Simulation Database and Model and Table 426-0014.

¹⁵ Statistics Canada, Table 426-001.

<http://www5.statcan.gc.ca/cansim/a26?lang=eng&retrLang=eng&id=4260017&paSer=&pattern=&stByVal=1&p1=1&p2=-1&tabMode=dataTable&csid=>. Accessed December 2012.

¹⁶ As per Bill C-463,

http://www.parl.gc.ca/content/hoc/Bills/411/Private/C-463/C-463_1/C-463_1.PDF. Accessed December, 2012.

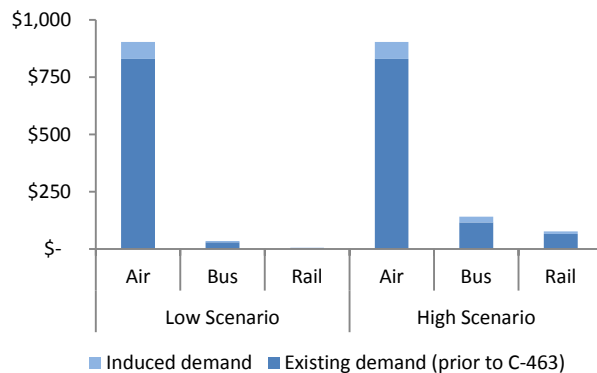
¹⁷ Calculated as the product of the percent of travel expense deductible and the marginal tax rate of travellers.

¹⁸ Gillen, D.W., W.G. Morrison and C. Stewart, *Air travel demand elasticities: concepts, issues and management*, Department of Finance, Government of Canada, January 2003.

¹⁹ Brons, M., Pels, E., Nijkamp, P. and P. Rietveld, *Price Elasticities of Demand for Passenger Air Travel; A Meta-Analysis*, 2001.

²⁰ Smyth, M. and B. Pearce, IATA Economics Briefing No. 9: Air Travel Demand, April 2008.

²¹ Smyth, M. and B. Pearce, IATA Economics Briefing No. 9: Air Travel Demand, April 2008.

Figure 2-3**Existing and Induced Expenditure on Travel Eligible Under Bill C-463, in 2017***Figures are in millions, \$; indexed to 2013*

Source: PBO calculation.

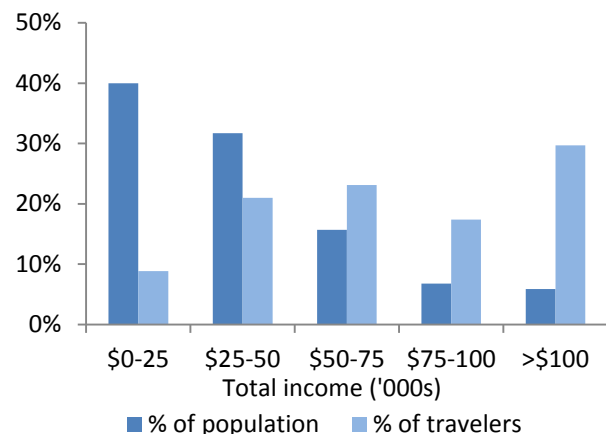
The sources of prospective induced demand are varied: some qualifying travellers' routes will remain unchanged, but they may substitute ineligible modes of transport for modes eligible under Bill C-463; others travellers may choose to substitute more proximate destinations in favour of travel destinations eligible for tax deductibility under Bill C-463; and others may be consumers that substitute non-travel spending for travel eligible under Bill C-463.²² The PBO does not attribute shares of anticipated increased demand to any specific type of induced behaviour.

The PBO acknowledges that long haul travelers' leisure trips may be of a longer total duration than short haul trips, and could result in higher total secondary expenditures commonly associated

with leisure travel (e.g. accommodations, dining, local transportation etc.).²³ This report does not quantify the economic or fiscal impact of these secondary effects.

Distribution of Benefits

The benefits of tax measures proposed under Bill C-463 are anticipated to concentrate to higher income earners (Figure 2-4). Based on surveys of Canadian travelers, it is anticipated that approximately 70 per cent of the tax benefits of the Bill would accrue to individuals earning an annual income in excess of \$50,000. This earnings segment represents approximately 28 per cent of Canadians over the age of 24.

Figure 2-4**Distribution of Benefits by Income Class, Bill C-463**

Sources: PBO calculation and Statistics Canada.

²² Smyth, M. and B. Pearce, IATA Economics Briefing No. 9: Air Travel Demand, April 2008.

²³ Canadian Travel Commission, Travel Characteristics Q4 2010. http://en-corporate.canada.travel/sites/default/files/pdf/Research/Stats-figures/Tourism-performance/Quarterly%20Travel%20Characteristics/2010_travelcharacteristicsq4-en.pdf. Accessed: December 2012.

3. Estimate of Fiscal Impact

If approved by Parliament, Bill C-463 would not come into force until January 1, 2017.

Accordingly, the fiscal impact of the Bill is projected to accrue from January 1, 2017 onward and is estimated according to the following calculation:

$$\begin{aligned} \text{Net impact on federal tax revenues} = & \\ & \text{Eligible ticket purchases} \\ & \times \text{Marginal tax rate} \\ & \times \text{Per cent deductible} \end{aligned}$$

In sum, the net impact on federal tax revenues of Bill C-463 is expected to be between \$90 and \$120 million in 2017 (expressed in 2013 constant dollars).²⁴ Detailed estimates are set out in Figure 3-1. The costs of Bill C-463 are expected to grow at a rate consistent with Canada's GDP beyond 2017.

On a per capita basis, Canadians are expected to spend approximately \$30 per year on eligible travel expenses in 2017.²⁵ As such, the \$2,000 upper threshold for annual travel expenses is not expected to be reached by most eligible taxpayers and will not have a material impact on the total cost of the Bill.

Figure 3-1

Effective Relative Net Travel Expense Impact, Bill C-463

Figures are in millions, \$; indexed to 2013

Mode	Per cent deductible ²⁶	Marginal tax rate	Eligible ticket purchases ²⁷		Net impact on federal tax revenues	
			High	Low	High	Low
Air	40%	22%	\$900	\$900	-\$80	-\$80
Bus	100%		\$140	\$35	-\$30	-\$8
Train	75%		\$80	\$20	-\$10	-\$3
Total*	-	-	\$1,130	\$940	-\$120	-\$90

Source: PBO calculation and Statistics Canada.

*Figures may not sum due to rounding.

The fiscal impact of Bill C-463 is assumed to be borne by reduced tax revenues, as an alternate revenue source has not been identified.

It is assumed that the incremental expense to the Canada Revenue Agency to administer the measures proposed in the Bill are not material to the overall cost estimate.

²⁴ PBO projections.

²⁵ PBO calculation.

²⁶ As per Bill C-463.

²⁷ Statistics Canada Table 426-001.