

# **PAPER C**

## **Tax Cuts: Keeping Promises, Creating Opportunities**

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# Ontario's Tax Cut Strategy \*

The Ontario Government has reduced taxes significantly over the past five years. Significant additional cuts are being proposed and will continue to be made in the future.

## *Tax Cuts Now and Low Taxes in the Future*

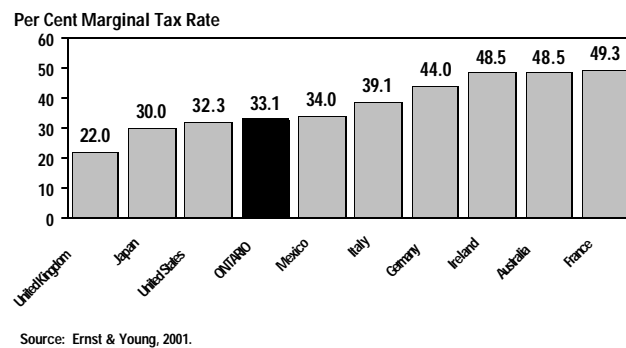
- T Making taxes competitive now
- T Taxpayer protection to guard against future increases
- T Balanced budgets to ensure we live within our means

Tax cuts are an important part of a balanced program to promote healthy economic growth, together with expenditure management and debt reduction. Today, balanced budget and taxpayer protection legislation guarantees the people of Ontario that their government is no longer running deficits and that tax increases are a thing of the past. They also have the government's continued commitment to cutting taxes as a way of maintaining and improving our economy and our competitive position in a global marketplace.

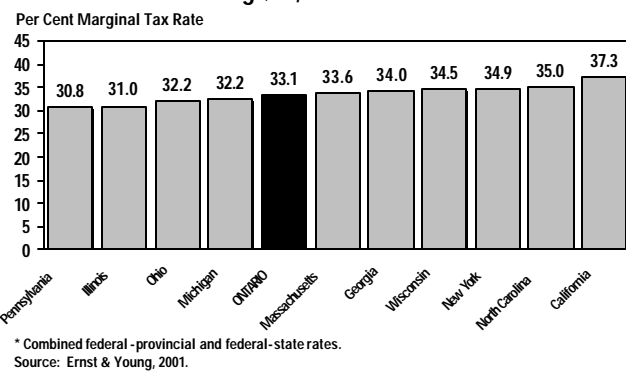
## Tax Cuts Work

In 1995, Ontario's personal income tax rate had reached an all-time high, at 58 per cent of basic federal tax. At that time, Ontario's personal income taxes were among the highest in North America.

## International Comparison of Personal Income Tax Rates, 2001 For Individuals Earning \$60,000



## Comparison of Ontario and U.S. Personal Income Tax Rates\*, 2001 For Individuals Earning \$60,000



\* Where applicable, statements made in this paper concerning measures proposed in this Budget are conditional on the approval of relevant legislation by the Legislature.

Since then, Ontario's income tax has been cut dramatically. In addition to significant tax rate decreases, Ontario has also moved to increase the value of certain non-refundable tax credits—for example, those recognizing the extra costs associated with pursuing an education or having a disability—and to index tax brackets and other non-refundable tax credits to Ontario's inflation rate. Taxpayers with low and middle incomes have benefited the most from these cuts.

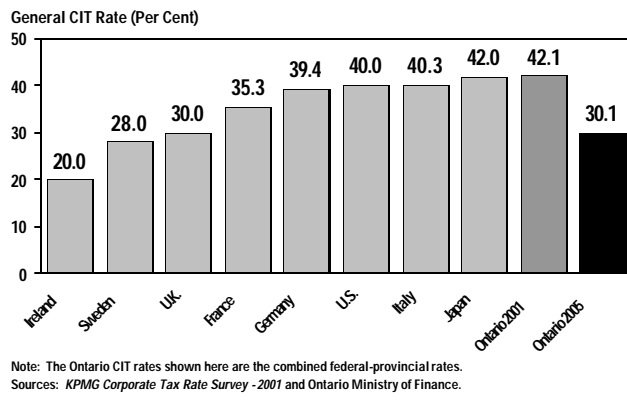
Businesses have benefited from the Province's reductions to profit-insensitive taxes. Ontario's payroll tax was eliminated for 88 per cent of private-sector employers and reduced for all other private-sector employers. Business education property taxes have been cut and municipal discretion to shift the local property tax burden onto businesses has been limited.

Small businesses have had their income tax rate cut, and the number of businesses that qualify for this lower rate has been increased. Ontario's general rate of corporate income tax is being reduced from the highest among industrialized countries to a level below all U.S. states.

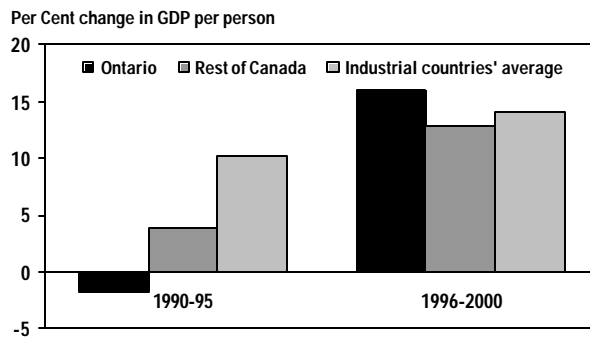
As a result of the tax cuts made by the Ontario Government, the Ontario economy is much more competitive and much stronger than it was five years ago.

Real GDP per person has grown by a remarkable 16.3 per cent in Ontario over the past four years. This is one of the strongest growth periods since 1960 for this important economic indicator. In the period following the introduction of this government's personal income tax cuts, Ontario's growth in real GDP per person has surpassed the average for industrialized countries.

### International Comparison of Corporate Income Tax Rates, 2001



### Sound Policies Lead to Strong Growth: Ontario Goes from Worst to First



Ontario's job growth has also been exceptional since tax cuts were first announced. Ontario's total employment has grown 16 per cent, compared to only 10.6 per cent in the rest of Canada, and 8.5 per cent in the United States.

This improved performance has been a significant achievement, but clearly there is still more to do.

### More Tax Cuts Are Needed

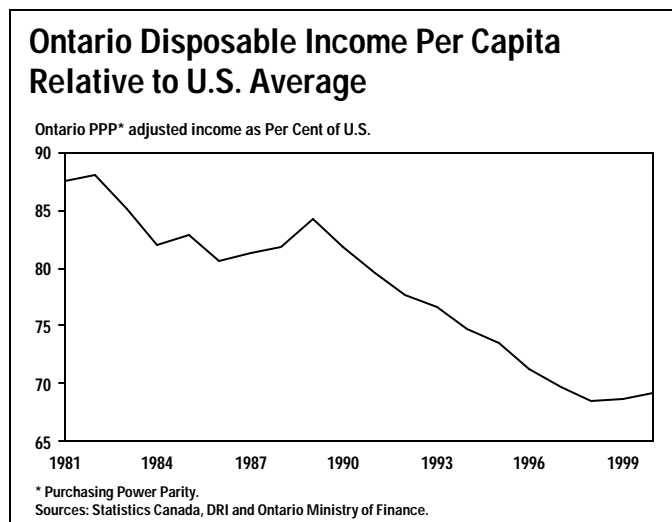
The Ontario Government's recent tax cuts come on the heels of 30 years of steady increases in tax rates. Taxes, when combined for all levels of government in Canada, rose from under 27 per cent of GDP in the 1960s to over 37 per cent in the 1990s. Over the same period, productivity growth and growth in the standard of living for people in Ontario declined.

The Ontario economy has been performing exceptionally well in the past five years, but there remains a lot of lost ground to recover. Real disposable income per person in Ontario actually fell from \$19,600 in 1989 to \$17,800 in 1996. This decrease resulted from a combination of job losses, weak salary growth and rising taxes prior to 1996.

People in Ontario, comparing their situation to that of friends and relatives living in the United States, are aware that their incomes have not grown nearly as much. At the beginning of the 1980s, the average level of personal disposable income in Ontario was close to 90 per cent of the U.S. average. While it has begun to rebound in recent years, it is still only about 70 per cent.

Higher business investment is critical to more rapid implementation of new technology, productivity growth and increases in the real earnings of Ontario workers. Canada cannot achieve the rate of investment it needs unless its corporate tax rates are competitive.

Governments in Canada have just begun to take action on the corporate tax side. Even after the initial reductions in corporate income tax rates that have occurred in the past year, Canadian corporate income tax rates remain among the highest in the world.



The high level of corporate taxation in Canada is one reason why Canadian investors have been moving their capital out of the country. In the years from 1995 to 2000, Canadian investors increased their foreign investments by \$255 billion, which is \$83 billion more than foreign investors brought into Canada.

### **Personal Income Tax Cuts: Improving Disposable Income**

The first stage of the Ontario Government's tax cuts, starting in 1996, focused on personal income tax cuts.

This focus reflected an economy that suffered from severely depressed demand conditions, inadequate incentives to earn income and take risks, and high unemployment. Personal income tax cuts provide a strong short-term demand stimulus and support higher long-term productivity growth.

- , Personal income tax cuts directly attack the problem of low disposable income by boosting the incomes of individuals, giving them the means to boost their spending.
- , Personal income tax cuts increase long-run economic growth. By allowing people to keep more of what they make, personal income tax cuts increase the incentives to work harder and make the investments that lead to higher income in the future.

#### **Ontario's Income Tax Cuts to Date**

On January 1, 1996, the Ontario personal income tax rate was 58 per cent of basic federal tax. By July 1, 1998, Ontario's income tax rate had been cut to 40.5 per cent of basic federal tax.

In addition to cutting the tax rate by 30 per cent, the government also increased Ontario's personal credits. These measures benefited all taxpayers. As well, the Ontario Tax Reduction program was enhanced, which amplified these tax cuts for individuals with lower incomes.

In its 1999 Budget, the government committed to further personal income tax reductions and implemented an additional five per cent across-the-board rate reduction. This brought Ontario's personal income tax rate down to 38.5 per cent of basic federal tax.

The 2000 Budget announced a new "Made-for-Ontario" income tax system, one that sets Ontario's tax brackets and tax rates independently of the federal government's income tax system. Straight away, the government used its new flexibility to implement important policies for the benefit of Ontario's taxpayers and economy.

- , The government cut the lowest tax rate, even when the federal government would not. The government also cut the middle tax rate.
- , All Ontario investors benefit from the plan to reduce the taxable proportion of capital gains to 50 per cent. Ultimately, all Canadians benefited as well when the federal government decided to follow Ontario's lead.
- , Ontario's high-tech research firms will have an improved ability to attract and retain highly skilled and mobile research employees as a result of the Ontario Research Employee Stock Option Credit.
- , Investors in Ontario mining companies would benefit from the additional Ontario flow-through shares incentive. This initiative was also followed by the federal government for the benefit of investors across Canada.

As well, the government implemented full protection against inflation-induced tax increases for the taxpayers of Ontario for the first time in 15 years. In this taxation year alone, Ontario's fully indexed personal income tax system is protecting Ontario taxpayers from \$290 million of hidden tax increases. People in Ontario will not pay more Ontario tax just because their salaries keep pace with inflation.

The 2000 Ontario Economic Outlook and Fiscal Review included more new tax cut announcements for the benefit of Ontario taxpayers. Tax credits for individuals attending post-secondary school, individuals with disabilities and the people who support them were all enriched. As well, the plan to reduce the taxable proportion of capital gains was accelerated in the 2000 Ontario Economic Outlook and Fiscal Review. Effective October 18, 2000, the taxable proportion of capital gains reported for Ontario income tax purposes dropped to 50 per cent.

Additional government actions have further supported working families. The 1998 Budget introduced the Ontario Child Care Supplement for Working Families, which, by providing a refundable tax credit of \$1,020 for each child under age seven, had the effect of increasing the tax savings for low- and moderate-income working families. In 1999, the annual benefit was increased by \$80 per child to \$1,100 per child under age seven. The single-parent supplement was introduced in the 2000 Budget, increasing the maximum benefit for single-parent families by \$210 per child to \$1,310 per child under age seven.

## Completing the 20 Per Cent Tax Cut

Beginning in 2002, Ontario's personal income tax rates are proposed to be cut again.

- , Over the next two years, Ontario's first and second tax rates would be cut to 5.65 per cent and 8.85 per cent, respectively.
- , On January 1, 2003, the threshold above which surtax becomes payable would be increased, effectively eliminating the first tier of the current two-tier surtax.

In 1999, the Government of Ontario committed to provide Ontario taxpayers with an additional \$4 billion in tax cut benefits over five years through a 20 per cent personal income tax reduction. Full implementation of the measures proposed in this Budget, combined with the personal income tax cuts announced in the 1999 and 2000 Ontario Budgets, would mean:

- , 95 per cent of taxpayers would see Ontario tax savings of 20 per cent or more;
- , average tax savings for taxpayers with incomes of up to \$100,000 would exceed 20 per cent;
- , the largest percentage reductions would be concentrated on taxpayers with lower and middle incomes; and
- , more than \$4 billion of additional tax savings would be delivered to Ontario taxpayers.

### Estimated Average Ontario Personal Income Tax (PIT) Savings from Proposed Tax Cuts, when Combined with Ontario PIT Cuts Announced in 1999 and 2000<sup>1</sup>, by Income Group

Income Group <sup>2</sup>	Ontario Taxpayers	Estimated Average PIT Savings
Less than \$16,160	10%	69.6%
\$16,160 - \$21,115	10%	42.6%
\$21,115 - \$26,015	10%	33.2%
\$26,015 - \$30,945	10%	31.1%
\$30,945 - \$36,400	10%	31.4%
\$36,400 - \$42,320	10%	28.1%
\$42,320 - \$49,765	10%	24.8%
\$49,765 - \$60,455	10%	22.5%
\$60,455 - \$82,510	10%	24.7%
\$82,510 - \$85,680	1%	25.2%
\$85,680 - \$89,160	1%	24.0%
\$89,160 - \$93,670	1%	23.2%
\$93,670 - \$98,540	1%	22.4%
\$98,540 - \$104,670	1%	21.4%
\$104,670 - \$113,695	1%	19.7%
\$113,695 - \$128,545	1%	18.3%
\$128,545 - \$157,190	1%	16.3%
\$157,190 - \$232,690	1%	13.6%
\$232,690 - \$347,700	0.5%	11.3%
\$347,700 and up	0.5%	10.2%
<b>Total</b>	<b>100%</b>	<b>32.1%</b>

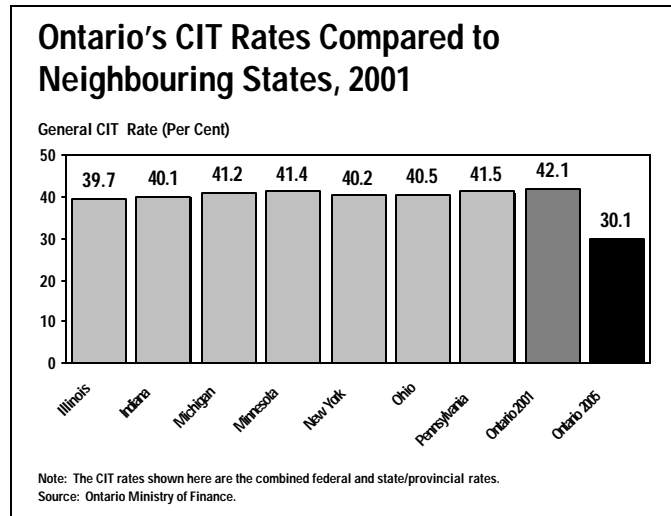
- (1) Includes Ontario's 1999 and 2000 rate cuts, indexation at estimated 2003 parameters, reduction of the capital gains inclusion rate to one-half and enhancement of tax credits for disability and education. Savings have been calculated in comparison to the tax system in place after Ontario's original PIT cuts.
- (2) The income groups divide Ontario taxpayers (before Ontario's original personal income tax cuts) into: nine deciles, each consisting of 560,000 taxpayers, with incomes up to \$82,510; nine percentiles, each containing 56,000 taxpayers, with incomes between \$82,510 and \$232,690; and two half-percentiles, consisting of 28,000 taxpayers each, with incomes over \$232,690.

## Business Tax Cuts: Creating Jobs Through Competitive Businesses

In 2000, the Ontario Government announced a series of tax cuts that would focus directly on investment, to boost long-term job creation and productivity growth.

The cut in the inclusion rate for capital gains income to 50 per cent will boost the incentives for entrepreneurial investment and risk-taking. It is a vital encouragement for the establishment of new businesses in leading areas of technology, which have been found to be the key to increases in economic growth.

In addition, the 2000 Budget announced an immediate one percentage point cut in all of the Corporate Income Tax (CIT) rates, and a further 0.5 percentage point cut on January 1, 2001. This was to be followed up by a medium-term plan—a commitment to further reduce rates to eight per cent—to make combined CIT rates in Ontario lower than rates in the U.S. neighbouring states by 2005.



Capital is highly mobile internationally, and it goes to the countries where it earns the highest after-tax rate of return.

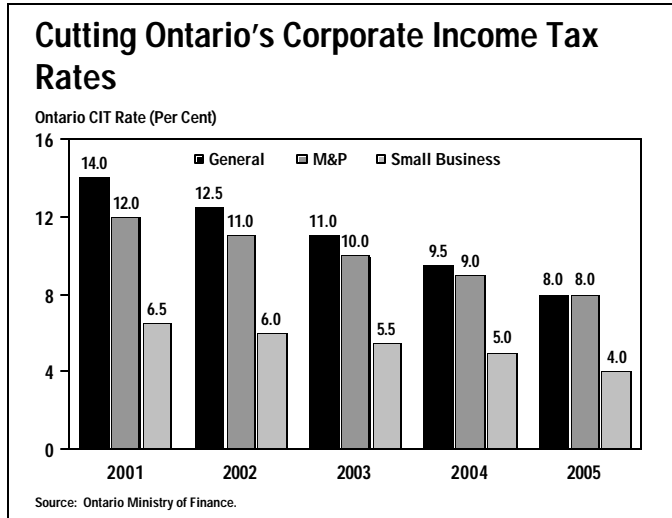
A country that has an above-average corporate tax rate will have a lower rate of investment. People who live and work in that country are ultimately the losers, since the jobs available to them will be at a lower technological level, on average, and will pay lower incomes.

Many of the countries that have enjoyed the strongest growth in standards of living in the past decade have cut their CIT rates to levels far below the Canadian average. These include Ireland, the United Kingdom, South Korea, Denmark, Norway and the Netherlands.

## Finalizing the Corporate Income Tax Rate Cut

In this Budget, the Ontario Government proposes to legislate a firm schedule to deliver the corporate tax cut plan it announced in last year's budget. These cuts would be completed in 2005.

Legislating the tax cut plan would provide investors with certainty and clear information on which to base their future investment plans in Ontario.



## Reducing and Simplifying Capital Tax

The capital tax discourages investment in capital, when more capital per worker is what is needed to boost productivity and standards of living. The capital tax is unrelated to profits, making it a fixed cost on businesses. In periods of economic slowdown when businesses are forced to cut costs, the capital tax forces them to cut in the areas where they have flexibility, which is chiefly wages. Therefore, the capital tax is a potential job killer.

The Business Tax Review Panel noted that, on an international basis, Canada is almost unique in having capital taxes. The Panel believed that the capital tax serves as a deterrent to attracting international investment.

The Business Tax Review Panel recommended that Ontario eliminate the capital tax for regular corporations and financial institutions. As a first step, it recommended that Ontario introduce a capital tax deduction for the first \$5 million of taxable capital.

This Budget proposes to provide a \$5 million capital tax deduction for all businesses effective January 1, 2002. This would increase capital available for reinvestment, simplify the tax system and remove capital tax liability for over 11,000 small and medium-sized businesses.

## **Tax Incentive Review**

In order to achieve certain economic and social objectives, Ontario provides targeted tax incentives, typically as deductions or tax credits, which reduce the tax an individual or corporation would otherwise have to pay. Targeted tax incentives can be an affordable and effective mechanism for achieving policy objectives.

However, once introduced, tax incentives tend to become fixtures of the tax system. Unlike other forms of government spending, they are not subject to regular review. The Business Tax Review Panel noted that, while tax incentives can be very effective, they add a source of complexity to the tax system and need to be reviewed to ensure that they continue to achieve the original policy intent.

The Province will conduct a review of tax incentives to determine if they are still necessary and effective in an environment of significantly reduced tax rates and lower tax burdens, and to address the concerns raised by the Business Tax Review Panel.

The government will also review certain targeted taxes, such as the Corporate Minimum Tax and the Tax for Fuel Conservation, to ensure that such measures are still appropriate.

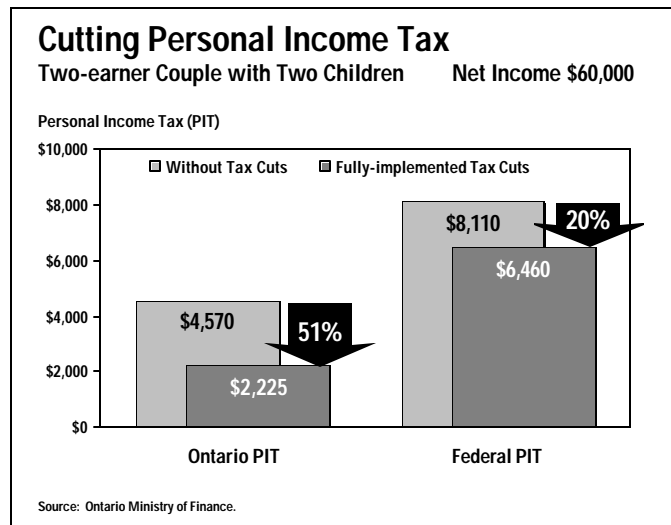
## **Federal Government Still Needs to Do More**

The Government of Ontario has repeatedly called on the federal government to follow Ontario's lead by enhancing the competitive economic advantage of Ontario and Canada, and improving disposable income by cutting federal taxes further.

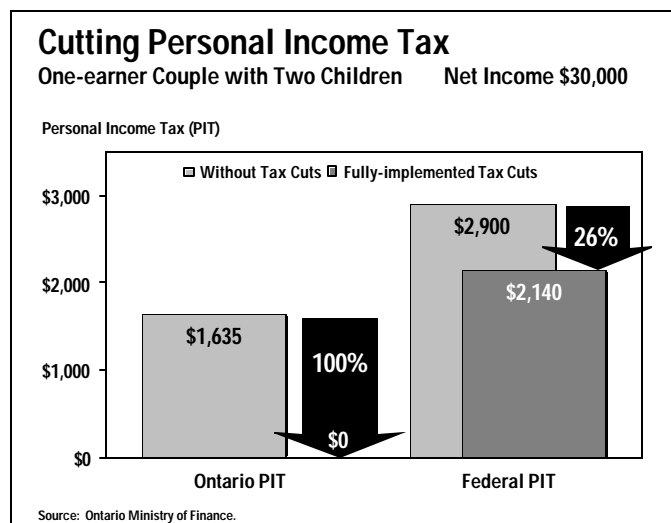
### **Bigger Federal Personal Income Tax Cuts Are Needed**

Ontario collects less than one-third of the income taxes paid by the people of Ontario. If the income tax burden on Ontario families is to be reduced significantly, then the federal government must also act, since the bulk of personal income taxes are levied by the federal government.

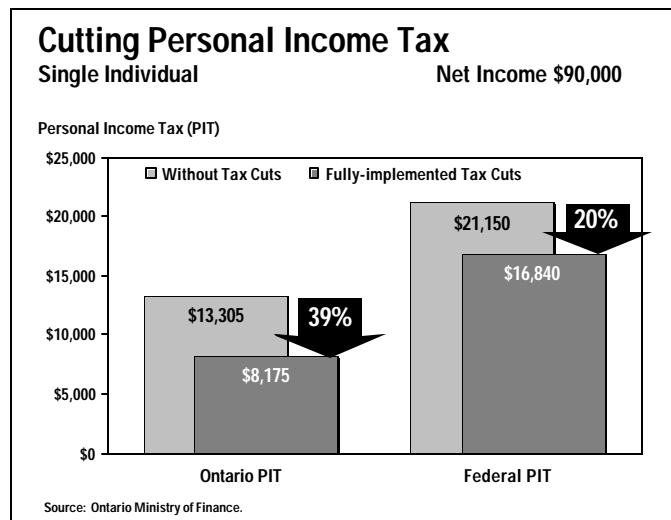
A couple with two children and net income of \$60,000 from two earners would save \$2,345 in Ontario personal income tax, or more than 50 per cent when the changes proposed in this Budget are added to tax cuts announced in previous budgets. Federal personal income tax cuts, when fully implemented, would save this family \$1,650, or 20 per cent. At that time, this family would pay about \$3 in federal tax for every \$1 of Ontario tax.



A couple with two children and net income of \$30,000 from one earner would pay \$1,635 less Ontario income tax when the changes proposed in this Budget are added to those announced in previous Ontario budgets. They would no longer pay Ontario income tax. In contrast, this family would continue to pay federal income tax of \$2,140, even after the proposed federal cuts deliver \$760, or 26 per cent, in income tax savings for this family.



A single individual earning \$90,000 would save \$5,130, or 39 per cent, from Ontario's personal income tax cuts, including those proposed in this Budget. Fully implemented federal income tax cuts would save this individual \$4,310, or only about 20 per cent. At that time, this individual would pay more than twice as much federal tax as Ontario tax.



Federal personal income taxes remain, on average, more than double the level of Ontario's personal income taxes, even after taking into consideration past and planned federal income tax cuts. With the measures proposed in this Budget, more than 735,000 individuals and families in Ontario would not pay Ontario personal income tax but would still pay federal income tax.

While Ontario's top marginal rate has been cut by over 20 per cent since 1995, the top marginal rate of federal tax has dropped by only about seven per cent. The relatively small cut in the top marginal rate of federal tax is a source of particular concern.

At all income levels, the federal government must do more to get federal personal income taxes down.

### Federal Business Taxes Are Too High

Canada's corporate income tax rates are also high compared to competing jurisdictions. Investment is very mobile, and companies will invest in Canada only if their after-tax income is competitive with other countries.

Ontario has set a target for a single lower overall rate of eight per cent for all large businesses by 2005—this is a 48 per cent cut in the general rate and a 40 per cent cut in the manufacturing and processing rate. By comparison, the federal government is cutting the general corporate rate by 24 per cent—only half of the Ontario cut.

The federal government needs to cut corporate rates deeper to improve our international competitiveness. If the federal government met the challenge in the 2000 Ontario Budget to match our corporate rate cuts, the combined federal-provincial rate, at 23 per cent, would be among the lowest in the world.

It is also time for the federal government to reform the manner in which it manages the nation's Employment Insurance (EI) program. The federal government continues to use EI premiums contributed by employers and employees as own-source revenue. It should, instead, establish a separate account for EI, which, like the Canada Pension Plan, would be externally managed and invested in market securities.

At the same time, EI premium rates continue to be unnecessarily high. Ontario has called on the federal government to reduce EI premiums immediately to below \$2 per \$100 of insurable earnings. This would fully offset the CPP contribution increases that have taken effect in 2001, and would ensure that there would be no further increase in the federal payroll tax burden this year.

# Details of Tax Changes

The following sections provide information on the taxation measures proposed in the Budget. For a precise description of these measures, the reader is advised to consult the amending legislation.

## Income Tax Act

### Personal Income Tax Rates

This Budget proposes further cuts to Ontario personal income tax rates.

- , Effective January 1, 2002, the first Ontario tax rate would be reduced from 6.2 per cent to 6.05 per cent of taxable income up to \$30,814 (indexed after 2001), and the middle Ontario tax rate would be reduced from 9.24 per cent to 9.15 per cent of taxable income between \$30,814 and \$61,629 (both amounts indexed after 2001).
- , Effective January 1, 2003, the first Ontario tax rate would be reduced further, to 5.65 per cent of taxable income up to \$30,814 (indexed after 2001), and the middle Ontario tax rate would be reduced further, to 8.85 per cent of taxable income between \$30,814 and \$61,629 (both amounts indexed after 2001).

### Surtax and Tax Reduction

Ontario's two-tiered surtax is calculated as a percentage of basic Ontario tax in excess of specified amounts. In 2001, the first surtax tier does not apply to taxpayers with incomes of less than \$53,650 and the second surtax tier does not apply to taxpayers with incomes of less than \$63,365. Automatic indexation of the surtax thresholds ensures that these income levels will increase to keep pace with inflation.

To eliminate the surtax payable by taxpayers who pay only the first-tier surtax, it is proposed that the basic Ontario tax threshold above which the first-tier surtax applies be raised to the same level as the threshold for the second surtax tier.

- , Effective January 1, 2003, the surtax would be calculated as 56 per cent of Ontario income tax in excess of \$4,491 (indexed after 2001).

As a result of this proposed change, about one-third of current surtax payers—more than 340,000 individuals—would no longer pay the personal income surtax.

The Ontario Tax Reduction reduces or eliminates Ontario personal income tax payable by taxpayers with low and moderate incomes. Automatic indexation of the Ontario Tax Reduction amounts ensures that taxpayers who benefit from the program will continue to do so, even if their incomes increase by the rate of inflation.

With the proposed changes to the first and middle tax rates, about 75,000 additional low-income taxpayers will be removed from Ontario's tax rolls and 580,000 additional taxpayers with modest incomes will have their Ontario tax further reduced by the Ontario Tax Reduction.

#### Alternative Minimum Tax

For 2001, Ontario alternative minimum tax (AMT) will be calculated as 38.75 per cent of the additional tax attributable to the federal AMT calculation, and would be added to Ontario tax calculated under the regular rules. The calculation for 2001 will be expressed as:

$$\text{Ontario AMT} = \text{Ontario Tax} + 38.75 \text{ per cent} \times (\text{Federal AMT} - \text{Federal Tax})$$

The 2001 rate change for the Ontario AMT calculation reflects the change to Ontario's tax rates and the proposed change to federal tax rates.

As a result of the changes to Ontario tax rates proposed in this Budget, the appropriate percentage for 2002 would be 37.81 per cent.

#### Medical Expenses Tax Credit

A claim for medical expenses paid for a dependant, other than a spouse, must be reduced where the dependant's net income exceeds the basic personal amount. For Ontario purposes, the claim made for 2001 by an individual for the medical expenses of a dependant will be reduced by 26.35 per cent of the amount by which the dependant's net income exceeds the basic personal amount. This reflects changes to Ontario's tax rates and proposed changes to federal tax rates.

As a result of the changes proposed to Ontario tax rates in this Budget, for 2002, the claim made by an individual for medical expenses of a dependant would be reduced by 25.71 per cent of the amount by which the dependant's net income exceeds the basic personal amount.

## Equity in Education Tax Credit

The Budget proposes a refundable tax credit, effective for the 2002 and subsequent taxation years, that would be provided in respect of kindergarten, elementary and secondary tuition fees at independent schools in Ontario. This credit would apply to the first \$7,000 per child of tuition fees exclusively and would not include, for example, expenses for books, sports, uniforms, computers, travel or boarding. Consultations will identify the appropriate framework for establishing eligibility for this credit.

This tax credit is proposed to be phased in over a five-year period, beginning with tuition fees paid in respect of instruction commencing after 2001. The proposed credit rates are:

Taxation Year	Tax Credit Rate
2002	10%
2003	20%
2004	30%
2005	40%
<b>2006 and subsequent taxation years</b>	<b>50%</b>

## In-year Measures

As announced in the 2000 Ontario Economic Outlook and Fiscal Review, enhancements are proposed to certain Ontario non-refundable credits. These enhancements would be effective January 1, 2001.

Non-refundable Credit	2000 Amount	Proposed 2001 Amount
Disability credit	\$4,293	\$6,000
Caregiver credit	\$2,386	\$3,500
Infirm dependant credit	\$2,386	\$3,500
Disability credit supplement for children with severe disabilities	\$2,941	\$3,500
Education credits		
Amount per month of full-time enrolment	\$200	\$400
Amount per month of part-time enrolment	\$60	\$120

These Ontario non-refundable tax credits are calculated using the lowest Ontario tax rate for the appropriate taxation year.

## Corporations Tax Act

### Cutting Corporate Income Tax Rates

The 2000 Budget announced the government's intention to cut both the general corporate income tax rate and the tax rate on income from manufacturing and processing, mining, logging, farming and fishing to eight per cent by 2005. That Budget presented the first two stages of the tax cuts, which were subsequently enacted into law. Those tax cuts reduced the general corporate income tax rate from 15.5 per cent before the 2000 Budget to 14 per cent on January 1, 2001. The tax rate on income from manufacturing and processing, mining, logging, farming and fishing was cut from 13.5 per cent to 12 per cent over the same period.

The following table outlines the government's proposed plan for implementing the remaining tax cuts to achieve the eight per cent tax rates.

	General Corporate Income Tax Rate*	Tax Rate on Income from Manufacturing and Processing, Mining, Logging, Farming and Fishing*
Current Tax Rate	14%	12%
Proposed Tax Rate:		
January 1, 2002	12.5%	11%
January 1, 2003	11%	10%
January 1, 2004	9.5%	9%
January 1, 2005	8%	8%

\*All tax rate reductions would be prorated for taxation years straddling the effective dates.

### Reducing the Capital Tax

#### Regular Corporations

In 1999, the capital tax exemption for small businesses was increased to \$2 million of taxable capital, with reduced capital tax rates applying to taxable capital between \$2 million and \$4 million. The full \$4 million threshold was to be phased in by January 1, 2003. Currently, businesses with taxable paid-up capital between \$2 million and \$3.2 million are eligible for reduced capital tax rates. It is proposed that:

- the capital tax exemption be replaced with a \$5 million deduction from taxable paid-up capital, effective January 1, 2002; and

, the gross revenue and total asset thresholds for using the Short-Form Corporations Tax Return be increased from \$1.5 million to \$3 million to reflect the \$5 million deduction. This would apply for taxation years commencing after December 31, 2001.

### **Financial Institutions**

, It is proposed that, effective January 1, 2002, the \$2 million capital deduction applied in determining adjusted taxable paid-up capital for financial institutions would be increased to \$5 million.

The proposed \$5 million capital tax deductions for both regular and financial institutions would be prorated for taxation years straddling January 1, 2002.

### Restoring Support for Research and Development

One of Ontario's most important tax-based incentives for research and development (R&D) is the Super Allowance, which provides over \$100 million in benefits to R&D performing firms.

In its 2000 budget, the federal government stated that provincial deductions for R&D in excess of actual expenditures would be treated as taxable government assistance. This federal action, if applied to the Super Allowance, would raise the cost of R&D investments in Ontario and could result in lower R&D expenditures in the province. Ontario businesses have expressed their concern over the adverse impact that the federal measure would have on the cost of R&D.

Recognizing the legitimate concerns expressed by Ontario's R&D industry, the 2000 Ontario Budget announced that Ontario would not adopt the federal measure. In this Budget, Ontario intends to take further action to reduce the adverse impact of the federal measure on Ontario R&D performers.

Ontario is proposing to suspend the R&D Super Allowance for two years and, in its place, allow corporations to exclude from Ontario taxable income the portion of the federal investment tax credit that relates to qualifying Ontario Scientific Research and Experimental Development (SR&ED) expenditures.

, This measure would be effective for a 24-month period, beginning with the first taxation year for which the federal super-deduction provision would apply to the corporation.

- , To qualify for the Ontario benefit under this proposal, the investment tax credit must:
  - be included in federal taxable income during the 24-month period; and
  - be in respect of qualifying Ontario SR&ED expenditures incurred by the corporation during the 24-month period or in the taxation year immediately preceding the 24-month period.

Ontario calls upon the federal government to revisit its 2000 Budget proposal and to ensure that federal legislation does not target Ontario's R&D Super Allowance.

### **Accelerating the Capital Gains Rate Reduction**

As proposed in the 2000 Ontario Economic Outlook and Fiscal Review, for dispositions of property on or after October 18, 2000, the inclusion rate for capital gains and losses would be reduced to 50 per cent.

### **Retail Sales Tax Act**

#### **Extending the Rebate for Alternative Fuel Vehicles to Electric Hybrids**

The rebate program for alternative fuel vehicles provides purchasers or long-term lessors of qualifying alternative fuel cars with a retail sales tax rebate of up to \$1,000. This program currently does not extend to the newly developed electric hybrid cars.

As a result, legislation will be introduced to extend the retail sales tax rebate to qualifying electric hybrid cars. The Ministry of Finance welcomes input from the industry. In general, a qualifying electric hybrid car would be one that combines an electric traction motor with another power unit, such as a conventional gas or diesel engine. To qualify for the proposed rebate, an electric hybrid car would be required to have:

- , regenerative braking capability to recover the energy released while slowing down or stopping; and
- , electric storage systems, such as batteries, ultra-capacitors, or flywheels.

It is proposed that qualifying electric hybrid cars delivered after May 9, 2001 be eligible for this rebate.

## Exempting Audio Books for People Who Are Blind

The government proposes to exempt from retail sales tax audio books purchased by people who are legally blind. The proposed measure would be effective on proclamation.

The government will consult with the Canadian National Institute for the Blind on implementation details.

## Succession Duty Act Supplementary Provisions Act

Succession duties were eliminated in 1979, in respect of persons who died after April 10 of that year. However, in certain instances, succession duties may continue to apply to estates of persons who died on or before that date. For example, the amount of an inheritance or the identity of a beneficiary may be uncertain where a life interest was granted to a spouse and the remainder interest to their children. There are fewer than 200 remaining estates for which payment of succession duties has been deferred until the occurrence of a future event.

In order to bring succession duties to an end, it is proposed that no further succession duty would be payable on or after May 9, 2001, other than amounts due before that day.

# Making the Tax System Fairer

## Revenue from Beer

It is proposed that, effective June 25, 2001, the ad valorem component of the brewers' basic fee would be eliminated.

- , The new basic fee rate for regular beer—beer shipped in containers with a capacity of less than 18 litres—would be 51.05 cents per litre.
- , The new basic fee rate for draught beer—beer shipped in containers with a capacity equal to or greater than 18 litres—would be 36.05 cents per litre.
- , The microbrewery fee rates would be based on the new regular and draught basic fee rates. The microbrewery reduction rates and thresholds are not proposed to change.
  - The rates on the first 25,000 hectolitres of beer shipped in Ontario would be 33.69 cents per litre for regular beer and 23.79 cents per litre for draught.
  - The rates on the next 50,000 hectolitres of beer shipped in Ontario would be 45.94 cents per litre for regular beer and 32.44 cents per litre for draught.

## Heritage Properties

To encourage the restoration and preservation of heritage buildings, the government proposes to give municipalities the ability to provide property tax relief to owners of buildings that are designated under the *Ontario Heritage Act* as being of architectural or historical value.

The government will consult with stakeholders to develop eligibility criteria and a relief mechanism that is equitable for property owners and administratively feasible for municipalities. It is proposed that this relief mechanism would take effect on January 1, 2002.

## **New Rental Apartment Buildings**

In 1998, the Province created the “new multi-residential property class” to enable municipalities to apply a lower tax rate to newly built rental apartment buildings. If adopted by a municipality, this class would apply to newly built multi-residential properties for the first eight years after construction, and then these properties would move into the regular multi-residential class.

To provide a greater incentive for the development of new affordable rental housing, the government intends to extend the time horizon of the new multi-residential property class from eight years to 35 years.

This change would take effect on January 1, 2002.

## Technical Amendments

### Changes to the Application of Retail Sales Tax to Trucks and Buses Registered under the International Registration Plan

On April 1, 2001, Ontario became a member of the International Registration Plan (IRP). Ontario's IRP membership will enhance the competitive position of Ontario's truck and bus industries by giving them improved access to U.S. markets.

To accommodate Ontario's membership in the IRP, Ontario proposes to amend the *Retail Sales Tax Act* as it applies to trucks and buses registered under the IRP and used in Ontario. Ontario is planning to implement an annual prorated sales tax to be collected at the time of registration. This would replace the retail sales tax normally applicable to these multijurisdictional vehicles. This taxation system is used in British Columbia, Saskatchewan and Manitoba.

- , Trucks and buses used only in Ontario would continue to be subject to the current retail sales tax system at the time of purchase.

In addition, under this proposal, trailers, repair parts and labour services for multijurisdictional trucks and buses registered under the IRP and used in Ontario would be exempt from retail sales tax at the time of purchase. The proposed rates have been developed to account for the Ontario proportion of the retail sales tax on trailers, repair parts and labour.

- , Trailers, repair parts and labour services for trucks and buses used only in Ontario would continue to be subject to the current retail sales tax system at the time of purchase.

The proposed measure would be payable each year upon registration of a multijurisdictional truck or bus, and would be calculated based on the vehicle's purchase price and the proportional distance travelled in Ontario by the vehicle during the previous year. The applicable tax rate would vary, depending on when the vehicle was acquired.

### Proposed Rates for Multijurisdictional Trucks and Buses

	Tax rate for multi-jurisdictional trucks registered under IRP (%)	Tax rate for multi-jurisdictional buses registered under IRP (%)
Acquisition year	3.669	3.285
First calendar year following the acquisition year	2.876	2.419
Second calendar year following the acquisition year	2.307	1.814
Third calendar year following the acquisition year	1.901	1.390
Fourth calendar year following the acquisition year	1.612	1.093
Fifth calendar year following the acquisition year	1.570	1.036
Sixth calendar year following the acquisition year	1.483	0.949
Seventh calendar year following the acquisition year	1.447	0.913
Eighth calendar year following the acquisition year	1.448	0.911
Ninth and subsequent calendar years following the acquisition year	1.475	0.934

Under this proposal, multijurisdictional trucks and buses previously purchased in Ontario may qualify for a transitional credit against the annual prorated tax. Rules would also be introduced to address taxation where there is a change in the use of a truck or bus.

The government proposes to implement the modified retail sales tax system for multijurisdictional vehicles as of October 1, 2001. The government will be seeking industry input on this proposal.

### Professional Corporations

It is proposed that technical amendments relating to professional corporations be made to the *Business Corporations Act*. The amendments would clarify that the liability for professional negligence of a shareholder of a professional corporation is not affected by the existence of the corporation or the fact that the corporation is a member of a partnership or limited liability partnership.

In addition, technical amendments are proposed to be made to various statutes governing regulated professionals to provide that the conditions, prohibitions and restrictions that currently apply to individuals who practise the particular profession would also apply to professional corporations.

## Other Technical Amendments

To improve administrative effectiveness and enforcement, to maintain the integrity and the equity of the tax system, and also to enhance legislative clarity, various other amendments will be proposed to the following Ontario statutes:

- , *Assessment Act*
- , *Capital Investment Plan Act, 1993*
- , *Commodity Futures Act*
- , *Corporations Tax Act*
- , *Education Act*
- , *Electricity Act, 1998*
- , *Employer Health Tax Act*
- , *Fuel Tax Act*
- , *Gasoline Tax Act*
- , *Income Tax Act*
- , *Land Transfer Tax Act*
- , *Mining Tax Act*
- , *Ministry of Revenue Act*
- , *Municipal Act*
- , *Ontario Property Assessment Corporation Act, 1997*
- , *Retail Sales Tax Act*
- , *Tobacco Tax Act*

# Improving Customer Service and Cutting Red Tape

This Budget builds on the measures introduced by the government in previous Budgets. Cutting red tape and improving customer service is an ongoing job, and this Budget introduces several new improvement initiatives.

## Quality Service in Tax Administration

Taxpayers have the right to demand and expect professionalism and courtesy in the administration of their tax system.

In order to enhance service quality and increase accountability, Ontario is developing specific service standards for tax administration. These standards, when finalized, will be used to measure our performance in administering tax laws with fairness, courtesy and common sense.

Results will be reported to the public annually, allowing taxpayers to hold the government and its employees accountable for the quality of service provided and the professional manner in which taxpayers are treated.

Consultations with key stakeholders on draft tax administration service standards will begin shortly, aimed at finalizing standards by September 1, 2001.

## Simplification of Tax Filing Procedures

Business people in Ontario want to create jobs, not fill out unnecessary or complicated paperwork. The following proposed measures would help to reduce the paperwork that businesses are required to file, while ensuring all taxpayers are treated fairly.

- , An administrative easement will be introduced to waive one late-filing penalty for Retail Sales Tax returns, where the business has otherwise had no previous late-filed returns over the past four years. This change would be applied retroactively as of July 1, 2000.
- , Corporations are currently required to pay monthly corporate tax instalments if annual tax payable in the current or preceding year is \$2,000 or more. To simplify instalment requirements for more small businesses, it is proposed that corporations be allowed to pay quarterly instalments if their tax payable in the current or preceding year is greater than or equal to \$2,000 and less than \$10,000. This change would apply to taxation years commencing in 2002.

- , For taxation years ending after 2000, corporations filing their Ontario corporate tax return would no longer be required to file a copy of their federal T2 return and related schedules, provided the federal documents have been filed with the Canada Customs and Revenue Agency (CCRA).
- , Effective immediately, it is proposed that gasoline, fuel and tobacco tax refund claims would no longer require copies of supporting documentation, where the annual claim is \$500 or less. However, supporting documentation must be retained and provided upon request.
- , The Ministry of Finance will accelerate its ongoing review of all tax forms to: eliminate unnecessary forms; improve the layout design and use of plain language; reduce the overall number of forms by introducing multipurpose forms; and explore opportunities for businesses to submit forms electronically.

### **Simplification of Retail Sales Tax Definitions and Rules**

Ontario recognizes the need for simpler and more effective definitions and rules in the retail sales tax system, such as those relating to the taxation of computer software. To that end, Ontario will consult with taxpayers and other interested groups on potential measures for a simpler retail sales tax.

### **Streamlined Tax Audit Procedures**

The Business Tax Review Panel recommended that the Province explore ways of simplifying and consolidating the audit process. The following measures are proposed:

- , More consolidated audits will be conducted across various tax programs, where feasible and the business is agreeable to the audit approach. Auditing multiple tax programs at the same time will mean a reduction in the overall time spent by tax auditors at the business location.
- , The Ministry of Finance will continue to work closely with the federal government to arrange more joint, multijurisdiction audits, where this is feasible and the business is agreeable to the audit approach.
- , Retail sales tax audits on small businesses will be streamlined. In most cases, this will mean that the typical small business owner can expect the auditor to be in and out of their place of business within two full working days.

## **A More Customer-Focused Tax Administration**

The government recognizes and values the role that small businesses play in providing feedback and suggestions on ways to improve customer service and cut red tape. The following measures will help foster a better working relationship between the tax administration and its customers and stakeholders.

- , A Small Business Advisory Committee will be formed, comprising small business representatives, key stakeholders and tax administration officials. The mandate of the committee will be to identify and discuss new ways of simplifying tax administration and cutting red tape, with a goal of implementing changes by 2002.
- , Tax Information Forums will be held across the province. These forums will provide small businesses with a one-stop opportunity to obtain information and ask questions on a variety of tax programs administered in Ontario.
- , The Ministry of Finance will continue to work with key stakeholders, such as Chambers of Commerce and other groups, to seek more opportunities to meet with them and explain tax administration rules and requirements.

## **Improved Customer Service Through Electronic Service Delivery**

In support of the government's goal for electronic service delivery, the following customer service measures will be implemented by 2002.

- , An Internet e-mail subscription service will be introduced. This service will send the user an e-mail announcement whenever new publications are released, key dates are announced, or a variety of other events occur. Small businesses, and all subscribers to the service, will have an effective and efficient means of staying on top of the latest changes.
- , A new "Tele-Tax" system will be implemented. Users of this integrated voice response (IVR) service will call an automated, self-serve telephone system and obtain recorded messages containing answers to frequently asked questions.
- , Customer service feedback and other survey tools will be available via the Internet. These tools will provide businesses with yet another way to engage the tax administration and suggest ways to simplify processes and cut red tape.

- , Retail sales tax interpretation rulings, which have general applicability to a wide audience, will be made available via the Internet. A search engine will make finding specific information quick and easy.
- , Corporate income and capital tax Information and Interpretation Bulletins will be revised to remove obsolete information and update statutory references. The revised Bulletins will be available on the Internet by June 30, 2001. Over the next two years, these Bulletins will undergo a major overhaul, and new Bulletins will be issued, incorporating current legislation, interpretation rulings and court decisions, and reflecting current trends and developments in the corporate community. These Bulletins will be organized by topic and updated on a timely basis.
- , General information changes, such as a business address or telephone number, will be accepted via the Internet. This service means that businesses will be able to inform tax administration staff of their general information changes 24 hours a day, seven days a week, whenever it's most convenient for them to do so.

## **Amendments to Financial Services Legislation**

It is proposed that various pieces of financial services legislation be amended to eliminate barriers to competitiveness, reduce costs of compliance, and increase efficiency and effectiveness.

### The Co-operative Corporations Act

Thirteen amendments are proposed to streamline the regulatory requirements for co-operatives. These amendments are intended to address the commitment in the 2000 Budget to streamline co-operative regulatory requirements. The proposed changes include:

- , removing the requirement for a corporate seal;
- , harmonizing requirements (regarding joint membership and articles of incorporation) between co-operatives with and without share capital;
- , clarifying policies respecting membership shares; and
- , introducing amendments intended to facilitate more efficient and less costly functioning of annual meetings.

### Credit Unions and Caisses Populaires Act, 1994

It is proposed that this Act be changed to permit the Deposit Insurance Corporation of Ontario (DICO) to invoice credit unions and caisses populaires for premiums within 120 days of the start of their fiscal year. This would allow premiums to be based on the previous year's audited financial statements.

### Insurance Act and Registered Insurance Brokers Act

It is proposed that the list of permissible investments for Ontario-incorporated insurance companies be updated to give provincially incorporated companies more flexibility in planning their investment strategies. Further amendments to insurance legislation are being considered to harmonize Ontario investment standards with those in other Canadian jurisdictions.

Proposed changes to the *Insurance Act* and the *Registered Insurance Brokers Act* would remove restrictions on foreign ownership of corporate agents and adjusters and brokerages.

### Loan and Trust Corporations Act

Changes are proposed to eliminate overlap and duplication in the regulation of the loan and trust sector. With these changes, the Province would no longer incorporate loan or trust companies. After a transition period, only federally incorporated companies would be able to operate in Ontario.

### Mortgage Brokers Act

A proposed change would exempt from regulatory requirements foreign banks that are allowed to operate in Canada under the federal *Bank Act*.

### Securities Act

Eight changes are proposed to clarify securities legislation, to reduce the cost of compliance for market participants, and to harmonize requirements with those of other Canadian jurisdictions. For example, a proposed amendment to permit the use of electronic communications for delivery of shareholder meeting materials (proxy material and information circulars) would reduce issuer mailings and associated costs.

<b>Proposed Benefits to Taxpayers: 2001 Budget Impact Summary</b>	<b>2001-02 Benefit (\$ Millions)</b>	<b>Full-Year Benefit (\$ Millions)</b>
<b>Personal Income Tax</b>		
20% PIT cut, remaining steps	60	975
In-year measure to enhance certain non-refundable tax credits	60	60
Equity in Education tax credit	15	300
<b>Corporations Tax</b>		
Corporate Income Tax rate cut, remaining steps	10	2,200
Reducing the Capital Tax	4	180
<b>Capital Gains</b>		
Accelerating the Capital Gains Reduction (62% to 50%)	520	500
<b>Retail Sales Tax</b>		
Exempting audio books for people who are blind	1	3
Extending the Rebate for Alternative Fuel Vehicles to electric hybrids	1	1
<b>Succession Duty Act Supplementary Provisions Act</b>	1	2
<b>Making the Tax System Fairer</b>		
Eliminating ad valorem component of brewers' basic fee	6	8
<b>Total Benefits to Taxpayers</b>	<b>678</b>	<b>4,229</b>