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OAB 2009

ONTARIO ALTERNATIVE BUDGET March 2009

Hit and Miss

ONTARIO'S 2009–10 BUDGET

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Ontario's 2009–10 budget is substantial and complex — it gets some things at least partly right, but leaves individual Ontarians hard hit by the recession in the lurch and misses many key opportunities to position the province for the future.

Ontario's big picture need was to fill the void left by the federal government's weak response to the recession: a limited stimulus package; an inadequate response to the needs of individual Canadians hard-hit by the recession; and a lack of focus that threatened to leave Ontario with little to show, long-term, for the billions of economic stimulus provided.

Measured against that need, the verdict on the budget is mixed.

The stimulus is better than what the federal government put on the table but it still doesn't go far enough. It does nothing to help Ontarians hit by the recession who can't collect Employment Insurance (EI) benefits. And while it talks a good line about green strategies for the future, its delivery is firmly fixed on the past.

Ontario is matching federal government infrastructure funding, which will result in a substantial increase in total infrastructure spending. Provincial spending on infrastructure will increase from $7.6 billion in 2008–9 to $12.7 billion in 2009–10 and $14.8 billion in 2010–11.

While Ontario came up with its matching share for the federal infrastructure funding program, it did nothing to address the problems that will be faced by municipalities and other transfer payment agencies in coming up with their matching shares. Ontario could have offered new funding to its transfer payment agencies to cover their share of the funds and make sure all of the announced infrastructure dollars actually get spent. It did not do so.

As a result, cash-strapped municipalities and other agencies are going to have to find $1.7 billion in new funds to match federal and provincial dollars. To the extent that the additional funding is taken up, it will impose additional financial burdens on agencies that are already dealing with their own recession-related issues. To the extent that the additional funding is not taken up, Ontario will fall short of its infrastructure funding targets.

A further problem with the federal budget was that too much of the stimulus was delivered through broad-based tax cuts. This, in turn, led to two problems. First, the economic effect of tax-delivered stimulus is extremely weak, relative to other forms of stimulus delivery. Second, broad-based tax cuts undermine fiscal capacity, reducing long-term ability to pay for public services and delaying the rebuilding of fiscal balances as the economy recovers. Ontario's budget actually compounds these problems by introducing just over $3.5 billion in broad-based tax cuts of its own, when fully implemented: $1.2 billion in a general personal income tax cut and $2.3 billion in corporate income tax cuts.

These cuts will have little stimulative impact, but will have the effect of delaying Ontario's fiscal recovery from the recession and therefore of limiting Ontario's public policy options in the future.

What assistance does the budget offer those hard hit by the recession?

On the positive side, the budget accelerates the increase in Ontario's child benefit to $1,100 by two years. And there is additional funding for retraining programs aimed at workers who have lost their jobs in the recession, although most of that funding actually comes from the federal government.

But on the critical issue of financial assistance for families devastated by job loss, Ontario took a political pass, with a single line of empty rhetoric about increasing pressure on the federal government to improve EI. A 2% increase in social assistance merely keeps pace with inflation. And the government's refusal to relax the asset limits in social assistance means that workers who don't qualify for or run out of EI will have to exhaust all of their financial assets — including their RSPs — before they can get any assistance.

To the extent that the enhancements in property and sales tax credits exceed additional taxes payable under the new harmonized sales tax system, these refundable credits will provide additional relief to low-income families. But because they are delivered only at tax time, so the full effect will be delayed until the spring of 2012.

It also contains nothing new or coherent to respond to the impact of the recession on Ontario's businesses and non-profit organizations. There's nothing in the budget to provide financial relief to non-profit groups who are caught in a squeeze between declining revenues and ballooning demands for services.

Many corporations — not just the major auto assembly plants — are confronted with very difficult plant closure decisions. Ontario can't create the demand needed to keep those facilities healthy in the long term. But it has a role to play in working with the corporate sector to keep the lights on, where it makes sense, so that there are plants for Ontario workers to be recalled to when the recession ends and demand recovers. Despite widespread calls for a flexible and innovative jobs commissioner program, Ontario has stuck with an inadequate status quo.

Does the budget add up to a plan for Ontario's future? Ontario's budgetary package is certainly more coherent, and more focused than the federal budget.

It superimposes a plan and a structure that will strengthen the long-term benefits from the program. The quality of that plan is another matter. There is a lot of rhetoric about green investments. But most of that is to be delivered through the electricity industry. Ontario's own investment in transportation, for example, is heavily tilted towards roads, rather than public transit.

It provides for some potentially valuable targeted tax credits for business investment — approximately $300 million a year when fully phased in — but gives up a significant slice of Ontario's fiscal capacity — $2.3 billion a year when fully implemented — in broad-based corporate income tax cuts. Ontario is jumping into the corporate tax cut race to the bottom with both feet despite the fact that even the Bush administration's tax plans would have left Canada's current total tax rates below U.S. rates. And despite the clear indications from the Obama administration that the era of tax giveaways to profitable corporations is over.

Beyond this report card, the budget is notable for three surprises — the move to tax harmonization, two important missing announcements, and a new initiatve that comes completely out of right field — significant corporate income tax cuts.

The budget offers no funding to implement the upcoming recommendations of the government's early learning advisor.

An addition to the mix is the big headline grabber in the budget: the announcement that Ontario will move to convert its retail sales tax to a value added tax and harmonize it with the federal GST.

Harmonization of the two sales tax systems administered in Ontario makes economic sense. A single tax will reduce administrative and compliance costs. More important, it will eliminate undesirable features of the retail sales tax that undermine the competitive position of Ontario's export- and import-competing industries. It will, however, result in increased costs for consumers since the base of the tax is broadened to include services and goods that are currently exempt from the retail sales tax.

The substantial increases in property and sales tax credits in the budget will offset this increase in consumption taxes for a significant proportion of Ontario families.

Most important, tax harmonization makes Ontario's fiscal capacity more secure. It takes Ontario's exported goods and services out of the consumption tax system, positioning those industries to compete outside the province. It reduces administrative overhead, both for the public and private sector. And it will help to maintain Ontario's revenue base as our consumption patterns continue to shift from traditionally defined goods to services.

The surprise from right field is a substantial cut in corporate income taxes. Coming on top of the substantial benefit delivered to the corporate sector through value-added tax harmonization at a time when Canada's corporate tax rates are already below U.S. rates, this measure is difficult to comprehend. Ontario has officially jumped into the corporate tax race to the bottom. In the short term, it will benefit corporations that are still profitable in the recession — i.e. corporations that don't need the help. In the long term, it will reduce Ontario's ability to fund public services by $2.3 billion, for no tangible benefit.

The contrast between the government's approach to corporate taxation and its refusal to provide additional assistance to unemployed Ontarians who either exhaust EI benefits or never qualify in the first place is stark.

The 2% increase in social assistance benefits in 2010–11 will cost $100 million. Its new corporate income tax cuts will cost $530 million that year, increasing to an estimated $2.3 billion in 2013–14.

Absent the corporate income tax cuts, Ontario could easily have afforded to make a substantial investment in a more generous and more effective social assistance system.

On the whole, Ontario's 2009–10 budget establishes a positive direction for the next few years. It provides substantial economic stimulus. It is in keeping with the view around the world that governments have a key role to play in rebuilding Ontario's. It imposes some coherence on what was a dangerously incoherent federal plan. It provides additional support for low-income families and individuals. It takes a bold step towards a more effective and efficient tax system, through harmonization of Ontario's consumption tax with the GST.

But it misses the opportunity to do much more. Ontario could have filled at least some of the gaping holes in the EI system by increasing and expanding access to social assistance benefits and suspending asset-stripping penalties. Or it could have taken the bold route and seized the opportunity to introduce real social assistance reform. Instead, it chose to waste fiscal capacity on substantial cuts in corporate income taxes — cuts that will benefit those corporations that don't need help in the short term and undermine Ontario's capacity to pay for public services in the long term.

Ontario could have guaranteed an infrastructure renewal program that truly positioned the province for the future. Instead, it relies heavily on cash-strapped local governments to find their share of required funding. And while its rhetoric is green and future oriented, its actual delivery is not. For all the talk about the importance of education for Ontario's future, the contains no new initiatives and no new funding for programs. For all of the talk about energy efficiency in a green economic future, there's no new funding for public transit.

A bold budget, right for the times, but one that simply misses too many opportunities.

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