Meeting the Need: Rebuilding Ontario's Ability to Pay for Public Services

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A number of clear conclusions emerge from an analysis of the Province's current fiscal situation:

- There will be a budgetary deficit for the fiscal year 2003-4 of $5.6 billion;
- With no change in policy, Ontario is headed for a deficit for 2004-5 of $2.5 billion;
- It is not possible for the government to deliver on all three of its key election promises: to rebuild public services with new investments of $5.9 billion; to balance the provincial budget in each year of the mandate; and to do so with no tax increases;
- The source of the budgetary dilemma faced by the government is not on the expenditure side – expenditures are at record lows as a share of Ontario's economy;
- The source of the government's budgetary dilemma is a shortfall of revenue raising capacity relative to public services needs;
- To deliver on the new investments promised in the election campaign, revenue must be increased by between $3.5 and $4.0 billion per year.

The Premier has been reported as ruling out tax increases as a starting point for public consultation in advance of the budget. That premise is not acceptable. It ignores the underlying causes for the province's fiscal difficulties; it is a recipe for a re-run of public services cuts on a scale comparable to the cuts imposed in the first years of the Harris regime.

Ontario's capacity to fund the services we need must be expanded. Since 1996, the province's annual revenue base has been reduced by $14 billion as a result of tax cuts. We are proposing a package of revenue enhancements that will restore approximately one quarter of that lost capacity.

Our capacity-rebuilding package has two objectives: to maximize the revenue generated by the current tax system by closing tax loopholes and tightening up tax administration and enforcement; and to generate new revenue from personal and corporate income taxes that will be paid by everyone in Ontario.

Maximizing revenue from the current system

Closing loopholes

Everyone in Ontario is aware of the Harris and Eves governments' cuts in personal income tax rates, from press releases if not from their own tax forms. Many people are aware of the corporate tax rate cuts that dominated the tax cut agenda in the later years of the Conservatives period in office. Far less visible was a series of more than 50 corporate tax loopholes opened up or expanded in successive budgets.

Tax loopholes give some taxpayers the opportunity to choose not to pay taxes that everyone else is obligated to pay. They are the ultimate in unfair taxation. Those loopholes should be closed.

Corporate tax loopholes introduced by the Harris and Eves governments now cost the people of Ontario over $1 billion a year in foregone revenue. These tax preferences are unfair; they are poorly targeted; they are ineffective; and they open up differences between the Federal and provincial corporate tax systems that complicate tax administration and create opportunities for tax avoidance.

Some of the corporate tax changes introduced in the Harris-Eves era were brought in to parallel changes in the Federal Income Tax Act. Those changes should remain in place. Other changes result from the Harris Government's decision to change funding for cultural industries from a grants system to a tax-based system. Those provisions should be converted to grants, in order to increase the transparency of the tax system and ensure accountability for public money.

Retaining changes introduced to harmonize with the Federal corporate income tax and converting arts and culture tax provisions into grants on a 1:1 basis would reduce the revenue recovery from eliminating corporate tax loopholes introduced by the previous government by $200 million.

The most expensive loopholes in Ontario's tax system are the various exemptions from the Employer Health Tax. The loopholes include the exemption for the first $400,000; exemptions for self-employed individuals; exemptions for income from stock options. All of these exemptions undermine the fairness of the system; all of these exemptions cost the people of this province a substantial amount in lost revenue; and none of these exemptions meets the test of being well targeted to an accepted public policy goal.

More important, exemptions from the Employer Health Tax are inconsistent with the history behind its creation and the role that it plays in funding the health care system. The EHT is the replacement for the OHIP premium. As such, it is the contribution expected of employers in return for the substantial competitive benefit they receive from the existence of public medicare in Ontario.

Eliminating all exemptions from the EHT would raise an additional $1.1 billion.

Bad tax enforcement creates the ultimate in tax unfairness: a tax that is paid by people who choose to respect the law and is not paid by people who choose not to respect the law.

Ontario's tax administration has been heavily and repeatedly criticized as inadequate in a series of toughly-worded reports from the Provincial Auditor. Large portions of Ontario's tax system are essentially unaudited, and generally known to be unaudited. We believe that in a tax system of $40 billion, enhanced enforcement should improve annual revenue by a minimum of $400 million, net of audit costs.

Recovering a portion of the revenue lost from tax cuts

Everyone in this province benefits from public services; everyone in this province will benefit from the renewal of Ontario's public services. We believe that the people of Ontario are prepared to pay modest tax increases in order to ensure that our services can be rebuilt.

We propose to increase each personal and corporate income tax rate by 5%. The bottom rate in the personal income tax system would be increased from 6.05% to 6.35%; the middle rate would be increased from 9.15% to 9.61%; the top rate would be increased from 11.16% to 11.72%.

Each corporate rate would be increased by 5%. For example, the small business rate would increase from 5% to 5.25%.

This increase would raise an additional $1.1 billion in personal income tax in 2004-5 — amounting to approximately 10% of the personal income tax cuts introduced since 1996.

We believe it is important that everyone in Ontario pay a fair share of the cost of rebuilding public services. By increasing tax rates at a constant percentage, we ensure that the cost of the change is linked to ability to pay. The median taxpayer in Ontario would pay an additional $70 — $1.30 a week; a taxpayer with an average income will pay roughly $150 — approximately $3.00 a week.

The proposed 5% increase in corporate tax rates will increase revenue by approximately $375 million.

Conclusion

The $5.9 billion in new investments in public services proposed by the Liberal party in its election platform is not the entire answer to the questions about services viability raised by Ontario's eight years of experience with the Harris-Eves Conservatives. The Ontario Alternative Budget estimates that the services gap created in those eight years is about double that amount.

Likewise, the $3.75 billion in additional revenue proposed here is not the entire solution to a revenue problem created by eight years of cuts amounting to more than $14 billion.

The $5.9 billion in services renewal is, however, what the people of Ontario elected the McGuinty Government to do, and it represents a welcome first step on the road to renewing public services in this provinces.

There is no avoiding the tax issue, unless the government is now prepared to abandon the commitment to services renewal that formed the core of its election campaign platform.

Federal transfers are not going to be the answer. Indeed, the rapid increase in Federal transfers resulting from the September 2000 and February 2003 first ministers meetings served to cover up the revenue shortfall created by the Conservatives' tax policies for two years.

Asset sales are not going to be the answer. The problem, as the Minister of Finance keeps saying, is structural. We have to rebuild the ability of our tax system to generate revenue for public services, year-in and year-out. Asset sales are a one-time thing. And many of the assets currently being discussed as being on the block for sale are either major revenue generators themselves (the LCBO, at over $1 billion a year) or could only be sold on the basis of an ongoing subsidy for programming (TVO).

Other revenue sources are also not the answer. They simply do not generate enough revenue.

We can rebuild our public services. The $5.9 billion in new investments proposed by the government in its election platform is a good first step. But before we take that first step, we have to rebuild the revenue base of the province.

And that means the Premier is going to have to disappoint the Canadian Taxpayers Federation and respond to the hopes expressed by the people of Ontario. Services cannot be rebuilt without increasing taxes; and it would be irresponsible to try to move from the current $5.6 billion deficit to a balanced budget in one year.

Our proposal would enable the government to deliver on its services commitments, and to balance the budget in the last year of its mandate.

Summary of revenue package

Revenue Recovery				
Personal Income Tax	$	1,060	million	Increase each marginal rate by 5.0%
Corporate tax				
5% increase in all rates	$	375	million	
Maximizing revenue from the current system				
Corporate Income Tax	$	1,050	million	Eliminate corporate tax loopholes
LESS	$	200	million	Convert arts industry deductions and credits into grants
Net gain from loopholes	$	850	million	
Employer Health Tax				
Eliminate loopholes	$	1,100	million	Eliminate exemptions from EHT
Tax enforcement	$	400	million	
TOTAL ADDITIONAL	$	3,785	million	

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