Ontario Budget

1979

The Honourable Frank S. Miller, Treasurer of Ontario

Ontario Budget

Presented by the Honourable Frank S. Miller,
Treasurer of Ontario
in the Legislative Assembly of Ontario,
Tuesday, April 10, 1979

Ministry of Treasury and Economics
Fiscal Policy Division

1979

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1979 Budget at a Glance

	1978-79	1979-80	Growth Rates	1979-80 Fiscal Swing
	($ million)		(%)	($ million)
Gross Provincial Product	90,800	100,700	+10.9	
Spending	14,482	15,558	+7.4	
Revenue	13,145	14,405	+9.6	
Cash Requirements	1,337	1,153		−184

1979 Budget Statement

Mr. Speaker:

This evening I am pleased to present to you, and to the Members, my first Budget. It is an honour to serve as Treasurer of Ontario and, under the leadership of the Honourable William G. Davis, to share with my colleagues the opportunity to mould the future of this great province.

In carrying out the responsibilities of the Treasurer of Ontario, my goal is clear: to continue the outstanding achievements which have benefitted this province so greatly, in order to guarantee future employment and prosperity and happiness for our citizens.

Without question, the most important problem facing Ontario today is the need to create more jobs. The employment creation record of the Province over the past few years has been outstanding. But because our labour force is growing so quickly—more than three times as quickly as Great Britain's or Germany's—we must further strengthen our efforts so that all new entrants to the labour force find employment.

In creating jobs we must not fan the flames of inflation. If we do so, we will do lasting damage to our economic prospects. While employment problems affect some of our people, inflation affects everyone. It is especially hard on the elderly and those on fixed incomes.

When I sat down to prepare this Budget, the issues of unemployment and inflation were the first priorities I had to face. I realized that Ontario is subject to national and international forces that strongly influence our economy. No one government can single-handedly wipe out inflation and unemployment. Also, while much of the responsibility for tackling these problems lies with the federal government, Ontario can and must provide responsible leadership and policy initiatives that will help create jobs and reduce inflation. I believe that the proposals I will place before you tonight will do just that.

The path to greater economic prosperity in Ontario is clear. Only by stimulating the private sector can we create lasting jobs and growing incomes for our citizens, as well as the taxable resources so essential to providing the high standard of public services our citizens have come to expect. The efforts of this Government must be concentrated on making sure that we create the confidence and atmosphere needed for private sector investment in Ontario.

The private sector flourishes best with a minimum of government regulation. In fact, one of the main reasons prompting me to enter politics was my perception as a small businessman of the need to encourage government to lighten the burden of regulation and interference on the business community in Ontario. To be candid, I also believe that businesses should prosper without a lot of government financial concessions. But, Mr. Speaker, we do not set the international rules of the game. When other jurisdictions are aggressively competing for new investment, we cannot bury our heads in the sand and let job opportunities slip outside Canadian borders into other countries. We must take effective action to make sure that Ontario's economic future is secure.

In the weeks before preparing this Budget, I met with many individuals and groups—small businessmen, consumers, corporations, union representatives, bankers and farmers. These meetings were very useful and I learned a great deal about the individual problems of each group. I want to thank them for the time they took to give me the benefit of their thinking about our economy and our way of life. I can assure them all that I have listened to their recommendations very carefully and have weighed them while preparing this Budget.

One point came up repeatedly in these conversations. If government keeps its own house in order, maintains a positive climate for the development of the private sector and aims for reasonable cost and salary increases, the outlook for our continued prosperity is very bright. This Government wholeheartedly shares those opinions, Mr. Speaker. Accordingly, this Budget proposes:

- to maintain a high quality of public services in Ontario;
- to help create more jobs;
- to provide incentives for economic growth and small business development;
- to continue our sound management of Provincial spending, thereby helping to contain inflation; and,
- to reduce the deficit.

Before outlining specific measures to achieve these objectives, I would like to review briefly the economic outlook for the province.

Ontario's Economic Prospects

Ontario's economy continued to perform well in 1978. Growth was 3.6 per cent in real terms and a record 133,000 more people were employed in Ontario than the year before. All of these jobs were created in the private sector. This was an outstanding accomplishment by any standard. I was particularly encouraged by the fact that our manufacturing output growth accelerated by almost one full percentage point, to 4.8 per cent, and 36,000 new jobs were created in the manufacturing sector. In part, our economic performance was assisted by the lower value of the Canadian dollar, which improved our export competitiveness, as well as by the temporary reduction in retail sales tax.

There were disappointments in the year as well. Because of the rapid growth in the number of young people entering the labour force, an unacceptably high level of unemployment has persisted. While this surge will pass in two or three years, currently almost 75 per cent of the unemployed in Ontario are young people under twenty-five and adult women. Reducing the rate of unemployment is a major challenge for all governments. Comparatively speaking, however, the Ontario record of job creation has been outstanding.

Job Growth in Ontario Leads Industrial Countries
(per cent)

	1970-1977 Average Annual Growth	
	Labour Force	Employment
Canada	3.2	2.9
Ontario	3.3	2.9
United States	2.4	2.0
Germany	1.1	0.6
Japan	0.3	0.2
United Kingdom	0.4	−0.2

Turning to the outlook, I have noted that many economists believe that the Canadian and Ontario economies will grow at a modestly slower rate this year. I have included a forecast for 1979 that reflects a consensus of economic forecasters both in and outside of government. It calls for a slight moderation in the rate of real growth in Ontario to 3.3 per cent. This moderation in growth is predicated on the assumption that the United States economy will experience some slowing down during 1979. Nevertheless, we can look forward to seeing well over 100,000 new jobs created in Ontario this year. I would like to observe that this year Ontario's Gross Provincial Product will for the first time exceed $100 billion. This landmark takes on even more significance when one realizes that Ontario's economy has tripled in size since 1969. At this point I would draw the attention of the Members to Budget Paper A, which provides a thorough review of the performance of the Ontario economy throughout the 1970s and looks at our prospects for the next decade.

I noted with interest that the federal Minister of Finance, in his November budget, referred to a recent survey which showed that 300 large corporations in Canada are planning to increase their spending on plant and equipment this year by an average of 8 per cent in real terms. I have also had a survey conducted of some 100 corporations in Ontario, which indicates that Ontario business is moving ahead with expansion plans at a healthy pace.

I am confident that, as we continue to provide a sound climate for investment in Ontario, our citizens will reap the benefits of better jobs and higher incomes. In fact, I personally would not be surprised if the forecasters have underestimated growth in 1979. It may turn out to be a year of better economic performance than 1978. This growth-oriented Budget is designed to make this happen.

Job Programs and Skill Training

I have emphasized the need to improve the climate for employment growth and investment in Ontario.

Mr. Speaker, we must continue to seek new ways to help our people, especially the young, to find lasting and rewarding employment. To do this the Government of Ontario has led the way with programs such as the Ontario Career Action Program and the Ontario Youth Employment Program. Last week, I announced the details of the OYEP program for 1979.

My Statement contains a table showing the funding and job creation levels of Ontario's programs for youth employment in 1979-80. In total we will be spending $79 million and creating directly some 70,000 jobs this year for young people in Ontario.

Ontario Youth Employment Programs

	Estimated 1979-80	
Program	Funding	Jobs
	($ million)	
Ontario Career Action (OCAP in Industry)	7.5	4,500
Ontario Career Action (OCAP in Government)	1.8	1,500
Experience*	19.5	13,610
Ontario Youth Employment (OYEP)	26.0	40,000
Regular Summer Replacement	20.0	8,500
Junior Ranger	4.4	1,990
Total	79.2	70,100

*Includes Agricrew Program, Junior Agriculturalist Program and the Ontario-Quebec Exchange Program.

When we look at the problem of unemployment, we are confronted with the paradox that many job vacancies exist while a large number of people are seeking work. During my pre-budget consultations, both employers and union representatives told me of their concerns about the shortage of skilled workers.

In fact, in some parts of our province, machines are lying idle because there is no one to operate them. My colleagues, the Honourable

Bette Stephenson, the Minister of Education, and the Honourable Robert Elgie, the Minister of Labour and Manpower, are developing long-term measures which will improve the situation through better training and closer coordination among unions, employers, job seekers and the educational system. We will support these efforts with a new program to assist employers directly to hire and train people in areas of critical skill shortages. This program will be financed through the Employment Development Fund which I will describe shortly. The details of this new thrust for skill training will be announced later in this Session. I am convinced that labour and industry leaders will cooperate with each other and with government to design and carry out practical skill training programs.

Providing Incentives for Growth and Employment

In preparing this Budget, I conducted a thorough review of our taxation system to see what changes might be made to stimulate business development and enhance confidence. In this regard I would direct the Members' attention to Budget Paper B, which discusses the appropriate fiscal policy for today's economy and looks at the changing role of fiscal policy over the past decade. At this stage I do not believe that any kind of across-the-board tax cut would be justified. But I do believe that some taxes bear particularly heavily on small business and generally hurt the climate of confidence in the province.

I would now like to outline additional incentives to create jobs and improve our economic performance.

Succession Duties

Mr. Speaker, in 1969 the Honourable Charles MacNaughton, then Treasurer, observed that the introduction of capital gains taxation would gradually eliminate the need for succession duties and gift taxes in Ontario. As revenues from capital gains increased, Ontario would be able to phase out succession duties and so avoid what many consider to be double taxation. At the time, the Province was prepared to vacate the succession duty field in return for a share of the federal estate tax. The federal government, however, unilaterally abandoned estate taxation in 1971 when it introduced the capital gains tax. The Province, therefore, continued to levy succession duties and gift taxes, although its long-run objective was to get rid of these taxes. Over the past seven years we have progressively reduced the burden of succession duties. Meanwhile our sister provinces have vacated the field one by one, leaving only Ontario and Quebec.

I am convinced that the continuation of this tax is hurting our economic performance and costing us jobs. Business people making investment decisions, particularly as to location, are bound to take into consideration the tax position of their estates in Ontario. Succession duties and gift taxes have been a source of great concern to farmers and small business owners in Ontario. In spite of the fact that less than 3 per cent of estates in Ontario are subject to tax, there is widespread opinion that the successors of the average citizen will be subject to tax. For estates which are taxable, complex and costly legal procedures are involved to keep businesses within families. As well, individuals often experience great difficulty in disposing of assets so that they may pay the duties. I am satisfied that the present combination of other taxes provides government with an adequate return as wealth is accumulated.

Mr. Speaker, as of midnight tonight there will be no succession duty or gift taxation in Ontario. Later I will be introducing bills to repeal The Succession Duty Act and The Gift Tax Act effective with respect to deaths or gifts occurring after midnight April 10, 1979. I should point out that the legislation will continue to apply to deaths occurring and gifts made up to midnight this day.

I estimate that the annual revenue loss from this change eventually will amount to some $50-$60 million a year. However, in this fiscal year, the revenue loss will be $28 million.

It is much more difficult to estimate the revenue gains and employment gains that will occur in Ontario due to the elimination of succession duties. However, I am satisfied that on balance Ontario will profit in many ways from this decision. Our citizens will have one less burdensome concern to deal with in planning their private lives. Provincial revenues are bound to increase as investors take advantage of this decision.

Mining Taxation

I would now like to turn to the mining industry. The importance of mining in Ontario is unquestioned. Almost 20 per cent of Ontario's dollar earnings from exports are from its mines. Many Northern Ontario communities depend entirely upon the mining industry for their employment. I am disturbed that this province has not seen a major new mine brought into operation for some years. Last year the federal government and the provinces reviewed the current situation in the mining industry. This review showed that high marginal tax rates were considered to be one of the most important problems facing the industry.

The Members will recall that several beneficial adjustments were made to the Ontario mining tax last year. Tonight I am proposing additional changes to further improve the investment climate for mining in Ontario. First, the top marginal mining tax rate will be reduced from 40 to 30 per cent; second, the basic exemption from mining tax will be increased from $100,000 to $250,000 of mining profits. This latter move will encourage the creation of more small mining companies and assist those already operating.

I am also proposing a modest reduction in the top processing allowance rates. This will bring them more closely into line with those offered in other provinces and will soften the impact of the rate reductions on our revenues. These measures affecting the Ontario mining industry will apply with respect to fiscal years of companies ending after April 10, 1979. Enabling legislation will be introduced tonight by my colleague, the Honourable James Auld, Minister of Natural Resources.

The Hospitality Industry

I would now like to discuss the situation in the province's hospitality industry. This important industry provides employment for over 400,000 people, or about 10 per cent of Ontario's labour force. In 1978, tourist spending in the province exceeded $5 billion, including $1 billion of sales to non-residents.

In the last two years, the Government has undertaken to stimulate this industry through the temporary removal of the sales tax on transient accommodation, and other measures. This positive support has helped produce a momentum in the industry that must be sustained. Accordingly, I propose the following:

- First, the sales tax on kitchen machinery and equipment used in restaurants serving the public will be temporarily withdrawn as of midnight tonight. This will provide restaurants with the same kind of exemptions currently available to manufacturers.
- Second, purchases of furniture and furnishings for use in the hospitality industry will also be temporarily exempt from the retail sales tax.

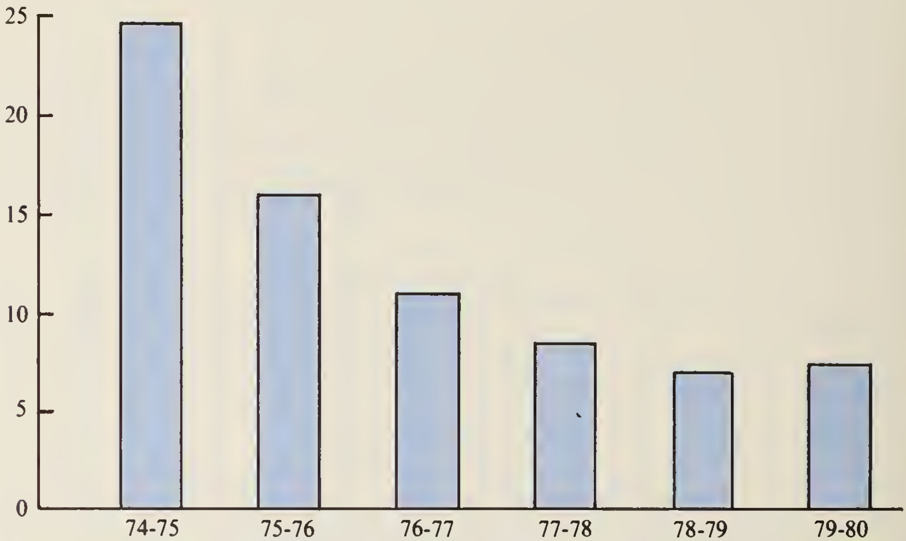
  These two exemptions will be available until March 31, 1981 and will provide the hospitality industry with an incentive to upgrade and expand its facilities.
- Third, the temporary sales tax exemption for transient accommodation that was originally scheduled to expire December 31, 1979 will be extended to March 31, 1981.

The combined additional cost of these measures to stimulate tourism will be $13 million in this fiscal year and $45 million on an annual basis.

Managing Expenditures

Mr. Speaker, one of the best incentives for economic development that any government can provide is to manage its spending and its affairs efficiently, and be seen to do so. This Province has led the way in Canada in containing public sector spending. A great deal of the credit for this must go to my predecessor, the Honourable Darcy McKeough. In the fiscal year just ended, we have held spending below the original Estimates for the third year in a row. This year, the Estimates provide for an increase in our ongoing expenditure base of only 6 per cent. When we add the Employment Development Fund Supplementary Estimates our total growth rate will be 7.4 per cent. This is still well below the projected growth rate of the economy.

Provincial Spending Growth Declines
(per cent)



I want to make it abundantly clear what our expenditure control policy is all about. We are not trimming the growth of Government spending because we cannot find the money to pay for high rates of growth. Ontario's credit is sound and its economy is strong. Rather we believe that the same high quality of our programs can be maintained without excessive cost escalation. We do this by demanding more efficiency. And we are getting it.

The Government will continue to allocate most of its resources to areas of high social priority, including health, education, and social service institutions. The existing high quality of Ontario's health services is being upgraded with the extension of the Home Care Program for the chronically ill to additional centres in the province. The budget of the Ministry of Community and Social Services has been increased by 6.9 per cent to provide greater emphasis on support services to the elderly and the handicapped. To enhance the participation of the physically handicapped in community activities, the five pilot projects providing special transit services will be made permanent. Additional funding has been made available to extend this program to other municipalities in Ontario.

Employment Development Fund for Ontario

Mr. Speaker, in addition to the measures I have just discussed, I would now like to outline details of another important new program to stimulate the development of our economy. This is the Employment Development Fund announced in the Speech from the Throne.

The Fund will be managed by a committee of Ministers called the Employment Development Board, which I shall chair. The Minister of Industry and Tourism will be the Vice-Chairman and his ministry will carry out the administrative functions of the Fund. The Provincial Secretary for Resources Development will also be on the Board. The major function of the Board will be to coordinate the Government's policies as they relate to providing direct economic development incentives to the private sector. The Board will also participate in the development of, and provide funding for, the new job training program to which I referred earlier.

The amount of the Fund has been set at $200 million for 1979-80. I would stress that the proceeds from the sales of our share of Syncrude and of Ontario Mortgage Corporation mortgages, as well as additional revenues the Province will raise from the corporate sector, are more than adequate to finance the Employment Development Fund this year. This means that ordinary taxpayers' dollars are not being diverted away from the normal programs of the Government.

To maximize the economic benefit to Ontario of the Employment Development Fund, the Board will encourage projects that:

- make a long-term contribution to employment;
- foster the development of needed job skills;
- have the potential for significant export development or import replacement;
- involve the development of new products and processes through Canadian-based innovation; and,
- stimulate key industries and regional development.

There are some people who have questioned why we should be giving such financial incentives to industry, particularly large and successful firms. Quite frankly, I was one of them. Nevertheless, I have concluded that we must follow this course of action. Many jurisdictions are aggressively competing for new investment. This is a challenge we cannot afford to ignore if we are determined that Ontario should get its fair share of new investment.

The financial incentives for the automotive and pulp and paper industries will be provided from this Fund. Further details on the operation of the Fund are provided in Appendix C to this Statement.

We must recognize that Ontario's pulp and paper industry is facing tough competition. At the same time, the industry is under pressure from this Government to clean up its pollution. The facts are simple. If we are going to impose high environmental standards, we must recognize the competitive and cyclical environment in which the industry operates. Therefore, it must receive special assistance. Mr. Speaker, who in this Assembly prefers the alternatives of continued damage to our environment or perhaps mill closures and whole towns out of work? Such alternatives simply are not acceptable to this Government.

Encouraging Investment in Small Business

I would now like to turn to the area of small business development. Let me state that I am a very strong supporter of two principles. First, I believe that the future success of our society is dependent upon the maintenance of a very strong commitment to free enterprise. Second, I believe that the bedrock strength of free enterprise lies in private equity investment. Individuals should be encouraged to take risks through the ownership of equity and hopefully most of them will turn a profit. I make no bones about this, Mr. Speaker, and I say woe betide those who think we can prosper in the future yet give up these principles.

Small Business Development Corporations

Members will recall that the Government introduced The Venture Investment Corporations Registration Act in 1977 to encourage corporations to increase the supply of venture capital and managerial advice to small business. To be candid, this program has not worked. There appear to be a number of reasons for this. First, the federal government chose not to support this initiative, thereby reducing the tax incentive for investors. Second, the incentive excluded individuals. Third, some of the provisions in the legislation may have been too restrictive.

I believe it is vitally important to make sure there is a stream of equity capital available to new enterprises. Ideally, the lure of profit in return for risk capital should be enough to attract investors. People today, however, receive such generous tax treatment under the personal income tax for much safer investments that they are reluctant to invest in new ventures. I believe we must do something about this.

Accordingly, I am proposing to introduce legislation this evening to encourage the development of new ventures in Ontario and to make it more attractive for more people to become directly involved in financing small business and building our economic future. Specifically, Mr. Speaker, I am advancing the following program:

- A Small Business Development Corporations Act will replace the existing venture investment corporations legislation.

- Individuals and corporations investing in Small Business Development Corporations (SBDCs) will receive a share credit from the Province equal to 30 per cent of their equity investment.
- The SBDCs will be empowered to invest in a broad range of new and expanding small business enterprises.

This means that if an individual purchased $1,000 worth of equity in an SBDC, the Province of Ontario would refund, directly, $300 to the private investor.

It is not possible to estimate with any precision the cost of this program. However, as the year progresses, I will set an upper limit to costs. Further details of the Small Business Development Corporations program are included in Appendix B to this Statement.

Capital Tax Reduction

Mr. Speaker, I would like to propose a further measure to assist small business. Perhaps the tax that creates the most problems for small businesses in Ontario is the capital tax. While rates are not high, this tax poses complex paperwork problems for many small firms.

In recognition of this problem and the nuisance of filling out a capital tax return, a reduced flat tax for small corporations was introduced in 1977. Tonight, I am proposing to extend this benefit. The flat tax for corporations with taxable capital in excess of $50,000 and up to $100,000 will be reduced from $100 to $50. For corporations with taxable capital in excess of $100,000 and up to $200,000, a flat tax of $100 will apply instead of the regular rate. Also, in order to smoothly phase small corporations into the regular rate, I will introduce a formula to apply to taxable capital in excess of $200,000 and up to $300,000.

I am proposing one additional measure to lighten the burden of this tax. Real hardship exists for some small businesses in a year in which they have lost money, yet still must pay full tax on their capital. In recognition of this, I am introducing, in lieu of the regular rate, a flat tax of $100, which will apply to corporations with taxable capital up to $1 million that have experienced a negative cash flow during the year.

I estimate that these capital tax changes will reduce revenues by $20 million in a full fiscal year but they will ease and simplify the capital tax for some 58,000 small businesses in Ontario. Large corporations will continue to pay tax at the regular rates.

Provincial-Local Relations

I would like to review briefly the area of provincial-local finance. Later this week, my colleague, the Honourable Tom Wells, Minister of Intergovernmental Affairs, will be tabling a document entitled *Ontario*

Assistance to Local Governments. This publication provides an overview of total transfers to the local sector and the details of the Province's unconditional grants in 1979.

There has been some criticism of the Government's announcement that total Provincial transfers to the local sector would be increased by 5 per cent in 1979-80. This increase was directly in line with the target growth rate the Government set for the total of its own regular ministry programs.

Mr. Speaker, politicians at every level of government worry about the amount of taxes that they must collect, and so they should. Predictably most politicians would rather see any level of government but their own raise taxes. Taxpayers, however, do not see it that way. They are concerned with the total amount of taxes they must pay. The obligation, therefore, rests with each level of government to contain the tax burden. We have to do this by controlling spending as much as possible. To the extent that tax increases are necessary, politicians at every level of government have to take the responsibility for raising them. We have not asked any more of local governments and their agencies than we have asked of our own ministries. If there is still a need to increase local revenues, then councils and school boards will have to accept that responsibility, just as I must do.

I am pleased to note that local governments have followed the Province's lead by achieving steadily decelerating growth rates in their spending. I estimate that total local spending in 1978 rose by only 8.2 per cent compared to a growth rate of 20 per cent in 1975. For 1979, it appears likely that the local sector will increase its spending by around 7 per cent. I find this progress in restraint at the local level most encouraging.

This restraint, combined with realistic increases in Provincial assistance, is reflected in local taxation developments. On average during 1978, residential property taxes per household rose only about 5 per cent and remained at about 2.6 per cent of average household income. In 1979, we expect increases in per household property taxes

Average Residential Property Taxes per Household, 1970 to 1978

	1970	1977	1978	78/70**	78/77
	($)	($)	($)	(%)	(%)
Municipal*	181	287	299	6.5	4.2
School Board	180	270	286	6.0	5.9
TOTAL	361	557	585	6.2	5.0
As per cent of Household Income	3.2	2.6	2.6		

*Including Special Charges.
**Compound Annual Growth Rate.

to average around 7 per cent. I would remind the Members that the Province's tax credits continue to modify considerably the impact of property taxes, particularly for low-income families and pensioners. This year some $375 million in property tax and rent relief will be provided through this program.

Financing of Health Care in Ontario

Mr. Speaker, the financing of health care in Ontario has been a contentious issue in this Assembly, and in this context I think it is useful to draw to your attention the magnitude of our existing health budget. This year the health budget will increase by $213 million to a total of $4.2 billion, or on average, $488 for every man, woman and child in Ontario.

Some of the Members participated in the review of health care financing conducted last year by the Select Committee on Health Care Costs and Financing. In spite of its best efforts, the Committee could not arrive at a consensus on the best way to pay for our health system.

The Government has considered the Committee's report and continues to study the issues. In so doing, we are aware of a number of important principles. We must continue to provide first rate health care on a universal basis as we are now doing; the health care system has to be adequately financed; and, we must continue to control costs, despite the public musings of the spendthrifts in Ottawa.

With these principles in mind, the Government continues to believe that OHIP premiums should be maintained. In my view, a visible financing link between individuals and their health care system is useful. In an area of government expenditure as massive as health care, it is important that people contribute some portion of costs through a public insurance system. Of equal importance, I do not believe that our economy should be subjected to the massive disturbance that would be caused by a shift away from health care premiums. I would remind the Members that about 70 per cent of health costs are financed out of general revenues. An analysis of the question of OHIP financing is included in Budget Paper D.

Mr. Speaker, we have made considerable progress in controlling the growth of health care spending. We have done so without reducing the quality of services provided. However, costs continue to escalate. Therefore, I propose to increase premiums by $1 per month for single people and $2 per month for families, effective for the benefit month of October. This modest increase of 5.3 per cent will be less than the growth in the cost of insured services which are projected to increase by 5.5 per cent. I need not remind the Members that elderly people in Ontario and those who receive social assistance do not pay premiums and will not be affected by this change. I estimate this measure will raise $40 million in this fiscal year.

Turning to the question of providing assistance to lower income people, we have studied the features of a possible new health tax credit for Ontario citizens. A credit might better ensure that all who are entitled to premium assistance actually get it. Budget Paper D lays out a possible design for a health tax credit. The Government will be interested in the views of the Members and of the public on the ideas outlined in this paper. In the meantime, lower income people remain eligible for assistance under the existing program operated by the Ministry of Health.

Improving the Balance between Revenue and Spending

Mr. Speaker, I now come to the most difficult part of the budget for any Treasurer, particularly a new one. I am going to talk about tax increases.

When I examined our tax structure, I was concerned not only with improving economic incentives but also with the overall level of revenue coming to the Province. For while we have pared down the growth of spending, our revenue growth rate also has been declining. Therefore, we still have a deficit level in Ontario which, in my view, should be reduced. For those interested, I would direct their attention to Budget Paper C which analyses Ontario's revenue and expenditure performance over the past several years.

Tax Actions

I will now propose a number of tax increases to restore a more appropriate balance between Provincial revenue and spending. I shall begin with the area of corporate taxation.

Corporate Taxation

I have outlined tax reductions for some businesses and given you the details of the new Employment Development Fund. While such actions unquestionably are needed, we must recognize that corporation profits, as a whole, have been growing at a healthy rate. It is only reasonable to expect the corporate sector to contribute a fair share of both the cost of incentive programs and the tax revenues required to improve the overall financial position of the Province.

At the same time, our industrial policy places a high priority on the need to upgrade manufacturing and to support small business. I propose, therefore, to maintain the low 10 per cent corporate income tax rate on small businesses and the 13 per cent rate on manufacturing and processing income, as well as on income from farming, fishing, mining and logging.

Effective midnight tonight, there will be a 14 per cent tax rate for all other corporation income. I anticipate additional revenues from this measure of some $36 million.

In addition, I propose to increase the capital tax rate on banks from $\frac{3}{5}$ to $\frac{4}{5}$ of one per cent, effective midnight this day. This measure will increase our revenues by some $5 million. The capital tax rate for loan and trust companies will remain unchanged.

Retail Sales Tax

Turning to the retail sales tax, I propose to expand the base of this tax by including all services relating to telecommunications. This will take effect midnight tonight. Currently only telephone and telegraph communications services are taxable. The major new area affected by this change will be telex and teletype communications. Cable television will be affected also. On average, cable T.V. subscribers will pay an additional 50¢ per month. This measure will augment Provincial revenues by $30 million this fiscal year.

Fuel Taxes

The gasoline tax and motor vehicle fuel tax rates have not been changed since 1972. Fuel taxes are not applied on an ad valorem basis and therefore revenues have grown slowly. In the meantime, the cost of building and maintaining our highways has continued to escalate Accordingly, I propose to raise the tax on both gasoline and diesel fuel by $\frac{4}{10}$ of 1¢ per litre to 4.6¢ and 5.9¢ per litre respectively. Mr. Speaker, contrary to what many people believe, revenues from road-users still fall below spending on highways, roads and related services.

I also propose to increase the tax rate on aviation fuel from .66¢ to 1.32¢ per litre. This tax has not been changed since 1968. Since that time, the Province has significantly increased its expenditures for building and upgrading airports, particularly in the North. With the $11 million the Government is planning to spend this year, the Province will have spent $27 million on airports since 1976.

Railway locomotives, unlike other commercial transportation vehicles, are at present exempt from the tax on diesel fuel. To improve equity among commercial carriers, I propose to impose a tax of 2.2¢ per litre on diesel fuel used in railway locomotives. I might mention that, until now, Newfoundland and Ontario were the only provinces which did not tax diesel fuel used in locomotives.

These gasoline and fuel tax changes will become effective midnight tonight and will add an additional $79 million to Provincial revenues in this fiscal year.

Alcohol and Tobacco

Mr. Speaker, I also propose to increase revenues from alcoholic beverages and tobacco.

With respect to alcoholic beverages I am making mark-up and licence fee changes effective April 30 to increase revenue by $22 million in 1979-80. The changes are as follows:

- Mark-ups on domestic spirits will be increased by the equivalent of 20¢ per 25 ounce bottle.
- Ontario table wine mark-ups will be increased by the equivalent of 20¢ per 26 ounce bottle.
- The licence fee on the production of beer for sale in Ontario will be increased by the equivalent of 10¢ per 24 bottle case.
- A licence fee on sales by Ontario wineries through their own stores will be reinstated at 10 per cent.
- The mark-up will be reduced on lower alcohol strength Ontario wine by the equivalent of 15¢ per bottle and the mark-up on Ontario brandy will be also reduced.
- Finally, there will be no mark-up increases for imported spirits and imported wine, or for other domestic wine.

Mr. Speaker, in spite of these changes Ontario continues to have the lowest beer prices in the Country, as well as the lowest prices for domestic spirits in any province with a sales tax. Ontario's prices are still the second lowest for imported scotch whiskey.

With respect to tobacco, the tax on a package of 20 cigarettes will be increased by 2¢ effective midnight this day. Also, the taxes on cut tobacco and cigars will be increased. Retailers will not be required to take inventory of existing tobacco stocks. This will lighten the load for retailers and allow cigarette products on hand to be sold at existing prices. These tobacco tax increases will yield some $22 million in additional revenues.

Land Transfer Tax

I propose to increase the basic rate of the land transfer tax to $\frac{2}{5}$ of one per cent on the first $45,000 of the value of the transaction and to $\frac{4}{5}$ of one per cent on the remainder. This change, which will take effect midnight tonight, is the first adjustment to the basic land transfer tax in seven years. I anticipate additional revenues of $20 million this fiscal year. As well, I am proposing to provide a tax-free rollover for transfers of land to family farm and small business corporations.

Fees and Licences

Many fees and licences are related to the costs of services and I believe that they should be reviewed regularly. This year, a number of fees and other charges will be increased. In total, I estimate that revenues will increase by some \$15 million as a result of these changes. My colleagues, whose ministries are involved, will announce the details in due course.

Tax Reductions

Before concluding taxation matters, Mr. Speaker, I would like to propose a number of other changes—changes that reduce taxes.

First, I propose to raise the retail sales tax exemption for all candy, confection and soft drinks to 49¢, effective midnight this day. This measure will provide a tax saving to consumers of \$16 million this fiscal year. The confectionery and soft drink industries employ over 12,000 people and play an important role in the Ontario economy. Recently, inflation has pushed the cost of many products over the 20¢ exemption level. This has created a number of problems for the industry and small retail vendors.

Second, I am proposing that with respect to admission fees, the ticket price exemption be increased from \$3.00 to \$3.50. The annual cost of this measure will be about \$1 million. Exemption from the 10 per cent tax will be available to all entertainment provided by organizations qualifying as charitable, non-profit, or amateur athletic associations under the Income Tax Act (Canada).

Third, all purchases of aircraft and aircraft parts will be exempt from retail sales tax for all carriers licensed to provide commercial public transportation and cargo services. This action will eliminate an administrative discrepancy between inter- and intra-provincial carriers, and will assist Ontario airline operators. It will cost \$4 million this fiscal year.

Fourth, to encourage energy conservation, promote safety and help homemakers cope with the cost of living, the following changes will be introduced. These measures will also be effective midnight today.

- The retail sales tax will be rebated on all materials purchased for incorporation into solar heating systems. The maximum rebate will be \$700. This measure will ensure that people who build their own solar heating units receive the same tax benefit available to those who buy factory built models.
- Household smoke alarms will be exempt from sales tax.
- In response to requests from consumers, I propose to provide a full sales tax exemption for yard goods and clothing patterns purchased for household use.

The cost of these retail sales tax reductions will be \$6 million.

In concluding my discussion of tax changes, let me inform the Members that my colleague, the Honourable Lorne Maeck, Minister of Revenue, will be introducing a bill later tonight which will maintain

Ontario's personal income tax rate at 44 per cent of basic federal income tax for 1979. This rate remains the second lowest in Canada. The Minister of Revenue will also be introducing other legislation to implement tax changes announced tonight.

Revenue Impact of Tax and Other Changes, 1979-80
($ million)

Increases	
Gasoline Tax	57
OHIP Premiums	40
Corporate Income Tax	36
Retail Sales Tax	30
Motor Vehicle Fuel Tax	22
Tobacco Tax	22
Alcohol	22
Land Transfer Tax	20
Fees and Licences	15
Capital Tax	5
Total Increase	+269
Decreases	
Succession Duties	−28
Capital Tax	−20
Retail Sales Tax:	
Confections	−16
Tourism	−13
Household Goods	−6
Other	−5
Total Decrease	−88
NET REVENUES	+181

1979 Fiscal Plan

Mr. Speaker, I would now like to sum up our financial position.

Looking at the fiscal year just ended, interim figures show that our total spending was $14.5 billion, an increase of 6.9 per cent, which was under the original target. I would like to commend my colleague, the Honourable George McCague, Chairman of the Management Board, for the fine job he has done in managing our expenditures. As I said earlier, for the third year in a row, we have spent less than was originally budgeted. Now that, Mr. Speaker, is what good management is all about.

Our revenues in the 1978-79 fiscal year were under $13.2 billion, with the result that net cash requirements amounted to $1.3 billion. This represents a substantial reduction of $425 million from the previous year. Details of this improvement in our financial position have been documented in the quarterly *Ontario Finances*.

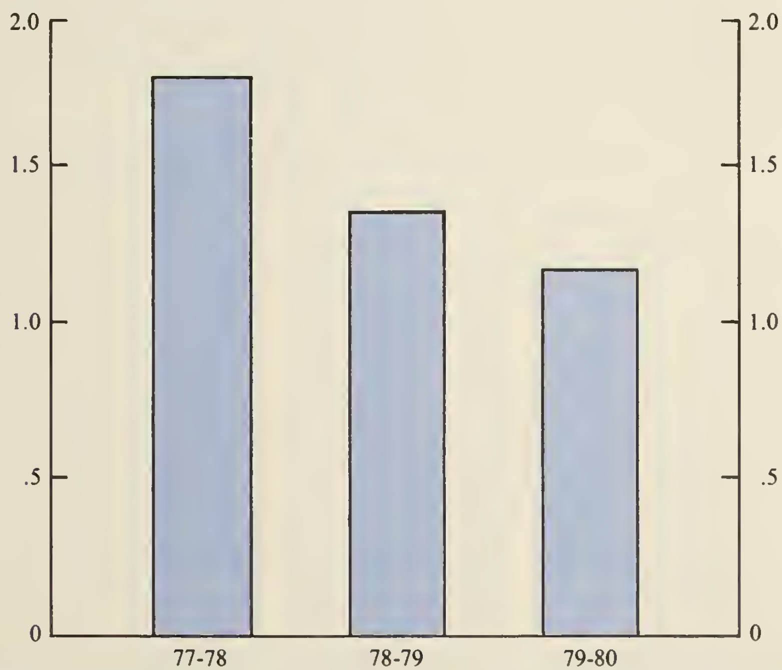
Ontario's 1979-80 Financial Plan
($ million)

	Interim 1978-79	Estimated 1979-80	Year-to-Year Change
Revenues	13,145	14,405	+1,260
Expenditures	14,482	15,558	+1,076
Net Cash Requirements	1,337	1,153	−184
Net Non-Public Borrowing	1,544	1,554	+10
Financing Flexibility	207	401	+194
Net Public Borrowing	105	−259	−364
Change in Liquid Reserves	312	142	−170

At the beginning of this Statement, I indicated that one of my objectives was to further reduce the Province's net cash requirements and establish a better balance between revenues and expenditures. The Government's expenditure plan, which the Members will be asked to approve, projects total spending—including the $200 million we have allocated to the Employment Development Fund—of $15.6 billion in 1979-80. The increase in ongoing spending, excluding the Fund, is only 6 per cent.

The tax changes I have proposed tonight will increase our revenues by $181 million, and all of these new revenues will be applied to reduce

Reducing Ontario's Cash Requirements
($ billion)



the deficit. The resulting net cash requirements of $1,153 million are well within the financing capacity provided by the Province's non-public borrowing sources. In fact, we will have additional financing flexibility this year of over $400 million. I plan to use part of this flexibility to reduce outstanding Treasury Bills by $195 million. This will help to alleviate upward pressure on interest rates and improve the availability of capital for the private sector.

As Members know, the bulk of our non-public borrowing comes from internal pension funds and the Canada Pension Plan. The entire pension system, both public and private, has been a matter of concern in recent years. In 1977 the Government established a Royal Commission on the Status of Pensions to examine the issues and make recommendations for improvement. Later this year the Government expects to receive the report of the very able Chairman of the Commission, Miss Donna Haley, Q.C.

Conclusion

And now, Mr. Speaker, may I just add this concluding word.

When I became Treasurer I wanted to set for myself a high standard. I could think of nothing better than to follow the creed of one of the finest Treasurers this province has ever known, the Honourable Leslie Miscampbell Frost. A new portrait of Mr. Frost hangs in the lobby of the building which also bears his name and beside it is a plaque quoting from his first Budget speech. He said:

> For the fine old Province of Ontario there will be a great future. We are building not only for these times; we are planning for a greater population; for industrial expansion; for prosperous farms and for happy, healthy people. We are laying the sure foundations for a greater and stronger Ontario.

Mr. Speaker, I am confident that the proposals which I have put before you will meet the needs of our people and help to build for the future. This Budget will—

- create more jobs for Ontario's young people.
- It will restrain inflation by keeping the cost of government in check.
- It will reduce the deficit.
- It will provide new incentives for job-creating investments.
- It will help our farms, small businesses and manufacturing industries to grow and prosper.
- It will eliminate the costs, delays and fears of inheritance taxes.
- It will improve the investment climate in Ontario.
- It will promote economic development and employment in the North. And,
- it will ensure a dynamic and prosperous future for all of the people in Ontario.

The Ontario Economy, 1977-1979

	1977	1978	1979	77/76	78/77	79/78
	($ billion)			(per cent)		
Total Output						
Gross Provincial Product	82.2	90.8	100.7	10.7	10.5	10.9
GPP (constant 1971 dollars)	47.9	49.6	51.3	3.6	3.6	3.3
Investment						
Machinery and Equipment	6.0	6.5	7.4	7.7	8.4	13.7
Non-Residential Construction	5.0	5.2	5.5	4.6	4.1	5.4
Residential Construction	3.7	3.7	4.0	3.7	−1.8	9.7
Other Components of Demand						
Housing Starts—Units (000)	79.1	71.7	71.0	—	—	—
Retail Sales	22.7	25.1	27.8	7.9	10.7	10.5
Exports	25.5	29.8	34.4	15.6	16.9	15.6
Imports	20.7	24.1	27.8	11.6	16.3	15.4
Income						
Personal Income	67.7	75.0	83.8	10.4	10.7	11.8
Corporate Profits (before taxes)	9.2	10.8	12.2	10.1	16.5	13.8
Prices						
GNE Deflator	—	—	—	6.9	6.7	7.4
Consumer Price Index	—	—	—	8.0	9.0	8.2
Jobs						
Labour Force (000)	3,994	4,147	4,279	2.8	3.8	3.2
Employment (000)	3,714	3,847	3,974	1.9	3.6	3.3
Unemployment Rate (% of labour force)	7.0	7.2	7.1	—	—	—

Source: Office of Economic Policy, Ontario Treasury.

Appendices

Appendix A

Details of Tax Changes

The purpose of this appendix is to provide a more detailed description of tax changes outlined in the Budget Statement. This is a concise summary only, and the reader is advised to consult the statutes for exact information.

The Corporations Tax Act, 1972

Income Tax Rate Increase

- The general rate for corporation income tax will be increased from 13 per cent to 14 per cent.
- The increase will not apply to:
  —income qualifying for the manufacturing and processing deduction for the purposes of the Income Tax Act (Canada);
  —income from mining, logging, farming and fishing; and,
  —income qualifying for the small business deduction for the purposes of The Corporations Tax Act, 1972.
- The corporation income tax rates in Ontario after the change are shown below.

	Manufacturing and Processing Income		Mining, Logging, Farming and Fishing Income		Income from Other Sources	
	Regular Rate	Small Bus. Rate	Regular Rate	Small Bus. Rate	Regular Rate	Small Bus. Rate
	(%)	(%)	(%)	(%)	(%)	(%)
Net Federal Rate	30	10	36	15	36	15
Ontario Rate	13	10	13	10	14	10
Combined Rate	43	20	49	25	50	25

Capital Tax Reductions for Small Corporations

- **Extension of the $50 Flat Tax**
  —The $50 flat tax will be extended to corporations with taxable capital before allocation to Ontario in excess of $50,000 and up to $100,000 at the close of their fiscal years. These corporations are currently subject to a $100 flat tax.
- **Extension of the $100 Flat Tax**
  —The $100 flat tax will be extended to corporations with taxable capital before allocation to Ontario in excess of $100,000 and up to $200,000 at the close of their fiscal years. These corporations are currently subject to the regular capital tax rate.

- **Notch Provision**
  A notch provision will be enacted to phase in the regular rate for corporations with taxable capital before allocation to Ontario in excess of $200,000 and up to $300,000.

Capital Tax Relief for Certain Corporations

- In lieu of the regular capital tax rate, a flat tax of $100 will apply to corporations with taxable capital before allocation to Ontario in excess of $200,000 and up to $1,000,000 if, in the taxation year, the corporation has a zero or negative taxable income for Ontario tax purposes before deducting the following:
  —capital cost allowances (including terminal loss);
  —allowance for purchased goodwill;
  —depletion allowances;
  —resource allowances;
  —3 per cent inventory allowance; and,
  —loss carryovers, donations or intercorporate dividends.

Capital Tax Rate Increase for Banks

- The capital tax rate for banks will be increased from $\frac{3}{5}$ of 1 per cent to $\frac{4}{5}$ of 1 per cent.

New Capital Tax Rates

ORDINARY CORPORATIONS	
Taxable Capital	Tax Rates
($)	
0-100,000	$ 50
100,000-200,000	$100
200,000-300,000	gradual phasing into the regular rate
Over 300,000	$\frac{3}{10}$ of 1%
LOAN AND TRUST CORPORATIONS	$\frac{3}{5}$ of 1%
BANKS	$\frac{4}{5}$ of 1%

The above changes under The Corporations Tax Act, 1972 will apply with respect to the fiscal years of corporations ending after April 10, 1979. For fiscal years that include April 10, 1979, the change in taxes will be prorated on the basis of the number of days that is subsequent to April 10, 1979.

All enquiries regarding corporation tax changes should be directed to:

Corporations Tax Branch
Ministry of Revenue
Parliament Buildings
Queen's Park
Toronto M7A 1Y1
(416) 965-4040

The Mining Tax Act, 1972

Mining Tax Rate Reductions

- The two highest marginal tax rates of 35 per cent and 40 per cent will be removed.
- The exemption from the mining tax will be increased from the first $100,000 to the first $250,000 of mining profits.
- The mining profits tax rates after the changes are shown below.

Mining Profits	Marginal Tax Rate
($)	(%)
up to 250,000	0
250,000-1,000,000	15
1 million-10 million	20
10 million-20 million	25
Over 20 million	30

Processing Allowance Rate Reductions

- The processing allowance rate will be reduced from 30 per cent to 25 per cent of the original capital cost of processing assets where ore is treated to the refining stage in Northern Ontario.
- The processing allowance rate will be reduced from 35 per cent to 30 per cent of the original capital cost of processing assets where a further processing stage such as semi-fabricating or alloying is carried out in Northern Ontario.
- The rates of processing allowance after the changes are shown below.

Treatment Stage	Rate
	(%)
Concentrator	8
Smelter	16
Refinery:	
—Canada	20
—Northern Ontario	25
Further Processing in Northern Ontario	30

- The processing allowance limitations of at least 15 per cent but not more than 65 per cent of combined mining and processing profits will continue to apply.

The above changes will apply with respect to fiscal years of companies ending after April 10, 1979. For fiscal years that include April 10, 1979, the change in the mining tax will be prorated on the basis of the number of days of that fiscal year that is subsequent to April 10, 1979.

All enquiries regarding mining tax changes should be directed to:

Taxation and Fiscal Policy Branch
Ministry of Treasury and Economics
Parliament Buildings
Queen's Park
Toronto M7A 1Z2
(416) 965-6869

The Retail Sales Tax Act

Taxation of Telecommunication Services, Including Cable and Pay Television

The 7 per cent tax will be extended to the following telecommunication services:

- teletypewriting;
- transmission of data, broadcasts or facsimiles through telephone or trunk lines or any other media;
- cable and pay television; and,
- any other form or means of telecommunication.

Effective: April 11, 1979.

Extension of Temporary Exemption for Taxable Accommodation

The temporary exemption from the 7 per cent tax on taxable accommodation (including hotels, motels, etc.) will be extended for a further 15 months and will now expire on March 31, 1981.

The exemption for American Plan accommodation will also be extended to March 31, 1981.

New Temporary Exemptions for the Tourism Industry

The 7 per cent tax will be withdrawn until March 31, 1981 on:

- furnishings purchased for use in hotels, motels, restaurants, etc; and,

- production equipment purchased for use in restaurants.

To be eligible for the exemptions, goods must be delivered on or before March 31, 1981. Details concerning qualifying equipment, furnishings and classes of business will be supplied by the Ministry of Revenue.

Effective: April 11, 1979.

Exemption for Candy, Confections and Soft Drinks Priced at 49 cents or less

The 7 per cent tax will be withdrawn on all candy, confections and soft drinks individually priced at 49 cents or less.

Effective: April 11, 1979.

Exemption for Admission to Places of Amusement

Exemption from the 10 per cent tax will be available to all entertainment provided by organizations qualifying as charitable, non-profit, or amateur athletic associations under the Income Tax Act (Canada).

Effective: July 1, 1979.

For admission to entertainment provided by other organizations, the exemption level will be increased from $3.00 to $3.50.

Effective: April 11, 1979.

Exemption for Commercial Aircraft

The exemption from the 7 per cent tax on purchases of aircraft and parts will be made available to all carriers licensed to provide commercial public transportation and cargo services.

Effective: April 11, 1979.

Rebate for Materials Incorporated into Self-Built Solar Heating Systems

Individuals who purchase taxable parts and materials to build their own solar heating system will be eligible for a rebate of the 7 per cent tax paid, to a maximum of $700, after the system is completed.

Effective: April 11, 1979.

Other Exemptions

The 7 per cent tax will be withdrawn on the following items:

- yard goods;

- clothing patterns; and,
- self-contained smoke alarms for household use.

Effective: April 11, 1979.

All enquiries regarding retail sales tax changes should be directed to:

Retail Sales Tax Branch
Ministry of Revenue
Parliament Buildings
Queen's Park
Toronto M7A 1X9

or

the nearest Retail Sales Tax District Office. For telephone enquiries in Toronto call 487-7161.

The Gasoline Tax Act, 1973

The tax rates will be increased as follows:

- for gasoline, from 4.2¢ to 4.6¢ per litre; and,
- for aviation fuel, from 0.66¢ to 1.32¢ per litre.

Effective: April 11, 1979.

The Motor Vehicle Fuel Tax Act

- The diesel fuel tax rate will be increased from 5.5¢ to 5.9¢ per litre.
- Fuel used in railway locomotives will be subject to tax at a rate of 2.2¢ per litre.

Effective: April 11, 1979.

All enquiries regarding gasoline and motor vehicle fuel taxes should be directed to:

Gasoline Tax Branch
Ministry of Revenue
Parliament Buildings
Queen's Park
Toronto M7A 1Y3
(416) 965-6352

The Tobacco Tax Act

Tax Rate Changes

- The tax on cigarettes will be increased from 22¢ to 24¢ per package of 20. Other package sizes will be subject to proportional increases.
- The tax rate on cigars will be restructured. The new tax rates will be:
  —3¢ if purchased at a retail price of 9¢ or less; and,
  —45 per cent if purchased at a retail price over 9¢.
- The tax rate on cut tobacco will be increased from 0.4¢ to 0.5¢ for each gram of tobacco.

Effective: April 11, 1979.

Inventories

Wholesalers will be required to declare their cigarette inventories as of midnight April 10, 1979, and to remit tax on such inventories as directed by the Ministry of Revenue.

All enquiries regarding tobacco tax matters should be directed to:

Gasoline Tax Branch
Ministry of Revenue
Parliament Buildings
Queen's Park
Toronto M7A 1Y3
(416) 965-2587

Revenue Changes for Alcoholic Beverages

The licence fee on the production of beer for sale in Ontario will be increased by $1.10 per hectolitre (5¢ per gallon) to a total of $12.87 per hectolitre (58.5¢ per gallon). This will be reflected in a 10¢ increase in the retail selling price of a case of 24 bottles of beer.

A licence fee of 10 per cent will be levied on the sales of Ontario's winery-owned or operated stores. The fee is based on total sales net of Ontario retail sales tax.

Mark-ups will be changed on domestic spirits and wines as follows:

- mark-ups on domestic spirits other than Ontario brandy will be increased by 4 percentage points. The mark-up on Ontario brandy will be reduced to 75 per cent;
- mark-ups on Ontario table wine, and other wine currently marked up at 47 per cent, will be increased to 58 per cent;

- mark-ups on Ontario wine with an alcohol content of seven per cent will be reduced from 70 to 58 per cent; and,
- mark-ups on Ontario fortified and dessert wine will be increased from 70 to 75 per cent.

Effective: April 30, 1979.

All enquiries regarding spirits, wine and beer price increases should be directed to:

Ministry of Consumer and Commercial Relations
Communications Services
Queen's Park
Toronto M7A 2H6
(416) 963-0339

The Succession Duty Act

- The Succession Duty Act is repealed, effective in respect of deaths occurring on or after midnight April 10, 1979.

The Gift Tax Act, 1972

- The Gift Tax Act, 1972 is repealed, effective in respect of gifts made on or after midnight April 10, 1979.

All enquiries regarding succession duty or gift tax changes should be directed to:

Succession Duty Branch
Ministry of Revenue
Parliament Buildings
Queen's Park
Toronto M7A 1Y2
(416) 965-1700

The Land Transfer Tax Act, 1974

- The rates of land transfer tax levied under section 2(1) of The Land Transfer Tax Act, 1974 are increased to 2/5 of 1 per cent on the first $45,000 of value of consideration and 4/5 of 1 per cent on the remainder.

- A tax-free rollover will be provided to Canadian residents for transfers of land to a family farm corporation or a family small business where the transferor is a shareholder in the transferee corporation.

Effective: April 11, 1979

All enquiries regarding land transfer tax changes should be directed to:

Land Transfer Tax Section
Succession Duty Branch
Ministry of Revenue
Queen's Park
Toronto M7A 1Y2
(416) 965-1061 or
(416) 965-1740 or
(416) 965-1774

The Income Tax Act

- The rate of Ontario personal income tax will remain at 44 per cent of basic federal tax.
- The level of taxable income for purposes of the Ontario tax reduction has been set at $1,770.

Effective: For the 1979 taxation year.

Other Fees and Licences

A number of changes in fees and licences will be introduced by various ministries. Dates of change and the new levels will be announced by the respective ministries at a later date.

Appendix B

Small Business Development Program

Introduction

To encourage equity investment in Ontario-based small business ventures the Government of Ontario is introducing a new share credit program. Incentives will be provided to investors who buy shares in Small Business Development Corporations (SBDCs) established for the purpose of directing the invested funds to qualifying businesses. Subject to certain conditions, investors may establish their own SBDCs through a straightforward registration procedure. However, investments in qualifying small business must be at arm's length of the SBDC.

Investment Incentive

- Individuals investing in SBDCs will receive a grant equal to 30 per cent of the cost of their equity shares of the SBDC.
- Corporations investing in SBDCs will receive a tax credit against Ontario income tax equal to 30 per cent of the cost of their equity shares of the SBDC.
- There will be no limit on the amount of investment per individual or corporate investor, but the total equity capital of each SBDC will be limited to $5 million.
- The incentives will be available only on new issues of SBDC shares.
- The incentive will be recaptured from the SBDC on the winding-up or the deregistration of the SBDC or upon the redemption or purchase of the shares by the SBDC.
- For individuals, upon receipt of their share certificates from the SBDC they may apply to the Ontario Ministry of Revenue for their share credit. A special statement concerning the share purchase will be provided by the SBDC to the Ministry of Revenue for this purpose.
- For corporations, the SBDC statement will be submitted to the Ministry of Revenue and when approved by the Ministry, installment payments of corporation taxes may be adjusted. Tax credits not fully applied in the year of investment may be carried forward indefinitely.

Small Business Development Corporations

- A straightforward system of registration for SBDCs will be established within the Ministry of Revenue.
- New corporations may be formed in Ontario and registered as SBDCs by filing a proposal containing prescribed information.
- The SBDCs must have issued and outstanding capital of a value of at least $250,000.
- All corporations applying to be registered as SBDCs must have as their objects assisting the development of small business through the provision of equity capital and management counselling.
- An SBDC must invest and maintain:
  - 40 per cent or more of its equity capital in eligible small businesses prior to the end of its first fiscal year;
  - 70 per cent or more of its equity capital in eligible small businesses prior to the end of its second fiscal year and throughout subsequent fiscal years.
- All investments made by an SBDC must be at arm's length of its major shareholders, officers, directors and associates.
- An SBDC must not hold more than 49 per cent of the equity shares of a small business.
- An SBDC will be subject in the usual manner to corporation income tax, but will be exempt from capital tax.
- The SBDC investment must be in equity shares of small business issued after the coming into force of the legislation and cannot be a rollover of existing equity.
- The Government reserves the right to limit the number of SBDCs.

Eligible Small Businesses

Eligible small businesses are those which meet the following criteria:

- They have no more than 100 full time employees.
- 75 per cent or more of their wages and salaries are paid in Ontario.
- They are primarily involved in manufacturing and processing, tourism or mineral exploration and development as defined by regulation, or in other prescribed industries.
- The investment is not used by the small business for the purpose of relending, investment in land or reinvestment outside Canada.
- They are Canadian controlled.

Corporate and individual investors and small businesses interested in receiving more information concerning the SBDC program should write for an explanatory pamphlet to:

SBDC Program
Ministry of Revenue
Parliament Buildings
Queen's Park
Toronto M7A 2B3
(416) 965-8903
(416) 965-2923

For information regarding the policy intent and background of the Program, contact:

Taxation and Fiscal Policy Branch
Ministry of Treasury and Economics
Parliament Buildings
Queen's Park
Toronto M7A 1Z2
(416) 965-6869

Appendix C

The Ontario Employment Development Fund

Introduction

The Government of Ontario has established a special $200 million temporary program to stimulate job creation and business investment in the province. This program, which is called the Employment Development Fund, will operate under the direction of a Board of Ministers. The Board will ensure that the Fund is selectively used in order to create jobs, enhance the province's competitive position and generally improve economic development in Ontario. Applications by Ontario's businesses for incentives from the Fund will be judged on a case-by-case basis in terms of how well they satisfy the objectives of the Board.

"One Window" Service

Businesses seeking Provincial financial incentives for $250,000 or more may apply to the Program Director of the Fund if they feel their project proposals reasonably satisfy the Government's general economic criteria outlined below. The main contact point for applications will be the Program Director, who will be responsible for coordinating the evaluation of proposals and for presenting them to the Board of Ministers for a final decision. The Board will consider the merits of each case and approve funding in light of competing requests and the funds available. The Program Director will also coordinate any proposals developed jointly by other Government ministries and the private sector. Applications for less than $250,000 should be directed to the Ontario Development Corporations. The Board of Ministers will assess the future role of the ODCs.

A General Guide to Assessing Potential Eligibility

To maximize the economic benefit to Ontario from the Employment Development Fund, the Board of Ministers will address itself to questions such as the following:

- Would the project go ahead in the absence of Government incentives?
- Does the project generate new jobs or investment in the province and/or protect existing jobs and investment?
- Has the applicant already maximized the access of his company to private sector financing?
- Has the applicant taken full advantage of incentives available from the federal government?

- Will the project encourage greater Canadian ownership and domestic sourcing of machinery, equipment, supplies and professional talent?
- Will it lead to development of new markets, especially for exports or to the replacement of imports?
- Does the project generate development in a slower growth area of the province?
- Will it improve the level of job skills and fill existing critical skill shortages?
- Does the project involve new or improved technology and products?

In considering the potential eligibility of a proposal, the businessman should evaluate his situation in light of such criteria. The Board seeks to maximize the further development of manufacturing across the province. However, the Board will also encourage businesses from all sectors to submit proposals where they feel the objectives of the Fund may be met.

Potential Incentives

The Board intends to be flexible. If it agrees to support a project, the form of assistance will be tailored to the particular situation, and may include grants, loans, loan guarantees, equity participation, interest and wage subsidies. For example, interest cost subsidies could bring borrowing costs in Ontario closer to those in competing jurisdictions; grants, loans or equity participation could improve the flow of essential competitive capital funds; loan guarantees could ensure private sector financing at market rates of interest; and wage-subsidies could encourage skill upgrading in areas of critical skill shortages.

For details concerning the Ontario Employment Development Fund contact:

The Program Director
Ontario Employment Development Fund
6th Floor, Hearst Block
900 Bay Street
Toronto M7A 2E1
(416) 965-4036

or

any of the 15 regional offices of the Ministry of Industry and Tourism.

Budget Papers

Presented for the information of
the Legislative Assembly of Ontario
by the Honourable Frank S. Miller,
Treasurer of Ontario and
Minister of Economics, April 10, 1979

Budget Paper A

Ontario's Economy: Prospects and Policies

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Ontario's Economy: Prospects and Policies

Introduction

Ontario's economic performance during the past decade has been shaped by a series of turbulent international events. Slow growth and high inflation have generated some skepticism about the economy's medium term prospects. Nonetheless, during the 1970s the Ontario economy has performed well relative to other industrial economies and is in a position to respond favourably to an international recovery. Critical to Ontario's success in this regard will be the framework of economic policies provided by the federal and provincial governments.

This paper provides a focus for economic policy in Ontario. Section I documents the relatively strong performance of the Ontario economy during the 1970s. Section II examines the critical factors which influence Ontario's medium term economic prospects. The third section outlines key principles and objectives to guide economic policy in the medium term.

I Strong Economic Performance in Ontario

Most industrial economies experienced a deep contraction and slow recovery following the OPEC oil embargo. Sheltered by a favourable energy situation, the Canadian and Ontario economies experienced a relatively smooth adjustment to higher energy prices and the resulting regional redistribution of wealth.[1] Moreover, Ontario's overall performance in terms of job and income growth during this very difficult period has been superior to that achieved elsewhere.

Income Growth

Growth in the Ontario economy from 1970 to 1977 exceeded that in such major industrial countries as Germany, the United Kingdom, and the United States. Overall, it outpaced average growth in the combined Organization for Economic Cooperation and Development (OECD) nations. Table 1 shows that the Ontario economy grew at an annual rate of 4.0 per cent in real terms during this period.

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[1] In part, this reflected Ontario's efforts to ensure that oil and gas price increases in Canada were phased in gradually to minimize the retarding effect on the economy. See the Hon. W. Darcy McKeough, "Ontario's Economic Recovery", *1975 Ontario Budget* (Toronto: Ministry of Treasury, Economics and Intergovernmental Affairs, 1975).

Growth in Ontario Outpaced Most Industrial Countries — Table 1
(per cent)

	Annual Growth*
Japan	5.4
Canada	4.8
Ontario	4.0
United States	3.2
Germany	2.4
United Kingdom	1.7
OECD Countries	2.4

Source: Statistics Canada, *Canadian Statistical Review*; United States Council of Economic Advisers, *Economic Indicators*; and OECD, *Main Economic Indicators*.
*Average annual growth in real Gross National Product, 1970-1977.

While Ontario citizens continued to enjoy above average per capita incomes, income growth did not keep pace with that in the rest of Canada during the 1970s. A commodity boom, especially in food and energy, favoured the more heavily resource-oriented regions of the country. Table 2 shows that a strong performance in Western Canada pulled the Canadian growth rate ahead of Ontario's. Also, national regional development and equalization policies have strengthened the Canadian common market in bringing more rapid income growth to Canada's less advantaged regions.

Regional Growth in Canada, 1970-77 — Table 2
(per cent)

	Annual Growth*
Atlantic Provinces	13.1
Quebec	12.7
Ontario	12.9
Prairie Provinces	16.8
British Columbia	15.8
Canada	13.7

Source: Statistics Canada, *Canadian Statistical Review*.
*Average annual growth in Gross Domestic Product, unadjusted for inflation, 1970-1977. Real income data are not available for all provinces.

World recession and slow recovery since 1973 had a greater impact in Ontario because of the susceptibility of its manufacturing and metal mining sectors to international cost and demand pressures. In particular, an overvalued dollar and rapid cost inflation through the 1971 to 1976 period made Ontario manufacturing less competitive internationally. However, Ontario has grown faster than other provinces in periods when markets for manufactured goods were strong. Sustained growth in foreign markets, coupled with moderation of domestic cost pressures and depreciation of the Canadian dollar during the past two years, have contributed to a healthy trade performance. This has resulted in significant opportunities for Ontario producers in export markets and in meeting foreign competition at home. As a consequence, growth in Ontario in both 1977 and 1978 exceeded that in the country as a whole and is expected to do so again in 1979.

Job Creation

Ontario's job creation record in the 1970s was unequalled among major industrial competitors, as shown in Table 3. Manufacturing employment in Ontario grew by some 70,000 jobs between 1970 and 1977 compared to net declines in the United States, Japan and Germany. Despite an unparalleled rate of growth in the number of new job seekers, the Ontario unemployment rate averaged significantly below that in the United States.

Job Growth in Ontario Leads Industrial Countries — Table 3
(per cent)

	1970-1977 Average Annual Growth	
	Labour Force	Employment
Canada	3.2	2.9
Ontario	3.3	2.9
United States	2.4	2.0
Germany	1.1	0.6
Japan	0.3	0.2
United Kingdom	0.4	−0.2

Source: See Table 1.

This impressive performance continued in 1978, with employment growth at 3.6 per cent, or 133,000 new jobs. Of these, 36,000 jobs were in Ontario's manufacturing industries. Nevertheless, despite the outstanding rate of job creation, the labour force grew at an even faster rate resulting in a rising unemployment rate in recent years. Dealing with this issue remains a major challenge for economic policy.

Cost Performance

Canada enjoyed moderate success in combating inflation in the early part of the decade. By mid 1974, however, the nation found it difficult to contain domestic inflationary pressures while avoiding the economic downturns experienced elsewhere. The greater susceptibility of the Canadian economy to international price effects contributed to higher inflation in Canada than in the United States. Consumer prices rose 80.2 per cent in Canada between 1970 and 1978 compared to 68.0 per cent in the United States.

A high-valued Canadian dollar early in the period and a dramatic deterioration in the relative Canadian cost performance in 1975 contributed to a marked decline in competitiveness vis-à-vis the United States. Table 4 shows that Canada's cost position in manufacturing diverged sharply from that in the United States in 1975 and 1976. Since 1977, however, Canadian manufacturing has restored its competitiveness. Lower wage settlements in Canada and the depreciation of the Canadian dollar have helped to slow relative unit cost increases. On the other hand, unit labour costs in the United States have been accelerating.

Unit Labour Cost Growth in Manufacturing — Table 4
(per cent)

	In Canadian Dollars	In U.S. Dollars	
	Canada	U.S.	Canada
1971	0.5	0.9	3.9
1972	3.1	0.4	5.2
1973	4.8	4.3	3.8
1974	12.9	16.2	15.4
1975	16.5	6.5	12.0
1976	8.6	3.9	12.0
1977	5.4	6.3	−2.2
1978*	3.3	6.9	−3.9
Cumulative Change 1971-1978	68.9	54.3	54.4

Source: United States Bureau of Labour Statistics, *Monthly Labour Review* and, Bank of Canada, *Bank of Canada Review*.

*Average of the first three quarters.

Canada's unit labour cost performance in relation to other major industrial nations during the 1970 to 1977 period was even better, as documented in Table 5, and significant further improvements were made in 1978.

Canada's Competitive Position has Improved — Table 5
(per cent)

	Manufacturing Unit Labour Costs 1970-77 Average Annual Change	
	Domestic Currency	U.S. Dollars
Canada	7.6	7.4
United States	5.4	5.4
Japan	11.6	16.3
France	9.2	11.1
Germany	5.8	12.9
United Kingdom	14.5	9.5

Source: United States Bureau of Labour Statistics, *Monthly Labour Review*.

This brief review indicates that despite domestic and international economic difficulties during the 1970s, substantial gains were achieved in terms of employment and incomes. In recent years the competitive position of the manufacturing sector has been restored. Ontario is now in a favourable position to respond vigorously to the economic opportunities of the 1980s.

II Challenges of the 1980s

Major domestic and international issues have emerged in the 1970s that will affect the performance of the Ontario economy during the next decade. These issues relate both to short-run concern about jobs, incomes and prices, and to the longer-term need to improve efficiency and ensure Ontario's competitive position. All are critical in formulating an integrated strategy for development in the medium term. They include:

- the need to control inflation;
- the need to create new job opportunities;
- the need to attract investment; and,
- the need to capture new markets.

Containing Inflation

Large price increases in food, resources and energy in the early 1970s produced substantial regional and international income redistribution which ultimately fueled double digit inflation in Canada. The experience of accelerating inflation led Canadians to attempt to insulate themselves against the effects of rising prices. As a result, in collective bargaining, shorter contracts and "cost of living" protection became more popular, and cost-plus pricing was more widely used. These responses have made it increasingly difficult for the country to absorb cost increases originating outside Canada or involving real shifts in wealth from one group in society to another.

Canada's domestic costs rose faster than those of the United States in the mid 1970s, while a high valued dollar further reduced the cost competitiveness of Canadian industry. The most immediate impact was in lost markets abroad for Canadian manufacturers, increased competition at home, and a substantial increase in Canada's tourism deficit.

Entrenched inflation and declining competitiveness had its impact on the effectiveness of government fiscal policy as well. Increased consumer spending on imports reduced the stimulative impact of public sector deficits. Moreover, concerns about the economy and inflation contributed to a sharp increase in personal savings and reduced domestic demand.

Creating Jobs

Dramatic growth in the labour force, particularly in the number of inexperienced and less skilled workers, has put enormous pressure on Ontario labour markets. Industry created jobs at a record rate. However, in some sectors more job creation would have required wages to fall below the minimum wage or below alternative levels of support available from the family and unemployment insurance.[2] Yet general demand stimulation to create even more jobs was hamstrung both by high imports and by the prospect of creating greater price pressures where skill and supply shortages existed. For these reasons, governments have looked increasingly to specific wage subsidies to aid in the process of introducing the young and inexperienced to the job market.[3]

Demographic changes during the next few years resulting from an uninterrupted decline in birth rates since 1960 will alleviate some of the recent difficulties associated with the dramatic increase in the number of young people entering Ontario's labour force. In comparison to annual increases averaging 38,000 in the 1970s, net increases in the number of young people in the labour force in the 1979 to 1985 period will average less than 2,000 annually. Meanwhile, programs which have been implemented to upgrade youth employability will have lasting advantages in terms of higher productivity through greater work experience and improved job search techniques.

Future Shifts in Ontario's Labour Force — Table 6

	Proportion of Total Labour Force		Average 1979-85	
	1978	1985	Change in Labour Force	Growth Rate
	(%)	(%)	(000's)	(%)
Adult Males*	45.9	46.4	51.0	2.5
Adult Females*	28.3	31.4	50.9	3.9
Youth**	25.8	22.2	1.7	0.1
Total	100.0	100.0	103.6	2.3

Source: Statistics Canada, *Labour Force Survey*, and Ontario Treasury estimates.
*Persons 25 years and older.
**Persons 15-24 years old.

The dynamics of Ontario's population structure have other implications for the composition of labour markets in the years ahead. Changing social attitudes, expanded employment opportunities, higher wage rates and inflation have contributed to a sharp increase in the

[2]For a discussion of this issue, see Ontario Treasury Staff Paper, *Youth Employment and the Ontario Economy*, June 1978.
[3]Examples are the Ontario Youth Employment Program and the Ontario Career Action Program.

proportion of women entering the labour force.[4] Between 1970 and 1978, the participation rate for women in the 25 to 54 age group rose dramatically from 46.9 per cent to 61.6 per cent. The corresponding participation rate for males has remained steady at just over 96 per cent.

More emphasis on expanding opportunities for working women will be needed in Ontario. Women will represent one-half of the annual increases in the Ontario labour force over the next six years, and by the mid 1980s close to 42 per cent of the total work force will be women.

Competing for Investment

International shifts in manufacturing investment will be of crucial significance to the future of Ontario. Increasing attention has been given to the shifting pattern of economic development throughout the world and North America. In the Canadian context, for example, it is now commonplace to discuss shifts in economic activity to the energy-rich provinces. Within the United States there has been a marked shift in economic activity from the industrial Northeastern states to the Southern Rim states. In Ontario, these shifting patterns have resulted in growing concern about the economy's ability to attract investment.

The net result has been to make all jurisdictions more eager to compete for investment and economic activity. In Ontario, the need to create jobs to meet unparalleled growth in the labour force served to heighten this awareness. Increasingly, the central focus of economic policy is on the need to maintain long-term international competitiveness to attract investment.

One measure of the attractiveness of Canada as an investment location is Canada's share of foreign manufacturing investment by U.S. multinationals. Despite the fact that no discernible trend is apparent in Canada's proportion of total investment, Table 7 shows that there are some important shifts. Most noticeable is the decline in the 1970s of investment in several high technology industries that are of particular significance to Ontario. These include electrical products, fabricated metals and the machinery and transportation products industries. On the other hand, a growing share of chemical industry investment is, in large part, responsible for maintaining Canada's overall investment position. The data suggest, however, that in the 1970s Canada lost some of its competitiveness in attracting international investment in a number of key manufacturing industries.

A similar pattern is reflected in the disturbing deficit in Canada's balance of payments in manufactured end products. A merchandise trade surplus of $3.5 billion in 1978 masked a deficit of $11.8 billion in finished products. Mounting deficits are particularly pronounced in several high skill manufacturing industries while the overall trade sur-

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[4]See Ontario Treasury Staff Paper, *Long Term Outlook for Labour Force Growth: Canada and Ontario*, June 1976.

Canada's Share of U.S. Multinational Foreign Investment in Manufacturing
(per cent)

Table 7

Industry	1966-70	1971-75	1976-78
Food Products	24.3	20.2	18.7
Paper and Allied	57.6	58.3	56.1
Chemical and Allied	14.0	24.3	28.4
Rubber Products	23.2	24.9	25.0
Primary Fabricated Metals	23.6	8.5	10.9
Machinery	14.6	11.0	10.5
Electrical	25.6	18.6	18.4
Transportation	31.1	21.2	25.3
Other Manufacturing	20.1	14.1	14.3
Total Manufacturing	22.2	20.6	20.9

Source: United States Department of Commerce, *Survey of Current Business.*

pluses are generated by exports of raw materials and semi-fabricated products. As shown in Table 8, imports are gaining dominance in key manufacturing industries. Moreover, Canada's competitive position in many resource commodities may be slowly eroding relative to several countries. In addition, Canada has a sizeable and growing reliance on imported managerial, technical and marketing services. For 1977 alone the deficit on this account is estimated to be over $1.3 billion.

High-Skill Industrial Competition is Increasing
(per cent)

Table 8

	Import Penetration*		
Industry	1965-70	1971-76	1977
Electrical Products	23.8	32.1	35.6
Transportation Equipment	51.2	68.2	75.1
Chemicals	25.1	28.9	31.3
Machinery	65.1	70.4	75.2
Metal Fabricating	12.3	15.4	15.8

Source: Economic Council of Canada, *A Time for Reason*, 1978.
*Percentage of the domestic market supplied by imports.

These data indicate a growing weakness in the generation of high productivity investments based on advanced technology and business skills. For an economy facing stiff competition in its traditional markets, maintaining and enhancing productivity growth will be of overriding significance to future prosperity.

Penetrating New Markets

Declining population growth in Canada and Ontario implies that domestic demand will not grow as strongly as in the past. Moreover, the composition of demand will be altered. Reduced rates of household formation and smaller families, for example, will trim the demand for housing and consumer durables. The composition of demand will also be affected by the changing age structure. In the private sector, these changes will result in shifting market opportunities which will require innovative adjustments and increased flexibility by both labour and business. Similarly, public sector expenditure priorities, especially in education and health, will be influenced by the population's changing age structure.

Population growth will also be slow in Canada's traditional markets. Thus, while a demographic slowdown at home will focus more attention on international trade as an engine of economic growth, the competition for established industrial markets and for investment can be expected to intensify. Potential markets in both OPEC and non-OPEC developing countries, however, represent major opportunities for expansion.

Many of these nations have both rapidly growing populations and rising per capita incomes. All industrialized nations are attempting to gain access to these markets. They have a head start in this process: as Table 9 shows, Canada's export trade is less oriented towards these nations.

Export Market Orientation, 1977 Table 9
(per cent)

Export Destination	All Industrial Countries	Canada
Industrial Countries	62.9	84.0
Oil Exporting Countries	9.3	2.7
Other Developing Countries	15.7	8.9
U.S.S.R., China, and East European Bloc	4.0	2.4
Other	8.1	2.0
Total	100.0	100.0

Source: C. D. Howe Research Institute, *Policy Review and Outlook, 1979.*

Although competition will be intense, Ontario is not without natural advantages. Expertise in resource development, transportation and communication systems, and health and education facilities as well as Canada's international goodwill, provide a firm foundation upon which to compete. Improved access to these markets may also require, however, a *quid pro quo* both in terms of reciprocal market access for labour intensive goods from the developing world and aid in the establishment and modernization of local production facilities. Considerable effort will be required in developing more effective marketing strategies if Canada is to gain a larger share of these new opportunities.

Depreciation of the Canadian dollar has provided a major boost to Ontario producers in capturing new markets at home and abroad.

Maximum benefits will accrue only if business reacts quickly. It is important that businessmen recognize that their increased competitiveness is something more than the transitory effect of an exchange rate fluctuation. Indeed, there is growing evidence that business expectations and expansion plans are now being formed on the basis of a more realistic value for the Canadian dollar and a more competitive cost structure.

III Economic Policy for the Medium Term

The challenges of the 1980s must be met head on by both federal and provincial economic policy. The Province has taken a leading role in this process. In 1978, two federal-provincial conferences of First Ministers on the economy resulted in an important consensus on economic policy in Canada. At the initial meeting Ontario set out two principles that have shaped many of the follow-up initiatives by the senior governments in Canada.[5] These were:

- that all governments in Canada contain their expenditure growth and reduce their regulatory activities to free up resources and encourage initiative in the private sector; and,
- that a positive private enterprise strategy be designed to provide incentives and opportunities for consumers, businesses and workers to stimulate the rate of private spending, investment, employment and productivity growth in the Canadian economy.

These two principles form an essential basis of economic policy in both the short and medium term. Moreover, Ontario has identified five basic economic priorities[6]:

- introduction of incentives to speed the integration of a rapidly growing and highly educated work force into productive employment;
- continued progress toward reducing the underlying rate of inflation in Canada;
- encouraging a more integrated national economy within Canada;
- maximizing the flow of domestic savings into equity support of Canadian enterprises; and,
- improving marketing capabilities and initiatives to gain access to foreign markets.

These priorities flow from the recognition of structural imbalances that have developed in Canada during the 1970s as well as the challenges of and prospects for job creation in the 1980s. Accordingly, the underlying theme of economic policy in Ontario for the medium term should

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[5]The Honourable William G. Davis, *An Economic Development Policy for Canada*, Conference of First Ministers on the Economy, February, 1978.

[6]The Honourable William G. Davis, *Economic Priorities for Canada*, Conference of First Ministers on the Economy, November, 1978.

be the enhancement of the province's international competitiveness. This will be achieved primarily by focusing economic policy on improving productivity, maintaining cost competitiveness and sustaining a competitive investment climate in Ontario.

Improving Productivity

In the long term, Ontario like other high wage jurisdictions, must compete in the skill-intensive industries. Low wage competition from developing countries implies few other options. In recognition of this reality, Ontario must achieve high productivity growth for both labour and capital. This higher productivity growth can be enhanced by:

- increased access to world markets;
- greater success in the innovation of new commercial products and processes;
- more rapid adjustment to changes in the demand for labour skills; and,
- wider application of existing technology and the rationalization of inefficient industrial structures.

Opening Doors Abroad

The inefficiencies of Canada's plant and equipment and, correspondingly, its low productivity performance can be corrected by the wider market access necessary to achieve economies of scale in production, finance and marketing. Market access, in turn, depends on two basic factors:

- the removal of foreign tariff and non-tariff barriers to trade; and,
- the strategic marketing, financial, managerial and technical strength of business. Indeed, productivity on the assembly line often depends on the effectiveness of head office activities.

The reduction of both tariff and non-tariff barriers expected at the conclusion of the GATT negotiations will offer significant new export opportunities to Ontario producers as well as increase the competition that can be expected in domestic markets. These competitive challenges should result in more efficient use of existing production technology and a rationalization (for example, through merger, joint venture and consortium) of industrial structures. The consequent improvement in the productivity performance of Ontario's producers will be felt in the capture of new and larger markets, and expanded and more rewarding job opportunities. Economic policy should be geared to facilitate those adjustments and to ease the dislocations that inevitably result from the reorganization of industry.

Innovation

While Ontario expects to achieve greater access to international markets through Canada's efforts at the GATT negotiations, a positive program to strengthen the innovation capacity of Ontario enterprise is also required. This implies more than simply a focus on the amount spent on scientific research and development. While this is clearly important, successful commercial innovation requires a whole range of business and technical skills and may occur in many fields other than those related solely to advanced technology. Indeed, the most profitable enterprises with the most rapidly growing, yet secure, work forces are those characterized by high skill intensity in both white and blue collar functions (e.g. technical, managerial, marketing, financial and industrial trades personnel). Most multinational enterprises are characterized by these features, as are the most dynamic of small enterprises.

It is "knowledge-intensive" activities, therefore, which must be a focus of economic policy. Finding adequate financing in domestic capital markets is often a problem for these enterprises, since there is little or no salvage value to a research and development effort or to a marketing campaign that has failed. Moreover, the institutionalization of savings in Canadian capital markets, in large measure a response to various tax incentives and regulatory initiatives, has resulted in a conservative approach to investment financing. Yet, financing is critical since their competitors in these high skill areas are formidable; they are the multinationals that were themselves survivors and winners in the innovation process. The 1979 Ontario Budget includes a proposal to spur investment in new ventures.[7]

There are also problems of encouraging multinational corporations to undertake more "high skill" activities in Canada. Nonetheless, the need to overcome these obstacles is evident. Not the least reason for this is that Ontario has a rapidly growing pool of college and university trained graduates. In the past decade, the Province has made an enormous investment in higher education. The emphasis must now be placed on achieving the fullest and most efficient utilization of these human resources and skills.

Ontario has taken the initiative in encouraging greater innovative efforts in Canadian industry. In last year's Budget, Ontario indicated its willingness to join the federal government in providing a powerful new incentive package. In the past year, the federal government acted to provide additional research and development incentives which Ontario has paralleled.

Upgrading Skills

There is a need to develop more industrial skill training. In the past, Ontario industry has relied excessively on the immigration of skilled industrial workers from abroad. However, this option is no longer readily available and it is now more attractive for Ontario's work force to acquire industrial skills because of higher wages in this sector.

[7]See Budget Statement and Appendix B.

Nonetheless, there is a need to improve the design and financing of on-the-job educational and skill acquisition programs.

Last June, Ontario convened a conference, Skills for Jobs, which brought together the major participants in the province's skill training process to explore new ways to upgrade the quality of Ontario's work force. As a result, Ontario is redesigning its skilled manpower training programs. To alleviate critical shortages of skilled workers in Ontario industry, the Province, in conjunction with the federal government, has launched a new Employer-Sponsored Skill Training Program.

Better Productivity in Services

Productivity growth in the service sector has lagged. Its future performance will be crucial to Ontario's competitiveness. Some parts of the service sector have already experienced rapid productivity growth. In transportation and communications, capital investment and technological innovation have been extensive. Other high productivity segments of the service sector are focused on the development of business and technical expertise and the sale of these services at home and abroad. Many of these enterprises, for example in marketing, finance, research and engineering, will continue to be high reward operations with growing market opportunities.

The ready availability of low skill, first-time job seekers has discouraged technological innovation and investment in many service industries. As demographic forces change, however, reduced availability of labour may require increased capital utilization and greater implementation of technological improvements. As a result, significant productivity improvements can be expected.

An Effective Anti-Inflation Policy

While it is important to increase market access and improve research and development and other skill-intensive activities, it is equally important to maintain a non-inflationary environment. Maintaining income increases at levels competitive with those of major trading partners is as important to retaining international competitiveness as is increasing productivity. The lessons of the recent past have been clear. Ontario's economy is very sensitive to international competition, and it is essential for job and income growth that domestic cost inflation not get out of line with that of Ontario's major trading partner, the United States.

The depreciated dollar and moderation in domestic wage pressures have aided substantially the competitive position of Ontario industry. Nonetheless, depreciation has resulted in large price increases for imports, and food prices continue to be highly volatile in response to crop failures and beef and hog cycles. The recent crisis in Iran has raised anew the prospect of increases in oil prices.

A key to containing domestic inflation will be to ensure that price increases emanating from commodity shortages or dollar depreciation are not fully reflected in domestic income demands. Paying higher money incomes in futile attempts to offset this can only lead to further inflation and a further decline in real income. While increasing productivity can help to offset these adverse effects, maintaining international competitiveness will also require an effective anti-inflation policy.

Ontario's Approach

The Province has implemented a four-fold anti-inflation policy. First, it has sought to limit its competition for resources with the private sector.[8] Specifically, Ontario has undertaken to hold its expenditure growth below the growth in Gross Provincial Product. Expenditure growth has been reduced from 24.7 per cent in 1974-75 to 6.9 per cent in 1978-79. In this way, the Province has made a substantial contribution to the overall task of absorbing uncontrollable price increases emanating from abroad. Second, the Province has undertaken to ensure that increases in compensation to its civil servants do not lead those in the private sector or set an inflationary standard. Third, the Government has embarked on a major program to review the costs and benefits of all new regulatory proposals in terms of their impact on inflation and employment. And fourth, the Government is taking new initiatives to stimulate investment and productivity growth in both the public and private sectors.

Sustaining a Competitive Investment Climate

As the world economy becomes increasingly competitive, government policies must become more attuned to those in other jurisdictions. This will involve the industrial regulatory framework, energy availability, competitive tax levels and greater cooperation among governments.

Meeting Basic Standards

Rigorous environmental and energy conservation standards must, of course, be met. The preservation and enhancement of the quality of life in Canada demand that environmental concerns be a major priority. Similarly, Canada's northern climate and energy-intensive industrial structure make energy conservation an essential part of efforts to remain internationally competitive and contain increases in the cost of living. Everyone benefits. To meet these standards, however, society in general must be prepared to share the costs of their implementation. Policy should, therefore, ensure an appropriate framework for achieving environmental quality and energy conservation with the least cost in terms of lost jobs and output.

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[8]For a full description of Ontario's approach to managing the public sector, see Budget Paper C.

Secure Energy Supplies

Escalating energy prices and energy supply vulnerability are among the most important economic issues facing industrialized countries today. Moreover, energy security has become a major factor affecting the investment decisions of many industries. Maintaining access to reliable and competitively priced energy supplies will provide Ontario with considerable advantage in attracting new investment in the future.

Ontario has urged a national energy policy that will promote Canada's self sufficiency in crude oil and ensure that oil and gas prices remain competitive with those faced by industry in the United States. Electrical energy capacity has been developed by Ontario Hydro that provides Ontario with access to a relatively cheap and reliable energy supply which is largely insulated from the dramatic and disruptive events on international coal and crude oil markets. In a world of increasing energy vulnerability, it will be important that economic policy continue to focus on ensuring a sound and secure energy future.

Competitive Tax Rates

Ontario has undertaken to ensure that its taxation system remains competitive with that in the United States. Tax studies done for Ontario indicate that the effective corporation tax in Ontario is highly competitive with those in neighbouring states.[9] A recent study released by the federal government concludes that business taxes in Canada are fully competitive. Indeed, it shows that manufacturing enjoys effective income tax rates averaging considerably below those south of the border. The same study indicates that the personal tax system in Canada also compares favourably with that in the United States.[10]

Manufacturing and small business have been specifically excluded from the one point increase in the Ontario corporate income tax rate proposed in the 1979 Budget.

Cooperation Among Governments

As jurisdictions become more interdependent, and growth in traditional markets slows, all governments will be involved in a search for ways to improve the efficiency and competitiveness of domestic industry. A great danger is that governments, both interprovincially and internationally, will become deeply enmeshed in destructive competition to protect old or gain new markets. Trade barriers, and the inevitable retaliation in all jurisdictions, rebound to the detriment of all. It is imperative that governments develop better cooperation to deal with the destructive as well as beneficial forces that flow from their increased interdependency.

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[9]The Honourable W. Darcy McKeough, Statement to Federal-Provincial Ministers of Finance, *An Agenda for Canadian Growth*, January 26, 1978.

[10]Canada, Department of Finance, *The Tax Systems of Canada and the United States*, November, 1978.

At recent conferences of First Ministers, Ontario took the position that constitutional revisions should provide for a strong Canadian common market in which the free flow of workers, goods, capital and services is assured. Moreover, Ontario has consistently supported Canada's active participation in the GATT multilateral trade negotiations which have as their objective the widespread reduction of both tariff and non-tariff barriers to world trade. It will be important, however, that the federal government spell out clearly the programs that will be available to assist industry in adjusting to the challenges and opportunities that will accompany the changing trade environment.

Conclusion

To meet many of the economic priorities outlined above, the Province has created a special Employment Development Fund. This temporary program will be managed by a Board chaired by the Treasurer of Ontario. The Ministry of Industry and Tourism will coordinate business applications for assistance. The Fund will play a vital role in providing selective support for innovative new ventures, ensuring a competitive investment climate, improving productivity performance and facilitating adjustment to new environmental standards. Complete details of the operation of the Fund are included in an appendix to the Budget Statement.

In addition, the Province has already taken many new initiatives to:

- improve skill training;
- increase employment in research and development;
- increase the flow of Canadian savings in support of indigenous entrepreneurship and business formation;
- increase foreign market access through bilateral and multilateral trade agreements;
- increase domestic investment through maintaining a stable and internationally competitive tax and regulatory environment; and,
- contain domestic inflation.

All of these initiatives are critical to achieving an economic environment in which the aspirations of Ontario's citizens can be fulfilled.

Budget Paper B

Problems and Progress in Federal-Provincial Fiscal Policy Coordination

Table of Contents

Problems and Progress in Federal-Provincial Fiscal Policy Coordination

Introduction

This paper reviews progress achieved in coordinating stabilization or "contra-cyclical" fiscal policies in Canada.[1] The first part of the paper briefly reviews the background to fiscal policy in Ontario. Part II examines Ontario's experience with traditional stabilization policy during the early 1970s. The consequences for fiscal policy of changes to the economic environment during the mid-1970s are discussed in Part III, and Ontario's experience with the sector-selective approach to stabilization in the post-1975 period is reviewed. In Part IV, important questions about the future direction of fiscal and economic policy in Canada are raised, and a framework for Ontario's fiscal policy actions for the 1980s is presented. Part V discusses problems and progress in the consultative process and outlines challenges that face Ontario and Canadian fiscal policy in the decade ahead.

I Background to Fiscal Policy in Ontario

Until the late 1960s, the Province's budgets were principally concerned with the need to finance public services in the most efficient and equitable way possible. The major priority in federal-provincial finance was revenue sharing appropriate to spending responsibilities. Deficit financing to stimulate the economy was not generally viewed as a responsibility of the Province. However, in addressing the need for a fundamental restructuring of public finance in Canada, the 1967 and 1968 Ontario Budgets discussed alternative ways of achieving co-ordination in federal-provincial fiscal policies.

The 1967 Budget stated:

> "In our view, the preferable option is where the federal government is primarily responsible for short-term contra-cyclical policy. The provinces, on the other hand, should gear their budgets around a longer-term growth policy taking care not to aggravate business cycles. . . ."[2]

This position was adopted pending study of the report by the Ontario Committee on Taxation. A paper prepared for that Com-

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[1] "Contra-cyclical" or "stabilization" are terms used to describe policy actions taken to smooth out the peaks and troughs of the economic cycle.

[2] Hon. C. MacNaughton, *Ontario Budget 1967* (Toronto: Department of Treasury, Queen's Printer, 1967) p. 9.

mittee argued that the growing size of the provincial-local sector (see Table 1) and the provinces' increasingly strong credit ratings, meant that effective contra-cyclical policy at the provincial level was feasible. Furthermore, it argued that the significant regional variation in economic performance in Canada made provincial fiscal policy a necessity.[3] The Smith Committee supported this view.[4]

Shares of Government Spending in Canada, 1950-1978 — Table 1

(percentage share of total government spending)

	1950	1960	1970	1978
Federal	57.0	56.2	40.3	41.7
Provincial and Local	43.0	43.8	59.7	58.3
Total	100.0	100.0	100.0	100.0

Source: Statistics Canada, National Income and Expenditure Accounts.

Subsequently, the 1968 Ontario Budget argued for a more flexible and coordinated approach to fiscal policy in Canada:

> "Such a system [consultative mechanism] should, first, permit the federal government to take fuller account of provincial operations in determining Canada-wide fiscal policy. Second, it should allow provincial policies to be more effectively developed in the context of national patterns."[5]

This view has guided Ontario's approach to federal-provincial fiscal policy matters throughout the 1970s. It is in this context that, in 1970, 1971 and again in 1975, the Province took unprecedented actions to stabilize the Ontario economy.

In fact, there are two distinct phases to Ontario fiscal policy in the seventies. These phases reveal a fundamental change in approach to stabilization actions in the post-1975 period that recognizes serious limitations in the traditional policy response.[6]

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[3]Clarence Barber, *Theory of Fiscal Policy Applied to a Province*, a study prepared for the Ontario Committee on Taxation (Toronto: Queen's Printer, 1967).

[4]*Report of the Ontario Committee on Taxation*, commonly known as the Smith Committee Report (Toronto: Queen's Printer, 1967), Volume 1, Chapter 3.

[5]Hon. C. MacNaughton, "The Budgetary Process", Budget Paper B, *Ontario Budget 1968* (Toronto: Department of Treasury and Economics, Queen's Printer, 1968) p. 56.

[6]In the earlier period, governments were guided by the Keynesian conventional wisdom. However, institutional and structural changes which have taken place during the 1970s have reduced both the scope for and the effectiveness of this conventional approach and led to the need for more selective actions. The Keynesian conventional wisdom runs as follows: During an economic downturn, unemployment rises and economic growth is slow. Government revenues are lower than they would otherwise be as growth in corporate profits and personal incomes also slows. On the other hand, government expenditures rise as the growing number of unemployed seek unemployment benefits or other social assistance. These revenue and expenditure changes automatically increase the budget deficit. At the same time, governments may make temporary increases in expenditures and reductions in taxes which also increase the deficit in order to create jobs and stimulate the economy. Conversely, as the economy gains momentum, corporate profits and personal incomes rise more rapidly and government revenues increase. The unemployment rate

II Phase 1: The Traditional Approach, 1970 to 1975

In 1970 and 1971, economic output in Ontario was below potential.[7] The extent of this shortfall is measured by the gap between actual and potential Gross Provincial Product (GPP) shown in the upper portion of Chart 1. It is also reflected in the relatively high unemployment rate, shown in the middle portion of the chart. Ontario's fiscal thrust during the three years from 1970 to 1972, as measured by net fiscal impact, is reflected in the lower part of the chart, and detailed in Table 2.[8]

A strongly expansionary thrust was imparted to the provincial economy in 1970 when the net fiscal impact of the Ontario budget amounted to $203 million, or 0.6 per cent of potential GPP. This is shown by the size of the bar below the neutral impact or zero line in Chart 1. Ontario sustained this stimulus in 1971 and reinforced it with a further $152 million stimulus which represented 0.4 per cent of GPP. Thus, the fiscal stimulus over the two years amounted to almost 1.0 per cent of GPP. This considerable fiscal thrust was reinforced by federal fiscal policy, although the federal stimulus measured relative to the Canadian economy was significantly smaller than that of Ontario measured relative to the provincial economy. Table 3 shows that the cumulative net fiscal impact of the federal government amounted to approximately 0.4 per cent and 0.2 per cent of potential Gross National Product (GNP) in 1970 and 1971 respectively. Chart 1 shows that the gap between actual and potential output closed in 1972 as the Ontario economy moved to its full capacity as a result of the complementary fiscal actions of the Provincial and federal governments. The strong economic recovery thus enabled Ontario to adopt a neutral fiscal policy for that year, as illustrated by the small bar in the lower part of Chart 1.

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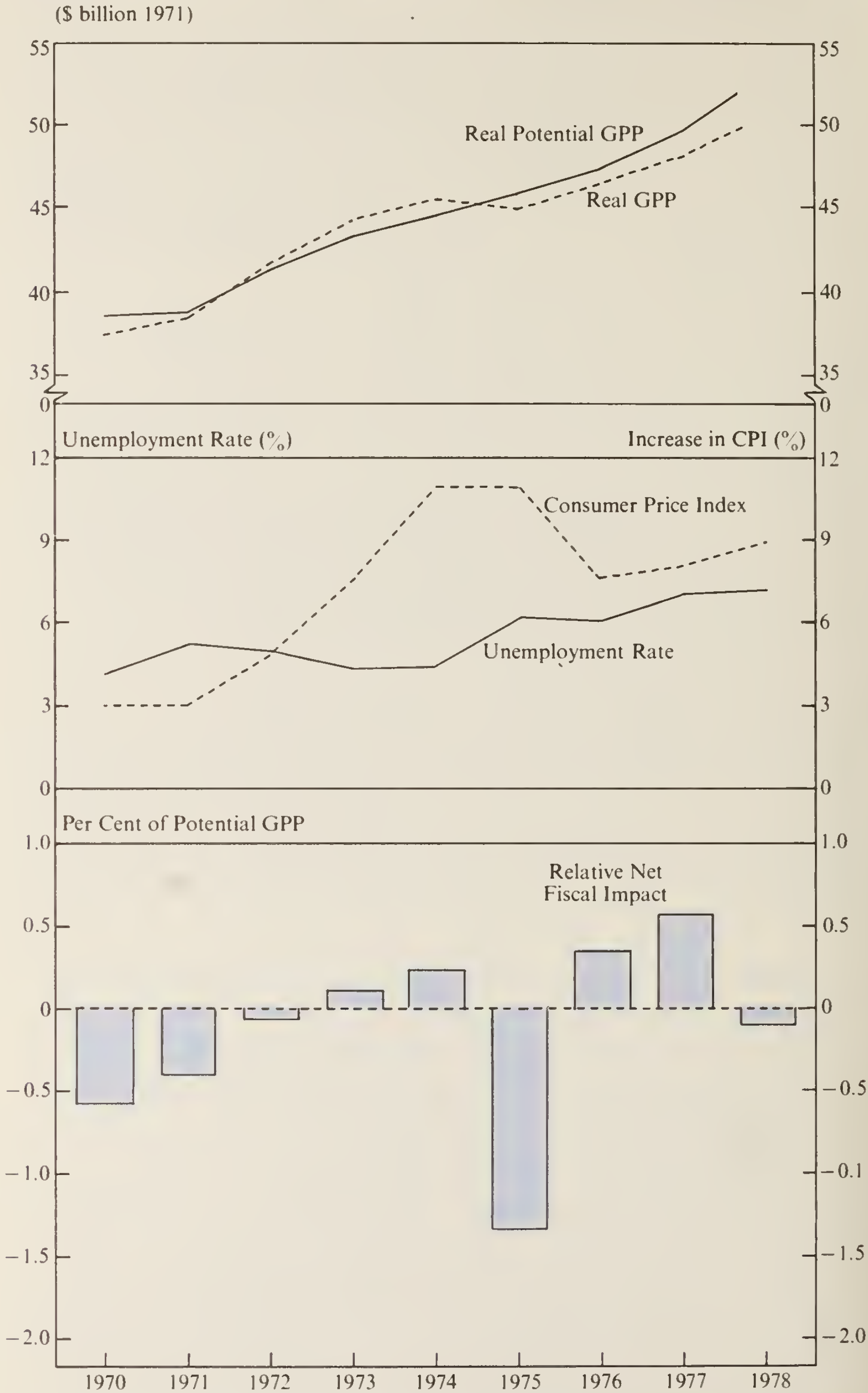
falls and there is a commensurate reduction in unemployment and welfare benefits. These improvements operate to reduce the deficits induced by the downturn. Consequently, the temporary measures taken to stimulate the economy can be repealed. In fact, if the economy recovers to the point where all resources are stretched to the limit, it may be necessary to reduce the deficit (or increase the surplus) through temporary tax increases or expenditure cuts to prevent inflationary pressures from building. In this way, deficits which were necessary when the economy experienced a downturn are financed during an upturn and period of overheating.

[7]For a detailed description of the estimation of potential output, see forthcoming staff paper "The Record of Fiscal Policy in Ontario and Canada".

[8]Net fiscal impact is a technical term that refers to the year-to-year change in the budget deficit or surplus position after certain adjustments have been made to take account of the economic situation. That is, it refers to the increase in the stimulation or contraction that the public sector imparts to the economy. For a more extensive discussion of the full-employment concept, see Ontario Tax Studies 15, *Re-assessing the Scope for Fiscal Policy in Canada* (Toronto: Ministry of Treasury, Economics and Intergovernmental Affairs, 1978) and Hon. W. Darcy McKeough, "New Directions in Economic Policy Management in Canada", Budget Paper A, *Ontario Budget 1971* (Toronto: Department of Treasury and Economics, 1971) pp. 39-58.

Ontario Fiscal Policy and Economic Performance, 1970-1978 — Chart 1



Source: Statistics Canada and Ontario Treasury estimates.

Fiscal Policy Indicators for the Government of Ontario

Table 2

($ million)

	1970	1971	1972	1973	1974	1975	1976	1977	1978
Actual Revenues	4,996	5,573	6,065	6,900	8,268	9,049	10,370	11,687	13,049
Actual Expenditures	5,044	5,935	6,451	7,182	8,487	10,513	11,762	12,966	14,651
National Accounts Surplus or Deficit	−48	−362	−386	−282	−219	−1,464	−1,392	−1,279	−1,602
Add: Revenue Gap	*	19	−21	−124	−135	156	171	381	504
Expenditure Gap	*	1	−1	−5	−5	7	7	12	14
Full-Employment Budget Surplus or Deficit	*	−342	−408	−411	−359	−1,301	−1,214	−886	−1,084
Less: Neutral Full-Employment Surplus or Deficit	*	*	−383	−466	−488	−409	−1,474	−1,365	−987
Net Fiscal Impact	−203	−152	−25	55	129	−892	260	481	−97
Relative Net Fiscal Impact (%)	−.56	−.37	−.06	.11	.22	−1.33	.34	.56	−.10

Source: Statistics Canada, National Income and Expenditure Accounts and Ontario Treasury estimates.

Notes:
1. Revenue gap refers to the difference between actual revenues and revenues that would be generated at potential levels of output.
2. Expenditure gap refers to the difference between actual expenditures and expenditures that would be made at potential levels of output.
3. Full-employment deficit refers to the deficit that the given budget plan would yield at potential.
4. Neutral full-employment deficit refers to the full-employment deficit that would be required for the deficit to be the same proportion of potential as in the previous year, i.e. for the full-employment deficit required to produce a neutral fiscal response.
5. Net fiscal impact refers to the difference between the full-employment deficit and the neutral full-employment deficit, i.e. the new stimulus or contraction provided by the budget.
6. Relative net fiscal impact refers to the net fiscal impact expressed as a per cent of potential output.
7. Negative signs indicate a deficit or an expansionary net fiscal impact.
8. * means not available. Figures are not shown because they are not comparable to other figures in this Table. They are based on an earlier estimation of the technical high-employment norm. The net fiscal impact figures are comparable, as the swing from 1969 to 1970 and from 1970 to 1971 is calculated using the earlier technical high-employment norm.

Table 3

Fiscal Policy Indicators for the Government of Canada

($ million)

	1970	1971	1972	1973	1974	1975	1976	1977	1978
Actual Revenues	15,296	16,996	19,283	22,497	29,599	31,238	35,058	35,798	37,520
Actual Expenditures	15,030	17,141	19,849	22,113	28,490	35,040	38,259	43,207	48,197
National Accounts Surplus or Deficit	266	−145	−566	384	1,109	−3,802	−3,201	−7,409	−10,677
Add: Revenue Gap	*	198	186	−88	−212	759	1,010	1,700	2,097
Expenditure Gap	*	84	148	−72	−157	594	716	1,129	1,474
Full-Employment Budget Surplus or Deficit	*	136	−232	224	740	−2,449	−1,475	−4,580	−7,106
Neutral Full-Employment Budget Surplus or Deficit	*	*	151	−269	267	854	−2,844	−1,647	−5,088
Net Fiscal Impact	−364	−173	−383	493	473	−3,303	1,369	−2,933	−2,018
Relative Net Fiscal Impact	−.41	−.17	−.36	.40	.32	−1.95	.70	−1.34	−.83

Source: Statistics Canada, National Income and Expenditure Accounts and Ontario Treasury estimates.

Notes: See Table 2.

During 1973 and 1974, the economy was overheated. Chart 1 shows that actual GPP exceeded "potential" GPP. That is, many Ontario industries were operating in excess of normal capacity levels of output. This was achieved by extending the working week and by substantially increasing shift work and overtime. However, this pace of activity is not sustainable over the longer term because supply shortages result and cost pressures increase. In fact, during this period the inflation rate accelerated to record levels in response to international pressures and domestic supply bottlenecks. Ontario reduced its full-employment deficit in both years to yield the appropriate contractionary response and slow the economy. This contractionary impact is shown by the bars extending above the zero line. During these two years, federal fiscal policy continued to operate in step with that of the Province.

In late 1974, the Ontario economy turned down as the international effects of the increase in OPEC oil prices were felt. To cushion the economy from the effects of this downturn, the Government undertook major stimulative actions in 1975.[9] As shown in Table 2, Ontario's full-employment deficit rose and provided an expansionary fiscal thrust of $900 million. In relative terms, this amounted to 1.3 per cent of potential output. This thrust exceeded the cumulative expansionary impact of the 1970 and 1971 Budgets and represented a major fiscal policy initiative by Ontario.[10]

The federal government also cushioned the 1975 downturn, as its budget moved from a full-employment surplus of $700 million in 1974 to a full-employment deficit of $2.4 billion in 1975. This provided an expansionary net fiscal impact equal to nearly 2 per cent of the Canadian economy's potential.

This brief review of fiscal policy during the 1970 to 1975 period indicates that Ontario and federal fiscal actions were complementary and generally appropriate to the needs of the Ontario and Canadian economies.

III Phase 2: The Sector-Selective Approach, 1976 Onwards

By 1976, it had become evident that a reappraisal of the traditional approach of general stimulation was required. While the Canadian and Ontario economies had weathered the energy crisis better than most,

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[9]Hon. W. Darcy McKeough, *Ontario Budget 1975* (Toronto: Ministry of Treasury, Economics and Intergovernmental Affairs, 1975); and, Hon. W. Darcy McKeough, *Supplementary Actions to the 1975 Ontario Budget* (Toronto: Ministry of Treasury, Economics and Intergovernmental Affairs, July 1975).

[10]The stimulatory measures in 1975 included a temporary reduction of the retail sales tax rate from 7 to 5 per cent, a temporary grant to first-time home buyers, a temporary rebate of the retail sales tax on purchases of new automobiles, and a temporary removal of the retail sales tax on production machinery and equipment, later extended.

they had not responded as expected to the very substantial 1975 fiscal stimulation. Unemployment remained high, real output continued to fall below potential, and double-digit inflation continued. As well, expected strong revenue growth did not materialize and budget deficits remained high. Rapid growth of government spending at all levels was seen as a significant contributor to inflation.[11]

A combination of factors reduced the effectiveness of the traditional Keynesian approach.[12] These factors include the increased openness of the Canadian economy, the changing composition of foreign trade, and certain structural tax and transfer payment changes.

Structural Changes and Reduced Fiscal Capacity

The structural tax and transfer payment changes are particularly significant. They have reduced the long-term revenue growth potential of the federal government and the provinces and are a major reason for the current high deficit levels.

Over the 1972 to 1975 period, the federal government unilaterally implemented changes to the personal income tax which in their revenue and redistributive effects exceeded all of the changes incorporated in the original 1971 tax reform package. More generous personal exemptions, new interest and dividend deductions, increased deduction limits for RRSPs, and the RHOSP deduction all lowered the growth potential of government revenues. The introduction of indexation in 1974 is the single largest change to the tax system made in the post-reform era.[13] This change by itself has dramatically reduced the growth potential of the personal income tax. By virtue of their tax collection agreements with Ottawa, all provinces except Quebec automatically parallel federal personal income tax changes.

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[11] References to the debate concerning the role of governments in causing inflation include: R. B. Crozier, *Deficit Financing and Inflation: Facts and Fictions* (Ottawa: The Conference Board in Canada, 1976); Robin Richardson, *Has Ottawa had a Policy Relapse: Misconception or Misdirection?* (Toronto: Loewen, Ondaatje, McCutcheon & Co. Ltd., 1976); and, John E. Pattison, *Government Deficits and Inflation Reconsidered* (Toronto: Ontario Economic Council, 1976).

[12] For documentation of the debate initiated by Ontario about the reduced scope of fiscal policy in Canada, see Ontario Tax Studies 15, *op. cit.; Policy Review and Outlook, 1979: Anticipating the Unexpected* (Montreal: C. D. Howe Research Institute, 1979) pp. 100-105; G. V. Jump and Dan Markovich, *The Short-Term Macroeconomic Impacts of the Federal Budget vs. Alternative Proposals by the Major Opposition Parties* (Toronto: Institute for Policy Analysis, University of Toronto, 1978) (privately circulated); Michael McCracken, *A Framework for Examining the Macroeconomic Impact of Unemployment Insurance* (Ottawa: Informetrica, 1978) (privately circulated).

[13] For details of the impact of tax reform and post-reform changes, see Ontario Tax Studies 13, *The Equity and Revenue Effects in Ontario of Personal Income Tax Reform: 1972-1975* (Toronto: Ministry of Treasury, Economics and Intergovernmental Affairs, 1977). For a discussion of the consequences of indexation of the personal income tax for revenue growth, see Ontario Tax Studies 9, *The Dynamic Impact of Indexing the Personal Income Tax* (Toronto: Ministry of Treasury, Economics and Intergovernmental Affairs, 1974).

Between 1970 and 1975, the federal government also reduced taxes on corporations. Lower rates of tax for the manufacturing and processing industries and fast write-offs for production machinery and equipment were introduced. These moves served to lower federal corporate tax yields and to slow the automatic recovery of corporate taxes during periods of economic upturn. Ontario paralleled the fast write-off in its own corporate income tax.

Significant changes were also made to the structure of federal transfer payments. In 1971, The Unemployment Insurance Act was amended. Benefit levels were effectively doubled, coverage was broadened, the entitlement provisions were liberalized and maximum benefits indexed according to the increase in the average wage. Benefits from Old Age Security, a universal transfer to those 65 and over, increased by 20 per cent in 1973. These benefits and the Guaranteed Income Supplement have been indexed quarterly by the Consumer Price Index since that time. Finally, in 1974 the average Family Allowance payment was about doubled to $20 per child. With the exception of a temporary suspension in 1977, this payment has been indexed annually by the Consumer Price Index. In 1979, the monthly payment was reduced from $26 to $20, and the funds saved were used to finance a child tax credit. Over the period, other transfer payments have also been indexed to compensate recipients for inflation.

The personal income tax changes resulted in a redistribution of income, compensated taxpayers for inflation and stimulated savings. In addition, the increases in transfer payments boosted the purchasing power of the elderly, the disadvantaged and families with children. The changes to the corporation income tax were essential to maintain the competitive position of Canada's manufacturing industries. However, in combination these structural changes helped to create a fundamental imbalance between public sector revenues and expenditures by putting upward pressure on expenditures and downward pressure on revenues. This has contributed to the reduced effectiveness and flexibility of general stimulation policies.

In Ontario, appreciation of changing economic circumstances and reduced fiscal capacity led in 1976 to a fiscal policy aimed at regaining control over rising deficits of the Province, thus providing the scope and flexibility for selective fiscal actions.

Sector-Selective Fiscal Policy

Ontario's fiscal policy in 1976 was designed to reduce inflation and to allow the private sector room to expand. This meant that the Government had to play an active role in ensuring that more resources could flow into private sector activities and not be pre-empted by government spending and borrowing. To achieve this, the Province strongly pursued the goal of expenditure restraint. It was particularly stringent within the area of its own administration. Targeted savings were fully realized.[14] Selective tax cuts were introduced to stimulate small business and encourage energy conservation. Revenue for these moves was secured by raising the insurance premiums tax rate, tobacco taxes and taxes on alcohol. OHIP premium levels were also raised, accompanied by broadened premium assistance, in order to establish a better relationship to rising health care costs. These revenue moves were chosen selectively for their minimal impact on economic activity. With this budget plan, Ontario reduced its full-employment deficit to $1.2 billion in 1976 from $1.3 billion in 1975, as shown in Table 2.

The 1977 Ontario Budget put forward a fiscal plan that maintained the policy of freeing up resources for the private sector. The Government announced the objective of achieving the capacity to balance the budget by 1980-81, mainly through a sustained policy of expenditure restraint. Selective tax increases would be made where necessary.[15] This was not an inflexible commitment; the Government acknowledged that changing social or economic conditions might override this goal in the short term and postpone the time frame for its accomplishment.

The tax policies and expenditure programs announced in the 1977 Ontario Budget were thus target specific. Expenditures were restrained, and new funding was provided for a number of important job-creating projects. The Ontario Youth Employment Program and the Community Youth Service Program, and capital spending projects all aimed to expand jobs. Incentives to encourage investment were introduced through an inventory allowance and extension of the fast write-off for manufacturing and processing machinery and equipment. As well, beginning in 1977, Ontario extended its retail sales tax exemption on production machinery and equipment.[16] The overall fiscal effect of the 1977 budget initiatives was to further reduce the full-employment deficit by over $0.3 billion to $0.9 billion.

The 1978 Ontario Budget continued the policy of restraint in spending in order to encourage price stability, improve business confidence and, most importantly, to provide room for job creation in the private sector. Special tax incentives were also introduced to improve the investment climate and stimulate economic activity. The original budget plan would have reduced the full-employment deficit slightly below the 1977 level. The post-Budget reduction in OHIP premiums was fully compensated for by the concurrent one point increase in corporation income tax and announced cuts in the Estimates. However, the Government of Ontario, along with eight other provinces,

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[14]Hon. W. Darcy McKeough, "Restraining Expenditure", Budget Paper C, *Ontario Budget 1976* (Toronto: Ministry of Treasury, Economics and Intergovernmental Affairs, 1976).

[15]Hon. W. Darcy McKeough, "Towards a Balanced Budget", Budget Paper C, *Ontario Budget 1977* (Toronto: Ministry of Treasury, Economics and Intergovernmental Affairs, 1977).

[16]Hon. W. Darcy McKeough, *Ontario's Economic Strategy for 1977* (Toronto: Ministry of Treasury, Economics and Intergovernmental Affairs, 1976).

undertook a temporary reduction in the retail sales tax rate. Hence the full-employment deficit rose to $1.1 billion. But because of the temporary nature of the retail sales tax rate reduction, it did not impair the Province's basic fiscal structure.[17]

In 1976, the federal government acknowledged in its own policies some awareness of changed conditions. It was clear that it saw containing inflation as the number one priority in that year. As Table 3 documents, the thrust of federal fiscal policy paralleled that of Ontario, and the federal full-employment deficit fell from $2.5 billion to $1.5 billion. However, in 1977, Ontario and federal fiscal policy began to diverge substantially. The federal government made additional permanent tax reductions and introduced new expenditure programs, thereby compounding its problem of fundamental imbalance in revenues and expenditures.[18] At the same time, Ottawa did not match Ontario's concerted effort to reduce expenditure growth. The federal gap between revenues and expenditures measured on a full-employment basis, widened sharply to $4.6 billion, or by $3.0 billion. In 1978, the federal full-employment deficit grew to over $7.1 billion. The escalation in the federal full-employment deficit since 1975 is shown in Chart 2.

IV The Shape of Fiscal Policy for the 1980s

New economic realities have required a basic re-thinking of the strategies necessary to accomplish the goals of stabilization policy. In 1977, Ontario presented a plan to achieve the capacity to balance the Provincial budget. A balanced budget capacity on the part of both the provincial and federal governments is essential to free up resources for the private sector and to provide governments with the scope to pursue policies of selective stimulus that work.

To be effective, stabilization policy should comprise mainly *temporary* changes to the tax structure and to expenditures. In this way, policy remains *flexible* to the needs of the economy. Permanent structural changes to taxes and expenditure programs should be made only with full consideration of their long run implications. The introduction of permanent structural changes that are not affordable in the longer term may eventually undermine the very goals they were designed to meet. The Province's discretionary actions have been specific,

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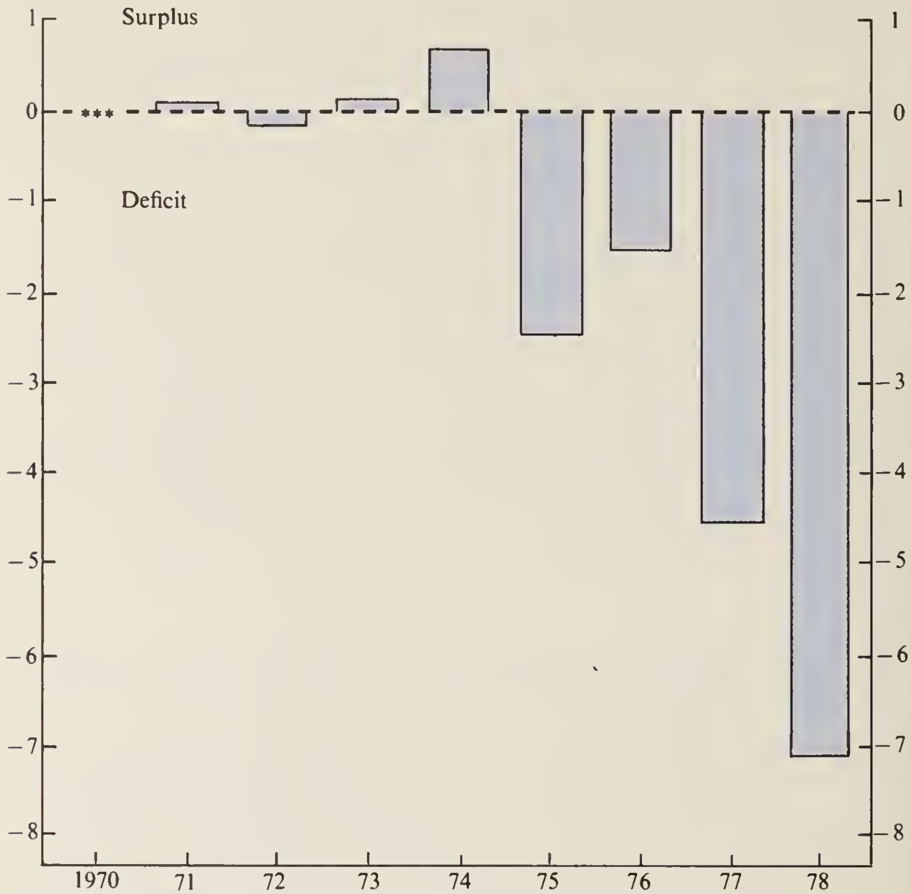
[17]For a discussion of the fiscal outlook, see Budget Paper C.

[18]Some of the major moves made by the federal government are: a child tax credit and increased employment expense deduction (March 1977), additional write-offs for research and development (April 1978), and an increase in the employment expense deduction, a reduction in UI premiums and a reduction of the manufacturer's sales tax rate (November 1978).

Federal Full-Employment Budget Position — Chart 2
($ billion 1971)



***Full-employment budget figures for 1970 are not shown because they are *not* comparable to figures from 1971 onward. They are based on an earlier estimation of the technical high-employment norm. The net fiscal impact figures shown for 1970 in Table 3 are comparable as the swing from 1969 to 1970 and from 1970 to 1971 is calculated using the earlier technical high-employment norm.

Source: Statistics Canada, National Income and Expenditure Accounts and Ontario Treasury estimates.

temporary and effective.[19] By contrast, federal policy has included structural changes, the effects of which have placed significant constraints on the long run development of fiscal policy in Canada.

Continuation of selective temporary measures is the key to fiscal policy in the future. Such measures should be implemented in the context of the requirement to restore long-term balance to public

[19]See the Hon. W. Darcy McKeough, "Economic Recovery in Ontario", Budget Paper A, *Ontario Budget 1976* (Toronto: Ministry of Treasury, Economics and Intergovernmental Affairs, 1976).

sector revenues and expenditures. The sectoral studies conducted jointly by government and the private sector are a step in this direction.[20]

In this Budget, Ontario is introducing a new program to stimulate the underlying strengths of the Ontario economy. Through the setting up of the Employment Development Fund and Board, Ontario is allocating $200 million to stimulate job creation and investment through selective support to new and expanding industrial ventures. The objective of this program is to use available Ontario funds to lever risk-taking and market-oriented innovation on the part of private investors. Experience will be gained by the joint federal and Ontario measures to provide assistance to the pulp and paper industry. This initiative also demonstrates the determination by government to direct incentives to those sectors and those companies which will make the most significant and viable long run contribution to the economic development of the provinces.

The Employment Development Board will coordinate and implement the Government's economic development priorities in a flexible and imaginative manner. The Board will allocate available funds on a case-by-case basis. Since the Fund will provide temporary and specific stimulus appropriate to the short-term needs of the economy, it will not represent a permanent increase in Government spending.

The criteria to be employed by the Board in allocating funds include:

- long-term contribution to Ontario employment;
- development of job skills that are in short supply;
- potential for significant export development or import replacement;
- development of new products and processes through Canadian-based innovation; and,
- development of viable economic sectors and improved regional development.

In the decisions of the Board, priority will be given to levering private sector capital and to avoiding duplication of assistance with other levels of government. Where governments join to support the same enterprise, this will be done on an agreed basis and in a coordinated way.

The Employment Development Fund acknowledges the fiscal constraints on the Ontario Government and aims to focus its support selectively on those activities within the province that will strengthen Ontario's capacity to take a strong position in an increasingly competitive world.

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[20]See, *A Report by the Second Tier Committee on Policies to Improve Canadian Competitiveness*, October, 1978, which summarizes the recommendations of the 23 sector task force.

V Improving the Consultative Process

There has been considerable progress in the 1970s toward improved consultation among governments in Canada on fiscal and economic matters. The Ministers of Finance meet regularly to discuss the economic and budget policy. More recently, First Ministers have begun to hold meetings to discuss major economic issues. They have established a number of important longer range and structural goals to guide Finance Ministers in coordinating annual budget plans.[21]

An excellent example of policy coordination among Finance Ministers occurred with the joint undertaking of a temporary cut in provincial retail sales tax rates in 1978. This action revealed both the merits and risks of an open and coordinated approach to national stabilization policy. It demonstrated that alternative strategies could be discussed among governments and that a consensus could be reached. It also demonstrated the vulnerability of intergovernmental discussions aimed at clear and rapid decisions in a context where not all of the participants have the capacity to act with the full support of their respective governments. In this instance, Quebec subsequently decided on a unique course of action. The process is vulnerable to such other thoughts on the part of each of the participants. This vulnerability is especially great because of the large number of governments involved. The experience well illustrates the challenge in striking a balance between too little and too much provincial participation in national policies.

On the other hand, frictions and problems have been caused by unilateral federal changes to the shared-tax bases and actions Ottawa has taken to control its expenditure growth by limiting transfers to the provinces. While limiting transfers to the provinces may remedy some of Ottawa's problems, the abruptness and general lack of coordination of these actions have complicated provincial fiscal planning and undermined federal-provincial relations.

The compromises made by all parties in order to develop the Established Programs Financing Arrangement clearly indicate that a strong cooperative spirit can exist in federal-provincial financial relations. Unfortunately Ontario is becoming increasingly concerned that, on the basis of recent federal actions, this spirit will be lost and we will again return to federal-provincial dealings which have often been marked by antagonism and confrontation.

The decade ahead will present a number of challenges to fiscal policy. The complexity and importance of these challenges demand that all levels of government in Canada work together to determine their implications and to provide a coordinated policy response. The

[21]See the Hon. William G. Davis, *An Economic Development Policy for Canada* and *Immediate Actions for Job Creation*—papers presented at the Federal-Provincial Conference of First Ministers, February 1978.

following are among the critical medium-term issues that must be addressed:

- the financing of the CPP and the problems of an ageing population;
- the shift in wealth and income toward the oil and gas rich provinces and the implications of this for regional balance and growth;
- the current account deficit in end-products and business services;
- the impact of government borrowing both domestically and abroad; and,
- the growth in competition in domestic and world markets occasioned both by changes in GATT and by increasing manufacturing and resource productivity in less developed countries.

Only good communication and coordinated planning will create the conditions necessary for the formation of an effective response to these challenges which will affect the economic health of each province and Canada as a whole.

Conclusion

In the late 1960s, Ontario undertook to share with the Government of Canada the pursuit of the goals of high employment, stable prices and sustained economic growth. Ontario adopted an aggressive approach to fiscal policy formulation and engaged in direct consultation and debate with Ottawa in order to achieve complementary and coordinated policies. Over the decade, Ontario has made frequent and constructive proposals for fiscal and economic policy development in Canada.

In the early 1970s, Ontario introduced a policy of budgetary stimulus and expanded deficits to overcome the recession of 1970 and 1971. This policy was put in place sooner and was relatively larger in Ontario than was the federal policy in relation to Canada. Again in 1975, Ontario responded to the economic downturn following the oil crisis of 1974 with expansionary actions of bigger impact than in the earlier period.

The reduced scope for generalized fiscal policy was evident by 1975 and Ontario chose measures which were selective, temporary and directed at those sectors of the economy where greatest gains could be achieved. Ontario's adoption of a more selective approach, developed within the context of a capacity to balance the Ontario budget, followed from the structural changes to the Canadian economy which have taken place during the 1970s. These changes include reduced government revenue growth, particularly as a consequence of the introduction of indexation in 1974, and upward pressure on expenditures from inflation. In addition, changes in the industrial structure of Canada, the composition of the labour force and the increased openness of the

Canadian economy have all reduced the effectiveness of efforts by government to lower unemployment.

The changed economic environment has made it necessary for government to assist selectively Ontario's industries that have significant growth potential for the 1980s.

Budget Paper C

Strengthening Fiscal Management

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Strengthening Fiscal Management

Introduction

Demands for government services are virtually unlimited, but the resources available to pay for them are not. When the economy is strong and not plagued by inflation, expectations rise and buoyant government revenues are available to finance more and better public services. Such was the case in Canada from the mid-sixties to mid-seventies.

A high level of economic performance must be sustained on a long-run basis to pay for upgraded services. However, since 1974 the sluggish performance of the Canadian economy has sharply reduced revenue growth while the cost of government, driven up by inflation, has continued to grow. This has resulted in large deficits, especially at the federal level. Federal and provincial tax and expenditure actions introduced to stimulate economic activity have contributed to these deficits. Despite these actions, the performance of the Canadian economy continues below potential and high deficit levels persist. Consequently, a reassessment of the roles of the federal and provincial governments in the management of fiscal policy and the regulation of the economy has been required.[1]

This paper describes the Government's approach to streamlining the public sector in Ontario. The basic components of this approach are:

- to ensure the capacity to achieve a balanced budget;
- to further reduce the size of the government sector and increase efficiency; and,
- to reduce government regulation.

The first section of the paper reviews the progress Ontario has achieved in improving its capacity to balance the budget. It indicates how revenue performance has fallen short while spending has been successfully restrained. It shows that the scope exists to reach a balanced budget in 1984 and reviews the performance of Ontario's revenues and expenditures. The second section outlines measures now being implemented to reduce the size of government, improve program effectiveness and cut bureaucratic regulation of the economy. The final section presents the detailed financial tables for the 1979 Budget.

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[1] For a discussion of the changing role of fiscal policy, see Budget Paper B. See also Ontario Tax Studies 15, *Reassessing the Scope for Fiscal Policy in Canada* (Toronto: Ministry of Treasury, Economics and Intergovernmental Affairs, 1978).

I Maintaining Expenditure Restraint

The 1977 Ontario Budget stated that the Province's objective was to have the capacity to balance the budget by 1981. It also said this was not an inflexible commitment. Any realistic fiscal plan must be sensitive to the performance of the economy and the need for short-term stabilization actions. However, the Province was determined to roll back its spending growth to a point well below revenue growth. It is the realization of this key goal which provides the capacity to balance the budget within a reasonably short period of years.

Ontario has come very close to meeting the expenditure targets set out in 1977. In 1978-79, for the third year in a row, spending was held below the Estimates. However, the pace of economic recovery has been less than anticipated and this has slowed revenue growth. In addition, selective tax reductions undertaken by the Province to stimulate the economy further reduced revenue yields. For example, the 1978 temporary cut in the retail sales tax reduced revenues by $144 million.[2] This fiscal year the Province will be implementing net tax increases, but will also introduce new initiatives to promote employment and economic growth.

As a result of these developments, a revised approach is required to long-range fiscal planning. As previously mentioned, the Government intends to continue its efforts to contain spending growth at a reasonable level. With this in mind, the long-range planning objective is to achieve a gradual reduction in cash requirements rather than to target for specific revenue and expenditure growth rates. A reduction in cash requirements toward a zero position over the medium term requires that an average differential in the range of 2.5 per cent between the rate of revenue growth and the rate of spending growth be maintained. Therefore, efforts will be directed towards holding spending growth below the rate of revenue growth in order that tax increases may not be required. Continued progress toward this relationship between revenues and expenditures will further strengthen the Province's fiscal flexibility.

Chart 1 illustrates the effect on cash requirements of maintaining a 2.5 per cent differential between revenue and spending growth. If this is achieved the Province could be in a surplus position by 1984.

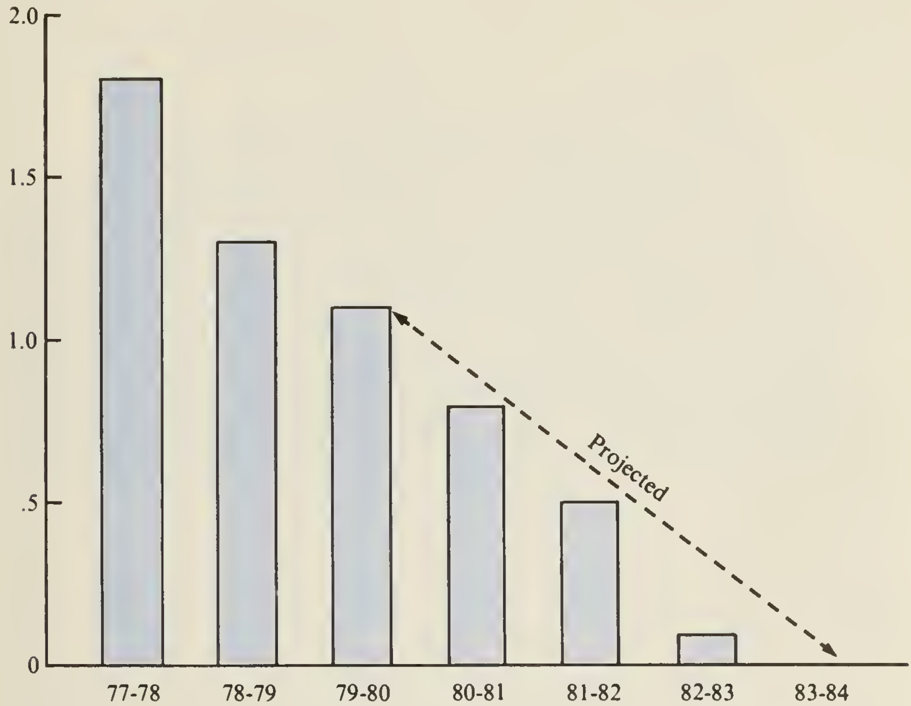
If spending growth were to be held to the rate of increase in revenues, Ontario's expenditures would continue to contract as a percentage of Gross Provincial Product (GPP). This in itself would be a significant accomplishment consistent with the objective set in February 1978 by Canada's First Ministers. To improve the capacity to balance the budget, however, requires a sustained effort to hold spending growth well below

[2]This figure represents Ontario's share of the joint federal-provincial economic stimulus program which reduced the rate of the retail sales tax from 7 per cent to 4 per cent for the period April 11 to October 7, 1978.

Progress in Reducing Ontario's Cash Requirements[1]

Chart 1

($ billion)



[1]Represents Provincial Budgetary and Non-Budgetary financial requirements, excluding Ontario Hydro.

the rate of increase in revenues. The next two parts of this section discuss the Province's revenue and expenditure performance in more detail.

Ontario's Revenue Performance

From the mid-sixties to the early seventies the provincial economy experienced rapid growth. During this period, Ontario's tax revenues grew faster than the economy and allowed the Province to underwrite fairly rapid expenditure growth to meet public demands for new and expanded programs and transfer payments. (See Chart 2.)

Since 1971, important changes have taken place in the Canadian tax structure. These changes have included both income redistribution measures and policies to maintain a competitive tax climate in Canada and Ontario. In the main, these changes have negatively affected the yield and growth rates of the major Provincial revenue sources—personal and corporate income taxes and the retail sales tax. In addition, since

Budgetary Revenue as a Per Cent of Gross Provincial Product
(per cent)

Chart 2

1975, economic growth has been below potential and this has further reduced tax yields. To illustrate the combined effect of these factors it can be noted that budgetary revenue grew by only 5.6 per cent in 1977.[3]

An assessment of the growth potential of major revenues is presented in Table 1. The growth in each revenue source is related to the overall growth in the economy. The measure thus created is known as "simple elasticity". When the simple elasticity of a tax exceeds the value of 1.0, the revenue yield from that tax will exceed the growth in nominal GPP. The table shows the decline in the responsiveness of the major taxes, as their elasticities have declined from well over 1.0 in the 1971 to 1977 period to less than 1.0 during the last two years.

Personal Income Tax

The table shows that the elasticity of personal income tax has declined significantly. This results primarily from indexing which neutralizes the tax yield gains from nominal income growth. This effect has been aggravated by recent high levels of inflation and relatively slow growth in real personal incomes.[4]

[3]The most significant factor in the low revenue growth performance in 1977-78 was a $285 million reduction in revenues under the "Revenue Guarantee". For further details, see the Hon. W. Darcy McKeough, "Federal-Provincial Fiscal Reforms" *Ontario Budget 1977* (Toronto: Ministry of Treasury, Economics and Intergovernmental Affairs, 1977).

[4]Ontario Tax Studies 9, *The Dynamic Impact of Indexing the Personal Income Tax* (Toronto: Ministry of Treasury, Economics and Intergovernmental Affairs, 1974) and Ontario Tax Studies 13, *The Equity and Revenue Effects in Ontario of Personal Income Tax Reform: 1972-1975* (Toronto: Ministry of Treasury, Economics and Intergovernmental Affairs, 1977).

Revenue Response to Economic Growth — Table 1

	7-Year Average 1971-72 to 1977-78	2-Year Average 1977-78 and 1978-79
Gross Provincial Product (%)	13.2	10.6
Budgetary Revenue* (%)	13.8	7.4
Elasticity		
Personal Income Tax	1.32	0.39
Corporate Income Tax	1.53	0.37
Retail Sales Tax	1.16	1.07
Other Revenue	0.75	0.39

*Revenue growth exclusive of tax changes.

Corporation Income Tax

Higher than anticipated costs of recent federal initiatives have contributed to lower revenue growth. These include the three per cent inventory valuation adjustment and fast write-offs for production machinery, measures that were paralleled by Ontario. An equally important factor is that from the mid 1970s until recently corporate profits before taxes have performed poorly. Furthermore, there has been some shifting of the tax base to the West. More recently, these factors have been modified to some degree by the lower value of the Canadian dollar. This has helped Ontario's exporting industries to improve their competitive position in world markets, which is having a positive impact on profits and corporation income tax revenues.

Retail Sales Tax

A number of factors have accounted for the lower yield of this tax. First, in 1975 the Province introduced an exemption for production machinery and equipment in order to stimulate investment. Second, a number of temporary reductions have been implemented to stimulate consumption, such as the two point general rate reduction and the auto sales tax rebate in 1975 and the three point rate reduction in 1978. Third, there is an ongoing shift in consumer and business spending patterns towards the consumption of services, many of which are not taxed.

Other Revenue

The Province relies on a number of other revenue sources to meet its financing requirements. These account for about 18 per cent of budgetary revenue, and include OHIP premiums, motor vehicle registration fees and revenues related to alcoholic beverages. Revenue from most of these items grows very slowly in the absence of discretionary rate changes. Consequently, this area has accounted for a declining portion of the Province's total revenue.

While revenue growth from the major taxes has slowed, these taxes exhibit the highest relative growth and their proportion of overall revenues is gradually increasing. This improving trend has been augmented by the agreement with Ottawa on Established Programs Financing which involves a transfer of personal income tax points from the federal to the provincial level.[5] Overall, the medium-term revenue outlook is for more buoyant growth than experienced during the past few years.

Success of Ontario's Spending Restraints

In a determined effort to reduce the cost of government, the Province initiated a major restraint program in 1975. While its vigorous application has not been without pain, the standard of Ontario's public services has remained high while spending growth has dropped significantly.

With spending growth now lower than the rate of inflation, real reductions in the cost of government are being achieved. Table 2 shows that Ontario's spending has been progressively reduced from a growth rate of 24.7 per cent in 1974-75 to 6.9 per cent for the fiscal year just ended. The local sector followed the Province's lead and considerably reduced its spending growth during the same period.

The federal government has also reduced its spending growth. However, Ottawa's net cash requirements, measured as a per cent of total spending, have grown inexorably, from 6.5 per cent in 1974-75 to 25.1 per cent in the fiscal year just ended. By contrast, Ontario's cash requirements for 1978-79 were 9.2 per cent of total spending.

Government Spending Growth Declines — Table 2

	FEDERAL[1]		ONTARIO		
			Provincial		Local[2]
	Percentage Increase in Expenditure	Deficit as Per Cent of Spending	Percentage Increase in Expenditure	Deficit as Per Cent of Spending	Percentage Increase in Expenditure
1974-75	28.3	6.5	24.7	9.9	14.1
1975-76	18.5	12.3	15.1	15.9	20.0
1976-77	10.4	13.1	10.1	10.6	11.2
1977-78	7.1	18.8	8.6	13.0	10.9
1978-79 (Interim)	9.5	25.1	6.9	9.2	8.2*
1979-80 (Estimated)	8.9	20.4	7.4[3]	7.4	7.1*

[1]Total outlays composed of budgetary expenditures plus net loans and advances. Deficit equals financial requirements excluding foreign exchange transactions.

[2]Local Government expenditure reported on calendar year basis.

[3]Includes funding for Employment Development Fund.

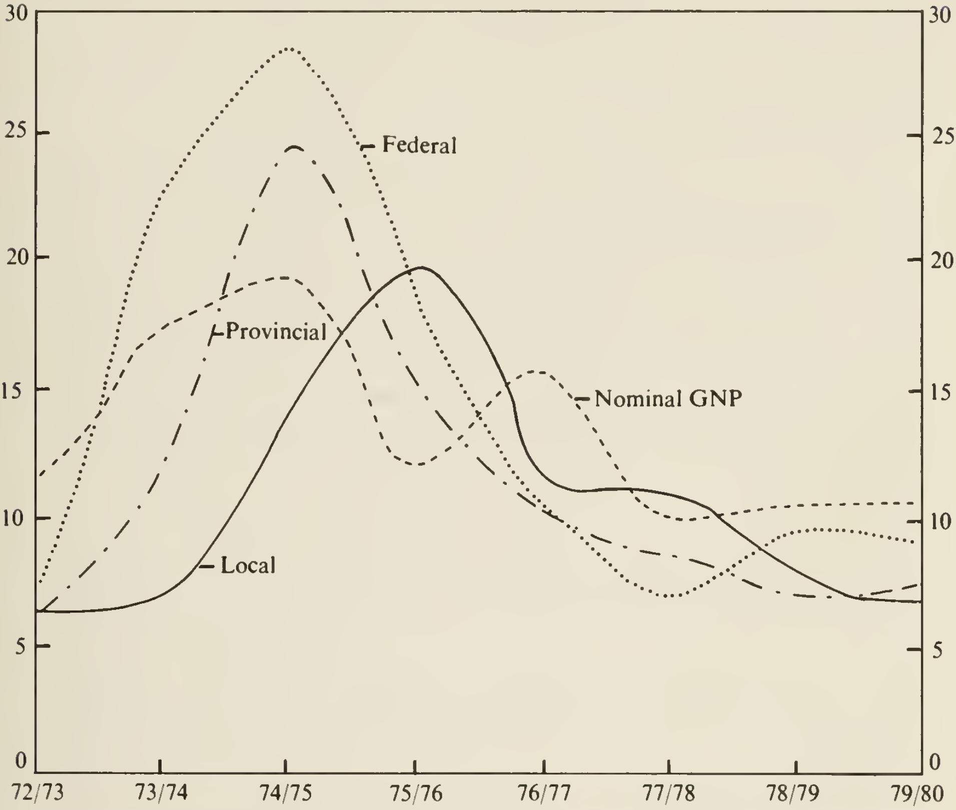
*Ontario Treasury estimates.

[5]See the Hon. W. Darcy McKeough, "Federal-Provincial Fiscal Reforms", *op. cit.*

The following chart clearly shows the significant decline in the size of the public sector in Ontario relative to the economy.

The Turnaround in Government Spending
(per cent growth)

Chart 3



II Managing the Public Sector

Significant reductions in spending growth have been recorded and this restraint effort will be sustained. This section outlines some measures which the Government is taking to ensure the continued success of the restraint program. It describes the in-year budget constraint process, measures to control the cost of manpower and progress towards deregulation.

Stretching the Budget Dollar

Savings of $1.3 billion have been found through program constraints and underspending during the last three years. Of this, some $1.0 billion was re-allocated to new priorities and to cover unavoidable budget overruns in some programs. This left over $300 million in net savings that were realized by holding spending below approved Estimates for three years in a row.

Spending under Budget for Three Years — Table 3

($ million)

	In-Year Reductions	In-Year Increases	Amount below Approved Estimates
1976-77	448	339	109
1977-78	512	358	154
1978-79	328	255	73
Net Savings over Three Years			336

While achieving these savings, the Government has been able to maintain existing services and respond to new priorities. This fact is demonstrated by the shifting composition of the Province's capital investments outlined in the following table. It shows that investments related to economic development and improving the natural and urban environment have increased whilst overall capital spending has been held in check. The table shows that reprivatization of financial activities through sale of assets such as resource holdings and mortgages has provided substantial flexibility to redeploy resources for other important priorities.

Changing Investment Priorities — Table 4

($ million)

	1976-77	1977-78	Interim 1978-79	Estimated 1979-80
Social Investments				
• educational	113	111	95	92
• health and welfare	155	175	154	150
• recreational and cultural	36	66	67	51
	304	352	316	293
Economic and Environmental				
• transportation	499	651	607	667
• environmental	280	263	285	293
• commercial loans	30	42	37	37
• other	13	15	10	13
• employment development	—	—	—	200
	822	971	939	1,210
Other				
• financial assets	238	119	35	4
• land	62	52	58	48
• miscellaneous	54	42	28	36
	354	213	121	88
Total	1,480	1,536	1,376	1,591

Controlling Manpower Costs

The public sector is the largest employer in Ontario. Directly or indirectly about 548,000 people are employed in the provincial public sector. In addition, the federal government employs some 221,500 persons. (See Table 5.) The former figure, which includes employees in the health, educational and municipal sectors as well as Ontario Hydro, accounts for 13 per cent of the Ontario labour force. In 1978-79, the Province spent \$1.4 billion on direct payroll costs and some 70 per cent of Provincial transfer payments end up as salaries and wages.

Public Sector Employment in Ontario, 1978 — Table 5

	Number	Per Cent of Total
Federal government	221,500	28.8
Province	83,300	10.8
Municipalities	124,000	16.1
School Boards	138,600	18.0
Ontario Hydro	27,900	3.6
Hospitals	110,800	14.4
Other	63,400	8.3
Total	769,500	100.0

Source: Statistics Canada, Civil Service Commission and Ontario Treasury.

Any successful effort to contain government spending must focus on the size of the public service and its wage bill. In addition, the quality and morale of the public service are important to achieving more efficient and cheerful delivery of services to the Ontario public. To accomplish these objectives the Government has implemented a three-point program.

First, a government-wide manpower control system was introduced in April 1977.[6] Prior to this, a complement control system was used which focused only on the number of regular staff. The new system is based on total payroll of the entire public service. This system puts emphasis on rigid cost control, but at the same time allows managers more flexibility to meet staff requirements as long as they stay within the spending ceilings.

Second, the Government continues to reduce the size of the Provincial civil service. The following table shows that, since the restraint program began in 1975, the size of the civil service has been reduced by 3,786 positions, a reduction of over 4 per cent.

Third, the Province is providing leadership to the economy as a whole by maintaining wage and salary increases at a fair but non-

[6] See Hon. J. A. C. Auld, *Manpower Control in the Ontario Government* (Toronto: The Management Board of Cabinet, 1977).

Ontario Public Service Reduced in Size — Table 6

	March 1 1975	Dec. 31 1978	Reduction Number	Reduction %
Total Staff*	87,109	83,323	3,786	4.3
% of Ontario Labour Force	2.3	2.0		

Source: Civil Service Commission, and Statistics Canada, *Labour Force Annual Averages, 1975-1978.*

*Excludes staff of Lieutenant Governor, Office of the Assembly, Ombudsman and the Provincial Auditor. Includes all other classified and unclassified staff and crown em-employees.

inflationary level. In the last four years, Ontario civil service pay increases have not led those in the private sector.

Speeding Up Decision-Making and Cutting Red Tape

The management challenge in the public sector involves not only internal cost control, but also unburdening citizens and business from the weight of government interference in their lives. The existing morass of government regulation impedes economic efficiency, slows down decision-making and chokes small businesses with needless red tape.

In February 1978, the Ontario Government announced it would "examine the statutes, regulations and related policies that currently govern business practices and procedures, and will modify or eliminate outmoded and restrictive requirements".[7] Improvement in the services offered to the general public was also undertaken as part of this exercise. Cabinet instructed all ministries to review internal administrative procedures and regulatory processes and to suggest improvements that would eliminate bottlenecks caused by excessive government regulation. The main thrust of this review is directed towards:

- examining the effectiveness of current legislation;
- reviewing the economic impact of all new regulations;
- encouraging more public involvement in the setting of regulations and improving public access to government;
- reducing the demands on businesses and the public for paperwork;
- better co-ordinating of government's role in land use and development; and,
- reducing the need for licensing of individuals and businesses.

The process of deregulation is challenging. Thousands of government regulations are administered by a multitude of ministries, boards, agencies and commissions. All regulations, procedures, practices, re-

[7]The Hon. Pauline M. McGibbon, Lieutenant Governor of the Province of Ontario, *Speech from the Throne*, February 21, 1978.

quirements and regulatory bodies were originally put in place for what were thought to be good reasons. Most regulations are perceived to benefit at least some group in society. Nevertheless, after one year the Government has been able to take some significant steps towards deregulation.

Progress Towards Deregulation and Improved Public Services

Ministry of Revenue

- repeal of The Land Speculation Tax Act;
- improvements in services to the public through better taxation information and assistance, e.g. distribution of new vendor information kit;
- an advanced ruling service which allows corporations greater certainty in corporate planning;
- elimination of the requirement for retail sales tax exemption applications for admission fees to events sponsored by charitable, non-profit and amateur athletic organizations.

Ministry of Consumer and Commercial Relations

- elimination of duplication in inspection services in Theatres Branch and L.L.B.O.;
- increased self-regulation by professional groups, e.g. insurance agents (scheduled for 1979);
- consolidation of The Elevators and Lifts Act and The Construction Hoists Act (scheduled for 1979).

Ministry of Natural Resources

- streamlining of law enforcement in Provincial Parks (scheduled for 1979).

Ministry of Transportation and Communications

- expanded list of commodities exempted from The Public Commercial Vehicles Act, reducing restrictions in the movement of goods (scheduled for 1979).

Ministry of the Environment

- simplification and streamlining of waste management regulations (scheduled for 1979).

Ministry of Industry and Tourism

- streamlining of permit and licensing procedures under The Tourism Act (scheduled for 1979);
- one-stop service for business assistance (scheduled for 1979).

Ministry of Treasury and Economics

- improving the payment of accounts by the Government (scheduled for 1979);
- simplification of accounting and auditing practices (scheduled for 1979).

Eliminating Regulatory Bodies

The Agencies Review Committee recommended the amalgamation or elimination of 46 boards, agencies and commissions.[8] Twelve licensing boards have been consolidated by the Ministry of Agriculture and Food into the Agricultural Licensing and Registration Review Board.[9] In addition, the following agencies have been eliminated:

- Liquor Advisory Council
- Liquor Advisory Committee
- Cemeteries Advisory Board
- Professional Credentials Committee for Public Health Nursing
- Minister's Advisory Board on Geriatric Studies (Community and Social Services)
- Minister's Advisory Committee on Vocational Rehabilitation (Community and Social Services)
- Artificial Insemination of Livestock Advisory Committee
- Dairy Herd Improvement Advisory Committee
- Ontario Food Council
- Pregnant Mare Urine Licence Review Board
- Advisory Council on the Ontario Teacher Education College
- Advisory Committee on Forensic Sciences
- Student Housing Corporation

Efficiency Incentives

The Government has introduced a program to provide incentives to ministries to improve their management and increase productivity. The program consists of two major elements:

- establishment of a productivity improvement capital fund to finance projects that require an initial one-time investment to generate subsequent annual cost reductions;
- development of a sharing formula that rewards ministries by permitting them to retain a portion of the net savings derived from cost-cutting and certain revenue-raising measures.

This program will motivate program managers to search for more efficient methods of service delivery. Ministries will share directly in the benefits through increased financial flexibility, while Ontario as a whole will benefit from the ensuing reductions in cash requirements.

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[8]The Hon. D. J. Wiseman, "Report of the Agencies Review Committee to the Management Board of Cabinet", November 29, 1978.

[9]The new Board encompasses the following Licence Review Boards: Agricultural Tile Drainage, Animals for Research, Artificial Insemination of Livestock, Dead Animal Disposal, Livestock Community Sales, Livestock and Livestock Products, Meat Inspection, Plant Diseases, Produce, Provincial Auctioneers, Riding Horse Establishment and the Produce Arbitration Board.

Reporting by Crown Agencies and Commissions

As indicated in the 1978 Budget, efforts to improve expenditure control in the public sector have been extended to include crown agencies. Twelve of the largest agencies now report to the Ministry of Treasury and Economics on a quarterly basis. These agencies generate annual gross revenues of $3.9 billion. Three of these agencies and commissions—Ontario Hydro, Liquor Control Board of Ontario and Workmen's Compensation Board—account for 88 per cent of the revenues. These agencies and commissions will be encouraged during the course of this fiscal year to begin publishing quarterly reports that will summarize their activities and improve the flow of information from the Ontario public sector.

Conclusion

In conclusion, the Province is committed to the philosophy of reducing the growth of the public sector. This paper has reviewed the progress made so far in improving Government efficiency. Central to this approach is a reduction in cash requirements that will provide increased financial and fiscal flexibility.

Financial Tables

Statement of Provincial Net Cash Requirements and Related Financing

Table C1

($ million)

	1976-77	1977-78	Interim 1978-79	Estimated 1979-80
Budgetary Transactions				
Revenue	10,514	11,099	12,288	13,446
Expenditure	11,743	12,920	13,985	15,105
Budgetary Deficit	1,229	1,821	1,697	1,659
Non-Budgetary Transactions				
Receipts and Credits	634	683	857	959
Disbursements and Charges	724	624	497	453
Non-Budgetary Deficit	90	(59)	(360)	(506)
NET CASH REQUIREMENTS	1,319	1,762	1,337	1,153
FINANCING				
Non-Public Borrowing				
Proceeds of Loans	1,367	1,586	1,566	1,580
Retirements of Loans	45	14	22	26
Net Non-Public Borrowing	1,322	1,572	1,544	1,554
Public Borrowing				
Proceeds of Loans	—	—	195	—
Retirements of Loans	230	66	90	259
Net Public Borrowing	(230)	(66)	105	(259)
Increase in Liquid Reserves	(227)	(256)	312	142
TOTAL FINANCING	**1,319**	**1,762**	**1,337**	**1,153**

Budgetary Revenue — Table C2
($ million)

	1976-77	1977-78	Interim 1978-79	Estimated 1979-80
Taxation				
Personal Income Tax[1]	1,782	2,447	2,735	2,971
Revenue Guarantee	496	210	44	5
Corporation Taxes				
Income Tax	791	734	938	995
Capital Tax	143	195	242	249
Insurance Premiums Tax	68	85	85	91
Mining Profits Tax	42	23	41	50
Retail Sales Tax	1,775	1,926	1,710	2,295
Gasoline Tax	508	523	540	607
Motor Vehicle Fuel Tax	79	85	94	122
Reciprocal Taxation	—	22	40	40
Tobacco Tax	157	206	260	292
Land Transfer Tax	52	62	67	92
Land Speculation Tax[2]	6	7	5	—
Race Tracks Tax	41	43	47	49
Succession Duty[3]	62	73	62	35
Income Tax—Public Utilities	5	8	15	6
Other Taxation	(1)	3	3	3
	6,006	6,652	6,928	7,902
Other Revenue				
Premiums—OHIP	799	830	975	1,035
LCBO Profits	302	327	360	412
Vehicle Registration Fees	223	267	298	310
Other Fees and Licences	202	219	250	264
Fines and Penalties	51	59	63	69
Ontario Lottery Profits	76	71	46	53
Royalties	42	49	55	58
Sales and Rentals	39	41	42	44
Utility Service Charges	36	48	47	48
Miscellaneous	57	57	61	101[4]
	1,827	1,968	2,197	2,394
Payments from the Federal Government (see Table C6)	2,236	2,040	2,736	2,730
Interest on Investments	445	439	427	420
TOTAL BUDGETARY REVENUE	**10,514**	**11,099**	**12,288**	**13,446**

[1]Net of tax credits of $418 million, $428 million, $434 million and $455 million for the 1976-77, 1977-78, 1978-79 and 1979-80 fiscal years.
[2]Repealed in November 1978.
[3]Repealed April 10, 1979.
[4]Includes $37 million profit from the sale of Syncrude Investment.

Budgetary Expenditure by Policy Field and Ministerial Responsibility

Table C3

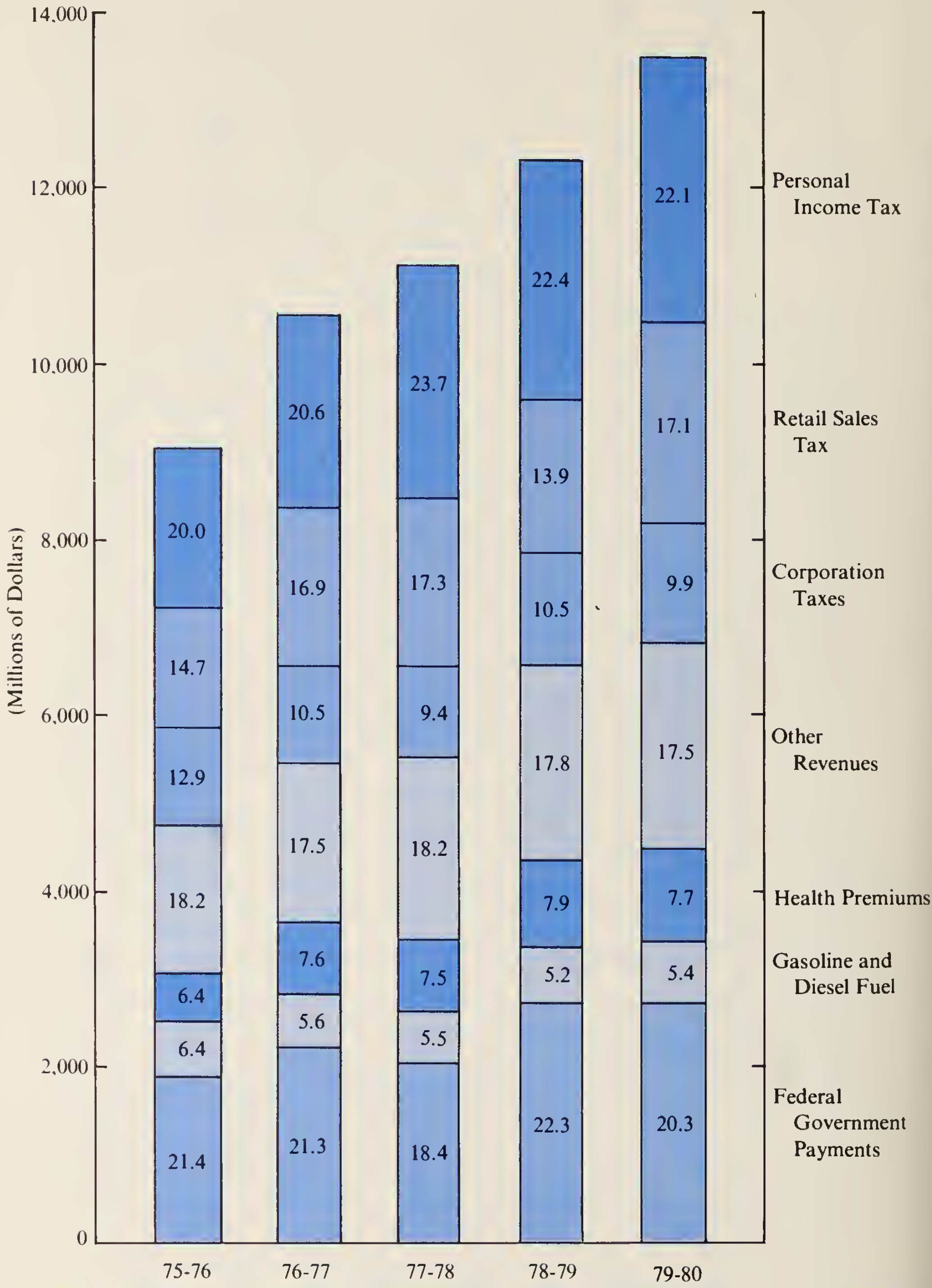
($ million)

	1976-77	1977-78	Interim 1978-79	Estimated 1979-80
Social Development Policy				
Health	3,349	3,631	3,970	4,183
Education	1,986	2,343	2,396	2,515
Colleges and Universities	1,158	1,257	1,373	1,430
Community and Social Services	1,034	1,137	1,234	1,318
Culture and Recreation	144	192	207	189
	7,671	8,560	9,180	9,635
Resources Development Policy				
Transportation and Communications	917	1,035	1,067	1,134
Natural Resources	234	243	247	261
Housing	157	172	181	227
Agriculture and Food	165	170	176	178
Environment	99	114	126	130
Industry and Tourism	56	53	61	65
Labour and Manpower	23	29	35	40
Energy	4	7	12	15
	1,655	1,823	1,905	2,050
Justice Policy				
Solicitor General	144	153	170	175
Attorney General	116	129	141	149
Correctional Services	107	118	130	131
Consumer and Commercial Relations	61	63	62	64
	428	463	503	519
Other Ministries				
Intergovernmental Affairs	461	390	509	547
Government Services	296	271	258	272
Revenue	198	195	194	195
Northern Affairs	87	113	130	141
Treasury and Economics	19	20	26	23
Employment Development Fund[1]	—	—	—	200
Assembly	17	30	22	19
Management Board	8	8	10	11
Ombudsman	3	4	4	4
Other	10	10	11	13
	1,099	1,041	1,164	1,425
Public Debt — Interest	890	1,033	1,233	1,388
Contingency Fund	—	—	—	88
TOTAL BUDGETARY EXPENDITURE	**11,743**	**12,920**	**13,985**	**15,105**

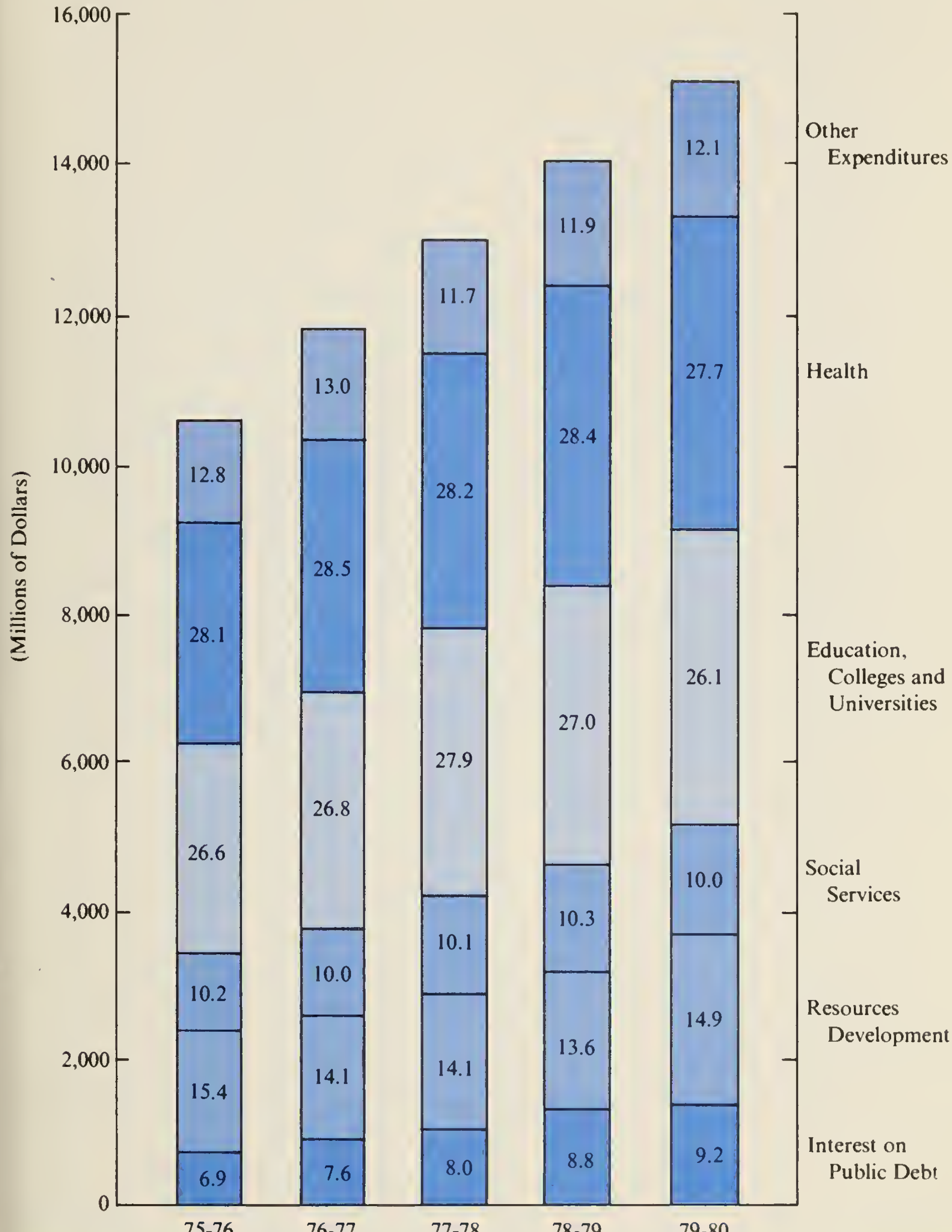
[1]Supplementary Estimates to be tabled in the Legislature.

Major Revenue Sources, 1975-76 to 1979-80 — Chart C1

(per cent of total)



Major Expenditure Functions, 1975-76 to 1979-80 — Chart C2
(per cent of total)



Details of Non-Budgetary Transactions — Table C4

($ million)

RECEIPTS	1976-77	1977-78	Interim 1978-79	Estimated 1979-80
Repayments of Loans, Advances and Investments				
Ontario Energy Corporation	—	—	—	105
Ontario Mortgage Corporation	28	21	143	100
Education Capital Aid Corporation	56	62	67	72
Investment in Environmental Protection	32	35	49	35
Universities Capital Aid Corporation	24	26	28	30
Nuclear Power Generating Station	20	22	21	25
Ontario Development Corporations	21	21	19	18
Loans to Public Hospitals	16	18	18	18
Ontario Housing Corporations	10	12	17	13
Tile Drainage Debentures	6	8	9	10
Municipal Improvement Corporation	4	5	5	4
Ontario Junior Farmers	3	4	4	4
Municipal Works Assistance	5	5	4	3
Ontario Land Corporation	—	10	—	—
Other	10	13	11	7
TOTAL RECEIPTS	235	262	395	444
DISBURSEMENTS				
Loans, Advances and Investments				
Investment in Environmental Protection	146	135	147	153
Education Capital Aid Corporation	77	81	71	69
Ontario Development Corporations	30	42	37	37
Ontario Land Corporation	—	4	20	19
Tile Drainage Debentures	16	19	18	18
Ontario Housing Corporations	36	30	26	10
Regional and Municipal Public Works	27	24	20	9
Municipal Improvement Corporation	16	3	1	8
Ontario Mortgage Corporation	180	86	15	4
Ontario Energy Corporation	—	—	20	—
Loans to Public Hospitals	35	30	—	—
Universities Capital Aid Corporation	33	34	—	—
Crop Insurance Commission	2	8	—	—
Other	9	3	2	2
TOTAL DISBURSEMENTS	**607**	**499**	**377**	**329**
NET INCREASE IN LENDING ACTIVITY	**372**	**237**	**(18)**	**(115)**

Details of Non-Budgetary Transactions — Table C5

($ million)

CREDITS	1976-77	1977-78	Interim 1978-79	Estimated 1979-80
Payments into Special Purpose Accounts				
Public Service Superannuation Fund	239	252	301	330
Superannuation Adjustment Fund				
Teachers' Superannuation Plan	44	53	61	67
Public Service Superannuation Plan	18	34	32	36
Province of Ontario Savings Deposits (net)	52	6	24	28
Motor Vehicle Accident Claims Fund	17	18	19	16
The Provincial Lottery	10	29	16	20
Other	19	29	9	18
TOTAL CREDITS	**399**	**421**	**462**	**515**
CHARGES				
Payments from Special Purpose Accounts				
Public Service Superannuation Fund	52	57	72	80
Motor Vehicle Accident Claims Fund	17	18	18	21
The Provincial Lottery	2	8	11	11
Ontario Energy Corporation	39	33	—	—
Other	7	9	19	12
TOTAL CHARGES	**117**	**125**	**120**	**124**
NET INCREASE IN SPECIAL PURPOSE ACCOUNTS	**282**	**296**	**342**	**391**

Federal Government Payments to Ontario — Table C6

($ million)

	1976-77	1977-78	Interim 1978-79	Estimated 1979-80
Established Programs Financing[1]	—	1,233	1,606	1,834
Hospital Insurance	1,027	29	29	30
Medical Care	360	8	—	—
Post-Secondary Education Payments	190	—	—	—
Extended Health Care Services[2]	—	167	188	210
Canada Assistance Plan	472	416	408	455
Adult Occupational Training	80	76	97	100
Bilingualism Development	35	31	44	26
Economic Development	14	21	13	15
Vocational Rehabilitation	10	11	12	13
Economic Stimulation[3]	—	—	288	—
Other Federal Payments	48	48	51	47
TOTAL PAYMENTS	**2,236**	**2,040**	**2,736**	**2,730**
Annual Per Cent Increase	15.9	(8.8)	34.1	(0.2)
Federal Payments as a Per Cent of Ontario Budgetary Revenue	21.3	18.4	22.3	20.3

[1]Replaces former transfers for Hospital Insurance, Medical Care, Post-Secondary Education, and Revenue Guarantee effective April 1, 1977.
[2]Replaces a portion of shared-costs previously paid under the Canada Assistance Plan.
[3]Federal share of the joint Federal-Provincial economic stimulus program which reduced the rate of the retail sales tax from 7 per cent to 4 per cent for the period April 11 to October 7, 1978.

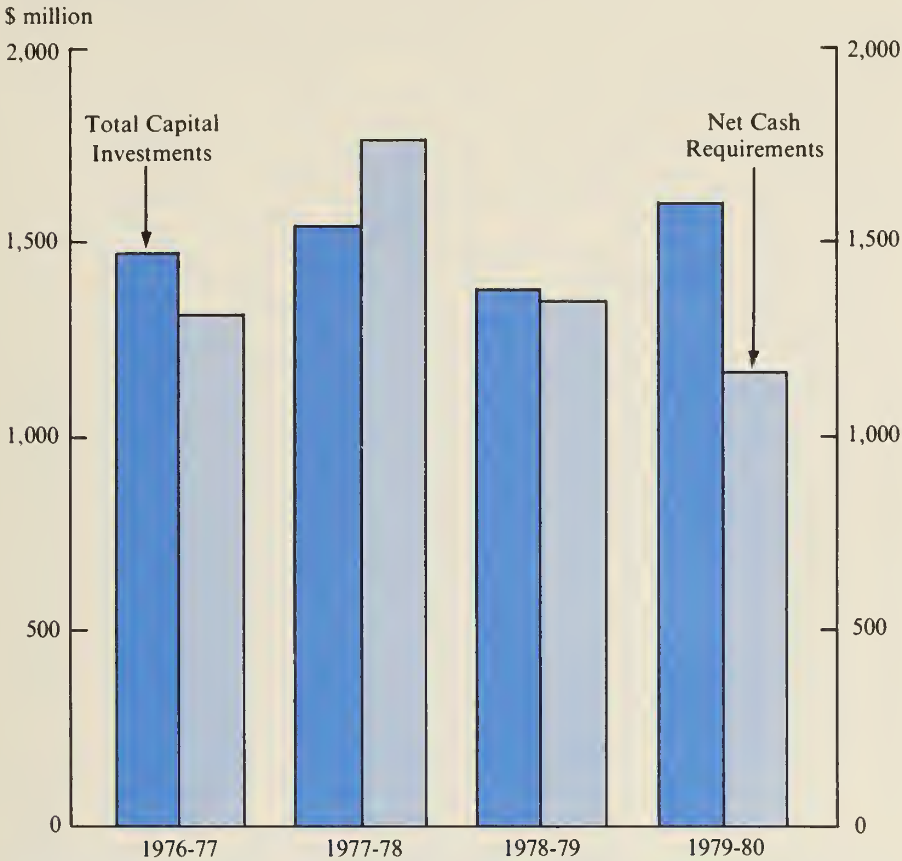
Ontario's Capital Investments — Table C7

($ million)

	1976-77	1977-78	Interim 1978-79	Estimated 1979-80
Physical Assets (roads, highways, bridges, water and sewer facilities, drainage and flood control, etc.)	695	814	787	868
Buildings (schools, universities, colleges, hospitals, housing projects)	382	414	365	350
Land (right-of-way and other)	91	84	86	72
Transportation Vehicles (buses, subway and street cars, etc.)	44	63	66	60
Financial Assets (mortgages, commercial loans, etc.)	268	161	72	41
Employment Development Fund	—	—	—	200
TOTAL INVESTMENTS	**1,480**	**1,536**	**1,376**	**1,591**

Total Capital Investments and Net Cash Requirements, 1976-77 to 1979-80

Chart C3



Financing

Table C8

($ million)

	1976-77	1977-78	Interim 1978-79	Estimated 1979-80
Non-Public Borrowing				
Canada Pension Plan	813	851	916	960
Teachers' Superannuation Fund	334	488	489	550
Municipal Employees' Retirement Fund	180	190	100	—
CMHC Pollution Control Loans	40	57	61	70
Retirements	(45)	(14)	(22)	(26)
Net Non-Public Borrowing	1,322	1,572	1,544	1,554
Public Borrowing				
Treasury Bills (net)	(195)	—	195	(195)
Debenture Issues	—	—	—	—
Debenture Retirements	(35)	(66)	(90)	(64)
Net Public Borrowing	(230)	(66)	105	(259)
Increase in Liquid Reserves	**(227)**	**(256)**	**312**	**142**
TOTAL FINANCING	**1,319**	**1,762**	**1,337**	**1,153**

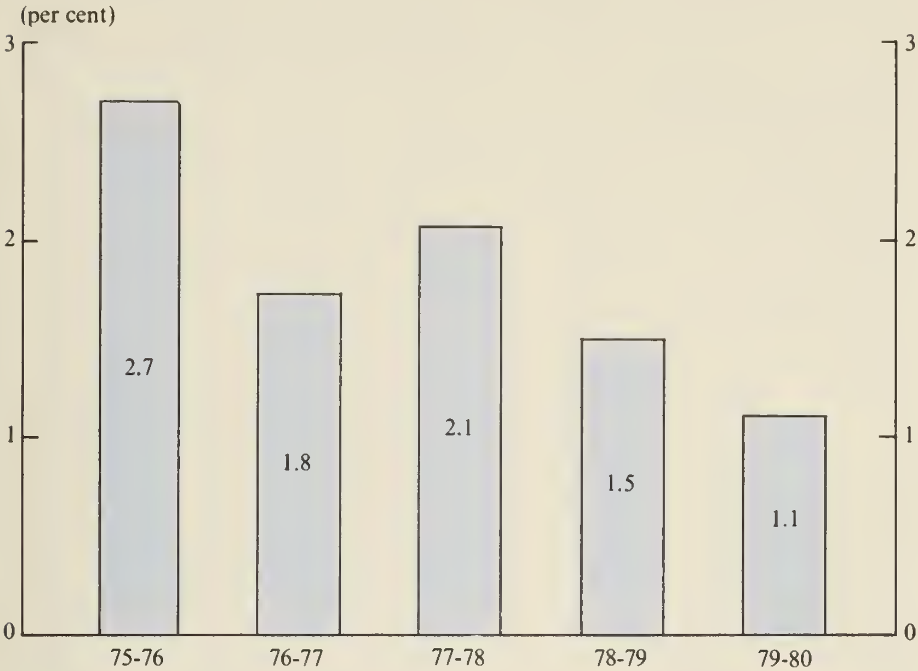
Reconciliation with Public Accounts of Provincial Net Cash Requirements and Financing

Table C8(a)

($ million)

	1976-77	1977-78	Interim 1978-79	Estimated 1979-80
Net Cash Requirements for Provincial Purposes	1,319	1,762	1,337	1,153
Net Cash Requirements for Ontario Hydro Transactions	269	392	667	—
Total Cash Requirements (per Public Accounts)	**1,588**	**2,154**	**2,004**	—
Financing for Provincial Purposes	1,319	1,762	1,337	1,153
Net U.S. Borrowing on behalf of Ontario Hydro	269	392	667	—
Total Financing (per Public Accounts)	**1,588**	**2,154**	**2,004**	—

Net Cash Requirements as a Per Cent of Gross Provincial Product, 1975-76 to 1979-80 — Chart C4



Ontario Payments to Local Governments and Agencies

Table C9

($ million)

	1976-77	1977-78	Interim 1978-79	Estimated 1979-80
Conditional Payments				
General Legislative Grants	1,693	1,870	1,969	2,054
Transportation	443	490	503	537
Social Assistance	162	183	212	228
Agriculture	56	57	61	61
Housing	42	37	34	45
Northern Affairs	15	22	26	30
Environment	18	29	35	29
Culture and Recreation	15	23	21	20
Health	14	13	18	17
Other	9	7	6	6
	2,467	2,731	2,885	3,027
Unconditional Payments				
General Support	97	109	134	149
Resource Equalization	88	98	109	114
Per Capita—Policing	109	56	93	94
Per Capita—General	98	42	76	77
Payments-in-lieu of Taxes	40	45	47	50
Northern Ontario Support	22	30	37	41
Other	25	18	15	18
	479	398	511	543
Payments to Local Agencies				
Children's Aid Societies	74	78	89	101
Homes for the Aged	82	85	89	93
Health Agencies	41	44	44	53
Conservation Authorities	26	30	34	32
Library Boards	20	22	22	23
	243	259	278	302
TOTAL TRANSFER PAYMENTS	**3,189**	**3,388**	**3,674**	**3,872**
Growth in Total Transfer Payments (%)	8.2	6.2	8.4	5.4

Public Service Strength in Ontario by Category, December 31, 1978[1] — Table C10

Ministry	Classified Staff	Unclassified Staff	Other Crown Employees	Total
Premier	48	18	—	66
Cabinet Office	33	3	—	36
Management Board	75	12	—	87
Civil Service Commission	178	65	—	243
Government Services	2,896	211	—	3,107
Revenue	3,863	40	—	3,903
Treasury and Economics	433	60	1	494
Intergovernmental Affairs	200	47	—	247
Northern Affairs	152	46	—	198
Justice Policy	15	1	—	16
Attorney General	2,977	1,642	369	4,988
Consumer and Commercial Relations	1,829	309	75	2,213
Correctional Services	4,495	862	56	5,413
Solicitor General	1,471	493	2	1,966
Resources Development Policy	18	72	1	91
Agriculture and Food	1,554	377	—	1,931
Energy	84	9	—	93
Environment	1,444	141	—	1,585
Housing	1,042	93	1,098	2,233
Industry and Tourism	556	149	—	705
Ontario Development Corporations	187	4	1	192
Labour and Manpower	1,146	59	12	1,217
Natural Resources	4,354	2,139	—	6,493
Transportation and Communications	10,302	2,006	132	12,440
Social Development Policy	39	21	—	60
Colleges and Universities	633	80	2	715
Community and Social Services	9,998	1,589	20	11,607
Culture and Recreation	888	327	—	1,215
Education	1,536	427	589	2,552
Health	11,434	1,023	—	12,457
O.P.P. Uniformed Staff and Security Guards	4,107	—	—	4,107
Environment Plant Operators	563	90	—	653
Total	68,550	12,415	2,358	83,323

[1]Excludes staff of the Lieutenant Governor, Office of the Assembly, Ombudsman and Provincial Auditor.

Wintario Lottery Proceeds
($ million)

Table C11

	1977-78	Interim 1978-79	Estimated 1979-80
Balance at beginning of year	78	85	59
Wintario Lottery Proceeds	71	46	53
	149	131	112
Less—Expenditure on approved projects and overhead costs	64	72	51
Balance at end of year	85	59	61

Provincial Lottery Proceeds
($ million)

Table C12

	1977-78	Interim 1978-79	Estimated 1979-80
Balance at beginning of year	8	29	34
Provincial Lottery Proceeds	29	16	20
	37	45	54
Less—Approved spending for health and environmental research	8	11	11
Balance at end of year	29	34	43

Ten-Year Review
($ million)

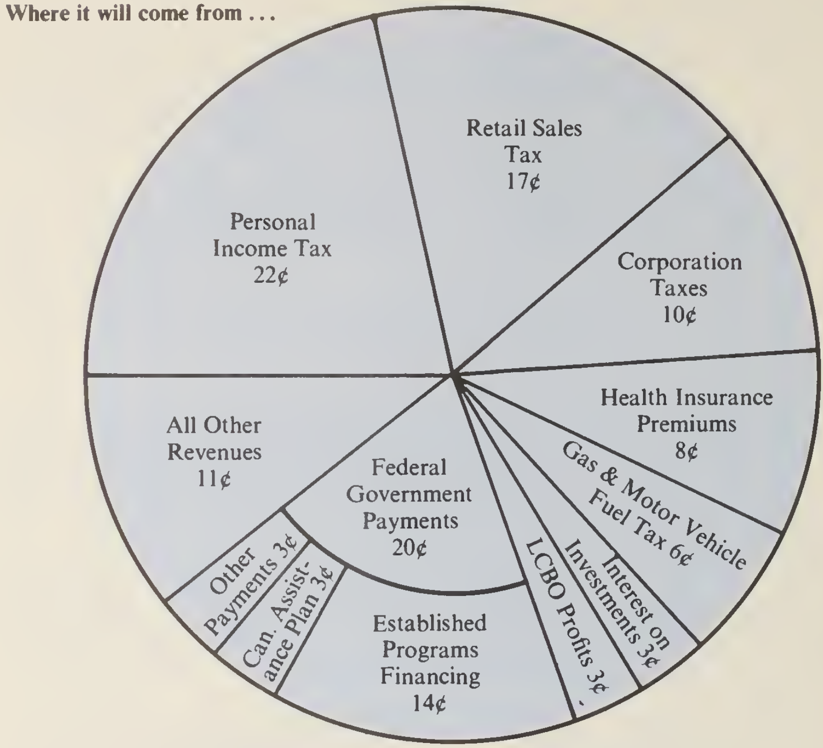
Table C13

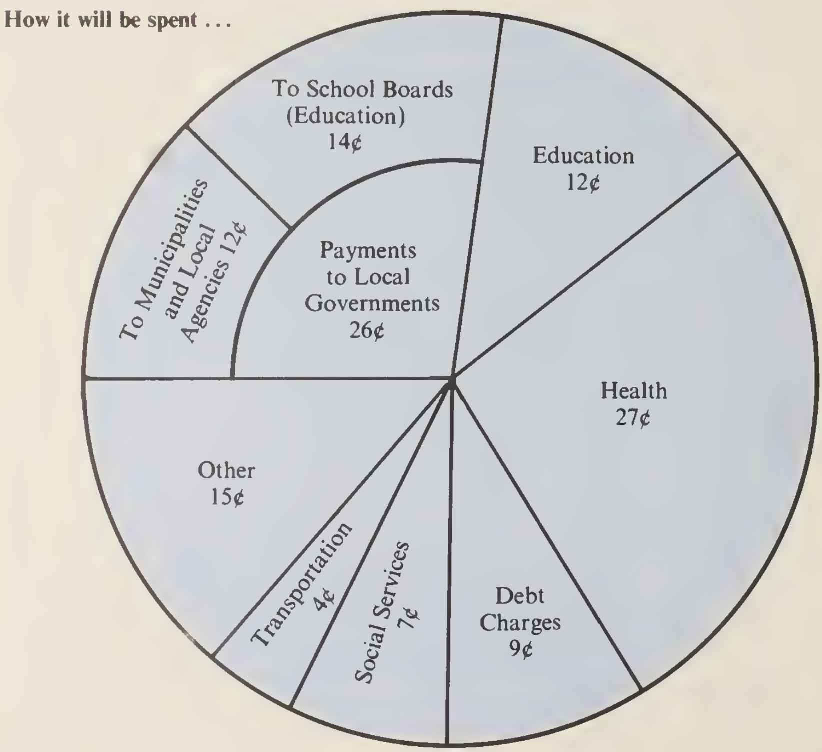
	1970-71	1971-72	1972-73	1973-74	1974-75	1975-76	1976-77	1977-78	Interim 1978-79	Estimated 1979-80
Financial Transactions										
Revenue	5,226	5,615	6,294	7,177	8,855	9,520	11,148	11,782	13,145	14,405
Expenditure	5,795	6,636	7,038	7,885	9,832	11,319	12,467	13,544	14,482	15,558
Net Cash Requirements	569	1,021	744	708	977	1,799	1,319	1,762	1,337	1,153
Financial Position										
Funded Debt (excluding Ontario Hydro)	4,237	5,270	6,300	7,008	7,844	9,818	10,895	12,364	14,039	15,342
Funded Debt per Capita (dollars)	551	677	798	873	962	1,190	1,307	1,467	1,653	1,791
Funded Debt as a Per Cent of Gross Provincial Product	12.0	13.7	14.5	13.9	13.1	15.0	14.7	15.0	15.5	15.3
U.S. Borrowing on behalf of Ontario Hydro	956	1,005	1,159	1,382	1,710	2,240	2,509	2,901	3,568	n.a.
Contingent Liabilities (mainly Ontario Hydro)	2,413	2,781	3,030	3,330	3,843	5,027	5,735	6,152	n.a.	n.a.

n.a.—not available

THE BUDGET DOLLAR

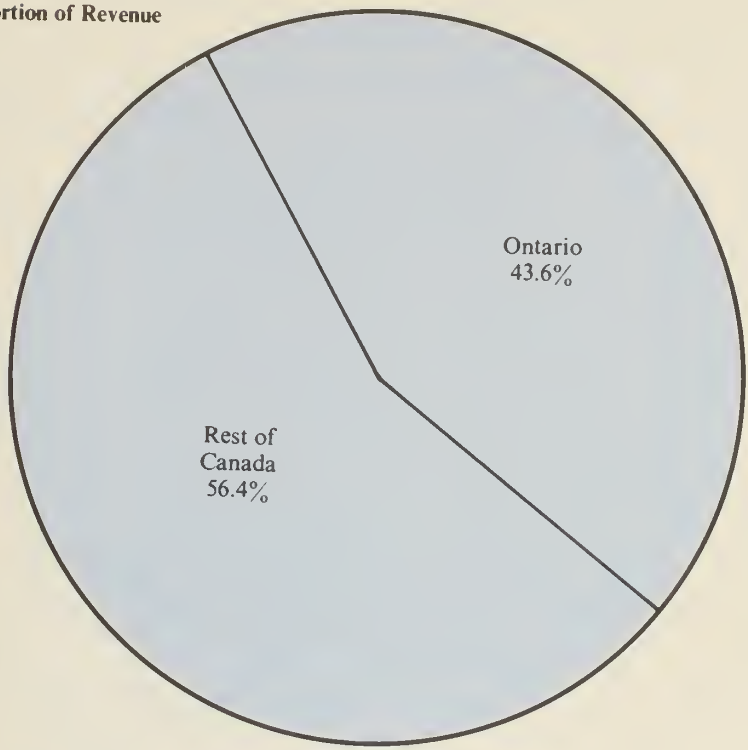
Fiscal Year 1979-80 Estimates



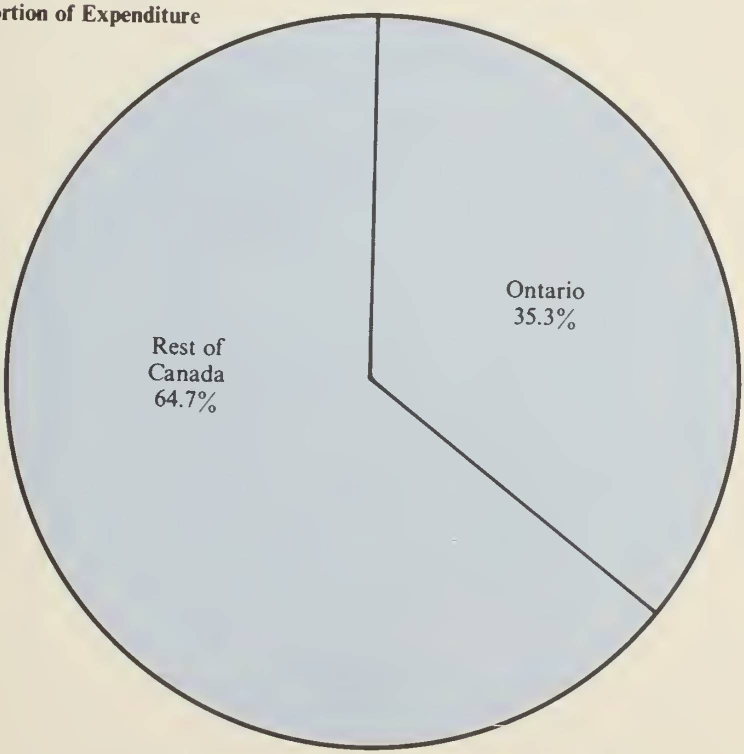


THE FEDERAL TAX DOLLAR IN ONTARIO AND THE REST OF CANADA 1978

Proportion of Revenue



Proportion of Expenditure



Budget Paper D

Financing OHIP in Ontario: A Discussion Paper

Table of Contents

Financing OHIP in Ontario: A Discussion Paper

Introduction

The financing of the Ontario Health Insurance Plan (OHIP) continues to be a matter of public interest and discussion. The Select Committee on Health Care Financing and Costs conducted a thoroughgoing review of this issue and submitted its report in October, 1978. This paper is presented to further public understanding of and discussion on this important issue. It outlines current issues related to the future financing of OHIP and discusses alternative methods to reduce the financing burden on lower income groups. The views of Members of the Legislature and of the interested public will assist the Government in developing longer term plans for the financing of OHIP in Ontario.

The first section of this paper outlines the background to the existing OHIP system and some of the financing and cost problems which it has presented. Section II describes in detail the current OHIP premium structure. Section III reviews alternatives to the present system. The last section outlines a proposal to relate OHIP premiums to health care costs and discusses alternative methods to provide relief from premiums to lower income people in Ontario.

I Background

Over 20 years ago, on January 1, 1959, Ontario, in partnership with the federal government, introduced a hospital insurance plan. This was followed six years later by a medical insurance plan that covered the 25 per cent of Ontarians not insured by private plans. Ten years ago, in 1969, medical insurance became a universal public plan cost-shared with the federal government. In 1972, the separate medical and hospital insurance systems were integrated into one system, the Ontario Health Insurance Plan.

This system has made available a very high standard of health care service to all citizens of Ontario. Also, this service is completely portable within Canada. It is understandable that a program which commands such a large share of public resources and that touches every citizen in the province would raise issues requiring resolution. In brief, these concerns relate to:

- the escalation of the costs of OHIP services;
- the nature of federal-provincial cost-sharing of health services; and,
- the low revenue growth of the premium system and the ability of various groups in society to pay premiums.

Controlling Costs

The burgeoning cost escalation which the system experienced, particularly in the mid 1970s, has been controlled through better health care management and the Government's restraint program.[1] To illustrate, insured services costs have increased at an average annual rate of 8.9 per cent in the past two fiscal years, compared to 19.1 per cent during the period 1972-73 to 1976-77. This reduction in cost growth has been achieved while maintaining high quality care.

Federal-Provincial Financing Arrangements

The shared-cost programs had their origin in the federal government's initiatives, beginning in the late 1950s, to provide a national standard of health care services. It accomplished this by offering to finance about one-half of the cost of services on condition that the provinces entered a national scheme with standards and eligible services determined by Ottawa. This led to the hospital insurance and medicare agreements.

There were a number of problems with those financing arrangements. The federal government was forced to pay on average 50 per cent of whatever provinces chose to spend and the provinces had limited incentives to cut costs. This open-ended arrangement contributed to fast-paced cost escalation. In addition, the system distorted provincial priorities and involved too much bureaucratic red tape.

In 1976, the two levels of government were able to substantially resolve these issues by agreeing to a new Established Programs Financing mechanism which covered both health and post-secondary education.[2] Under this new arrangement the old shared-cost programs were abandoned. They were replaced with the transfer from the federal government to the provinces of additional points of personal income tax plus a cash payment. These funds are not earmarked for either health or education, but rather form part of the general revenues of the Province. This landmark agreement resolved one of the major areas of concern in health care financing.

Bridging the Financing Gap

With the introduction of universal health care in 1969, Ontario's share of the cost was almost entirely financed by premium revenues. A financing problem arose because, in the absence of premium

[1]For an analysis of the nature of OHIP cost escalation, see the Hon. W. D. McKeough, "Financing Health Insurance in Ontario", *Ontario Budget 1976* (Toronto: Ministry of Treasury, Economics and Intergovernmental Affairs, 1976).

[2]For a review of federal-provincial financing of health care services and a description of the new Established Program Financing arrangements, see the Hon. W. D. McKeough, "Federal-Provincial Fiscal Reforms", *Ontario Budget 1977* (Toronto: Ministry of Treasury, Economics and Intergovernmental Affairs, 1977).

hikes, premium revenues grew by only about 2 per cent per year—in line with the growth of new subscribers. Costs, on the other hand, were escalating far more rapidly. For example, in 1974-75, a year in which premium rates did not increase, the Province received an additional $18 million from premiums. In the same year health costs increased by over $400 million. To fill the resulting financing gap required a fast-growing claim on the general revenues of the Province—from virtually zero in 1969-70 to over $700 million in 1975-76.[3]

To re-establish the contribution of premium revenues at a more realistic level of overall health costs, the Province moved in both 1976 and 1978 to increase premium levels. However, the proposed 1978 increase was not fully acceptable to the Legislature and was reduced by one-half by the Government. Subsequently, a Select Committee of the Legislature was established to examine the issue of health care financing. The committee studied the issue for three months but was unable to reach unanimous agreement on the best way to finance OHIP.[4]

The challenge remains— Ontario must settle on a method of financing health care that will generate adequate revenue growth without, in itself, encouraging the escalation of health delivery costs. Such a method must also be compatible with the broader economic priorities of the Province and, equally important, it must not impose undue financial hardship on any segment of society.

The next section of the paper reviews the existing OHIP premium system.

II The OHIP Premium System

Premiums have helped to finance health care in Ontario since 1959. In part, they were an extension of the charging concept used by private insurance carriers, but were adapted to the principle of universality. Every individual and every family pays the same rate regardless of risk considerations and, in contrast to private insurance, premiums cover less than the full cost of services. When the hospital insurance and medicare systems were amalgamated into OHIP in 1972, a consolidated premium system was established. There are two premium levels, one for individuals and the other for families. Family rates are double the single rate and do not vary with family size. Table 1 shows the premium levels in effect since the inception of OHIP in 1972.

Some subscribers pay their premiums directly to the Ministry of Health, but the majority of OHIP participants are members of groups for which the employer remits the premiums. As well, a large percentage of these employees have all or a part of their OHIP premiums paid by

[3]For an analysis of the nature and growth of this financing gap, see the Hon. W. D. McKeough, "Financing Health Insurance in Ontario", *op. cit.*

[4]*Report of the Select Committee on Health Care Financing and Costs* (Toronto: Legislature of Ontario, 1978).

OHIP Premium Rates — Table 1
(dollars)

Fiscal Year	Single	Family
1972-73	132	264
1973-74	132	264
1974-75	132	264
1975-76	132	264
1976-77	192*	384*
1977-78	192	384
1978-79	228**	456**

*Effective in respect of coverage August 1, 1976 and after.
**Effective in respect of coverage August 1, 1978 and after.

their employer as part of their compensation. The most recent estimates suggest that over 80 per cent of subscribers are in groups and close to 90 per cent of the premium liability of these employees is paid by their employers.

The increases in premium rates have been less than the growth in costs. This is illustrated in Table 2, which shows that on a per capita basis, despite two increases in premium rates, premiums have grown less than either incomes or insured costs.

Premiums Lag Growth in Health Spending and Incomes — Table 2
(dollars)

Fiscal Year	Per Capita Premium	Per Capita Insured Health Expenditure	Per Capita Personal Income
1972-73	66	205	4,443
1973-74	67	214	5,012
1974-75	68	261	5,806
1975-76	70	301	6,542
1976-77	96	343	7,412
1977-78	99	366	8,100
1978-79E	115	395	8,959
Growth over 6 years	74%	93%	102%

Source: Statistics Canada, Ontario Public Accounts and Ontario Treasury estimates.

Table 3 shows the contribution of premiums, federal transfers and general revenue to the financing of health care during the past seven years. Until 1975-76, the portion financed by premiums fell steadily to a low of 23 per cent of total costs. Premium increases in 1976 and 1978 helped to restore their relative contribution. In 1978-79, premium revenues represented 29 per cent of total insured health service costs. The table also shows the transition to the Established Programs Financing arrangements in 1977.

Sources of Revenue for Insured Health Services — Table 3

($ million)

Fiscal Year	Premiums +	Federal Transfers +	General Revenue =	Insured Services Costs	Premiums as % of Total
1972-73	520	746	340	1,606	32
1973-74	530	777	397	1,704	31
1974-75	548	927	644	2,119	26
1975-76	573	1,137	767	2,477	23
1976-77	799	1,387	649	2,835	28
1977-78	830	37*	2,198*	3,065	27
1978-79E	975	29*	2,336*	3,340	29

*New fiscal arrangements effective for 1977-78 replaced the cost-sharing agreements previously in effect. As a result, federal transfers are reflected in general revenue via personal income tax sharing and cash grants.

Note: Total financing is based on total expenditures on insured services—doctors, hospitals, home care, extended care health insurance and ambulance services. Insured services represent about 85% of Provincial spending on health.

Who Pays Premiums?

Determining the impact of OHIP premiums relative to subscriber income is a complex exercise. While the levy is clearly not related to income, employee compensation practices cloud the picture. Since the bulk of employee premiums are paid by employers, as part of fringe benefit packages, it would be argued by some that corporations are relieving many people from the burden of premiums. However, premiums paid by employers can be viewed as a form of compensation. Certainly the treatment of these payments as a taxable benefit reinforces this view.

This argument aside, under Ontario's premium assistance program low-income individuals and families may receive premium relief from the Ministry of Health. This assistance is related to taxable income. Table 4 illustrates the provisions of the current arrangements. As well,

OHIP Premium Relief for Low-Income People — Table 4

	Taxable Income	Level of Assistance
	($)	(%)
Single Person	0-2,500	100
	2,500-3,000	75
	3,000-3,500	50
	3,500-4,000	25
Family	0-3,000	100
	3,000-4,000	75
	4,000-4,500	50
	4,500-5,000	25

persons aged 65 and over, social assistance recipients, persons on veterans' pensions and persons with temporary financial difficulties, do not pay OHIP premiums. In 1978-79, it is estimated that premium assistance and exemptions cost the Government $340 million.

The Current System: Points at Issue

The existing premium system poses two problems. First, unless discretionary rate changes are made on a regular basis, premium revenue growth will not keep pace with cost growth. Second, the Province's low-income premium subsidy program is not delivering benefits to all those who are entitled to them. An analysis of taxation data indicates that only one-third of eligible recipients are actually claiming assistance from the Ministry of Health—200,000 out of a possible 600,000 people. This shortfall is particularly evident in the area of partial assistance. In 1978 only 2,000 people filed for partial assistance.

There are two avenues to remedy these difficulties with the current system. The first is to make adjustments within the current premium system. The second is to abandon premiums completely in favour of another financing mechanism. The next section examines the alternatives to premiums.

III Examining the Alternatives to Premiums

Any method chosen to finance OHIP insured services in Ontario should ideally be consistent with the following objectives.

- *Revenue Growth:* Revenues should keep pace with increases in health care spending in order to avoid continually growing claims on other revenue sources.
- *Neutrality:* The revenue system itself should not bias utilization of services one way or the other.
- *Equity:* No undue financing burden should be placed on any group in society.
- *Consistency with Economic and Fiscal Objectives:* A health revenue system must be compatible with other policies of the Province.
- *Administrative Simplicity:* The revenue system should be simple, efficient and minimize government red tape for both citizens and businesses.

A number of alternatives to the OHIP premium system can be quickly ruled out on the basis of these principles. For example, a system of user-fees designed to fully replace premium revenues would be administratively complex. It would violate the principle of universality in that many people would experience extreme financial difficulty in gaining needed access to health care. A gargantuan user-fee system raising some $1 billion in revenue is not a realistic option.

It has been suggested that lottery profits be used as a method for financing health care. However, these profits come nowhere close to the level required to finance health care needs. In 1978-79 lottery profits totalled some $62 million, or about 6 per cent of current premium revenue and less than 2 per cent of health care costs in that year. Furthermore, there is a finite limit to the demand for lottery tickets and the intense competition among governments makes profits from lotteries uncertain and unstable. This, and the voluntary nature of lottery revenues makes them an unsuitable source of financing for ongoing operating expenditures of any kind. LCBO profits and tobacco taxes are also commonly suggested as alternatives, but these would have to be tripled or quadrupled to meet OHIP financing needs. Clearly, this is also unrealistic.

Only personal income tax, corporation income tax, retail sales tax or some form of payroll tax have a base large enough to yield the funds required. They also possess growth potential, though for the 1980s, growth will not be what it was in the late 1960s and early 1970s.[5]

The 7 per cent rate of retail sales tax currently generates over $2 billion in annual revenue. In theory, if the tax rate increased by 50 per cent, it could generate an amount equal to current premium revenues. However, an Ontario sales tax rate of greater than 10 per cent would weaken consumer demand and cause severe economic problems. Also, such higher rates of retail sales tax would hurt people with low incomes.

The Ontario corporation income tax currently yields some $1 billion in revenue. If this tax were used to replace premium revenues the rate on Ontario corporations would have to double. Such a move would in one stroke wipe out Ontario's competitive climate for new investment and job growth and drive existing Ontario corporations into other jurisdictions.[6]

Another alternative that might be considered is a payroll tax, which would involve a percentage levy on all wages and salaries. There are two basic ways to implement such a tax. Either employees and employers could share the cost, as they do in the case of Unemployment Insurance and the Canada Pension Plan, or the employer could carry the entire burden of the tax. In both cases, self-employed people would pay a tax on their earned income and subscribers without employment income would pay nothing. To replace current premium revenue, a tax of almost 2 per cent of earned income would be required.[7]

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[5]See Budget Paper C for details of Ontario's major taxes.

[6]For analysis of Ontario's economic prospects and the challenges facing the province in the 1980s, see Budget Paper A.

[7]*An Overview of Financing Insured Health Services in Ontario*, a study submitted by Ontario Treasury to the Select Committee on Health Care Financing and Costs (Toronto: Ministry of Treasury, Economics and Intergovernmental Affairs, 1978), mimeo.

From the individual's point of view, the levying of the payroll tax on employers would be preferable. All costs for the individual with respect to OHIP would seem to "disappear" as the employer's contribution would not be treated as a taxable benefit. Also the problem of lower income people having to pay their premiums directly would be eliminated. However, there are a number of significant problems associated with this alternative.

First, it would drive up the cost of doing business for many employers in Ontario and contribute to inflation. Second, it would create a particularly heavy burden for labour-intensive industries, some of which are already having difficulty meeting costs. The impact would be almost crippling on industries such as tourism which have a high payroll and a low rate of return on investment. Third, the system would involve a complex administrative apparatus which would create particular problems and costs for small businesses. Fourth, since the levy would not be a taxable benefit, but would presumably be deductible for corporate income tax purposes, it would involve additional revenue loss through the corporation and personal income taxes. Finally, it would impact on the collective bargaining process, as firms try to bargain back some of the cost of the new tax.

Another drawback to the payroll tax is that such a measure would involve the creation of a new taxation structure in Ontario. Given the present economic circumstances and the need to encourage a healthy climate for investment and job creation, the prudence of such a course of action is questionable.

Splitting the rate between employers and employees reduces the problems for the corporate sector, but does not eliminate them. Although the overall burden on the corporate sector is reduced, there is still the problem of shifts in the tax burden within the corporate sector. There would also be a disturbing shift in the burden among individuals. As well, the administrative mechanism would become more complicated and the problem of substantial government revenue losses from the personal income tax would remain. The question of what happens to employer-paid OHIP premiums also complicates matters. A new payroll tax would again require a complete renegotiation of benefit packages. To many, it would be unrealistic to regress to a system where employees pay directly when employers pay such a large proportion of OHIP premiums now.

The remaining financing alternative for OHIP is the personal income tax. This was the option to which the Select Committee devoted a great deal of its attention. In fact, both the Liberal and New Democratic members of the Committee opted for refinancing via personal income tax although with some differences as to how it would be implemented.

The personal income tax option is appealing for a number of reasons. Even with indexing, the revenue growth of this tax substantially exceeds premium revenue growth. The necessary tax increase could be collected with virtually no increase in administrative costs and the existing premium administration system could be scrapped, thus saving Government overhead and relieving employers from administering the current system. The tax is progressive, and thus the entire system of health care would be financed primarily on the basis of ability-to-pay.

On the other hand some strong counter arguments can be advanced. With premiums currently raising some $1 billion, the required adjustment in the personal income tax would be 13.5 points. This 30 per cent rate increase in Ontario income tax would create a significant disturbance in the tax system which could reverberate throughout the economy, even if it is phased in over a period of time. With the province poised for a significant take-off in job creating investment, many would question the wisdom of eroding individual initiative and incentive, which could certainly result from such a large tax hike. There would also be the issue of employers returning the benefits of their current contributions to employees.

This major tax shift would involve a significant "loading up" on the personal income tax base. To some degree this would remove balance from the overall tax structure and would reduce the flexibility of the Government to use the income tax system to meet other policy objectives. Thus, while the personal income tax option appears to meet certain criteria, it has serious consequences for the stability and flexibility of the tax structure, and for the performance of the economy. It would not be consistent with the current economic and fiscal objectives of the Government.

Of course, it is also feasible to opt for some combination of increases in major taxes, but the defects outlined above still remain. An across-the-board increase in the Province's major taxes would damage Ontario's competitive position, reduce individual initiative and lower consumption. There would still be administrative complications, implications for collective bargaining and changes in government revenue. A shift in the tax base of $1 billion, no matter how expressed, is a major restructuring of the tax system and will be accompanied by sizeable disturbances.

IV Improving the Balance and Equity of Health Financing

The previous section examined alternatives to the existing premium system. None of the arguments in their favour is sufficiently compelling to substantiate the need to shift $1 billion within the Ontario tax base. Such major restructuring requires unquestionable justification which at this time does not appear to exist.

At the same time, OHIP premiums meet a number of the criteria outlined at the beginning of the previous section. The system:

- is neutral in that it does not excessively encourage or penalize utilization of health services;
- is consistent with the Province's economic and fiscal objectives designed to encourage a healthy rate of job creation and investment; and,
- functions through an established, smooth-running administrative system.

As well, many taxpayers like the idea of earmarked revenues as they can more readily see value for their health care dollar. In this way Ontarians may prefer to flow their money through directly to the health care system. In its own way, the current system makes taxpayers at every income level conscious of the relationship between utilization of health services and their cost.

Nevertheless, the dilemma still remains. OHIP premium revenues do not grow fast enough and the payment of flat rate premiums may cause hardship for some lower income people. This section presents alternatives to deal with these issues within the premium financing concept.

Balanced Revenue Growth

The 1979 Budget proposes to increase monthly OHIP premiums by $1 for a single person and $2 for a family. This is an increase of 5.3 per cent which approximates the projected growth in costs in OHIP insured services this year. There may be merit in tying premium levels to the growth in costs of insured services because:

- the growth in premium revenues would keep pace with costs;
- the Government would neither reap a fiscal dividend nor suffer a fiscal shortfall from this financing system; and,
- subscribers would be directly conscious of the growth in costs of their insurance program.

Assisting Low-Income Subscribers

The Government believes that the existing system to exempt pensioners and people on social assistance from the payment of OHIP premiums is fair. This system delivers some $275 million in direct benefits to these groups.

However, as noted earlier in this paper, the existing system for subsidizing lower income persons does not appear to be working as well as intended. Many people simply do not claim the benefits to which they are entitled.

There are three possible responses to this situation.

First, it may be argued that if people do not seek assistance, they do not need it. The Ontario Government does not accept this view. All lower income people in need of assistance should receive it. Second, it would be possible to improve public awareness of the existing assistance program through an enhanced public information program. This option will be explored. Third, a tax credit related to OHIP premiums could be implemented. This alternative was recommended by the Select Committee.

The balance of this section examines a possible tax credit mechanism.

A Health Tax Credit

The tax credit concept was pioneered by Ontario. In 1969 the Honourable C. S. MacNaughton first proposed that the tax credit mechanism should be used to offset the burdens of certain taxes on lower income people. In 1972 and 1973, Ontario introduced the property tax, sales tax and pensioner credits, programs that have formed a model for other jurisdictions. This mechanism could be used to alleviate low-income people from all or part of their premium burden. The following describes how such a credit could work in Ontario.

Credit Eligibility

All persons resident in Ontario as of December 31, who have paid for OHIP coverage during the year, would be eligible to apply for a credit. Paid coverage would include situations where the premium was paid by the credit claimant, the spouse of the claimant, or an employer of the claimant or of his or her spouse. Only one spouse per married couple would be allowed to claim.

Persons on social assistance, single persons aged 65 or more, families where one or both spouses are aged 65 or more, and persons in receipt of veterans' pensions would not be eligible because they are fully exempt from premiums.

Levels of Relief

The amount of relief delivered is affected by a number of criteria, principally the pattern of progressivity desired and the amount of revenue to be foregone. It is the Government's view that any initial credit should be designed to approximate as closely as possible the existing lower income subsidy arrangements. This would still result in a substantial increase in cost to the Government since the take-up of the credit is expected to be significantly greater than it is under the existing system. Over time, the level of relief could be reviewed.

To parallel the level of current assistance, the credit would have two formulae—one for single persons and one for families. One possible approach is shown in Table 5.

A Possible OHIP Credit Format	Table 5
Single Certificate Holder OHIP Credit = Premium Paid – 15% (Taxable Income – \$2,500)	
Family Certificate Holder OHIP Credit = Premium Paid – 20% (Family Taxable Income – \$3,000)	

As an example of the impact of the credit, a family subscriber with \$4,100 family taxable income would receive a credit entitlement of:

$$\$480 - .2\ (\$4{,}100 - \$3{,}000)$$
$$= \$260.$$

The effective premium for this subscriber would thus be \$220.

For most Ontarians, this system would produce an identical pattern of relief to the existing subsidy program. It covers a slightly larger taxable income spectrum than the current system—cutting out at \$4,100 taxable income for a single person and \$5,400 for a family.

The pattern of relief resulting from this credit alternative is compared to the current assistance program in Table 6. While the credit encompasses a broader range of taxable income than the premium assistance program, there are some instances where a few taxfilers would be theoretically worse off under the credit program as a result of the "notches" in the current system. However, all of these individuals and families will be in the partial assistance ranges in which only 2,000 people are currently enrolled. In other words, the majority of those people are not presently claiming any assistance.

Cost Considerations

It is anticipated that the credit system outlined in Table 5 would, on a family income basis, cost in the neighbourhood of \$175 million and assist close to 600,000 Ontarians. Since \$65 million is already spent on the existing subsidy program, the net additional cost to the Provincial Treasury would be \$110 million.

The introduction of an OHIP credit would make redundant the taxable income subsidy program. As a consequence, that program would be eliminated. However, the changeover from one to the other poses a problem. While current premium assistance is paid concurrently, credits would be delivered after year end. Thus, low-income persons currently receiving premium assistance would have to pay premiums in advance of receiving their credits. Therefore, if a new credit is implemented, it would be preferable to grandfather existing subsidy recipients. On this basis, premium assistance would be continued in the first year *only* of the credit program. These premiums "paid" by the Government on behalf of the individual or family would be eligible for the credit. As a result, net additional costs in respect of the first

Comparison of Assistance: Subsidies versus Credits — Table 6
(dollars)

Single Taxable Income	Current System		Credit System	
	Assistance	Net Premium	Credit	Net Premium
2,500	240	0	240	0
2,700	180	60	210	30
3,100	120	120	150	90
3,400	120	120	105	135
3,600	60	180	75	165
3,800	60	180	45	195
Family Taxable Income	**Assistance**	**Net Premium**	**Credit**	**Net Premium**
3,000	480	0	480	0
3,200	360	120	440	40
3,800	360	120	320	160
4,200	240	240	240	240
4,600	120	360	160	320
5,000	0	480	80	400

Note: The credit entitlement is based upon the structure outlined in Table 5.

year of entitlement would be $175 million due to the doubling up of assistance and credits for a segment of the population.

After the first year of the credit, the taxable income assistance program would be eliminated. Persons now eligible for premium assistance by virtue of low taxable incomes would be required to pay for coverage and would be eligible to claim a credit at year end.

Family Income and the Personal Income Tax System

The current subsidy system operates on a family income basis. That is, the combined income of both spouses is used in determining eligibility for the amount of assistance. It is the Government's view that any new health tax credit should incorporate the concept of family income. Not only would this result in a pattern of relief most similar to the current assistance scheme, but it also represents the most equitable way to proceed as it concentrates monies spent on the lowest income Ontarians.

The Government recognizes that the personal income tax currently does not operate on the basis of family income. The federal government, however, has initiated the use of family income in its child tax credit program. Consequently, Ontario will, in its discussions with the federal government, explore the implementation of the family income concept for purposes of a health tax credit.

This is an important concern in determining whether or not a health tax credit could be introduced. If family income is not feasible in the short-term, the Government could consider implementing a health tax credit based on principal taxfiler income, the concept employed under the current property tax credit system. However, employing such an approach in determining credit entitlement would cost the Government an additional $35 million per year—without adding to the equity of the program. Consequently, the principal filer option needs to be approached cautiously.

Calculating the Credit

The new credit would be claimed on a supplement to the income tax form.

For the bulk of certificate holders, determining OHIP coverage for the year is a straightforward exercise. They are fully covered for the year and pay their own premiums (as defined earlier) for that coverage. However, for some persons, paid coverage for the year is complicated by certain factors such as moving into Ontario, turning 65, marriage or separation. There are three options to deal with this.

OHIP receipts can be sent to all subscribers. From these, they may easily determine their credit entitlement. This would require the Ministry of Health to provide receipts for paid OHIP coverage to over 2.5 million certificate holders, which is a massive undertaking. However, with the cooperation of employers, this task can be accomplished.

An alternative is to develop a procedure whereby persons would determine if their taxable income qualifies them for a credit and then request information on paid premium coverage for the year from the Ministry of Health. This would reduce the clientele for receipts to a more manageable 700,000 but would cause delays in the already lengthy taxfiling process.

A third option is to avoid the requirement for receipts by determining credit entitlement strictly on the basis of filing status, with certain arbitrary rules of thumb. This approach is much simpler from the taxpayers' point of view, but it involves less control over credit entitlement. Compliance would be based only on a post-audit of some returns.

Conclusion

The financing of OHIP is a complex issue, and is clearly one which is subject to considerable debate. The proposals outlined in this paper will contribute to the discussion of the future financing of health care. This will assist the Government in developing longer run policies for OHIP in Ontario.