



## Commentary: Ontario Budget 2009

**Today, the Ontario government brought down a very important budget. The McGuinty government is hoping to stimulate the economy with \$32.5 billion in infrastructure spending and \$700 million in skills training. Unlike past budgets, it is not merely tax-and-spend. The budget included a substantive change to sales tax and tax cuts also made their presence known. As a result, we expect to see budget deficits for years to come – pretty much in keeping with the times, since jurisdictions around the world are stimulating their economies.**

**Most businesses and individuals will like what they see – for now. One day we will have to pay the piper, in the form of higher taxes, or reduced services.**

### Retail sales tax reform

On July 1, 2010, Ontario's Retail Sales Tax ("RST") will be converted to a value-added tax combined with the federal Goods and Services Tax ("GST") to create a federally-administered single sales tax. The rate would be 13%.

There are two major impacts of moving the RST to a GST-like system:

- Most services and many goods, which are currently exempt from RST, will be subject to tax for the first time
- Most businesses will be able to claim Input Tax Credits ("ITCs") in respect of the taxes paid. This way, the tax will effectively be removed.

### Expenses not qualifying for input tax credits

For the first five years, large businesses (with taxable annual sales exceeding \$10 million) and financial institutions will be unable to claim input tax credits on certain expenses, including meals, entertainment, vehicles weighing under 3,000 kilograms, and fuel for these vehicles. Telecommunications (excluding internet and toll-free) and energy (excluding used in production) are also restricted. The restrictions will be phased out over the succeeding three years.

### New housing rebate

Buyers of new housing would be eligible for rebates. The rebate for new primary residences costing under \$400,000 would be 6% of the purchase price, with the rebate amount reduced for homes priced between \$400,000 and \$500,000. Homes exceeding \$500,000 in price would not qualify for a rebate.

This rebate would be in addition to the existing federal GST rebate. The federal rebate is 1.8% of the purchase price up to \$350,000; it is phased out completely at \$450,000.

### Small business transition support

Ostensibly to help small business owners make changes to their point-of-sale and accounting systems, Ontario is providing a credit. Businesses other than financial institutions, with less than \$2 million in annual revenues will receive up to \$1,000.

### Small suppliers

As with GST, small suppliers (with total taxable sales of \$30,000 or less in the prior year or \$50,000 or less in the case of a public service body) would not be required to register, collect or remit.

### Point-of-sale rebates

Rebates will be instituted for the provincial portion of the tax, providing a partial exemption for books, children's clothing and footwear, children's car seats, diapers and feminine hygiene products. These items are currently exempt from RST.

### Vendor compensation

With the RST, vendors are compensated for the effort of collecting the tax. Vendor compensation will end after March 31, 2010.

## Corporate tax

The budget proposes to cut corporate income tax rates:

Ontario's Proposed Corporate Income Tax Rate Cut Plan			
Date	General	Manufacturing & Processing	Small Business
Current	14.0%	12.0%	5.5%
July 1, 2010	12.0	10.0	4.5
July 1, 2011	11.5	10.0	4.5
July 1, 2012	11.0	10.0	4.5
July 1, 2013	10.0	10.0	4.5

The overall (corporate and personal combined) top marginal tax rates for income earned by a corporation, paid out by dividends, are as follows:

Top Marginal Corporate and Personal Income Tax Rate			
Date	General	Manufacturing & Processing	Small Business
2009	48.4%	46.9%	42.7%
2010	48.6	47.1	43.0
2011	48.3	47.2	43.0
2012	47.9	47.2	43.0
2013	47.2	47.2	43.0

The top marginal rate on salary is 46.4% for all years.

In 2009, there can be an overall advantage achieved by earning income through a corporation and paying dividends rather than salary.

Small business income	\$100,000	\$200,000	\$300,000	\$400,000
Taxes (income, CPP, EHT) using salary	31,896	78,423	125,858	173,293
Tax using dividends	25,196	66,179	108,849	151,519
Savings	6,700	12,244	17,009	21,774

### Surtax

Currently, the benefit of the Ontario small business deduction is gradually phased out by a 4.25% corporate surtax on taxable income in excess of \$500,000. The benefit and the surtax are eliminated once taxable income reaches \$1.5 million. The surtax created double-taxation anomalies in this income range, and was widely criticized.

The surtax will be eliminated July 1, 2010.

### Corporate Minimum Tax ("CMT")

CMT is applicable to a corporation (or associated group) with total assets exceeding \$5 million or annual revenues over \$10 million. The tax is levied on the adjusted financial statement income. The CMT is payable to the extent it exceeds the regular tax.

For taxation years ending after June 30, 2010, the budget proposes to:

- Raise the asset and revenue thresholds to \$50 million and \$100 million respectively, and
- Reduce the tax rate from 4% to 2.7%

## Personal tax

The budget contains many personal income tax measures, including:

### Rate reduction

Effective January 1, 2010, the first tax bracket rate, applicable to income up to \$36,848, will be cut from 6.05% to 5.05%. This is the lowest tax rate in Canada on this income bracket. The maximum savings will be \$368.

The rates on other income remain mostly unchanged. These rates reach up to 17.41% - near the high end of the scale.

### Surtax thresholds

At present, Ontario imposes a 20% surtax (tax on tax) at income of about \$65,000 and an additional 36% surtax at income of about \$76,000. For 2010 and later years, the budget proposes to lower the thresholds marginally. This change will mostly recapture the rate reduction of the lowest bracket for taxpayers above those income levels. The maximum additional cost will be \$156.

### Dividend tax credit rates

Dividends from Canadian corporations are paid out of earnings that have already been taxed at the corporate level. To recognize this fact, recipients are entitled to a credit.

As corporate tax rates fall, the credit is also being reduced. Effective January 1, 2010, the credit on eligible dividends (generally those paid by large corporations) will be reduced from the planned 2010 rate of 7.7% to 6.4% (the actual 2009 rate was only 7.4%). For other (mostly small business) dividends the credit is being reduced from 5.13% to 4.5%.

### Ontario sales tax transition benefit

To buy the support of Ontarians for the transition to the new sales tax system, direct payments will be delivered to Ontario tax filers 18 years of age or over.

A single person without any children and income up to \$80,000 would receive a benefit of \$100 in each of June 2010, December 2010 and June 2011. The maximum benefit to a single person would be reduced by 5% of income over \$80,000. The payments to a family with income up to \$160,000 would be \$330 in June 2010 and \$335 in each of December 2010 and June 2011. The maximum benefit to a family would be reduced by 5% of income over \$160,000.

## Corporate Credits

To get maximum political benefit, governments prefer to target for spending and tax incentives. Broad-based tax reductions have been demonstrated to be better for the economy, but they don't yield as many votes. Since this government knows it is elected by votes, not dollars, it has enhanced a number of tax credits:

- Innovation
- Film and Television
- Production Services
- Interactive Digital Media
- Computer Animation and Special Effects
- Book Publishing
- Co-operative Education
- Apprenticeship Training

## Personal Credits

The Ontario Property and Sales Tax Credits will be replaced by two new credits: the Ontario Sales Tax Credit and the Ontario Property Tax Credit. The benefits of these credits are being enhanced by significant increase in the income thresholds at which the benefits begin to be clawed back. The maximum benefit and thresholds will also be indexed for inflation.



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