2017 Document: Fiscal Plan Context

Office of the Budget
MINISTRY of FINANCE

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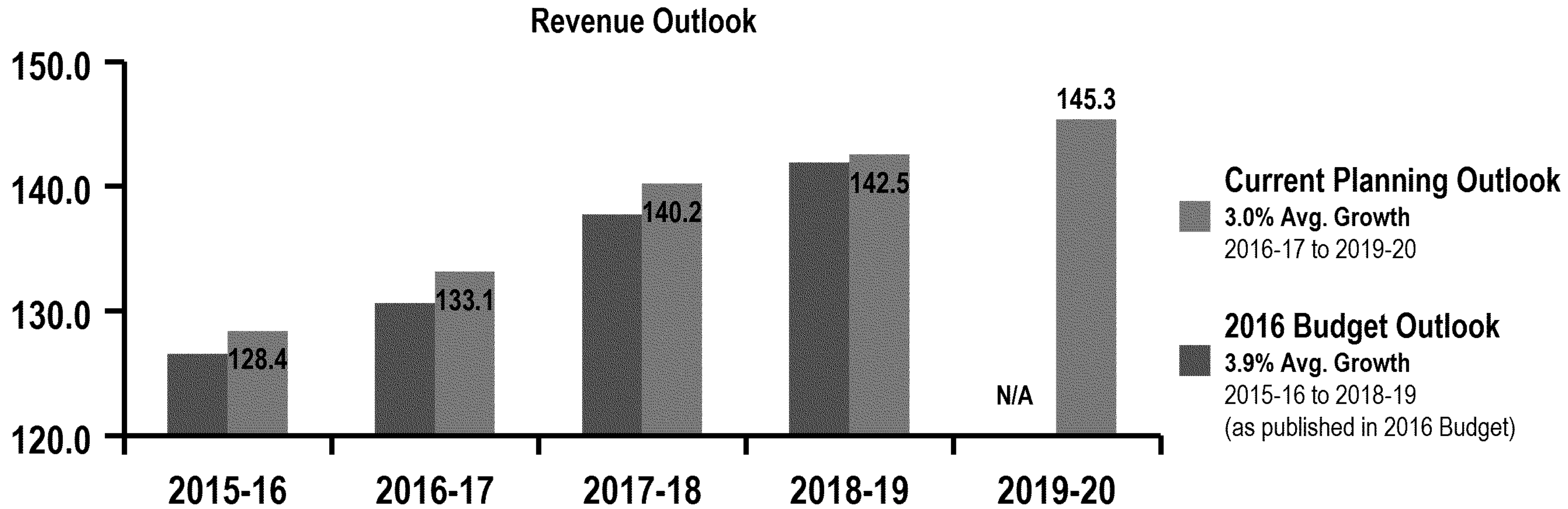
Purpose

- Review the **current fiscal challenge** in light of the government's **fiscal anchors**.
- Outline the **potential tools** that could support the achievement of the government's fiscal objectives and key investments.

Evolution of the Fiscal Plan and Current Challenge

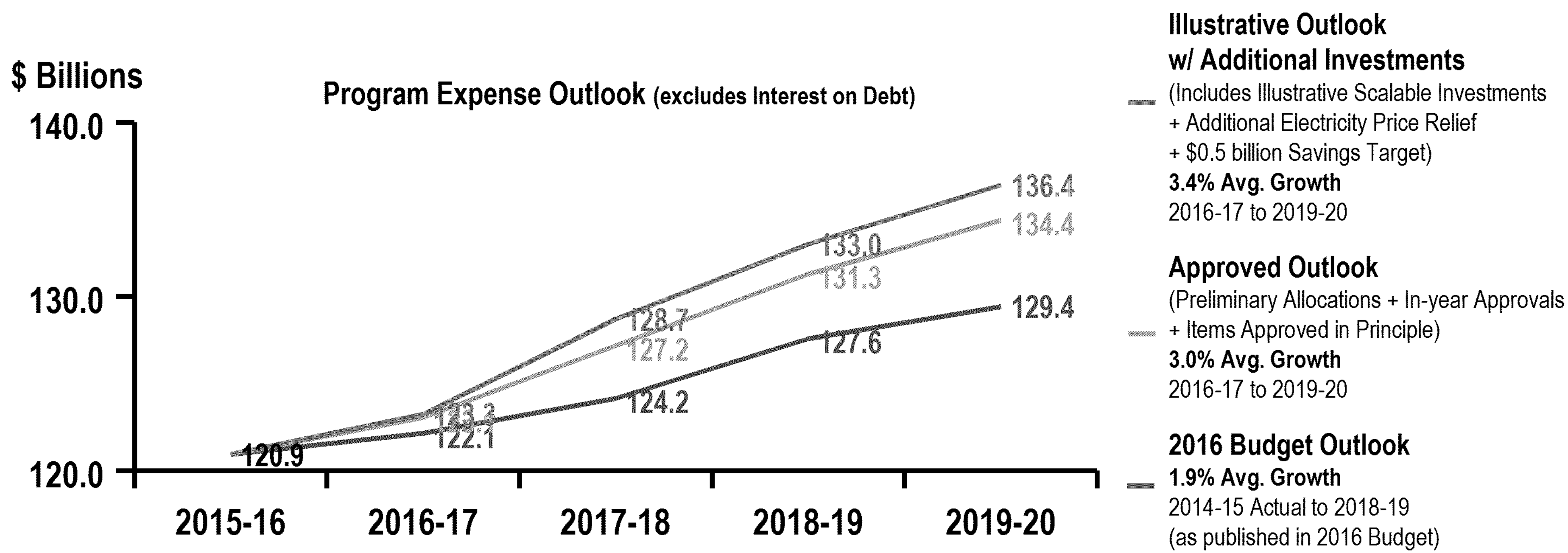
Fiscal Context – Revenue Growth – 2016 Budget to Current



Key Revenue Changes since the 2016 Budget

- Higher than forecasted taxation revenue by $2.3 billion in 2017-18 and $2.9 billion in 2018-19, partially offset by:
  - Lower projected equalization by $(0.9) billion in 2017-18 and $(1.6) billion in 2018-19.
  - Lower Cap and Trade proceeds projection of $0.1 billion in 2017-18, rising to $0.5 billion in 2019-20. Note that expense outlook also reflects these changes.
  - IFRS accounting impact from the consolidation of OPG and Hydro One of $0.4 billion in 2017-18, rising to $0.7 billion by 2019-20.
- Lower earnings from sale of Hydro One and re-profiling final tranche from 2018-19 to 2017-18, resulting in a $0.1 billion decrease in 2017-18, and a $0.7 billion decrease in 2018-19.

Fiscal Context – Expense Growth – 2016 Budget to Current



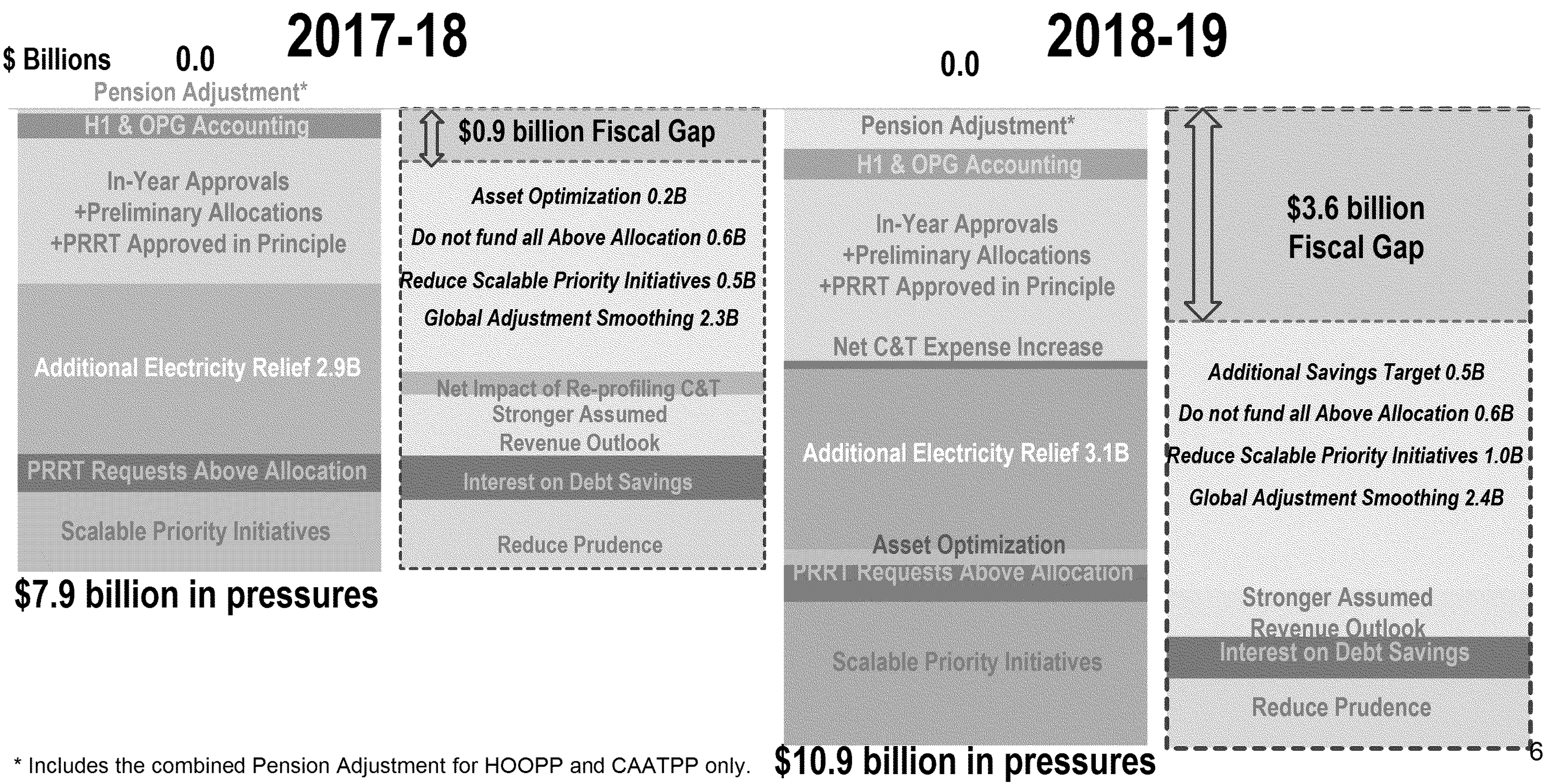
	2015-16	2016-17	2017-18	2018-19	2019-20
Interest on Debt	11.0	11.4	11.7	12.4	12.6
Reserve	-	0.4	0.7	0.8	1.0

Key Drivers of Expense Growth since the 2016 Budget

- Since the 2016 Budget, preliminary allocations, other new expense approvals, including the Electricity Cost Relief announced in the fall, and recent PRRT decisions, grow to **$4.2 billion by 2019-20**.
- Potential scalable priority initiatives could amount to about $1.8 billion by 2019-20.
- Potential additional Electricity Cost Relief of $0.8 billion by 2019-20 (pending accounting treatment).
- Assumes additional savings targets of $0.5 billion in 2018-19 and 2019-20.

The Fiscal Challenge

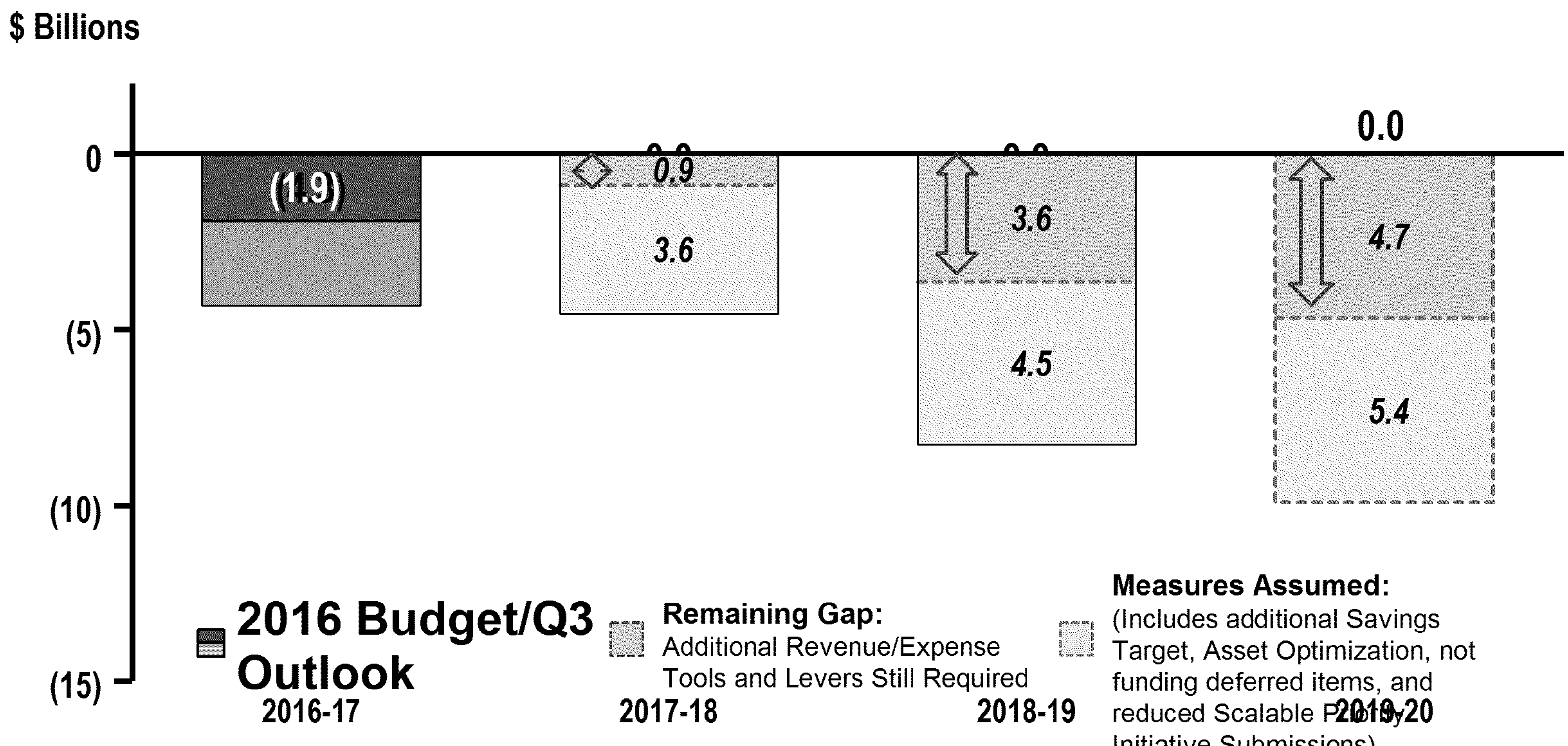
- The 2016 Budget outlined a plan to balance the budget in 2017-18 and remain balanced in 2018-19, however **changes since the Budget have created a gap compared to the government's fiscal targets.**
- In order to accommodate fiscal pressures in 2017-18 and 2018-19, a number of tools have been taken on.



* Includes the combined Pension Adjustment for HOOPP and CAATPP only.

Assessing and Addressing the Fiscal Challenge

- Without additional effort, the fiscal gap is **$0.9 billion in 2017-18, $3.6 billion in 2018-19, and $4.7 billion in 2019-20**.
- Continuing to assume fiscal anchors of **balanced budgets** over the forecast horizon **will require identifying additional revenue or expense tools/levers** to address the fiscal challenge.



Other Factors That Could Further Impact the Gap

Revenue

- Revisions to economic outlook
- Potential revisions to cap-and-trade proceeds based on auction results in 2017.
- Adjustments to the government's asset optimization strategy
- Remaining 2015 CIT & PIT tax assessment information and ongoing tax receipts from provincially administered taxes
- PRRT updates (revised revenue outlooks from ministries, agencies and government business enterprises)
- Implications of Federal Budget

Expense

- 2017 Document initiatives / PRRT Deferred
- Labour settlements
- Interest on debt forecast updates
- Alignment of climate change investments with available proceeds
- Impact of expense pressures that ministries have been asked to manage
- Pension Expense Updates

Accounting risks:

- Further updates to accounting Framework for OPG and Hydro One (IFRS)

Prudence

- Build the reserve back up to mitigate adverse impacts to the fiscal plan
- Resetting the contingency funds to accommodate expense risks and pressures

- Potential improvement to gap
- Potential improvement or deterioration to gap
- Potential deterioration to gap

Approaches to Closing the Gap

Potential Tools to Achieve Fiscal Targets

There are a number of revenue and expense measures that could be considered to achieve fiscal targets.

Additional Revenue Measures	**Federal Revenue Strategy**

• Determine the scope for revenue tools, including:
  • Targeted Tax Changes
  • Non-tax revenue
  • Federal tax measures
	• Engagement strategy with the federal government to maximize new federal funding, including:
	  • Equalization Protection
	  • Funding for climate change initiatives
	  • Infrastructure*
	  • Health funding*

Additional Expense Measures	**Prudence**

• Determine the scope for expense measures, including:
  • Undertaking additional transformative initiatives
  • Revisiting in year approvals
  • Timing/scaling funding of mandate letter commitments*
  • Additional savings targets*
  • Program Review
• Further Interest on Debt Savings*
	• What is the appropriate level of prudence to build into the fiscal plan?
	  • Further reductions to the reserve* or Contingency Fund*, or
	  • Pushing the revenue forecast or interest on debt forecast beyond current expectations, increases vulnerability to future downward forecast revisions

* Indicates tool that is already built into planning assumptions -- limiting potential additional fiscal effort from these tools.

Potential Revenue Tools

A number of revenue tools could be considered as part of the strategy required to close the fiscal gap.

Potential 2017 Document Revenue Measures

- Increases to **tobacco and beer** tax revenue of up to $0.1 billion each year between 2017-18 and 2019-20
- Increasing the **insurance premium tax** by 1 percentage point, which could generate up to $0.3 billion in 2017-18, and up to $0.4 billion by 2019-20
- Increase planned **education property tax** adjustment from 1% to 2% annually, which could generate up to $0.1 billion in 2017-18. If this was extended to 2019-20, it could generate up to $0.3 billion
- Use a greater proportion of **Cap and Trade proceeds** against in-plan GHG reduction expenditures (e.g., revisit $0.6 billion for in-plan initiatives in 2018-19 and 2019-20)
- Lobby the federal government to **remove preferential tax treatment for businesses** that benefit from a 50% income tax deduction on expenses related to meals and entertainment. This could generate $0.2 billion in 2017-18, and up to $0.3 billion by 2019-20
- Approach other provinces to create consensus for **pressing the federal government on sharing tax revenue** from certain income tax measures that have a substantial provincial connection (e.g. tax on disposition of certain properties by a non-resident)
- As part of an integrated strategy on revenue integrity, the province will undertake a thorough policy and legislative review of all taxes, including those shared with the federal government, to eliminate loopholes and ensure fairness for all taxpayers. The Province will also move forward to strengthen administration of existing laws, through public education and increased enforcement, enhanced partnerships with the Canada Revenue Agency and strengthening Ontario's ability to address underground economy activity through information sharing legislation.

Summary of Potential Revenue Tools

$ Millions	2017-18	2018-19	2019-20
Increases to Tobacco and Alcohol Taxes*			
Tobacco Tax of 1 cent per cigarette	40	39	38
Alcohol Tax of 6 cents per litre	14	41	59
Total Tobacco/Alcohol Tax	**54**	**80**	**97**
Increases to the Insurance Premium Tax	270	380	395
Increase Planned Education Property Tax	85	180	310
Total Potential Tax Tools	**409**	**640**	**802**
Other Potential Tax Tools			
Lobby for Federal Reform of Corporate Meals and Entertainment Tax Allowances	**170**	**250**	**340**

*Tobacco tax increases are equivalent to an additional cost of $2.00 per carton of 200 cigarettes. Alcohol tax increases are equivalent to an additional 50 cents per 24-case of beer (by November 2018). This would bring the total increase to $1.00 including the 25 cent per year increase over two years announced in the *2015 Budget*.

Expense Tools: Program Reviews with Savings Targets

- Initiate a systematic program review process with the goal of identifying savings that would materialize beginning in 2018-19.
- Buy-in from the Cabinet and ministries is an essential condition for the program review process to meet is objectives.
- If approved, the program review process would be launched in Spring 2017 and include:
  - Developing savings targets for ministries taking into account the overall allocation of ministries, current mandate commitments and non-discretionary pressures.
  - Ministries would be asked to propose plans to implement savings targets that avoid across-the-board reductions. Instead, the savings plans to be informed by evidence of effectiveness of programs and focus on PRRT principles (relevance, effectiveness, efficiency and sustainability of programs)
  - Where services are offered by multiple ministries, costing reviews involving multiple ministries can be initiated to identify the most effective mode of delivery. External support would be provided, as necessary, to maximize impact and outcomes.
  - PRRT Sub-Committee can be used to provide oversight and direction to ministries in the development phase.
  - Ministries would be asked to report back in the 2018-19 PRRT for approval of their plans.

Revisiting Prudence

- The fiscal plan historically includes various sources of prudence to protect the Province's overall fiscal performance against the impact of unexpected changes in the economic, revenue and expense outlooks.
- The overall, and specific sources, of prudence across the fiscal could be "re-balanced" and re-set in order to help free up fiscal room.
- However, some forms of prudence are more explicit than others – and the reduction of such elements of prudence may undermine the credibility of the fiscal plan.
- Key sources of prudence to review include:
  - The **reserve** (*required by the Fiscal Transparency and Accountability Act, 2004*) is included on top of fiscal outcome projected by the revenue and total expense outlooks (i.e. added to the deficit).
  - The **Contingency Fund**, which is included in the program spending outlook on a multi-year basis (however only explicitly published for plan year). The Contingency Fund is often set as a combination of expense pressures expected to materialize and notionally set aside (i.e. future compensation), as well as an unallocated portion in order to be available for other unknown pressures (i.e. extra forest firefighting, disaster relief, etc.
  - The **economic forecast** used for planning purposes, is set slightly below the private sector average.
  - The **interest on debt expense forecast** incorporates higher interest rate assumptions in the out-years.

Potential Tools to Achieve Fiscal Targets

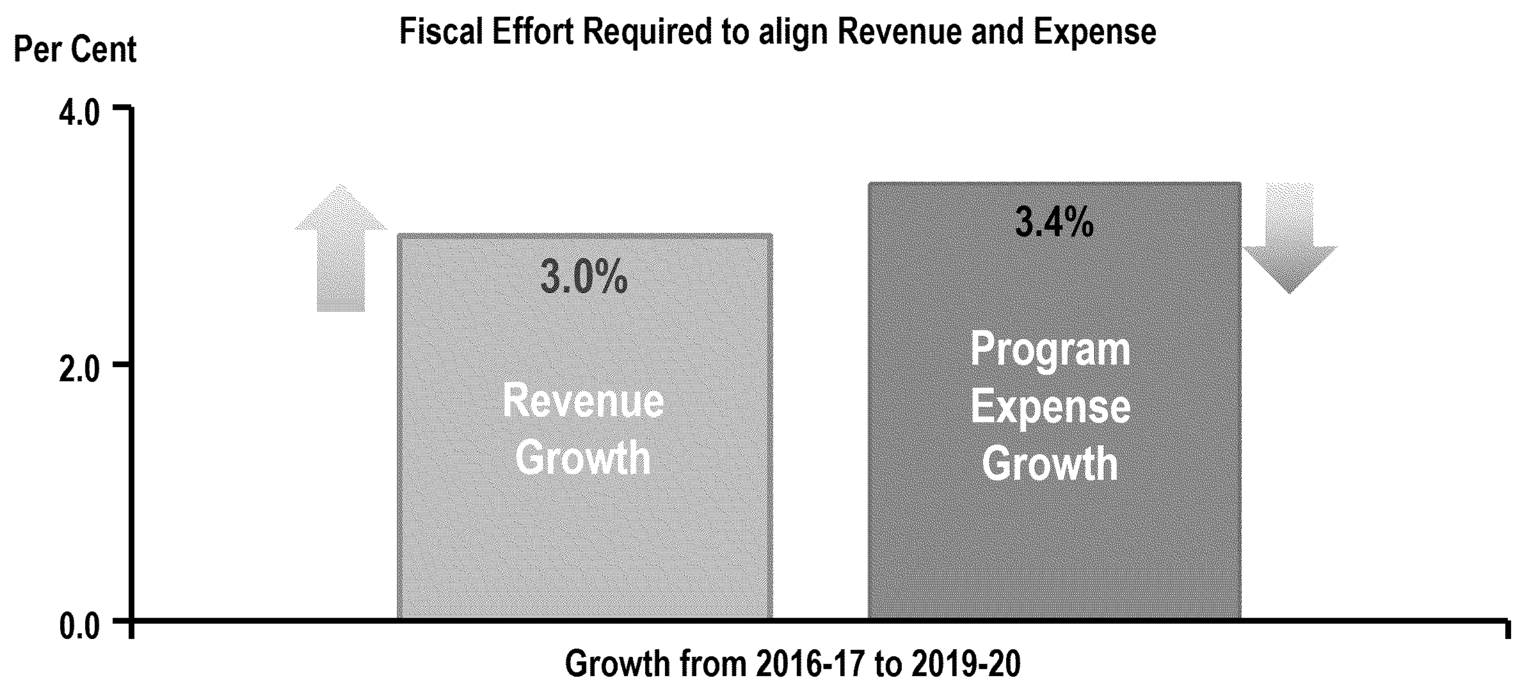
Achieving balance while making new investments will require significant spending constraint or revenue generation, particularly in 2018-19 and 2019-20. Some potential revenue and expense tools include:

Revenue	Expense

• Several revenue tools could be considered to close the fiscal gap, including:
  • Targeted **tax changes**
  • **Non-tax revenue**
  • Strategy on **revenue integrity**
• Engagement with the **federal government** to maximize federal funding.
	• A **systematic program review process** with the goal of identifying savings that would materialize beginning in 2018-19.
	  • **Savings targets for ministries** taking into account the overall allocation, current mandate commitments, and non-discretionary pressures.
	  • **Costing reviews** where services are offered by multiple ministries **to identify the most effective mode of delivery.**

Managing Revenue and Expense Growth

- Over the medium-term outlook, program expense growth exceeds revenue growth in each year.
- Achieving a balanced plan over the outlook period and providing room for investments will require significant fiscal effort to either constrain program spending and/or increase revenue, so that revenue and expense are more aligned, particularly in 2018-19 and 2019-20.
- This will require the consideration of all viable revenue and expense tools/levers.
- An ongoing mismatch between revenue and expense growth results in a structural deficit.



Key Takeaways

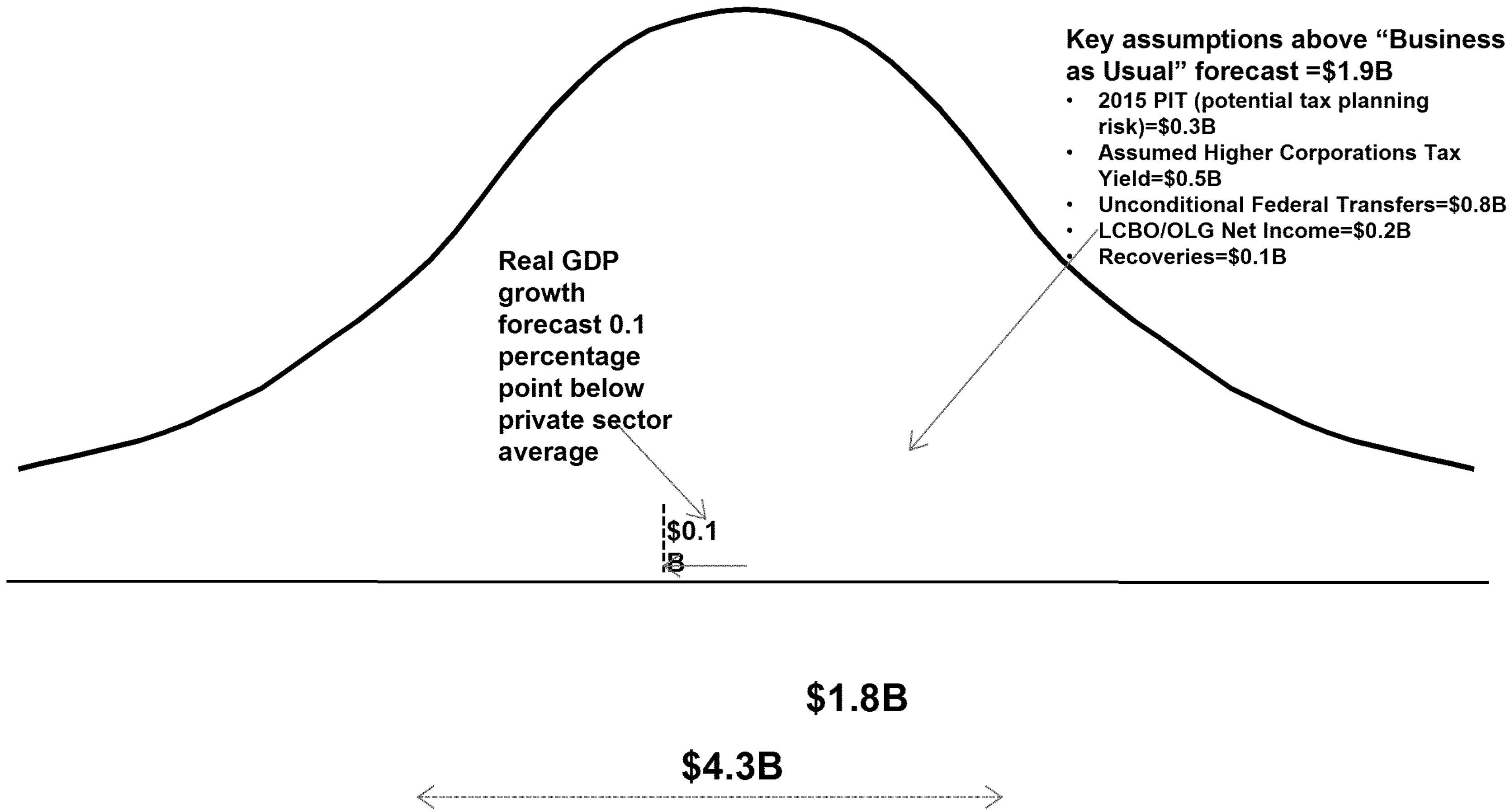
- The **2017 Document** approach will need to **reconcile** the commitment to **balance** with the desire to make **investments in priority areas**
- **Achieving fiscal objectives** while investing in new priorities will **require** the consideration of all **viable revenue and expense tools**
  - Success of a **Program Review** exercise will require the buy-in and **commitment of** all **Cabinet** members to constrain program spending
- Regardless of tools taken on, **not all priorities can be funded** as part of the **2017 Document** – this will require **choices and trade-offs** about what to **fund now** and what can be considered as part of the 2018 Document.

Appendix

Program Expense Growth

$ Billions	16-17	17-18	18-19	19-20	20-21	Avg. Annl 15-16 to 19-20	Avg. Annl 16-17 to 19-20
2016 Budget Program Expense	**122.1**	**124.2**	**127.6**	**129.4**	**131.6**	1.7%	1.9%
Annual growth	1.0%	1.7%	2.8%	1.4%	1.7%		
Change in pension accounting	0.0	0.1	0.7	0.8	0.8		
In-year changes and allocation adjustments	0.9	1.9	1.8	2.7	3.0		
Preliminary Allocations Outlook	**123.1**	**126.2**	**130.1**	**132.9**	**135.4**	2.4%	2.6%
Annual growth	1.8%	2.5%	3.1%	2.2%	1.9%		
Expenses with revenue offsets and other changes		0.6	0.5	0.2	0.2		
Approved-in-principle above Preliminary Allocation		0.3	0.7	1.3	1.3		
Outlook with Approved-in-Principle		**127.2**	**131.3**	**134.4**	**136.9**	2.7%	3.0%
Annual growth		3.3%	3.3%	2.4%	1.9%		
Scenario 1: Scalable Initiatives (Illustrative)		0.9	1.5	1.8	1.8		
Outlook including Scalable (Illustrative)		**128.0**	**132.8**	**136.1**	**138.8**	3.0%	3.4%
Annual growth		4.1%	3.7%	2.6%	1.9%		
Deferred Items		0.6	0.3	0.3	0.3		
Outlook including Deferred Items		**128.6**	**133.1**	**136.4**	**139.1**	3.1%	3.5%
Annual growth		4.5%	3.5%	2.5%	1.9%		
Scenario 2: Scalable Initiatives (High-end options)		1.4	2.5	3.2	3.7		
Outlook including Scalable (High-end)		**128.5**	**133.8**	**137.6**	**140.6**	3.3%	3.8%
Annual growth		4.5%	4.1%	2.9%	2.2%		
Deferred Items		0.6	0.3	0.3	0.3		
Outlook including Deferred Items		**129.1**	**134.1**	**137.9**	**141.0**	3.3%	3.9%
Annual growth		4.9%	3.8%	2.9%	2.2%		

Broad Range of Risks Around Current 2017-18 Revenue Outlook



Current Revenue Outlook

Current Outlook						
$ Billions	**2015-16**	**2016-17**	**2017-18**	**2018-19**	**2019-20**	**Avg. Growth**
Total Taxation Revenues	91.8	94.8	98.3	103.1	107.1	*3.9%*
Government of Canada Transfers	22.9	24.5	26.2	25.7	24.6	*1.8%*
Government Business Enterprises	4.9	5.2	5.1	5.4	5.7	*3.7%*
Other Non-Tax Revenues	8.8	8.6	10.5	8.4	8.0	*-2.2%*
Total Revenues	**128.4**	**133.1**	**140.2**	**142.5**	**145.3**	*3.2%*
Nominal GDP Growth(%)	4.9	4.5	4.1	4.1	4.1	*4.2%*

Note: average growth rates are calculated from 2015-16

Key Assumptions Built in Revenue Outlook

2015 PIT (potential tax planning risk)	–	0.7	0.7	0.7	0.7
Stronger 2015 HST	–	0.8	0.5	0.5	0.5
Assumed Higher Corporations Tax Yield	–	0.3	0.5	0.7	0.7
Equalization Forecast	2.4	2.3	1.4	0.7	0.7
Public Transit Infrastructure Fund (PTIF)	–	–	1.1	0.4	–
Unconditional Federal Transfers					
- Infrastructure, Homecare, Training	–	0.1	0.8	1.3	0.0
IFRS for HOL and OPG	–	0.0	-0.4	-0.5	-0.7
Debt Retirement Charge ends 2018-19	0.9	0.6	0.6	0.0	0.0
Asset Optimization (Net Impact)	0.9	1.0	1.0	-0.1	-0.4
Cap and Trade Proceeds Assumptions	0.0	0.0	1.8	1.4	1.4

- **Taxation revenues**, reflecting the current economic forecast, are projected to grow at 3.9% over the 2016-17 to 2019-20 period. This is roughly in-line with the average nominal GDP growth of 4.2% over the same period.
- **Government of Canada Transfers** are based on existing federal provincial agreements including public transit infrastructure fund, new strategic investment funds and revised assumptions for unconditional federal transfers including infrastructure, homecare and training.
- **Net income of Government Business Enterprises** are based on 2016 Budget projections, adjusted upwards for mid-year improvement in OLG and LCBO, and also for OPG and IFRS Consolidation risks.
- **Other Non-Tax revenues** are based on 2016 Budget outlook projections for Ministry and Government Organizations, updated for asset optimization and cap & trade proceeds, as well as for recoveries of prior- year-expenditures and new NTR offsets.

Variance from 2016 Budget

Current Outlook:Change from 2016 Budget Outlook				
$ Billions	**2015-16**	**2016-17**	**2017-18**	**2018-19**
Total Taxation Revenues	1.1	3.0	2.3	2.9
Government of Canada Transfers	0.0	-0.2	0.4	-0.9
Government Business Enterprises	0.6	0.2	-0.2	-0.3
Other Non-Tax Revenues	0.2	-0.5	-0.1	-1.0
Total Revenues	**1.8**	**2.5**	**2.5**	**0.6**

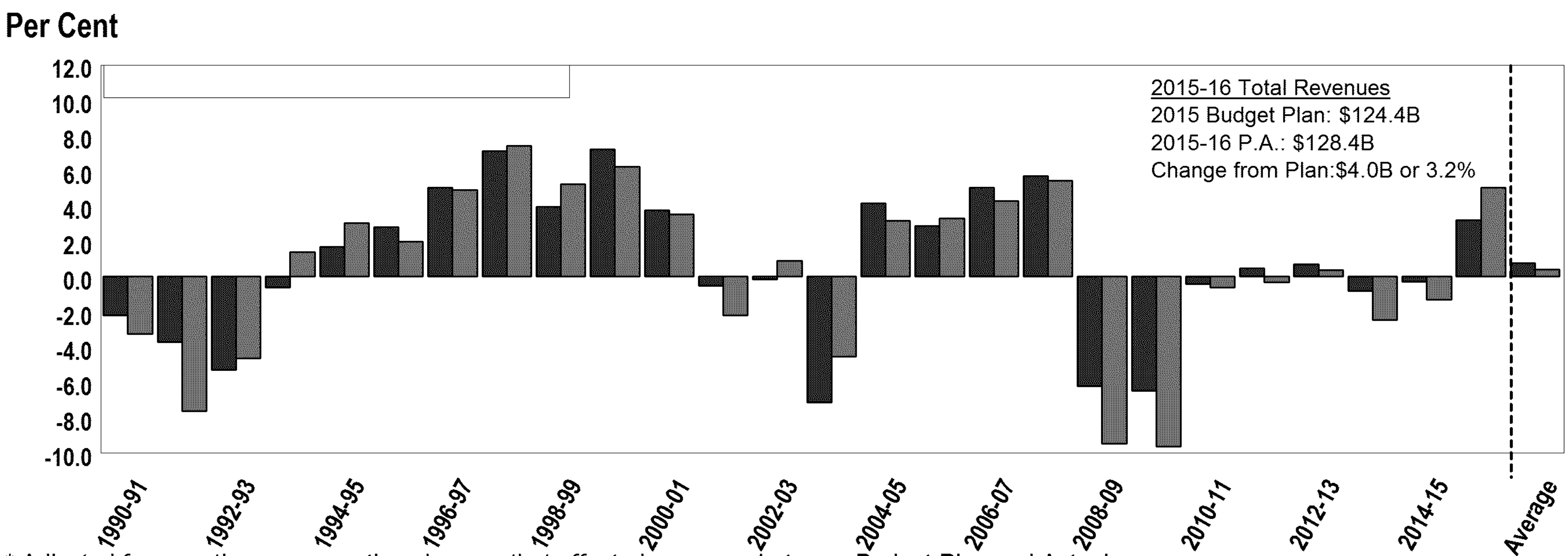
Taxation Revenues:
Reflects stronger economy. Consistent with higher nominal GDP projection due to upward revision to growth in 2014 to 2016.

Government of Canada Transfers:
Mainly due to lower Equalization revenues resulting from Ontario's stronger economic and revenue outlook. This is partly offset by public transit infrastructure fund.

Government Business Enterprises:
Mainly due to higher-than-projected net income for 2016-17 and 2017-18 and lower in 2017-18 and 2018-19 due to IFRS related consolidation adjustment

Other Non-Tax Revenues:
Largely due to updated forecast related to asset optimization, cap and trade proceeds, and miscellaneous revenues (mainly recoveries of prior year expenditure)

Revenue Variance – From Budget Plan to Actual*



* Adjusted for reporting or accounting changes that affected revenues between Budget Plan and Actual

- Actual revenue results for a fiscal year are released in the Public Accounts about 16-17 months after the Budget Plan.
- Over the past 26 years, Plan to Actual variances have averaged +0.8% for total revenue and +0.4% for taxation revenue.
  - This relatively small under-estimate of revenues in the Budget Plan largely reflects some modest prudence built into the Budget economic forecast.
  - Although the average variance is relatively small in any given year, it can be significant (up to +/- 10% over the past 26 years).
  - The total variance from plan in 2015-16 reflects $1.5 billion higher net revenues from Hydro One ownership broadening while all other tax and non-tax revenues are $2.5 billion higher than plan.
- Post-recession from 2010-11 to 2014-15, variances have been relatively small.
  - The dollar variance from Plan averaged -$0.1 billion, or -0.1 per cent for total revenues, and -$1.2 billion or -1.4 per cent for taxation revenues.
  - In absolute terms, the dollar variance from Plan averaged $0.6 billion, or 0.5 per cent for total revenues and $1.3 billion or 1.6 per cent for taxation revenues.

Federal Revenue Strategy

- The current revenue outlook continues to assume additional revenue for home care, labour market, and infrastructure – that will be unconditional in nature (i.e. support in-plan spending, no incrementality).
- While Ontario and the federal government have signed agreements in a number of areas, there are additional opportunities to maximize new federal funding, minimize the negative impact of conditions on new programs, and leverage federal investment to support provincially-planned programs.
- The lead-up and delivery of the 2017 Federal Budget, expected in the coming weeks, provides an important opportunity to assert Ontario's expectations around federal revenue.

Program Area	Example
Federal health funding	Continue to work on adequate, sustainable and principled health funding, or use approach to federal offer as leverage for success in other areas.
Equalization program	**Defensive tactic:** ensure GDP constraint acts as a 'top-up' as currently described in legislation **Offensive tactic:** push for 'protection' from year-over-year declines in transfer entitlements.
Climate change funding	With the release of the Pan-Canadian Framework on Climate Change, the federal government will likely begin funding through new environmental programs, including the Low Carbon Economy Fund.
Early learning and child care	Work to ensure National Framework and bilateral agreements provide Ontario flexibility to direct federal funding to in-plan expenditures and support Provincial priority areas.
Infrastructure	Ontario continues to work with the federal government on the next phase of its infrastructure plan, including limiting the federal government's use of incrementality provisions.
Indigenous files	Maximize opportunities to leverage historic $8.4 billion planned federal spending, both to make Ontario's planned investments (health, TRC response, anti-violence) go further and reduce downstream costs associated with inaction/failure to address root causes.
Innovation Agenda	Ontario will likely have a number of programs that are aligned with the Innovation Agenda, and should look for opportunities to leverage funding to provincial priorities.

Potential Revenue Tools: Tobacco

Preliminary Estimate ($ millions)	2016-17	2017-18	2018-19	2019-20	2020-21
Increase tobacco taxes by one cent per cigarette and per gram of tobacco product (equivalent to $2.00 per carton of 200 cigarettes) in Budget 2017 - This increase is projected to result in up to $40M in new tobacco tax revenues in 2017/18, as compared to current projections - The government could also continue with planned annual inflation-based increases scheduled to begin on June 1, 2017 - There is a risk that the after the tax increase anticipated revenues would not be fully realized due to an increase in the contraband tobacco market	-	Up to $40M	Up to $39M	Up to $38M	Up to $37M

Potential Revenue Tools: Tobacco

Considerations

- Tobacco tax revenues are dependent on a number of factors, including most importantly the size of the contraband tobacco market, currently estimated to be up to 30% of the total tobacco market in Ontario.
- There is a risk that larger tax increases can drive consumers to the contraband market, and therefore undermine revenue projections.
- Budget 2016 amended O. Reg 5/05: “Tobacco Tax Rates” to schedule annual tax increases by an amount based on inflation to ensure that at a minimum, the tobacco tax rate remains consistent on a real dollar basis over time.
- Budget 2016 included a tobacco tax increase equivalent to $3 per carton of 200 cigarettes. Preliminary revenue figures suggest that this will have resulted in up to $70M in new revenues.

	Cigarettes (per 200)	**Fine-cut** (per gram)	**Cigars** (per cigar)
Federal excise duty	**$21.03**	**13.140¢**	**The greater of: $0.08226 per cigar and 82% of the sale price**
Manitoba	$59.00	28.500¢	75% retail selling price to $5.00 max
North West Territories	$57.20	26.600¢	75% of retail price
Nova Scotia	$55.04	26.000¢	60% of retail price
Alberta	$50.00	37.500¢	129% taxable price to $7.83 max.
Saskatchewan	$50.00	25.000¢	100% of taxable value to $5.00 max
Nunavut	$50.00	20.000¢	75% of retail price
Prince Edward Island	$50.00	21.500¢	71.6% of retail price
Newfoundland & Labrador	$49.00	40.000¢	125% of purchase price
British Columbia	$47.80	23.900¢	90.5% of the taxable price, to $7.00 max
New Brunswick	$44.52	22.260¢	75% of retail price
Yukon	$42.00	21.000¢	130% of taxable price
Ontario	**$30.95**	**15.475¢**	**56.6% of retail price**
Quebec	$29.80	14.900¢	80% of taxable price

Potential Revenue Tools: Alcohol

Preliminary Estimate ($ millions)	2016-17	2017-18	2018-19	2019-20	2020-21
Beer tax/LCBO mark-up increase of 6¢ per litre in Nov 2017 and Nov 2018	-	13.5	41.1	58.5	58.5

General Considerations

- Majority of Premier's Advisory Council recommendations implemented and built into the fiscal plan: $182M from the beer and wine sectors by 2019-20.
- Some changes since Budget plan will reduce expected revenue, including:
  - $10M in 2018-19 from planned but likely cancelled competitive tendering pilot program, $1.5M decrease from change to the minimum price treatment of cider, $3.6 million annual decrease from elimination of LCBO Special Occasion Permit fee.
  - New small producer support programs estimated to cost $1.9M in 2017-18, $1.7M in 2018-19 and $1.7M in 2019-20. If approved, MOF has committed to increase dividend to the CRF to offset program allocation to OMAFRA.
- Proposed options would build on policy direction to:
  - more closely harmonize the relative tax burden among beer, wine and spirits; and
  - support LCBO in introducing strategies that use its buying power to reduce operating costs.

Increase beer basic tax/LCBO mark-up by 6 cents/L in Nov. 2017 and 2018 (instead of scheduled 3 cents/L increases)

- Full impact would not be realized until 2019-20.
- Would require legislative change to *Alcohol and Gaming Regulation and Public Protection Act*.
  - Consumer prices would increase by 50 cents per 24-case of beer each of November 2017 and 2018 instead of 25 cents per 24 case each year as announced in the 2015 Budget.
- Brewers may respond by cancelling price caps for certain products.
  - The large brewers committed to cap consumer prices of some of their most popular brands until May 2017.
  - Timing of 2017 Budget announcements could affect brewers' response.

Potential Revenue Tools: Insurance Premium Tax

Preliminary Estimate ($ millions)	2016-17	2017-18	2018-19	2019-20	2020-21
Increase IPT Rates (1 Percentage Point) *Excludes RST on insurance premiums Increase IPT rates on all forms of insurance (except automobile insurance) by 1 percentage point.	-	270	380	395	410

Considerations

- IPT is a tax on insurance premiums collected and paid to the province by insurance companies in respect of people living in Ontario and property situated in Ontario.
  - IPT rates are calculated on the gross premiums payable under life, accident and sickness, casualty and property contracts.
  - IPT rates are currently 2% for Life, Accident and Sickness, 3% for Casualty, and 3.5% for Property.
- In addition to the IPT, which is a corporate tax, Ontario applies 8% Retail Sales Tax to certain insurance premiums (including property insurance, group life and health insurance, but excluding individual life and health insurance and auto insurance). Quebec (9% QST) and Manitoba (8% RST) also apply provincial sales tax to insurance premiums in addition to the IPT.
  - While the HST does not apply to insurance premiums, insurance companies generally do not receive input tax credits.
- Based on all types of insurance, IPT revenue is approximately $1.2 billion annually (or 10% of corporate income tax revenue) and is paid by about 1,200 companies.
- Ontario currently has the lowest IPT rates for casualty insurance and life, accident and sickness insurance and the 2nd lowest IPT rate on property insurance of all the provinces.
  - If Ontario increased its IPT rates by 1 percentage point, compared to other provinces:
    - Life, Accident, and Sickness IPT rates would move from the lowest to 4th lowest; Casualty IPT rates would move from the lowest to 5th lowest; and, Property IPT rates would move from 2nd lowest to 6th lowest.

Potential Revenue Tools: Insurance Premium Tax

- Alberta and Newfoundland recently increased their IPT rates by 1 percentage point.
  - Alberta announced the IPT rate increase on March 26, 2015 (2015 Budget), effective April 1, 2016
  - Newfoundland announced the IPT rate increase on April 14, 2016 (2016 Budget), effective July 1, 2016.
- All of Ontario's 5 major banks own separate insurance companies that offer some type of insurance to consumers.
- Most U.S. states impose "retaliatory taxes" on insurance premiums for "foreign" insurers operating in the state's jurisdiction, but incorporated out of state. The retaliatory tax is computed as the difference between a state's IPT, licenses and other fees (in aggregate) and that of the jurisdiction in which the insurance company is incorporated.
  - In 1976, Ontario increased its IPT rates however the change was reversed for life and health premiums in the 1978 Budget because of retaliatory taxes applied by U.S. States to Ontario-based insurance companies operating in the U.S.
  - Unlike other provinces, Ontario has a number of life insurers with U.S. operations which could be subject to additional retaliatory taxes on their U.S. business.
- Automobile insurance has been excluded from this option to conform to Ontario's commitment to lower the cost of auto insurance for Ontario's nearly ten million drivers.
  - Insurance companies cannot cross subsidize the cost of higher IPT rates on life, health and property insurance by increasing auto insurance premiums because the Financial Services Commission of Ontario (FSCO) approves rates that insurers can charge for private passenger auto insurance.
- Increased cost of the IPT to insurance companies would likely be passed on to consumers.
- Stakeholder organizations would likely oppose any increase to the IPT (e.g., Canadian Life and Health Insurance Association, Insurance Bureau of Canada, Insurance Brokers Association of Ontario).
- Would require legislative amendments to the *Corporations Tax Act* and the *Taxpayer Protection Act*, 1999.
- The potential impact of this option on the Ontario insurance industry is uncertain since the impact on specific insurance companies would be based on several factors such as the location of operations, corporate structure and type of insurance products offered.
  - In general, IPT revenue is estimated to change from approximately $1.2 billion to $1.5 billion annually.

Potential Revenue Tools: Increase Education Property Tax Revenue

Preliminary Cumulative Estimate ($ millions)	2016-17	2017-18	2018-19	2019-20	2020-21
Increase Education Property Tax (EPT) Revenue adjustment to 2% from 1%	25	85	180	310	460

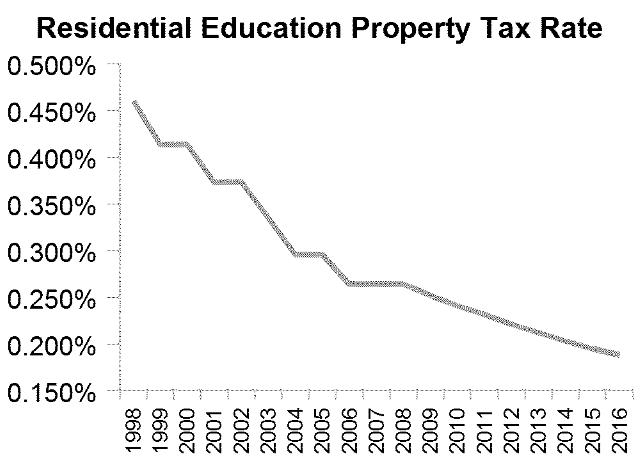
Considerations

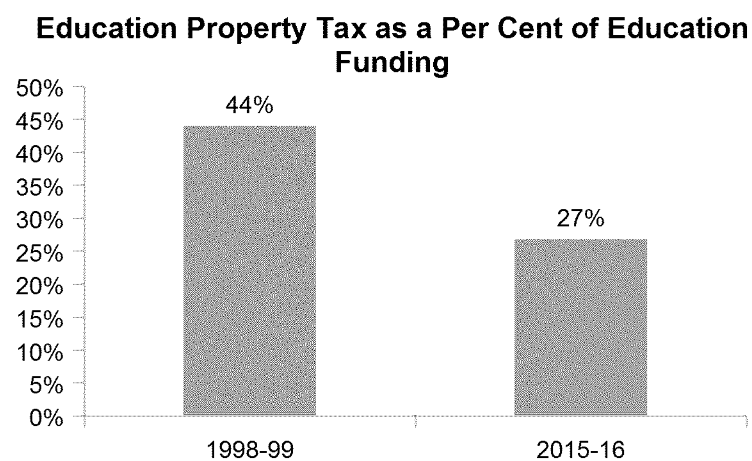
- The *2016 Budget* announced technical adjustments to the provincially prescribed property tax rate calculation used to set annual municipal and EPT rates.
  - This technical adjustment included a 1% EPT revenue increase for 3 years (starting in 2016) to account for current and historical in-year changes such as assessment appeal losses.
- The 1% adjustment was successfully implemented in 2016 with virtually no stakeholder reaction from municipalities or taxpayers. As a result, there may be an opportunity to adjust EPT rate setting policy going forward.
- Under the proposed option, the planned 2017 1% annual technical adjustment would be increased to 2%. Continued annual 2% increases would raise more than $450M by 2020-21.
  - By contrast, freezing EPT at the 2016 rates could raise more than $1.2 billion by 2020-21, which would be equivalent to an annual EPT revenue increase of approximately 5%.
- Given that EPT rates would continue to decrease under this proposal, this option could be implemented without amending the Taxpayer Protection Act.
  - However, there is a risk that larger EPT increases could be criticized as a tax increase
  - While the impact on Ontario homeowners would vary based on property value, the average impact in 2017 would be $7, or approximately $2 for every $100,000 of assessed value.
- Consideration would have to be given to how this option would be communicated, as the previous change was designed as a temporary technical adjustment.

Potential Revenue Tools: Increase Education Property Tax Revenue

Context:

- Since 1998, EPT rates have been reset annually to offset reassessment impacts.
  - For example, residential EPT rates have been reduced by 55% since 1998, from 0.460% to 0.188% in 2016.
- As a result, the share of education expenditures funded by property taxes has decreased from nearly 44% in 1998-99 to 27% currently.
- Therefore, it has been necessary for provincial transfers to school boards to offset the decline in the share of education expenditures funded by property taxes.
- If EPT had been maintained at 44% of education funding, provincial EPT revenues would have been $4.2B higher annually.
- This option is consistent with EPT revenue policies used in other jurisdictions, such as British Columbia, where the school tax rate is reset annually to allow revenues to increase by the rate of inflation.
  - There has been minimal criticism of the province's policy for school tax rate setting
- Revenue projections are based on estimated reassessment impacts. Beyond 2021, there is an increased risk that revenue projections would be affected by lower than anticipated reassessment impacts.





Potential Revenue Tools: Reform of Corporate Meals and Entertainment Tax Allowances

Preliminary Estimate ($ millions)	2016-17	2017-18	2018-19	2019-20	2020-21
Corporate Meals and Entertainment (M&E) Tax Allowances Lobby the federal government to remove the 50% income tax deduction on M&E expenses.	20	170	250	340	340

*Estimates are based on 2016 federal tax expenditures and assume a Jan. 1, 2017 effective date phased-in over 4 years.

Considerations

- Businesses can also qualify for a 50% input tax credit (ITC) for Harmonized Sales Tax (HST).
- M&E involves a personal benefit but the benefit is not taxed in the hands of the recipient.
- Some entertainment expenses (club dues, golf green fees) currently do not give rise to any income tax deduction or ITC.
- In the 2016 federal Budget the federal government announced they would be undertaking a comprehensive review of federal tax expenditures.
  - The tax treatment of corporate meals and entertainment may be included in the federal tax expenditure review.
- Ontario could request that the federal government review federal legislation to remove this tax preference.
  - The restriction on M&E could also be focused on certain items (e.g. corporate boxes, unreasonable meal expenses, etc.)
  - An Ontario administered alternative (e.g., surtax) would not be viable.
- In 2012, Minister Duncan wrote a letter to the federal Minister of Finance requesting that certain business expenses such as private seats and corporate boxes not be subsidized for corporate or sales tax purposes.
  - The federal government did not make any changes with respect to this request.
- A change of this nature would directly impact companies claiming the deduction and could have indirect impacts on the hospitality industry. The extent of these impacts would require further analysis.

Potential Revenue Tools: Revenue Integrity

Tax Avoidance

- A new unit reporting to MOF and MAG will expand the capacity to review policy and legislation to identify gaps and tax avoidance opportunities. The unit will leverage private-sector expertise and focus on federally-administered income taxes. The new unit will develop up-to-date anti-avoidance measures in cooperation with the federal government. This will build on previous and ongoing measures to strengthen Ontario taxes (e.g., Employer Health Tax, Land Transfer Tax).

Corporate Transparency and Beneficial Ownership

- TPD and MGCS staff are participating in a federally-led working group to strengthen corporate transparency and ensure Canadian corporations are not used for criminal activities, such as money laundering, or evading tax obligations to Canadian or foreign governments.

Tax Evasion and Underground Economy

- The Ministry of Finance will explore additional opportunities to enhance revenue integrity through enhanced compliance partnerships with the Canada Revenue Agency.
- The ministry will continue to collaborate with others on initiatives aimed at addressing non-compliance with tax and other regulatory requirements in particular sectors of the economy.
- Leveraging recent legislative amendments, the Ministry of Finance will continue to work with key partners to identify areas at a high risk of underground economic activity through the integration and analysis of business-related data;
- The ministry will launch a pilot project in the retail and hospitality sectors to test software that prevents the use of sales suppression technology;
- The ministry will continue to work with municipal and provincial law enforcement, such as the Ontario Provincial Police's Contraband Tobacco Enforcement Team to address the presence of contraband tobacco; and
- The Province will raise awareness of the importance of revenue integrity and educate the public on the risks and potential liabilities associated with participation in the UE.