

BUDGET PAPER C: PERSONAL INCOME TAXES

This section presents more detailed information on the Prince Edward Island Personal Income Tax cut and the reductions associated with recent federal announcements. The paper also discusses the pattern of Personal Income Tax rates across Canada. Finally, the concept of Tax-on-Income is described.

PRINCE EDWARD ISLAND TAX REDUCTIONS

“The Provincial personal income tax rate, as expressed as a percentage of the Federal basic tax, will be reduced by a full percentage point, from 59.5 per cent to 58.5 per cent. Furthermore, this reduction will be effective January 1, 1999 so that Islanders will enjoy the full year benefit.” - Hon. Patricia J. Mella, April 6, 1999

This rate change will benefit all who pay Personal Income Tax on Prince Edward Island, some 65,000 Islanders. Coupled with Income Tax reductions at the federal level, this produces significant tax savings for Prince Edward Island.

The Federal Budget of February 16, 1999, announced two reductions to Personal Income Taxes which will take full effect in the 2000 tax year. The Federal Government increased the Basic Personal Exemption by \$675 and removed the income threshold that had been applied in 1998. It also eliminated the Federal Surtax paid by those earning income above \$50,000.

The increase in the basic exemption reduces provincial income tax paid by Prince Edward Islanders by \$4.6 million, given that the provincial tax is calculated as a percentage of an individual's Basic Federal Tax. The 1 percentage point rate reduction provides further annual savings of \$2.2 million.

Provincial income tax will thus fall by a total of \$6.8 million, a reduction of 5 per cent from current revenues.

The elimination of the federal surtax has no impact on provincial income tax, but will reduce federal tax paid by Islanders by an additional \$2.4 million when fully implemented. The change in the personal exemption itself reduces federal income tax by \$7.7 million. Thus combined provincial and federal tax announcements will lower total Personal Income Tax paid by Prince Edward Islanders by \$16.8 million by the year 2000. These changes are summarized in Table C.1.

Table C.1 - Full-year Savings⁽¹⁾ for Prince Edward Island Taxpayers, 1999 Budget Announcements

	All Island Taxpayers	Average Island Taxpayer
Provincial Tax Rate Decrease	\$2.2 million	\$34
Federal Tax Decreases - 1999 Budget	\$10.0 million	\$155
Induced Provincial Tax Decreases	\$4.6 million	\$71
Total Tax Reduction	\$16.8 million	\$260

NOTES:

⁽¹⁾ Provincial rate reduction effective January 1, 1999. Federal measures effective July 1, 1999, with full-year application in 2000.

Source: Provincial Treasury Estimates

PROVINCIAL PERSONAL INCOME TAX RATES

There has been considerable re-alignment of provincial tax rates in the past four years, with all provinces having introduced modest to pronounced reductions to various taxes. Ontario was the lead province in instituting their reductions to the Personal Income Tax (PIT) rate. Alberta followed and has been quite aggressive in meeting or bettering Ontario's rate reductions. The Prince Edward Island Government is conscious of the widening disparity in income tax rates between the richer and poorer provinces.

In 1997, Prince Edward Island introduced an exemption in its sales tax base for clothing and footwear. As well, the Province's removal of Video Lottery Terminals from non-licensed sites was a significant cut to provincial revenues. However, the Province has not adjusted its Personal Income Tax rate since 1991 when the rate was increased from 57 per cent. In response to tight financial circumstances, the Province's high income surtax threshold was lowered in 1997, which expanded the surtax base and increased its effective rate of the surtax.

This Budget extends tax relief to all Prince Edward Island taxpayers by cutting the tax rate to 58.5 per cent of Basic Federal Tax.

Between 1995 and 1998, Ontario cut its PIT rate from 58.5 per cent to 40.5 per cent of Basic Federal Tax. They also reduced their high income surtax and introduced tax credits for low income families. Such aggressive measures have been followed by other provinces - or bettered as in the case of Alberta. Alberta decreased its PIT basic rate to 44 per cent in 1999, down from 45.5 per cent. While this basic rate as a percentage of Basic Federal Tax is higher than in Ontario, Alberta's high income surtax, at 8 per cent, is lower than Ontario's, which can range as high as 53 per cent. British Columbia has had less fiscal room to cut their tax rates, but in the 1998 Budget, they decreased their PIT rate from 50.5 per cent to 49.5 per cent and decreased their surtax from 26 to 19 per cent on tax owing above \$8,660.

The following table shows the announced PIT rate changes by province from 1996 to 1999. Light

shading indicates a tax cut, darker shading shows a tax increase.

Table C.2 - Provincial Personal Income Tax Rates: 1996 and 1999

	Tax Rate		Surtax Rate			Surtax Threshold		Taxable Income At Surtax Threshold	
	1996	1999	1996	1999	1996	1999	1996	1999	
Newfoundland	69.0%	69.0%	10%	10%	\$7,900	\$7,900	\$59,813	\$59,816	
PEI	59.5%	58.5%	10%	10%	\$12,500	\$5,200	\$92,776	\$49,462	
Nova Scotia	59.5%	57.5%	10%	10%	\$10,000	\$10,000	\$78,287	\$80,301	
New Brunswick	64.0%	60.0%	8%	8%	\$13,500	\$13,500	\$93,070	\$96,646	
Québec ⁽¹⁾									
Ontario	56.0%	40.5%	low 20%	20%	\$5,310	\$4,058	\$52,323	\$52,356	
			high 33%	53%	\$7,635	\$5,218	\$67,347	\$62,419	
Manitoba ⁽²⁾	52.0%	50.0%							
Saskatchewan	50.0%	48.0%	15%	15%	\$4,000	\$4,000	\$39,203	\$40,839	
Alberta	45.5%	44.0%	8%	8%	\$3,500	\$3,500	\$45,400	\$46,450	
British Columbia	52.0%	49.5%	low 30%	30%	\$5,300	\$5,300	\$55,054	\$56,220	
			high 51.5%	49%	\$8,915	\$8,660	\$79,451	\$79,469	

LEGEND: Light Shading = TAX DECREASE Dark Shading = TAX INCREASE

NOTES:

⁽¹⁾ Quebec's personal income tax system is not directly comparable with other provinces. Moderate tax cuts were implemented between 1996 and 1999.

⁽²⁾ Manitoba's surtax is not directly comparable with other provinces. It was unchanged between 1996 and 1999.

Source: Provincial Treasury

Within the Maritimes, Nova Scotia dropped its PIT rate from 59.5 to 57.5 in 1998. New Brunswick reduced its rate from 63 to 61 per cent in 1998 and to 60 per cent in 1999, and has made a commitment to further reductions as fiscal conditions permit.

TAX-ON-INCOME

Revenue Canada collects Personal Income Taxes on behalf of all provinces, with the exception of the Province of Quebec. Ontario, Quebec and Alberta also administer their own corporate income taxes. The collection of income taxes by Revenue Canada is governed by Federal Provincial Tax Collection Agreements (TCA's) and all provinces have the right to administer their own taxes if they so choose. However there are significant administrative costs involved with independent provincial administration. In addition there are enormous advantages to Canadians in having a common tax system across the country for both levels of government. Revenue Canada administers the collection of provincial income taxes at essentially no cost to provinces, although special provincial tax credits involve administration charges.

Under the present TCA's provinces express their tax rate as a percent of Basic Federal Tax. Prince

Edward Island's rate is 58.5 per cent in 1999.

The Federal Government has agreed to amend the TCA's to allow provinces to levy a provincial income tax directly on Taxable Income rather than to compel provinces to raise their taxes as a percentage of Basic Federal Tax. Revenue Canada has indicated that this system will be available in 2001. For an Island taxpayer in the 17 per cent federal bracket, for example, the effective rate of provincial tax on income is 10 per cent in 1999. Thus this new system should provide a more clear indication to Island taxpayers of their actual rate of provincial income tax.

The new system will also allow provinces to establish their own income brackets and rates of tax on these brackets, entirely independently from the federal brackets and rates. Federal rate changes would therefore not alter the provincial tax, as happens at present. Provinces will also be able to establish a distinct block of non-refundable tax credits, such as personal exemptions, to be multiplied by the lowest provincial tax rate. However all provinces would still be required to accept the federal definition of taxable income.

Provinces will be able to move from the present Tax on Tax system to this new Tax on Income system at their discretion after 2001. Some provinces such as Alberta have already indicated their intention to do this. The Government of Prince Edward Island will assess the desirability of this fundamental change in the interim years.