

BUDGET PAPER C: PERSONAL INCOME TAXES

This section presents detail on the changes to Provincial Personal Income Taxes which become effective during fiscal year 2000-01.

I. PRINCE EDWARD ISLAND TAX REDUCTIONS

“In 1999 I was pleased to put into effect the Province’s first ever reduction to our Personal Income Tax rate. Today I am taking tax reduction even further. I am pleased to announce a significant program of income tax measures for 2000 and beyond that will deliver broad-based reductions for all taxpayers and targeted reductions for thousands of low income Island families.”

- Hon. Patricia J. Mella, March 17, 2000.

Three complementary provincial income tax reduction measures take effect in the 2000 Taxation Year which will reduce income tax paid by Prince Edward Islanders by a total of \$10 million in 2000 and \$12.2 million in 2001, when all measures will be in full effect. This represents 7 per cent of total provincial income tax collections. In conjunction with the tax reductions introduced in the 2000 Federal Budget, new measures introduced this year will result in a tax cut for Islanders of \$24 million in 2001.

These tax reduction measures will be incorporated in full into a new Tax on Income system in 2001.

The combined Prince Edward Island tax reductions in the 1999 and 2000 provincial budgets total \$19.0 million, which amounts to a provincial income tax cut of 12 per cent. When added to federal reductions from both years, annual Personal Income Tax savings for Prince Edward Islanders are \$41.1 million, as detailed in Table C.1.

Table C.1 - Full-year Savings for Prince Edward Island Taxpayers: 1999 and 2000 Budget Announcements

	1999 Budget	2000 Budget ⁽¹⁾	Total
A. Provincial Tax Rate Decrease	\$2.2 million	\$2.2 million	\$4.4 million
B. Low Income Tax Reduction		\$3.0 million	\$3.0 million
C. Pass-Through Federal Tax Reductions	\$4.6 million	\$7.0 million	\$11.6 million
Total Provincial Income Tax Reductions	\$6.8 million	\$12.2 million	\$19.0 million
Total Federal Income Tax Reductions	\$10.1 million	\$12.0 million	\$22.1 million
Total Tax Reductions on PEI	\$16.9 million	\$24.2 million	\$41.1 million

⁽¹⁾ Provincial rate reduction and Low Income Tax Reduction effective January 1, 2000. Bracket measures effective July 1, 2000, with full-year application in 2001.

Source: Provincial Treasury Estimates

A. Prince Edward Island General Tax Rate Reduction

Effective January 1, 2000 Prince Edward Island’s Personal Income Tax rate is reduced by a full percentage point, from the current 58.5 per cent to 57.5 per cent of Basic Federal Tax. This measure will reduce tax payable for each of Prince Edward Island’s 66,300 taxpayers by a total of \$2.2 million in 2000/01.

This rate reduction follows Prince Edward Island’s first ever income tax rate decrease in 1999, when the general tax rate was reduced from 59.5 per cent to 58.5 per cent.

B. Low Income Tax Reduction

Prince Edward Island will introduce a Low Income Tax Reduction program, effective January 1, 2000, which will reduce Provincial Personal Income Tax for low income families, and eliminate it altogether in many cases.

The Low Income Tax Reduction will eliminate provincial income tax for an estimated 4,860 low income tax payers and provide benefit to total of 17,200 Island individuals and families. All told 26 per cent of Islanders who pay tax will benefit from this measure. The impact of this measure will be to reduce tax payable by \$3 million in 2000/01.

The Prince Edward Island Low Income Tax Reduction is a non-refundable credit which is based on family size and combined family income. The value of the credit is the sum of :

- a) \$250
- b) \$250 for the spouse or equivalent-to-spouse
- c) \$200 for each dependent child;

It applies in full to families whose combined income is \$15,000 or less and at a reduced rate for families with income in excess of \$15,000. Each family calculates its maximum credit which is then reduced by 5 per cent of the combined family income in excess of \$15,000. The credit applies up to the amount of provincial tax payable.

For example, a married couple with three children and a combined family income of \$23,000 is eligible for a credit of \$700 which is calculated as follows:

**Table C.2 - Calculating the Low Income Tax Reduction - Credit Amounts
Married couple with three children, Combined Family Income of \$23,000**

	<i>Wife</i>	<i>Husband</i>	<i>3 Children</i>		<i>Gross Credit</i>
Total credits for 5 family members =	\$250 +	\$250 +	(3 x \$200)	=	\$1,100
<i>minus</i>					
<u>Income reduction amount</u>	=	<i>5% of family income in excess of \$15,000</i>		=	<u>- \$400</u>
Low Income Tax Reduction					\$700

This married couple with three children and an income of \$23,000 would pay approximately \$663

in provincial Personal Income Tax in 2000 before the Low Income Tax Reduction. With the Low Income Tax Reduction in place, this family will apply its credit of \$700 against the \$663 in tax payable, to reduce their provincial income tax to \$0.

Subject to confirmation by Canada Customs and Revenue Agency (formerly Revenue Canada), it is intended that Prince Edward Island's Combined Family Income will be calculated as Net Income (line 236) for single individuals or the sum of Net Income for married or common-law couples. It is further intended that the value of the credit will be transferable between spouses, so that any amount not used by one spouse may be used to reduce taxes payable by the other.

Further examples are presented below for a range of family types and income levels. Several examples are calculated for families with incomes greater than \$15,000 to show how the credit reduction interacts with provincial tax payable.

Table C.3 - Low Income Tax Reduction Examples by Family Type and Income

<p><i>Example 1 - Single person with no children</i> A single individual earning \$15,000 with no children is eligible for the maximum credit of \$250 that will reduce that person's typical provincial income tax payable from \$583 to \$333.</p> <p><i>Example 2 - Single person with two children</i> A single parent earning \$20,000 who has two children is eligible for a credit of \$450 that will reduce that family's typical provincial Personal Income Tax payable from \$408 to \$0.</p> <p><i>Example 3 - Married couple with two children</i> A single-earner family with two children and \$22,000 in annual income typically pays \$578 in provincial tax and so their credit of \$550 will reduce their provincial income tax to \$28.</p> <p><i>Example 4 - Single senior with no dependents</i> A single senior with income of \$15,000 will be credited \$250 in Low Income Tax Reduction that will reduce his/her tax payable from a typical amount of \$284 to \$34.</p>

There are some 32,300 tax filers who currently pay no provincial tax. With the Low Income Tax Reduction in place, this figure will rise to 37,200. Depending on family type, the threshold at which Islanders begin to pay tax will be significantly higher under the new program. For example, a single person living alone currently begins to pay provincial tax at an annual income of approximately \$7,500. With the Low Income Tax Reduction, no tax will be payable below approximately \$10,440 in annual income.

This tax measure will be of particular benefit to single parents, seniors and families with children. The Low Income Tax Reduction will provide tax relief to 42.7 per cent of all single parents and will eliminate provincial tax entirely for 11.2 per cent of this group. Slightly more than 50 per cent of all seniors on Prince Edward Island will benefit from the tax reduction. By far the most broadly affected group of tax payers to benefit will be families with several children. The Low Income Tax Reduction will provide tax relief to 76.3 per cent of all families with more

than two children.

Among tax payers with annual family incomes less than \$25,000, 93 per cent will see provincial taxes reduced and 24 per cent will be removed from provincial income tax rolls.

C. Pass-Through Federal Tax Reductions

Prince Edward Island is committed to passing through the full benefit of tax reductions that were announced in the federal budget. The Province's lowered income tax rate of 57.5 will apply to the 2000 federal tax base and so tax payers will benefit both from federal tax reductions and induced reductions to their provincial tax payable.

Specifically, the impact of the upward revision to the Basic Personal Amount and income thresholds identified in the federal budget, as well as the reduction in the middle income tax rate from 26 per cent to 24 per cent in 2001, will be passed through to the full benefit of Island tax payers.

These tax reduction measures will form the basis of Prince Edward Island's Tax on Income system that will come into effect in 2001, as will be discussed below.

D. Combined Tax Savings

The impact of these tax reduction measures will vary with income and family structure. Table C.4 presents several examples of typical tax savings from 2000 budget measures.

Table C.4 - Combined Tax Savings, By Family Type and Annual Income: 2001

	Single Pensioner	Single Parent 1 Child	Married Couple 2 Children	
Income	\$15,000	\$18,000	\$20,000	\$45,000
A. General Rate Change	\$11	\$7	\$9	\$60
B. Low Income Tax Reduction	\$250	\$331	\$251	-
C. Induced Provincial Changes	\$23	\$42	\$42	\$261
Total Provincial Reductions	\$284	\$380	\$302	\$321
Total Federal Reductions	\$39	\$72	\$72	\$448
Provincial & Federal Reductions	\$323	\$452	\$374	\$769

Source: Provincial Treasury Estimates

II. TAX ON INCOME

Beginning in 2001, Prince Edward Island, and other provinces, will adopt a new approach to calculating provincial Personal Income Taxes that will enhance transparency of the tax system and allow the Province greater autonomy in devising income tax policy.

Prince Edward Islanders will continue to file a single Personal Income Tax return to Canada Customs and Revenue Agency (CCRA, formerly Revenue Canada), but the new tax return will specify provincial income thresholds, tax rates and non-refundable credits, such as the Basic Personal Exemption and Spousal Amounts.

The collection of income taxes by CCRA is governed by Federal Provincial Tax Collection Agreements 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 major advantages to Canadians in having a common tax system across the country for both levels of government. This will continue under the Tax on Income system.

Under the present Tax on Tax system familiar to Canadians, provinces express their tax rate as a percent of Basic Federal Tax. In the case of Prince Edward Island, the rate was 59.5 per cent in 1998, falling to 58.5 per cent in 1999 and to 57.5 per cent in 2000. The Federal Government has agreed to administer provincial income tax as a percentage of Taxable Income rather than as a percentage of Basic Federal Tax. Under the new system Island taxpayers will see their true rate of provincial income tax on taxable income.

In addition to setting provincial income brackets and rates of tax on these brackets, 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 will still be required to accept the federal definition of taxable income. The new system means that most federal tax changes will no longer result in automatic changes to provincial tax revenues.

Prince Edward Island Tax Rates and Thresholds - January 1, 2001

“In its move to a Tax on Income system, Prince Edward Island will adopt the federal income thresholds and rates that will be effective on January 1, 2001 and so ensure that the tax reductions for 2001 described in the federal Budget are passed on in full to Island tax payers.”

- Hon. Patricia J. Mella, March 17, 2000

To ensure that the move to Tax on Income in 2001 is revenue neutral for Island tax payers, the Government of Prince Edward Island will base its new provincial income tax rates and brackets on the rates and thresholds used by the Federal Government *effective January 1, 2001* as

specified in the Federal Budget of February 29, 2000.

A straight conversion of the current provincial Tax on Tax rate of 57.5 per cent to a system of provincial income tax brackets and rates is accomplished by multiplying federal rates by that same 57.5 per cent to determine the equivalent provincial rates. These figures are presented in Table C.5.

Table C.5 - Estimated ⁽¹⁾ Income Tax Rates and Thresholds: January 1, 2001

Effective Federal Tax Brackets	Federal Tax Rate	Provincial Tax Rate	
		Calculation	Rate
\$0 - \$7,361	0%	0% x 57.5%	0%
to \$30,544	17%	17% x 57.5%	9.8%
to \$61,089	24%	24% x 57.5%	13.8%
above \$61,089	29%	29% x 57.5%	16.7%

⁽¹⁾ The 2000 Federal Budget documents did not specify exact thresholds for January 1, 2001. The thresholds used here are based on the 2000 income thresholds and basic personal amount, increased by an estimated inflation factor of 1.8%.

Source: Provincial Treasury Estimates

Prince Edward Island will mirror the federal income tax system entirely in its first year of Tax on Income. The Province will maintain its new Low Income Tax Reduction and its previously established credits and surtax under the new system. Prince Edward Island will accept the January 2001 federal Basic Personal Amount of approximately \$7,361, below which no tax is payable. Thus Prince Edward Island will have three taxable income brackets with a low bracket rate of 9.8%, a middle bracket rate of 13.8% and a top bracket rate of 16.7%.

Prince Edward Islanders will first see the new provincial Tax on Income forms in the spring of 2002 when they complete their tax returns for the 2001 Taxation Year.