

Tax Memo

2009 Ontario Budget: Harmony in Sales Tax and Cuts in Corporate Tax

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Introduction

On Thursday, March 26, 2009, Ontario's Minister of Finance, Dwight Duncan, presented the province's 2009 budget. As expected, the budget introduces a blended sales tax rate of 13% on July 1, 2010. The budget also includes other significant tax changes.

For corporations, the general income tax rate will decrease in stages from 14% to 10% by July 1, 2013, while on July 1, 2010, the manufacturing and processing rate will decline from 12% to 10% and the small business rate will drop from 5.5% to 4.5%. As well, for taxation years ending after June 30, 2010, the Corporate Minimum Tax (CMT) rate will be reduced to 2.7% and the asset and revenue thresholds above which the CMT will apply will increase.

On January 1, 2010, the lowest personal income tax rate will drop, but the thresholds at which the surtax applies will be reduced. Commencing 2010, the dividend tax credit rate will decrease on both eligible and non-eligible dividends, as a result of proposed corporate tax rate reductions.

The budget also enhances several targeted tax incentives, including film and digital media incentives, the Ontario Innovation Tax Credit and tax credits that support employee training.

For more information on how these measures affect you or your corporation, please contact your PricewaterhouseCoopers adviser or any of the individuals listed on our website at www.pwc.com/ca/taxcontacts.

Business Tax Measures

Corporate income tax rates

The budget decreases corporate income tax rates as follows:

Effective date ¹		General rate	M&P rate	Small business rate	Small business deduction surtax rate ²	
					General	M&P
					Before July 1, 2010	14%
July 1, 2010	12%	10%	4.5%	0%		
July 1, 2011	11.5%					
July 1, 2012	11%					
July 1, 2013	10%					

- Rates are pro-rated for taxation years straddling the effective date.
- A surtax claws back the benefit of the small business deduction when taxable income of associated corporations exceeds \$500,000 and eliminates it completely once taxable income, on an associated basis, reaches \$1,500,000. The surtax will be eliminated on July 1, 2010.

Combined corporate income tax rates

As a result of previously announced federal changes and Ontario's budget announcement on corporate income tax rate reductions, the following combined federal/Ontario rates apply to December 31 year ends:

- General and manufacturing income:

	General ¹	M&P
2008	33.5%	31.5%
2009	33%	31%
2010	30.99%	28.99%
2011	28.25%	26.5%
2012	26.25%	25%
2013	25.50%	
2014	25%	

- The rates do not apply to the income of credit unions, most deposit insurance corporations, mutual fund corporations, mortgage investment corporations and investment corporations.

- Canadian-controlled private corporations:

	Active business income				Investment income
	To \$400,000	\$400,000 to \$500,000	\$500,000 to \$1,500,000		
			Non-M&P	M&P	
2008	16.5%	25%	37.75%	34.75%	48.67%
2009	16.5%		37.25%	34.25%	
2010	16%		33.10%	30.60%	47.66%
2011	15.5%		28.25%	26.5%	46.41%
2012			26.25%		45.92%
2013			25.50%	25%	45.16%
2014			25%		44.67%

Corporate Minimum Tax

The budget decreases the corporate minimum tax (CMT) rate and increases the thresholds at which corporations are subject to CMT, as follows:

CMT rate	For taxation years ending	
	before July 1, 2010	after June 30, 2010
4%	\$5 million	\$50 million
2.7%	\$10 million	\$100 million

- Thresholds apply on an associated basis.

Capital taxes

The budget does not revise capital tax rates. Capital tax:

- was eliminated on January 1, 2007, for certain manufacturing and resource corporations; and
- will be eliminated on July 1, 2010, for other corporations.

Film and digital media incentives

The budget contains measures that demonstrate Ontario's commitment to the Entertainment and Creative Cluster and the importance of the growing digital media sector. These measures include enhancements to the province's film and digital media tax credits.

Ontario Film and Television Tax Credit and Ontario Production Services Tax Credit

The Ontario Film and Television Tax Credit (OFTTC) is a refundable tax credit for labour expenditures related to certified domestic film and television productions in Ontario. The Ontario Production Services Tax Credit (OPSTC) is a refundable tax credit for labour expenditures related to qualifying foreign film and television production services and non-certified domestic film and television productions in Ontario.

The budget repeats a recent announcement that makes both the 35% OFTTC rate and the 25% OPSTC rate permanent. These rates had been scheduled to drop to 20% and 11%, respectively, for labour expenditures incurred after December 31, 2009.

Ontario Interactive Digital Media Tax Credit

The Ontario Interactive Digital Media Tax Credit (OIDMTC) is a refundable tax credit that reduces the cost of developing interactive digital media products, such as video games, certain electronic products and interactive websites, in Ontario.

The budget proposes the following permanent enhancements to the OIDMTC for qualifying expenditures incurred after March 26, 2009:

- the credit rates will increase to:
 - 40% for all qualifying corporations, regardless of size, that develop and market their own eligible products, up from 30% for small corporations and 25% for large corporations; and
 - 35% for corporations that develop eligible products under a fee-for-service arrangement, up from 25%;
- the OIDMTC will be extended to digital media game developers that incur a minimum of \$1 million of eligible labour expenditures over a 36 month period for fee-for-service work done in Ontario in respect of an eligible product. The requirement to deal at arm's length with the purchaser and to develop all, or substantially all, of the eligible product in Ontario will not apply to corporations that meet the minimum expenditure test;
- corporations will be allowed to claim 100% of payments to eligible arm's length contractors that are attributable to the salaries and wages of the contractor's employees, up from 50% for corporations that develop and market their own products and nil if the eligible products were developed under a fee-for-service arrangement.

Ontario Computer Animation and Special Effects Tax Credit

The Ontario Computer Animation and Special Effects (OCASE) tax credit is a 20% refundable tax credit for eligible labour expenditures related to digital animation and special effects in qualifying film and television productions.

Enhancements to the OCASE for qualifying expenditures incurred after March 26, 2009:

- increase eligible labour expenditures to 100% from 50% paid to arm's length unincorporated individuals and partnerships providing freelance services;
- expand eligible labour expenditures to include 100% paid to arm's length incorporated individuals providing freelance services (however, the incorporated individual is precluded from claiming the credit directly); and
- streamline administration by relaxing the requirement that an eligible animation or visual effect be created primarily with digital technologies.

Ontario Innovation Tax Credit (OITC)

The budget enhances Ontario's scientific research and experimental development (SR&ED) incentives by paralleling enhancements to the federal SR&ED tax credit proposed in the 2009 federal budget. The Ontario enhancements, which will be introduced after the implementing federal legislation is enacted, will apply if the previous taxation year ends after 2008. The changes are as follows:

		Existing	Proposed
OITC expenditure limit		\$3 million	
Phase-out range	Taxable income	\$400,000 to \$700,000	\$500,000 to \$800,000
	Taxable capital	\$25 million to \$50 million	

Ontario Book Publishing Tax Credit

Ontario's Book Publishing Tax Credit is a 30% refundable tax credit for Ontario book publishing corporations. For qualifying expenditures incurred after March 26, 2009:

- there is no limit on the number of books by a Canadian author in an eligible category of writing that will qualify for the credit (previously only the first three of these books qualified); and
- direct expenses that reasonably relate to publishing an electronic version of an eligible book will qualify for the credit.

Tax credits that support employee training

The budget enhances tax credits that encourage employers to hire and train employees.

Co-operative Education Tax Credit

The Co-operative Education Tax Credit is a refundable tax credit that is available to businesses that employ post-secondary school students who are enrolled in a qualifying co-operative education program at eligible educational institutions. Enhancements that apply to eligible expenditures incurred after March 26, 2009:

- increase the credit rates to:
 - 30% from 15% for small businesses; and
 - 25% from 10% for others; and
- increase the maximum tax credit to \$3,000 from \$1,000 per placement.

Apprenticeship Training Tax Credit

The Apprenticeship Training Tax Credit (ATTC) provides corporations and unincorporated businesses a refundable tax credit on salaries and wages paid to eligible

apprentices. Enhancements that apply to expenditures incurred after March 26, 2009:

- increase the credit rates:
 - from 30% to 45% for small businesses; and
 - from 25% to 35% for others;
- increase the maximum annual credit from \$5,000 to \$10,000;
- provide that salary and wages paid during the first 48 months (up from the first 36 months) of an apprenticeship program will be eligible for the credit; and
- make the ATTC permanent (previously, it was available only for apprentices who begin their apprenticeship program before January 1, 2012 and salaries and wages paid before January 1, 2015).

Ontario political contributions

The budget repeats a December 30, 2008 announcement that the tax deduction that was available to corporations making eligible Ontario political contributions will be converted into a non-refundable tax credit, effective for taxation years ending after December 31, 2008.

Personal Tax Measures

Personal income tax rates

The budget reduces Ontario's lowest tax rate on January 1, 2010 as follows:

		2008	2009	2010
Ontario income tax rates and thresholds	Highest	11.16%		
		\$72,041	\$73,698 ¹	
		9.15%		
		\$36,020	\$36,848 ¹	
	Lowest	6.05%		5.05%
		\$0		

1. Thresholds will be indexed for 2010.

Surtax rates

The budget does not change the surtax rates, but does decrease the surtax thresholds for 2010 as follows:

	2008	2009	2010
2 nd -tier tax rate		36%	
Ontario tax	> \$5,249	> \$5,370	> \$5,091 ¹
1 st -tier tax rate		20%	
Ontario tax	> \$4,162	> \$4,257	> \$3,978 ¹

1. The 2010 threshold will be further adjusted for inflation.

Top 2009 Personal Tax Rates

Top combined 2009 personal tax rates are outlined in the table below. The budget did not reduce the top marginal tax rate for ordinary income or capital gains.

Top 2009 Personal Tax Rates

(Taxable income above \$126,264)	Ordinary income & interest	Capital gains	Canadian dividends	
			Eligible	Non-eligible
Federal only	29.00%	14.50%	14.55%	19.58%
Alberta	39.00%	19.50%	14.55%	27.71%
British Columbia	43.70%	21.85%	19.92%	32.71%
Manitoba	46.40%	23.20%	23.83%	38.21%
New Brunswick	46.00%	23.00%	21.80%	34.21%
Newfoundland and Labrador	44.50%	22.25%	27.38%	32.71%
Non-resident ¹	42.92%	21.46%	21.53%	28.98%
Northwest Territories	43.05%	21.53%	18.25%	29.65%
Nova Scotia	48.25%	24.13%	28.35%	33.06%
Nunavut	40.50%	20.25%	22.24%	28.96%
Ontario	46.41%	23.20%	23.06%	31.34%
Prince Edward Island	47.37%	23.69%	24.44%	38.15%
Quebec	48.22%	24.11%	29.69%	36.35%
Saskatchewan	44.00%	22.00%	20.35%	30.83%
Yukon	42.40%	21.20%	17.23%	30.49%

1. Non-resident rates for interest and dividends apply only in limited circumstances.

The table below shows the combined federal and Ontario income tax payable at various income levels and the additional tax due to the health premium.

		Approximate combined tax excluding the Health Premium		Addition due to Health Premium	
		2008	2009	2008	2009
		Taxable income	\$500,000	\$213,688	\$212,888
	\$250,000	\$97,664	\$96,864		\$900
	\$150,000	\$51,254	\$50,454		\$750
	\$100,000	\$28,745	\$28,037		\$600
	\$50,000	\$9,841	\$9,497		\$300
	\$30,000	\$4,350	\$4,230		\$300

Dividend tax rates

As a result of proposed corporate tax rate reductions, commencing 2010, the dividend tax credit rate will decrease:

- for eligible dividends from 7.7% to 6.4%; and
- for non-eligible dividends from 5.13% to 4.5%.

These and previously announced Ontario and federal changes follow:

	Eligible dividends (%)				
	2008	2009	2010	2011	After 2011
Dividend gross-up	45				
Dividend tax credit (on grossed-up dividend)	7	7.4	6.4		
Top combined rate	23.96	23.06	26.57	28.19	29.54

1. Assumes top federal/Ontario marginal income tax rate remains 46.41%.

	Non-eligible dividends (%)		
	2008	2009	After 2009
Dividend gross-up	25		
Dividend tax credit (on grossed-up dividend)	5.13		4.5
Top combined rate	31.34		32.57

1. Assumes top federal/Ontario marginal income tax rate remains 46.41%.

The increasing effective tax rates after 2009 on eligible and non-eligible dividends are intended to ensure that combined corporate and personal tax on business income earned through a corporation is roughly the same as the tax payable by an individual who earns that income directly.

Harmonization relief

Payments to eligible individuals

To smooth the transition to the harmonized sales tax system, payments will be made to eligible individuals in each of June 2010, December 2010 and June 2011. Ontario tax filers aged 18 and over with incomes below \$82,000 for singles and \$166,700 (\$166,600 for June 2010) for families will qualify. The maximum total benefit will be \$300 for single individuals and \$1,000 for single parents or couples.

Ontario Property Tax Credit and Ontario Sales Tax Credit

The existing combined property and sales tax credits will be replaced by two separate credits commencing in 2010:

- the Ontario Sales Tax Credit will be refundable and paid quarterly starting July 2010. The maximum annual benefit will be \$260 for each adult and child, but will be reduced by 4% of family income over \$20,000 for single people and \$25,000 for families.
- the Ontario Property Tax Credit will be capped at \$900 for non-seniors and at \$1,025 for seniors. The credit will be reduced by 2% of family income over \$20,000 for single people and \$25,000 for families.

Tax relief for seniors

Senior Homeowners Property Tax Grant

The budget confirms Ontario's 2008 budget announcement that the Senior Homeowners Property Tax Grant will increase from \$250 to \$500 in 2010. The maximum grant can be obtained by seniors who pay at least \$500 in property taxes and have incomes not exceeding \$35,000 for single seniors or \$45,000 for senior couples. The maximum grant is reduced proportionately when income exceeds these thresholds and is eliminated once income reaches \$50,000 for single seniors and \$60,000 for senior couples.

Seniors apply for the grant when filing their income tax returns.

Property and Sales Tax Credits for Seniors

The budget increases the income threshold at which the Ontario Property and Sales Tax Credits for senior couples are reduced. The new threshold will be announced when the federal government finalizes the Old Age Security and Guaranteed Income Supplement amounts for 2009.

As mentioned above, commencing 2010, this credit will be replaced with a new Ontario Sales Tax Credit and new Ontario Property Tax Credit.

Ontario Child Benefit

The 2007 budget introduced the Ontario Child Benefit (OCB) to assist low-income families with children under age 18. The OCB was to be phased in over five years when the maximum annual OCB level per child would increase to \$1,100 starting July 1, 2011. This budget accelerates the maximum annual \$1,100 OCB to July 1, 2009. The budget also states that the government is committed to a maximum OCB level of \$1,310 annually per child within five years.

Locked-In Accounts

The following changes will increase access to locked-in accounts:

- commencing January 1, 2010, unlocking permitted on purchase from new Life Income Funds (LIFs) will increase from 25% to 50%, allowing new LIF owners to unlock an additional 25% of amounts previously transferred into their existing fund (remaining old LIFs and Locked-in Retirement Income Funds (LRIFs) will be harmonized with the new rules, and current new LIF owners can unlock the additional 25%); and
- financial hardship application withdrawal fees for Ontario locked-in accounts will be waived for two years for applications approved after March 31, 2009.

Ontario Sales Tax Harmonization

Commencing July 1, 2010, Ontario's Retail Sales Tax will be converted to a value-added tax. It will be combined with the federal GST to create a federally administered single sales tax (HST). The HST will have a combined rate of 13%. Transitional measures will ease the transition to the new HST.

For more on the transitional measures and insights on how harmonization will affect your industry, click on

this [link](#) or go to www.pwc.com/ca/tax for our industry-focused sales tax harmonization *Tax Memos*.

Other Tax Measures

Pension reform

Further to a December 2008 announcement, the budget includes proposals intended to provide:

- temporary solvency relief to pension plans affected by the turmoil in the financial markets; and
- greater transparency to pension plan members while protecting the security of pension benefits.

To modernize Ontario's pension system the budget includes measures that:

- address the pension division on marriage breakdown; and
- accommodate phased retirement programs.

Tobacco tax

The budget includes measures intended to strengthen tobacco-related enforcement activities.

Technical amendments

Ontario will amend its provincial statutes to improve effectiveness and enforcement, as well as to enhance legislative clarity and flexibility.

Tax-Free Savings Accounts

Technical amendments will also allow designated beneficiaries to receive Tax-Free Savings Accounts (TFSA) outside of a will in the same way that beneficiaries can receive Registered Retirement Savings Plan (RRSP) proceeds. The TFSA could also pass to the designated beneficiary without being subject to Estate Administration Tax.

Federal harmonization

The budget states that Ontario will automatically adopt several 2009 federal budget measures, once the relevant federal legislative and regulatory changes are enacted. Measures that will be paralleled include proposals that:

- increase the amount that can be withdrawn from an RRSP by first-time home buyers without incurring tax; and
- enhance capital cost allowance:
 - for computers and software; and
 - for manufacturing and processing (M&P) assets (Ontario requests that the federal government extend this enhancement to M&P assets acquired before 2014).

See our *Tax Memo*, "2009 Federal Budget: Big Spending, Little Tax Relief" at www.pwc.com/ca/budget for more information.

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