Institute for COMPETITIVENESS & PROSPERITY

Press Release, May 1, 2013

Institute calls on government to focus on growth, not just cuts

New research by the Institute for Competitiveness & Prosperity explores how Ontario can improve the efficiency and effectiveness of its revenue generation and spending while tackling debt

Toronto – Government plays a key role in boosting the prosperity and competitiveness of the province, especially in times of economic hardship. The task of how to improve the Ontario government's efficiency has become a widespread topic of debate. While most observers have looked at cost-cutting measures and administrative inefficiencies within the government, a central concern is missing from the debate: how to get Ontario back on a path of strong growth. In its latest Working Paper, *Making sense of public dollars: Ontario government revenue, spending and debt*, the Institute looks at how Ontario's fiscal policy can be used as a tool for rebuilding and enhancing the province's economic strengths.

The Institute analyzed trends in Ontario's revenue generation and spending going back to 1989 and found that overall, the province has a number of surprising strengths. The Ontario government spends less per capita and as a percentage of GDP than all other Canadian provinces. The government has also reformed its tax structure by lowering capital and corporate taxes and introducing the HST, making the system more efficient. However, Ontario faces a number of challenges that pose a potential risk to the sustainability of the public service. The longstanding deficit and growing debt are a pressing concern as the cost of servicing debt has escalated to become the third-largest government expense after health care and education.

The Institute found that a possibly more problematic issue, though, is that Ontario is not spending in the right areas to promote economic competitiveness and growth. Its spending on education and infrastructure—the two areas most linked to productivity and economic growth—are significantly lower than that in other provinces. This means Ontario is not spending enough on investments in future prosperity.

Ontario also needs to improve on the revenue side. Changes to the tax system can be made to encourage innovation, investment, and business growth. Ontario also fails to capture the full revenue it's due through user fees, the Equalization system, and a complicated system that elicits aggressive tax planning.

Ontario needs to focus on what will restore economic growth. The Institute believes most of the government's fiscal problems can be solved by creating sustainable and efficient revenue streams while spending to promote prosperity. The viability of Ontario's public services and programs depends on strong economic foundations. Re-orienting the budget towards this goal will ease the government's fiscal burden and make the province more prosperous and competitive for years to come.

"The best government is not a big or small one, but a smart one," said Roger Martin, Dean of the University of Toronto's Joseph L. Rotman School of Management and Chairman of the Institute for Competitiveness & Prosperity. "The government needs to apply innovative policymaking to all facets of the public sector, so that Ontarians can benefit from strong economic growth and sound public services for the future."

Tasks for Ontario

- Support a competitive business environment while ensuring the tax system is fair and equitable.
- Balance current consumption needs with investment in future prosperity.
- Monitor and control public debt.

Ontario's challenges

- The Ontario economy is expected to grow at a modest rate of 1.8 to 2.0 percent annually in the coming years, putting downward pressure on public finances.
- Ontario's population is rapidly aging, increasing current and future health care expenses for the government.
- Many businesses are motivated to stay small and stagnant through differential tax treatment for small businesses and select industries.
- Tax rates on capital gains and corporations have been significantly reduced, but continue to discourage business investment and growth.
- Ontario underinvests in education and infrastructure relative to other provinces, putting its future prosperity at risk.
- Ontario's deficit and debt-to-GDP ratio sharply increased during the 2009 recession, prompting the government to implement an aggressive deficit-reduction plan.

Recommendation highlights

- Prioritize Ontario's future prosperity by increasing investment in education to match per capita spending levels in other provinces.
- Control the deficit and debt-to-GDP ratio to stop the rise in interest payments, but also focus on using debt for productive ends. Debt should be used to invest in what is needed for economic growth.
- Phase out the small business marginal tax rate by gradually increasing it for corporate incomes up to $500,000 so that it merges with the general corporate tax rate. This will reduce the incentives for businesses to stay small.
- Adopt the Nordic Dual Income Tax system to reduce taxes on capital gains, thereby encouraging savings and investment.
- Reward innovation by adopting a patent box on corporate tax returns so that companies can be taxed at a lower rate on patented products.
- Find new revenue tools for transportation construction in the Toronto region and expand infrastructure investment across the province to boost trade and economic growth.

About the Institute
The Institute for Competitiveness & Prosperity is an independent not-for-profit organization established in 2001 to serve as the research arm of Ontario's Task Force on Competitiveness, Productivity and Economic Progress. The Institute is supported by the Ontario Ministry of Economic Development and Innovation. Working Papers published by the Institute are primarily intended to inform the work of the Task Force. In addition, they are designed to raise public awareness and stimulate debate on a range of issues related to competitiveness and prosperity.

The complete report can be downloaded directly from:
http://www.competeprosper.ca/download.php?file=ICAP132_WP16_Final.pdf
For more information contact Jamison Steeve, Executive Director of the Institute for Competitiveness & Prosperity at 416.946.7585