

Provincial Personal Income Tax Revenue and Related Credits and Reductions

Personal income tax is by far the largest source of revenue for the Province of Ontario. For the 1998/99 fiscal year, the province received approximately \$17.2 billion in personal income taxes net of \$1 billion in tax credits, which represents 31% of total revenues.

With the exception of Quebec, all Canadian provinces and territories have entered into a personal income tax collection agreement with the federal government. The original Tax Collection Agreement between the Province of Ontario and the federal government was signed on April 24, 1962, and has subsequently been amended on a number of occasions, often through side agreements or letters between the respective parties. Under the terms of this Agreement, the federal government processes and collects Ontario personal income taxes, processes claims for personal income tax credits and reductions provided for under provincial legislation, and remits the net proceeds to the province.

Other significant provisions of Ontario's Tax Collection Agreement include requirements that the province:

- base its income taxes on only one rate of basic federal tax (changeable in multiples of one half of one percent);
- mirror federal requirements for such things as rates of interest and penalties imposed on outstanding amounts, the manner in which installment payments are to be made, and the rates at which deductions from income are to be withheld at source;
- accept that enforcement and investigation strategies on behalf of the province are the sole responsibility of the federal government; and
- accept as final all decisions of the Minister of National Revenue with respect to the administration of tax legislation.

As a result, the Ministry of Finance has no direct role in the collection or administration of personal income tax in Ontario.

Except for a fee of approximately one percent of the value of the nine provincial tax credits processed, a fee of about \$8 million per year, the federal government does not charge Ontario for the collection and administration of its provincial income taxes and assumes responsibility for all bad debts. In exchange, the federal government retains all non-tax revenues such as interest and penalties.

For each taxation year, the Ministry receives a Statement of Income Taxes Payable to the Provinces and Territories and accompanying notes, which is audited by the Auditor General of Canada. Although the Auditor General's opinion provides assurance over the assessment and distribution of income taxes payable to the provinces and territories, under the terms of reference, neither the Statement nor the opinion would be expected to address many of the issues raised in this report such as the use of revenue forecasts and the timing of cash flows. In that respect, the Notes to the Statement of Income Taxes Payable to the Provinces and Territories also caution that, when verifying a taxpayer's return, Revenue Canada uses criteria which are generally less exacting than the provisions of the income tax acts and regulations. These criteria cover all areas of a tax return, including the determination of the taxpayer's province or territory of residence.

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AUDIT OBJECTIVES AND SCOPE

Our audit objectives were to assess whether the Ministry of Finance had adequate requirements and controls in place to ensure that:

- personal income taxes payable to Ontario were correctly determined and remitted to the province on a timely basis; and
- the correct amount of tax credits, tax reductions and Guaranteed Annual Income Supplement program (GAINS) benefits were provided to eligible individuals.

For our second objective, we focused on the Property and Sales Tax Credits and the Labour Sponsored Investment Fund Tax Credit, which together accounted for 98% of the value of the nine provincial tax credits administered by the federal government.

The scope of our work included a review and analysis of relevant ministry files and administrative procedures as well as interviews with appropriate Ministry of Finance staff at the Macroeconomics Analysis and Policy Branch, Tax Design and Legislation Branch, Taxation Policy Branch, and Tax Credits and Grants Branch. We also interviewed senior staff at Revenue Canada and the federal Department of Finance, given the significance of their departments' involvement in the process of collecting provincial personal income tax.

Prior to commencing our audit field work, we identified the audit criteria to be used to address our audit objectives. These criteria were reviewed and agreed to by senior management at the Ministry.

We conducted our audit during the period September 1998 to March 1999, with emphasis on the procedures in place with respect to tax revenues and credits processed for the 1997 taxation year. Our audit was conducted in accordance with the standards for assurance engagements, encompassing value for money and compliance, established by the Canadian Institute of Chartered Accountants, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

The work of the Ministry's Audit Services Branch did not affect the scope of our work because the Branch had not reviewed or issued a report on personal income tax revenues, tax credits, tax reductions or GAINS during the last three years.

OVERALL AUDIT CONCLUSIONS

Although a number of amendments have been made to Ontario's original Tax Collection Agreement over the years, we noted that many of these were administrative in nature, with the result that many of the underlying principles and practices governing the original agreement have remained the same.

We concluded that the Ministry did not have the necessary information to assess whether personal income taxes were correctly determined. In addition, we concluded that personal income taxes paid ought to be remitted to the province in a more timely manner.

More specifically, in-year cash flows of personal income tax revenue to Ontario by the federal government have always been based on federal forecasts of provincial income tax revenues for that year and actual tax revenues from the two previous taxation years. While such an approach may have been the preferable or only practical option in the early 1960s when the original agreement was implemented, it is no longer adequate in our view. Significant advances in computer technology and administrative systems should make it possible to now provide more accurate and timely cash flows to Ontario, based on actual personal income taxes paid to the federal government during the year. In that regard, we noted that:

- For the last three completed taxation years, in-year personal income tax cash flows to Ontario, which were based on revenue forecasts, were much less than the amounts collected by Revenue Canada for each of those years. We estimated that the province's interests costs associated with these tax flow deficiencies totalled \$189 million for those years.
- Although Revenue Canada has significantly advanced its due dates for employer remittances in recent years, it has not similarly advanced the date of its own scheduled remittances to Ontario. This results in delayed cash flows of hundreds of millions of dollars to the province.

The federal government also does not share with Ontario the interest and penalties revenue received in excess of bad debts written off from Ontario personal income tax payers. The Ministry estimated that the federal benefit from retaining this net revenue could exceed \$50 million per year. However, at the time of our audit, the federal government had not provided the Ministry with the data required to verify the actual federal benefit.

We also noted that the Tax Collection Agreement imposes a number of significant limitations on the province with respect to the implementation of tax policy changes and administrative practices, the necessity and advisability of which are no longer clear. For example:

- The Ministry has very little input into or information about Revenue Canada's audit strategy or coverage of taxpayers liable for Ontario personal income tax.
- The Tax Collection Agreement restricts the flexibility of the province to pursue its own tax policies.

With respect to the implementation and administration of Ontario tax credits and tax reductions, we noted that:

- Although it is not specified in the Tax Collection Agreement, in practice the province must obtain approval from the federal government to implement Ontario-specific tax credits. We understand that in some instances such approval has been denied.

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- Although the Ministry had established a desired level of audit coverage for all property and sales tax credits claims, actual coverage by Revenue Canada was less than half of the Ministry's desired level. Notwithstanding, \$5.7 million in ineligible claims were identified in the 1996 taxation year. Expanding audit coverage to the desired level would likely provide similarly favourable results.
- Contrary to its own requirements, the Ministry had not completed audits of Labour Sponsored Investment Funds at least once every two years for their compliance with legislated investment requirements and the adequacy of their internal controls over the issuance of tax credit certificates.
- Revenue Canada did not verify some of the information necessary to establish taxpayers' eligibility for Ontario tax reductions.

DETAILED AUDIT OBSERVATIONS

TIMING OF PERSONAL INCOME TAX FLOWS

USE OF REVENUE FORECASTS

The federal government annually prepares forecasts of expected provincial and territorial income tax revenues, which are the basis of in-year personal income tax payments to the provinces and territories. The first forecast is prepared in January of each year and is based on such things as expected gross domestic product, employment statistics, projected changes in the consumer price index, tax rate changes, if any, and actual taxable income from the second previous taxation year. The revenue forecasts are normally revised in August and November of each year based on updated information including actual tax assessments issued to that date for the previous taxation year, policy changes and the latest economic data.

The final determination of provincial personal income tax revenue is made by Revenue Canada in February of the second following year since most, if not all, income tax returns have been filed and assessed at that time.

The Ministry of Finance provides some input into the federal government's revenue forecasts with respect to the expected effect of provincial surtaxes, tax reductions and tax credits. However, on a combined basis, these items account for a relatively small amount of the total revenues forecast.

Copies of the federal government's revenue forecasts are sent to the Ministry of Finance for its review. However, there is no requirement that the Ministry approve the revenue forecasts even though they have significant impacts on the province's cash flow.

We compared the revenue forecasts, and consequent in-year provincial income tax payments to Ontario, to the final determination of Ontario personal income tax revenues for the last three completed taxation years. We found that forecast revenues, and therefore in-year cash flows, were much less than the final determination of personal income tax revenues, as illustrated in the following table.

**Underestimation of Revenue Forecasts and
Associated Interest Costs, 1995-97**

Taxation Year	Underestimation (\$ millions)	Interest Cost (\$ millions)
1995	280	35.5
1996	390	42.7
1997	1,394	110.8
		189.0

*Source: Based on Ministry of Finance data and
Office of the Provincial Auditor*

We noted that the underestimated amounts of tax revenues were paid to Ontario between January and March of the second following year, or on average 20 months after they were received by Revenue Canada. We also noted that the Tax Collection Agreement does not provide for any interest payment to compensate Ontario for this delay. Using Ontario's short term borrowing rates, we estimated that the cost of the cash flow deficiencies to the province for those years totalled \$189 million, as shown in the above table.

PAYMENT FLOWS

Revenue Canada requires employers to withhold personal income tax amounts from employees during the year and remit them to Revenue Canada based on predetermined schedules that vary with the size and classification of the employer. Similarly, self-employed individuals are required to make income tax installment payments during the year.

Revenue Canada in turn remits the provincial or territorial portion of the taxes collected to the provinces and territories based on requirements in effect under the tax collection agreements. For 1997, in-year payments to Ontario were as shown in the following table.

Ontario's In-Year Payment Schedule, 1997

February 19 to August 28	27 equal payments based on the original revenue forecasts.
September 9 to November 27	12 equal payments based on the first revised revenue forecast prepared in August.
December 8 to February 9	9 equal payments based on the second revised revenue forecast prepared in November.

Source: Department of Finance

Since the inception of the original Tax Collection Agreement, Revenue Canada has continuously advanced its due dates for income taxes withheld at source by employers. For example, since January 1, 1990, large employers with average monthly remittances of \$50,000 or more have been required to remit their source deductions within three working days of the end of the pay week. It is estimated that 73% of all withholding taxes are remitted by these types of employers.

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However, in-year personal income tax payments by the federal government to the provinces and territories have not been advanced to the same degree, which has resulted in a benefit to the federal government at the expense of the provinces and territories.

Because of provincial and territorial concerns on this issue, the federal government in 1997 undertook a study of its provincial and territorial personal income tax inflows and outflows for the 1995 taxation year. The study concluded that the 1995 cash flows favoured the federal government and that the federal government's total interest benefit was approximately \$100 million for that year. Fifty-two million dollars of that amount related to Ontario.

As a result of this study, Ontario received a one-time payment of \$52 million in early 1998 in respect of the 1997 taxation year. There was no compensation for any other previous years. The federal government also agreed to advance the first payment to Ontario from mid-February in 1997 to the end of January for 1998 and subsequent years.

However, potentially significant cash flow deficiencies and resultant costs to Ontario remain. For example, for 1999 Revenue Canada received provincial and territorial personal income tax remittances as early as January 12 while the earliest payment to Ontario was January 28. As a result, Revenue Canada still collected hundreds of millions of dollars in Ontario personal income taxes before the first installment was remitted to the province.

With advances in information technology, including electronic transfers of funds, that have been made since the Tax Collection Agreement was first signed in 1962, the federal government should now be able to forward to the province its share of personal income taxes as soon as employers have remitted them to Revenue Canada.

In addition, we noted that for 1995, the year studied by the federal government, the underestimation of Ontario's income tax revenue forecast was the least of the last three completed tax years. We also note that the benefit to the federal government and resultant cost to the province can vary significantly from year to year due to the timing of cash flows and changes in interest rates.

Recommendations

To ensure that payments of Ontario personal income taxes are remitted to the province in the correct amount and on a more timely basis, the Ministry should consider negotiating the necessary amendments to the Tax Collection Agreement pertaining to cash flows.

As long as in-year payments to Ontario continue to be based on revenue forecasts and are subject to delay, the Ministry should seek compensation for the cash flow deficiencies for each year.

Ministry Response

The Ministry agrees that advances in information technology may make it possible for the federal government to base its payments to Ontario on actual income tax receipts and for these payments to be remitted to the province on a more timely basis. The Ministry is currently examining this issue, including the question of whether the payment system generally benefits the federal government. For example, though the federal government underpaid Ontario from 1995 to 1997, Ontario was overpaid by a much larger amount from 1990 to 1994, with associated interest savings.

INTEREST AND PENALTIES

According to the Ministry, the federal government has always been permitted to retain all non-tax revenues such as interest and penalties in exchange for assuming responsibility for bad debts.

However, the Ministry does not regularly receive the necessary information from the federal government to assess whether such an arrangement continues to be justified. In our view, the non-tax revenues have likely increased significantly in recent years for the following reasons:

- the more frequent and advanced employer remittance requirements have resulted in increased interest and penalty revenues;
- interest calculations have been changed from simple interest to daily compounded interest;
- outstanding accounts receivable on which interest is charged have increased significantly faster than the write-offs of bad debts; and
- interest rates charged on outstanding balances are now 2% higher than the rates paid on prepayments or refunds.

The Ministry estimates that the federal government's benefit of retaining non-tax revenues from Ontario taxpayers in excess of bad debts written off could exceed \$50 million per year. However, at the time of our audit, the federal government had not provided the Ministry with the necessary data to verify the actual amount of the benefit.

Recommendations

To assess whether the federal government's retention of non-tax revenues is equitable, the Ministry should periodically receive the necessary information about non-tax revenues and accounts written off in respect of Ontario personal income tax.

The Ministry should use this information to consider whether it is beneficial to renegotiate the terms of the Tax Collection Agreement as it pertains to the sharing of interest and penalties revenues.

Ministry Response

The Ministry agrees with the recommendations.

Over the past two years, the federal government has provided some data on non-tax revenues and accounts written off in respect of provincial income tax. However, this data has not been sufficient to properly evaluate whether the federal government's retention of non-tax revenues is equitable. The Ministry continues to pursue with the federal government the collection of better data and its receipt on a timely basis.

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AUDITS OF PERSONAL INCOME TAX RETURNS

Taxpayers are liable for provincial or territorial personal income tax levied by the jurisdiction in which they declare their principal residence on December 31 of the tax year, regardless of where they lived or worked during the year.

Although Revenue Canada collects and otherwise administers Ontario's personal income tax on its behalf, ultimately the responsibility remains with the Ministry to satisfy itself that the overall audit procedures and controls in place meet its requirements, and are adequate to ensure that Ontario personal income tax is correctly determined and remitted in compliance with provincial legislation.

However, we found that the Ministry had very little input into or information from Revenue Canada about its audit procedures for the collection of Ontario personal income tax or its audit strategy, plans and coverage of Ontario-based taxpayer returns. For example, under the terms of the current Tax Collection Agreement, the Ministry cannot establish or negotiate requirements for such things as audit coverage, selection criteria or the nature of the audit work to be performed. As a result, the Ministry cannot assess whether Revenue Canada's efforts met its expectations or were adequate in these areas.

Similarly, Revenue Canada did not routinely provide the Ministry with information such as:

- the number or percentage of Ontario-based taxpayer returns audited or how that compared to other provinces, territories or the country as a whole;
- the types and income levels of taxpayers selected for audit or the reasons for their selection;
- special audit initiatives; and
- audit results.

It is Revenue Canada's view that when it audits a tax return for the completeness and accuracy of basic federal income tax, it is also satisfying the interests of the provinces and territories since their personal income tax is a function of basic federal tax.

We noted that the Tax Collection Agreement provides that the Minister or Deputy Minister of Finance can request that the Minister of National Revenue make available for examination by the province:

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- any returns or other documents that relate solely both to the tax payable under the federal act and the tax payable under the provincial act in respect of any year during the term of the Agreement; and
 - such other information with respect to assessments, collections and payments as the Minister of National Revenue deems advisable.

However, we were advised that the Ministry has not conducted its own audits of personal income tax returns because the federal government has not committed to issue the resulting reassessments, if any.

Recommendation

In order to obtain assurance that the declaration and payment of personal income taxes to which the Province is entitled are in the correct amount, the Ministry should:

- **establish minimum audit requirements and renegotiate the Tax Collection Agreement with the federal government to require Revenue Canada to meet the Ministry's requirements for such things as audit coverage, selection criteria and nature of the work to be performed; and**
- **obtain the necessary information from Revenue Canada to be able to assess whether it has met the Ministry's requirements.**

Ministry Response

As noted in the report, under the current Tax Collection Agreement the Ministry has no right to establish minimum audit requirements, nor to receive information to permit monitoring of Revenue Canada's performance in ensuring adequate compliance. The Ministry agrees that the recommendation has merit and will pursue it with the federal government.

TAX POLICY IMPLICATIONS

Although the Tax Collection Agreement between the federal government and the province has been beneficial to Ontario in a number of important respects, it also has imposed some significant restrictions on the Province. For example:

- By requiring that Ontario personal income tax be based on only one rate of basic federal income tax, changeable in multiples of one half of one percent, the Agreement has ensured that:
 - All changes to federal taxable income, tax credits or tax rates are automatically reflected in Ontario personal income tax irrespective of whether or not the province concurs with the changes. For example, the Ministry has estimated that the provisions of the 1999 federal budget will result in a decrease of about \$300 million in provincial personal income taxes for the province's 2000/01 fiscal year. We note that the province could compensate for such a decrease by increasing its own personal income tax rate, but may choose not to do so.

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- Under the “tax on tax” structure required in the existing Agreement, Ontario cannot impose personal income taxes at variable rates other than as a fixed percentage of the variable rates inherent in the federal tax brackets. Instead it must rely on more complex and indirect measures, such as selective tax reduction programs, targeted tax credits and high-income surtaxes, to attempt to achieve its desired tax effects.

We were advised that the federal government has agreed in principle that for the year 2001 and later years, provinces in tax collection agreements may apply provincial tax brackets and rates to taxable income rather than to basic federal tax. This option will provide Ontario with the opportunity to establish tax brackets and rates of its own choosing.

- As previously noted, Ontario is essentially excluded from the decision making process with respect to its *Income Tax Act* enforcement and investigation strategies because those are the sole responsibility of the federal government, and all decisions of the Minister of National Revenue are final.
- Although not specifically detailed in the Agreement, in practice, Ontario must obtain the approval of the federal government for the implementation of Ontario-specific tax credits by Revenue Canada. In some cases federal approval has been denied. For example, we understand the federal government refused to administer a provincial tax credit for donations to the Crown in excess of 75% of a donor’s annual net income.

Recommendation

The Ministry should consider whether the benefits under the Tax Collection Agreement continue to outweigh the restrictions, and if considered advisable, renegotiate the Tax Collection Agreement in line with provincial interests.

Ministry Response

In formulating tax policy, the Ministry will continue to consider the benefits available under the Tax Collection Agreement and assess whether they exceed the restrictions imposed by that agreement. The Government has already indicated its desire to have a personal income tax system designed to meet Ontario-specific needs.

RELATED TAX CREDITS AND REDUCTIONS

PROPERTY AND SALES TAX CREDITS

The purpose of the Ontario refundable property and sales tax credits is to reduce the impact of municipal property tax and provincial sales tax on low to moderate income earners in Ontario.

Eligibility for the property tax credit is dependent on the amount of property tax paid, either directly to a municipality in Ontario or indirectly through rent, adjusted by the combined spousal net income in excess of minimum amounts. The basic sales tax credit is \$100 for each

individual over 16 years old; \$100 for his or her spouse; and \$50 for each dependent child under the age of 18 years. The combined maximum available credit is \$1,000 per year.

Claims for refundable tax credits are submitted to, and processed by, Revenue Canada as part of a taxpayer's annual income tax and benefit return. For the 1997 tax year, Revenue Canada processed 2.2 million claims for these tax credits having a total value of \$960 million. Although enforcement initiatives are also the responsibility of Revenue Canada, the Ministry has identified seven audit selection criteria to be used by Revenue Canada in selecting files for audit.

Revenue Canada recovers the estimated value of these credits from Ontario by deducting 24 equal installments from Ontario's personal income tax remittances between April and September of each year. Final adjustments are made as part of the regular provincial income tax settlement process in February of the second following year.

Revenue Canada charges Ontario a variable fee for the administration and enforcement of the property and sales tax credits, which is based on the per capita value of credits issued. This fee averages approximately \$8 million per year.

Our review of the audit process for property and sales tax credits noted the following concerns:

- Revenue Canada's audit coverage of property and sales tax credit claims was low, since the actual coverage was less than half of the desired amount.
- For the 1996 taxation year, Revenue Canada audited approximately 46,000 out of 197,000 claims that met at least one of the Ministry's seven selection criteria. Of the claims audited, 45% were either disqualified or reduced, resulting in \$5.7 million in recoveries for Ontario, or \$270 per claim. Audit results were similar in the prior year.

Based on these results, we estimated that if all claims meeting the Ministry's selection criteria were audited, an additional \$16 million per year would be recovered on behalf of the Province of Ontario.

- Revenue Canada did not randomly select any claims that did not meet the Ministry's selection criteria. As a result, the vast majority of claims processed were not subject to audit or review.

We also noted that, in addition to the above audits, Revenue Canada computer-matched the property and sales tax credit claims by spouses to determine whether there were duplicate claims. Approximately 1% of matched claims were found to be duplicates and were recovered on behalf of the province.

Although the Ministry would like Revenue Canada to audit more claims for the property and sales tax credits, Revenue Canada has not agreed to do so without additional compensation.

As a result of Revenue Canada's position, in 1993/94 the Ministry undertook a pilot project and itself audited an additional sample of approximately 9,900 property and sales tax credit claims for the 1991 taxation year, based on information provided by Revenue Canada. The Ministry identified a claims adjustment rate of 59% having a total value of about \$1.3 million, or seven times the cost of its effort. However, although Revenue Canada issued the necessary tax reassessments to recover the overpaid claims for that year, it refused to extend the project for other taxation years because, in its view, there was the potential for confusion to the taxpayer of having more than one tax administration.

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Recommendations

In order to reduce the incidence of false or inaccurate claims, the Ministry should negotiate with Revenue Canada the audit coverage of property and sales tax credit claims to ensure that Revenue Canada annually audits more, if not all, of the claims meeting at least one of the Ministry's seven selection criteria.

In addition, the Ministry should request that Revenue Canada audit a random sample from the remaining tax credit claims processed to ensure that any claim may be subject to audit and so that the degree of overpayments can be assessed for the program as a whole.

Ministry Response

In the past, requests for increased audit coverage have been refused. With the inception of the Canada Customs and Revenue Agency (CCRA) later this year, such new programs may be available but at a cost. A cost/benefit analysis of increased audit coverage will be carried out.

A random sample is planned as part of the compliance program for the 1998 taxation year.

LABOUR SPONSORED INVESTMENT FUNDS

The Labour Sponsored Investment Fund (LSIF) program was originally established in 1991 under Ontario's *Labour Sponsored Venture Capital Corporations Act*, which was replaced by the *Community Small Business Investment Funds Act* in December 1997. The program provides a tax credit for investments in LSIFs, which in turn are encouraged to invest in Eligible Small Businesses (ESBs).

For 1998, the amount of the tax credit is 15% of the value of shares purchased, up to an annual maximum of \$5,000. This translates into a maximum provincial tax credit of \$750 plus an equivalent matching federal credit. The total value of LSIF tax credits allowed by the province in 1997, the most recently completed taxation year, was \$18 million. Revenue Canada processes the credit through the income tax system.

The Ministry of Finance is responsible for approving LSIFs and regularly auditing them and the ESBs in which they invest. For example, audits of LSIFs include ensuring that they comply with the investment requirements of the Act and that adequate internal controls are in place for the issuance of tax credit receipts.

The Ministry's goal is to audit each of the 17 active LSIFs at least once every two years, and an ESB when an initial investment is made with follow-up audit work whenever subsequent additional investments are made in the business.

We found that only seven audits of LSIFs have been completed by the Ministry in the last three years. Audits of the remaining 10 LSIFs were in various stages of completion. The Ministry's audit coverage of ESBs was also low. Of the 366 ESBs in which investments have been made

as at March 31, 1999, only 24 have had audits completed. Management informed us that audit coverage of LSIFs and ESBs was low due to a shortage of audit resources.

To help ensure that the tax credit is only provided to eligible taxpayers, the Ministry has also developed a computer matching procedure to identify potentially ineligible claims. This procedure involves comparing LSIFs' records of purchases of their shares with subsequent taxpayer claims for the related tax credit. We noted that the Ministry had experienced substantial problems in getting the matching procedure to work. This resulted in a delay in resolving 1,700 accounts with discrepancies, representing \$1.1 million in potentially ineligible claims for 1995, that caused them to become statute barred. In addition, there is a risk that 1,750 accounts, totalling \$715,000 in unmatched claims from the 1996 taxation year submitted to Revenue Canada, will also be uncollectible unless promptly acted upon by Revenue Canada.

Recommendation

In order to help ensure that Labour Sponsored Investment Funds and Eligible Small Businesses comply with the terms and conditions of the *Community Small Business Investment Funds Act*, the Ministry should increase its audit coverage to its target level. This would also permit excessive or ineligible claims to be identified, reassessed and collected on a timely basis.

Ministry Response

Four additional auditors were hired in early 1999. The Ministry anticipates that its audit targets will be achieved in the 1999/2000 fiscal year.

Revenue Canada has undertaken to conduct a review of the potentially ineligible 1996 accounts by October 1999. Any resulting reassessments will be issued well before statute-barred dates in the year 2000.

ONTARIO TAX REDUCTION

The purpose of the Ontario Tax Reduction is to reduce or eliminate Ontario personal income tax for low-income earners. For 1997, the basic reduction was \$171 and the additional amount for each dependent child and disabled dependant was \$334. The deduction must be claimed by the spouse with the higher income and is reduced or eliminated for taxpayers whose Ontario personal income tax payable is greater than the sum of the basic tax reduction and the amounts for dependants.

For the 1997 taxation year, Revenue Canada allowed approximately 1.1 million claims for Ontario tax reductions having a total value of \$208 million.

However, the Ministry was advised that starting in 1993 (the year in which the Child Tax Benefit replaced Family Allowance, non-refundable tax credits for children and the Child Tax Credit), Revenue Canada could not verify claims for dependent children for Ontario tax reduction purposes. As a result, there is no assurance that Ontario tax reductions are correctly determined and only provided to eligible individuals.

Recommendation

In order to help ensure that Ontario tax reductions are only provided to eligible individuals, and in the correct amount, the Ministry should negotiate minimum verification requirements with Revenue Canada so that it verifies, at least on a sample basis, claims for dependent children.

Ministry Response

The Ministry will explore with Revenue Canada various options to improve verification of Ontario tax reduction claims.

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GUARANTEED ANNUAL INCOME SUPPLEMENT

The Province of Ontario makes direct payments under its Guaranteed Annual Income Supplement program (GAINS) to qualifying Ontario senior citizens whose income from all sources falls below the level guaranteed by the province (1998: \$11,784 single and \$19,484 a couple). For the fiscal year ending March 31, 1998, approximately 108,700 recipients received provincial GAINS benefits totalling \$82 million. The monthly payment ranged between \$2.50 and \$83 per recipient.

Seniors are only eligible for the provincial supplement if they receive federal Old Age Security (OAS) payments and Guaranteed Income Supplement (GIS), have been a permanent resident of Ontario for the past 12 months, and have total income from all sources below the level guaranteed by the Province.

Eligibility for provincial GAINS benefits is determined primarily by an individual's eligibility for federal OAS and GIS. The federal government provides information on eligible individuals on a monthly basis to the Ministry to update its GAINS payment system.

We reviewed controls over several aspects of the GAINS program, including tests on the computerized master file for conditions that should not exist, such as checking that payments were not made in the following month to GAINS recipients who had died during 1997, and that monthly payments did not exceed the maximum amount payable. We also reviewed controls over accounts receivable, write-off procedures and the protection of data from unauthorized access.

We found that controls were adequate.