

## Foreword



In Budget 2008, the GNWT committed to taking a number of measures necessary to put its fiscal house in order, including raising new revenues, starting in the 2009-10 fiscal year. This revenue will provide additional resources to fund important programs and services for Northerners.

- How should additional revenues be raised?

The question is more complex than you might think. We can raise revenues simply by increasing taxes or creating new fees; however, the way it's done can have significant consequences for individuals, families, and businesses. An approach that's not well thought out can hurt the economy, discourage investment, or even push people into leaving the territory. So it's important that the GNWT carefully examines options, and takes a measured and balanced approach that is consistent with the NWT's long-term vision and goals.

This paper provides some basic information about where the NWT currently gets its revenues and looks at new options for raising money. It identifies different approaches that could be used and discusses their pros and cons. Because the options the GNWT adopts will affect all NWT residents, having the input of Northerners is important. No decisions have yet been made. I encourage you to provide your comments to the contacts listed at the end of this booklet.

A handwritten signature in black ink that reads "J.M. Miltenberger". The signature is written in a cursive, flowing style.

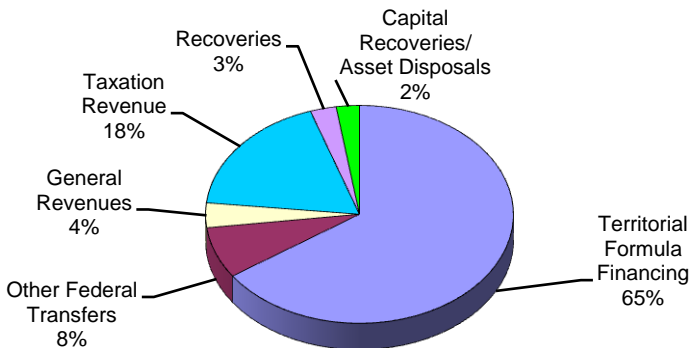
Hon. J. Michael Miltenberger  
Minister of Finance

## Why do we need taxes?

The person who enjoys paying taxes is likely rare, if she or he exists at all. But most people recognize that taxes play a necessary and important part in making societies work. The fundamental purpose of taxes is to raise the revenue necessary to fund programs and services for residents, like education and health care. Taxes may also be used to promote economic growth, encourage certain activities (saving for post-secondary education) or discourage certain behaviour (smoking). The challenge is to balance these goals, which are sometimes at odds with each other, and to spread the tax burden fairly in society.

### Total 2008-09 GNWT Revenue by Source

- *Almost three-quarters of GNWT revenues come from the federal government. The GNWT has no direct control over these revenues.*
- *The other one-quarter of GNWT revenues comes from “own-sources” such as taxes and fees. The GNWT has direct control over these revenues. The GNWT collects about \$220 million each year in taxes and \$90 million from fees and other own sources. About 42% of taxes (or \$92 million) come from the business sector and 58% (\$128 million) from individuals.*



## How Government Revenues Change

The size of Government revenues changes for two main reasons:

## 1. **Economic and Population Growth**

- When the economy grows, more tax revenues are collected.
- Employment goes up. More people work and make a good living.
- There are more demands for goods and services. New businesses are created, and existing ones expand to take advantage of the opportunities.

A growing population is also good for the NWT:

- Increased supply of labour for the economy.
- More opportunities for businesses to sell goods and services.
- Larger tax base.
- More federal funding to offset increased demands for programs and services. For each new NWT resident, the GNWT will receive an additional \$22,000 in federal Territorial Formula Financing.

The NWT economy is expected to continue growing as major resource projects such as the Mackenzie Gas Project, construction of other oil and gas fields, and new diamond mines proceed.

## 2. **Tax Rate Changes**

Raising tax rates is another way to raise revenues. Changing tax rates can affect the economy and population. High taxes can reduce economic and population growth as businesses shrink to cut costs, and people make decisions about where and how to live and work.

The labour force and investment capital are mobile and they usually favour jurisdictions with low taxes. The NWT's closest competition in this regard is Alberta, which has the lowest tax rates in Canada. Keeping tax rates competitive is important for future economic growth and prosperity of Northerners.

### **Issues**

- *The GNWT does not receive any royalties from natural resource developments.*
- *18% of employment income earned in the NWT during 2007 was earned by non-residents.*

*The NWT has:*

- *income tax rates that are below the national average,*
- *the highest tobacco taxes and liquor mark-ups in Canada,*
- *no sales tax or hotel tax,*
- *no capital tax.*

## How Should It Be Done?

Choosing the right tax measure(s) can't be made arbitrarily. The choice should reflect sound tax policy, and support the NWT's long-term goals.

### **Sound Tax Policy**

- *Making it fair to all.*
- *Maintaining a broad base.*
- *Keeping it simple.*
- *Avoiding unnecessary distortions.*
- *Showing fiscal responsibility.*
- *Encouraging economic development.*

## What We Can and Cannot Do

The Northwest Territories is a territory, not a province. Despite this distinction, the GNWT has almost the same options and limitations on its taxation power as those of provincial governments.

As a territory, the GNWT can't collect royalties or production taxes on non-renewable resources.

Like other provinces and territories, the GNWT can impose direct taxes on its residents and businesses.

Like other provinces and territories, except Quebec, the GNWT has a Tax Collection Agreement with the federal government. This agreement provides a harmonized income tax system and simplifies the filing of personal and corporate income tax returns by tax payers.

## Current Trends in Tax Policy

In recent years, the federal government and many provincial governments have been reducing both personal and corporate income taxes. On the other hand, they are also considering other tax measures that encourage either investment or improvements in areas like the environment and energy conservation. For example, increasing sales taxes on consumption and removing taxes on investment will encourage more saving and investment. Carbon taxes have received lots of attention lately as a way to fight climate change due to greenhouse gas emissions, and are imposed on the consumption of fossil fuels, such as oil and gasoline.

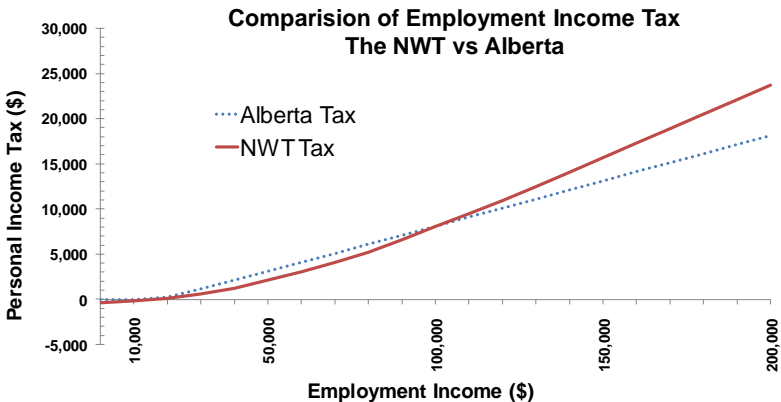
- Lowering personal income tax allows citizens to have more after-tax income to spend and/or save.
- Lowering corporate income tax promotes economic growth; allowing businesses to create more jobs, expand, or provide higher returns to investors.
- Increasing consumption taxes encourages saving and investment; and can discourage certain types of consumption.

## Tax Options to Consider

The GNWT Department of Finance has researched a number of options for raising new revenues. Each of these options is presented below with some general analysis and observations. (You can find more detailed analysis in the document titled *Revenue Options*, which is available on-line at [www.fin.gov.nt.ca](http://www.fin.gov.nt.ca)).

### 1. Personal Income Tax

The NWT personal income tax system taxes high income earners at higher rates than lower income residents. All other provinces and territories use this approach, except for Alberta – our closest competitor for labour. Alberta imposes a flat rate of 10% on all levels of personal income.



The NWT tax system benefits individuals with lower incomes, while Alberta's system favours higher-income earners. A single individual earning over \$100,000 pays more tax in NWT than in Alberta.

Consequently, many high-income earners (even those with families) maintain a permanent residence in Alberta instead of the NWT. Even though their income is earned in the NWT, no personal income tax flows to the GNWT and the GNWT doesn't receive any population-related benefits from these workers.

Raising personal income tax rates could:

- make the NWT less attractive as a place to live, encouraging taxpayers to maintain a residence elsewhere to avoid high NWT taxes.
- create a higher tax burden for lower-income residents who already pay higher costs of living in the territory.

## 2. Corporate Income Tax

Province/Territory	Corporate Income Tax	
	Small (%)	Large (%)
Northwest Territories	4.0	11.5
Nunavut	4.0	12.0
Yukon	4.0	15.0
British Columbia	3.5	11.0
Alberta	3.0	10.0
Saskatchewan	4.5	12.0
Manitoba	2.0	13.0
Ontario	5.5	14.0
Quebec	8.0	11.4
New Brunswick	5.0	13.0
Nova Scotia	5.0	16.0
Prince Edward Island	3.2	16.0
Newfoundland and Labrador	5.0	14.0

All provinces and territories have two corporate income tax rates: a general (large) rate and a small rate that applies to income earned by small Canadian-Controlled private corporations, up to a threshold, which varies by province.

Raising the corporate income tax rates could:

- generate more revenue - an increase of 1% to the general corporate tax rate could raise an additional \$8 million per year.
- make the NWT a less attractive place to invest. The NWT has already changed its general corporate tax rate three times in the last six years – once to increase and twice to decrease. Another general corporate income tax increase could give the impression that the NWT is not a stable and predictable place to invest.

## 3. Payroll Tax

The GNWT introduced a payroll tax in 1993 that generates over \$36 million annually. Increasing the rate from 2% to 3% of employment income would generate about \$20 million in additional revenue. The payroll tax increases the tax burden of taxpayers with

employment income compared to taxpayers with other sources of income.

#### 4. Cost of Living Tax Credit

The Cost of Living Tax Credit was introduced at the same time as the payroll tax, and provides a refundable tax credit, ranging from \$350 to \$942 per person, to all NWT filers over the age of 18. Reducing the Cost of Living Tax Credit would generate more revenue for the GNWT; however, it would not support the government's goal of reducing the cost of living.

#### 5. Fuel Tax

NWT fuel tax rates are among the lowest in Canada and have remained unchanged since 1997.

An increase in fuel tax rates could encourage greater conservation of fossil fuels and reduce greenhouse gas emissions, but could also:

- increase the costs of consumer goods due to higher transportation costs.
- increase the costs of doing business in the territory, especially for the resource sector. And
- increase electricity costs since considerable power generation in the NWT relies on diesel.

<i>Fuel Type</i>	<i>Tax Rate (¢/Litre)</i>
<i>Gasoline - on highway</i>	10.7
<i>Gasoline - off highway</i>	6.4
<i>Aviation</i>	1.0
<i>Motive Diesel</i>	9.1
<i>Other Diesel</i>	3.1
<i>Railway Diesel</i>	11.4
<i>Heating Fuel</i>	nil

#### 6. Tobacco Taxes

NWT tobacco tax rates are among the highest in Canada, and have not changed since 2003.

Raising tobacco tax rates could reduce consumption but may also increase smuggling and tax evasion. While there is not a lot of evidence of cigarette smuggling into the NWT despite the \$7.25 per carton price difference between Yellowknife and Alberta, the larger the price differential, the more incentive for illegal activities.

#### 7. Liquor Mark-ups

The NWT Liquor Commission controls the sale of liquor in the NWT.

- Price mark-ups are based on volume and liquor type plus allocation of overheads, making them difficult to compare with other jurisdictions.
- Mark-ups have not changed since 2003.
- A 10% increase in mark-ups would generate an additional \$1.2 million per year.
- Like tobacco, raising liquor prices may increase smuggling from other jurisdictions.

## 8. *Property Tax*

### ***Non-Tax Based Communities***

- *The GNWT collects property taxes but passes on the general tax portion to community governments.*
- *Communities can set their own general mill rates.*
- *The GNWT sets education mill rate for all communities except Yellowknife.*

### ***Municipal Taxation Authorities (MTAs)***

*The MTAs are Inuvik, Fort Simpson, Fort Smith, Hay River, Norman Wells and Yellowknife.*

- *Responsible for collecting property taxes.*
- *Yellowknife remits the education portion of the property tax to the two school districts.*
- *Other Municipal Taxation Authorities remit the education portion of the property tax to the GNWT.*

A 10% increase in mill rates would raise about \$2 million annually. This represents about \$30 per house in General Taxation Area communities.

## 9. *Insurance Tax*

All provinces and territories levy taxes on insurance premiums. The GNWT imposes a 3% tax on all insurance premiums and an additional 1% tax on fire insurance premiums. Revenues in 2007-08 were \$3.5 million.

Increasing the general tax rate applicable to all premiums to 4% would raise an additional \$1.2 million in revenue per year. Any tax increase would ultimately be passed on to policy holders.

## *10. Non-tax Revenues: Fees, Licences, Permits and Charges*

Fees, licences, permits and charges are designed to partially recover the costs of delivering the services to users.

## *11. Potential New Taxes and Fees*

### *Capital Tax*

A capital tax is a tax on a corporation's paid-up capital such as retained earnings, capital stock or long-term debt.

Capital taxes are complex and perceived to reduce economic competitiveness. Corporations oppose these taxes since the tax is payable whether the company is profitable or not.

The federal government eliminated its capital tax in 2006, and the five provinces with general capital taxes have announced their intention to do the same by 2011.

The GNWT could raise about \$12 million a year by imposing a 0.3% capital tax on the paid-up capital of general corporations. There would likely be significant costs to the GNWT to administer a capital tax. The new tax would also undermine the government's objectives of attracting investment and fostering greater opportunities for Northerners.

### *Resource Income Taxes*

The GNWT does not have the authority to collect royalties on NWT non-renewable resources; however, it could impose a mining income tax and an oil and gas income tax.

Resource income taxes would ensure that the GNWT receives some revenue directly from resource development, but they would increase the tax burden on corporations that are already paying royalties to the federal government.

Resource companies pay significant amounts to the GNWT in income, property and fuel taxes. Given the significance of the resource sector to the economy of the NWT, the costs to the government of resource development, and the fact that royalties and other resource revenues currently go to the federal government, it may be appropriate to levy an industry-specific income tax.

## *Sales Tax*

Sales taxes are an important source of revenue for many provinces. Five provinces (British Columbia, Saskatchewan, Manitoba, Ontario and Prince Edward Island) have retail sales taxes. In 1997, Newfoundland and Labrador, Nova Scotia, and New Brunswick harmonized their sales taxes with the federal Goods and Services Tax (GST). Quebec's sales tax, with minor exceptions, is also harmonized with the GST. Alberta and the three territories do not have general sales taxes.

The GNWT could impose a territorial sales tax. A 5% sales tax could generate about \$30 million per year.

The GNWT could also impose an 8% sales tax harmonized with the GST. A harmonized sales tax administered by the federal government would generate about \$59 million in revenue a year for the NWT, with little administrative cost.

Both sales taxes would increase the cost of living for Northerners, unless there were additional tax credits to offset this tax burden.

## *Hotel Room Tax*

All provinces have hotel room taxes, while all three territories do not. A 5% hotel room tax would generate approximately \$2.5 million each year for the GNWT.

If implemented, the tax would result in additional administration costs for both accommodation operators and the GNWT.

## *Carbon Tax*

A carbon tax is imposed on the consumption of carbon-based fuel products.

Quebec imposed a carbon tax in 2006. A similar tax structure in the NWT would generate about \$4 million annually.

British Columbia has recently introduced a broad-based, revenue-neutral carbon tax that, when fully implemented, will raise the price of gasoline by 7.24 cents per litre, and diesel by 8.27 cents per litre. Applying British Columbia's model to the NWT would generate an additional \$41 million per year.

Imposing a carbon tax would increase the cost of living in the NWT.

## *Health Insurance Premiums*

Only Alberta, Ontario, and British Columbia currently charge health care premiums. Alberta is eliminating its health care premiums as of January 1, 2009.

The NWT could introduce a health care premium. Adopting the Ontario premium structure could raise \$9 million per year for GNWT, including assistance given to low-income families. However, this would add to the cost of living in the NWT.

## *Highway Toll*

The GNWT could impose a highway toll on commercial trucks travelling on all-weather highways in the territory, and use the revenue for highway capital projects. The toll, however, would increase transportation costs, which in turn would raise the cost of goods and services in the NWT.

## *Airport Improvement Fee or Departure Tax*

Many airports in Canada impose airport improvement fees, ranging from \$5 to \$40 dollars per departing passenger, to raise revenue for airport capital projects.

An estimated \$3.5 million could be generated by charging a \$30 per person fee or tax on air travellers leaving the NWT.

## **Questions to Consider**

There are many options available to ensure the GNWT has sufficient revenue for programs and services that are important to NWT residents. Each option has advantages and disadvantages.

This raises questions to consider such as:

- What are the best options to help the NWT achieve its long-term goals?
- Which approach is better for the NWT: increasing taxes on the current economy, or increasing revenues by increasing the size of the economy and population?
- Is the NWT's current tax system designed in a way that helps achieve NWT's objectives? Is it competitive in today's global economy? What kinds of changes might be appropriate?

- How can we use the tax system to encourage more people to live, work and invest in the NWT? Should the NWT consider a shift away from income taxes towards consumption taxes?
- How should the GNWT raise necessary revenues to fund programs and services while keeping the costs of living affordable for NWT residents?

In the coming weeks the GNWT will be consulting Northerners about these and other questions. We encourage your input. After all, it's your tax dollar.

The GNWT is committed to ensuring that the NWT's tax structure is competitive, is able to fund essential programs and services, and works for NWT residents. Your input and ideas will help achieve these goals.

Copies of this paper and a more comprehensive discussion of the GNWT's revenue options are available on the Department of Finance website at [www.fin.gov.nt.ca/](http://www.fin.gov.nt.ca/).

You can submit your comments on NWT revenue options:

By mail to:

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Fiscal Policy Division  
Department of Finance  
PO Box 1320  
Yellowknife NT X1A 2L9

Or by e-mail to:

[Revenue\\_Options@gov.nt.ca](mailto:Revenue_Options@gov.nt.ca)