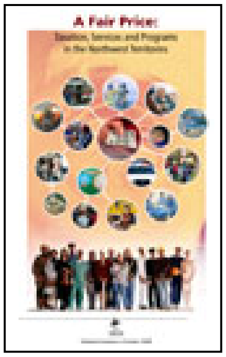

A Fair Price

Taxation, Services and Programs
in the Northwest Territories

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Executive Summary

The Government of the Northwest Territories (Government, GNWT) has commenced a public consultation on the subject of raising its revenues in order to address a projected budget shortfall. This report discusses the government's two consultation documents: the Revenue Options Paper and the Revenue Options Summary. It then examines the tax proposals discussed in those documents.

NON-FISCAL POLICY GOALS – TAX BADS, NOT GOODS

In addition to raising revenues, the tax system can be used to address a wide range of public policy goals: promoting economic growth, redistributing income among people and regions, promoting some activities, and discouraging others. Reducing the price of "goods" (e.g. education and personal savings) will increase the supply of them, while increasing the price of "bads" (e.g. tobacco and alcohol use, pollution) will discourage them. Internalizing non-market costs and benefits ("externalities") also helps to boost economic efficiency and equity. While the Revenue Options Paper provides a good listing of public policy goals that can be addressed through the tax system, other government communications seem to downplay or ignore goals other than promoting economic activity, growth and savings.

ANTI-TAX BIAS?

Taxes are, of course, necessary to provide essential public goods and services; they are the "price we pay for civilization." Thus, an anti-tax bias should have no place in a public consultation about taxes.

Unfortunately, it appears that the Revenue Options Summary has just such a bias. In a number of places it asserts the negative impacts of taxes without providing any support for those assertions, while ignoring the downsides of lower taxes, such as deficits or program cuts. Unfortunately, being the shorter of the two, it is the document that will be read by more people.

The Revenue Options Paper is a more balanced document, but it makes the mistake of suggesting that tax cuts can sometimes pay for themselves through increased economic activity. This argument has been debunked and is not supported by serious economists. It should not have found its way into the Paper.

Because of the anti-tax bias in these key documents, which is likely to sway public input, this report recommends that the current round of consultations be ended, and the documents withdrawn. A new round of consultations should be commenced, based on balanced documents and communications.

GROWING THE BASE VS. RAISING TAXES

The Paper and Summary propose two main options for raising net revenues: growing the tax base and increasing tax rates. On the former point, they fail to quantify the revenues that could be raised, or the costs that would be incurred, by growing either the population or the economy. Furthermore, they fail to clearly explain how fiscal policy would accomplish either population growth or economic growth to the extent needed to raise *net* revenues significantly. Thus, it is difficult to treat growing the tax base as a serious option.

Unfortunately, the other option presented – increasing tax rates – is undercut by an apparent anti-tax bias, as noted above. The documents further imply that the two are incompatible options, with no supporting evidence for this.

TAXATION CHANGES NEEDED

A number of changes to the tax system could be made in order to further social, environmental and economic goals, while raising revenues.

Corporate and resource income taxes, and savings

The NWT is unlikely to obtain royalty collection powers any time soon, nor would it do so without a reduction in federal transfer payments. This said, rents (a.k.a. supernormal, windfall or excess profits) from natural resources development could also be collected via a resource income tax, as outlined in the Revenue Options Paper. Such a tax should be implemented, and would raise on the order of hundreds of millions of dollars per year.

Such a tax would obviate the need for any increase in general corporate income taxes. However, the GNWT should work with other jurisdictions to stop the “race to the bottom” of corporate income tax cuts.

Rents arising from the extraction of natural capital (non-renewable resources) should not be spent on regular government operations, but should be converted to other forms of capital. In the future, when non-renewable resources are depleted, the NWT will be reliant on such investments. The GNWT should establish a Territorial Trust Fund to collect resource income tax revenues and make investments that will pay off in future when the resource economy dwindles.

Capital tax

Some corporations are able to avoid paying income tax by using accounting techniques to hide income. In order to capture some of this revenue leakage, a capital tax should be phased in over two years, raising $12.6 million per year.

Personal income taxes

Despite high and rising average incomes, inequality and poverty are serious problems in the NWT. The lowest income bracket tax rate should be reduced by 3%, the next lowest by 2%, and the next by 1%. Further annual 1% reductions for each bracket should be carried out for another three years, meaning that no income tax would be paid on the first $35,986 earned by anyone in the NWT. This would reduce revenues by $40 million by the fourth year.

Payroll taxes

The GNWT loses on the order of $12 million dollars per year due to some people earning incomes in the NWT but claiming a residence and paying taxes elsewhere. A payroll tax would help reduce this leakage, which occurs mainly in the upper ranges of incomes. Payroll taxes should be increased from 2% to 2.5% for wages and salaries above the 75th percentile of today’s income distribution, and reduced for lower amounts so that the total net revenue impact is zero.

Hotel tax and airport departure tax

A hotel tax and an airport departure tax also would help address the loss of revenue caused by people working in the NWT but living and paying taxes elsewhere. Such taxes are unlikely to affect tourism, considering their small proportion of overall travel costs. A hotel tax of 8% and an airport departure tax of $40 per flight should be instituted immediately, raising about $8.7 million per year.

Tobacco taxes

Tobacco is the number one preventable cause of death in the country, killing over 40,000 Canadians per year, and the NWT smoking rate is more than double the national rate. Taxation has been proven effective at reducing tobacco consumption, particularly among teenagers, and NWT tobacco taxes haven’t been raised in five years. Tobacco taxes should be increased to the current limit set in legislation, raising approximately $1.3 million per year, and by similar amounts in following years. There is little evidence to suggest that smuggling is an issue, but if it became one it should be addressed by law enforcement rather than by making tobacco cheaper.

Liquor revenues

Alcohol consumption costs Canada $14.6 billion per year in health impacts, lost productivity and law enforcement costs. The incidence of heavy drinking in the NWT is three to four times that of Canada as a whole. Alcohol price increases reduce consumption, yet the NWT liquor markup hasn’t been increased in five years. The markup should be increased by 40% over two years, which would raise prices of beer, wine and spirits by roughly 15% or less, and would raise about $4.8 million in annual revenues.

Commercial freight toll
The true costs of road transport include not only road building and maintenance, but also air pollution, CO_2 emissions and a host of other costs that create economic distortions. In the NWT, fuel taxes not only fail to cover the full costs of road use, they fail to cover even the financial costs. A toll of five cents per tonne-kilometre on non-local, commercial trucking should be phased in over two years, and would raise $15 million per year.

Fuel taxes and a carbon tax
Fuel taxes can help to reduce carbon emissions and conserve non-renewable fossil fuel resources. Transportation fuel taxes in the NWT are "among the lowest in Canada" and significantly below the national average. The Government has failed to allow fuel taxes to increase since 1997, letting them slip significantly against total fuel prices. Transportation fuel taxes should be restored to 1997 values over two years, and heating fuel taxes over four years. This would raise $17.8 million per year, and should be used to finance an intensive program of home energy efficiency retrofits over the next four years.

Climate change is a serious problem, especially for northerners, who have every reason to urge the world to reduce greenhouse gas emissions. However, their credibility is compromised when northern governments fail to take serious action on climate change emissions. Serious action means putting a price on emissions. Carbon taxes are now supported by a wide range of stakeholders, and several Canadian jurisdictions are moving toward them. A modest carbon tax, along the lines of the one instituted in BC, should be adopted and phased in over four years, thus raising on the order of $41 million per year.

TAXES THAT DON'T NEED TO BE CHANGED

The Revenue Options Paper discusses several other taxes, but they are not necessary to serve important public policy goals, and the other taxes discussed in this report will raise sufficient revenues. Some of these other tax options do deserve further brief comment.

Sales tax
A sales tax would be regressive, and would need to be offset by income supports, tax adjustments, and exemptions for necessities. It would encourage personal savings and investment, but other, targeted consumption taxes (e.g. tobacco, fuel, alcohol) will also serve that goal.

Healthcare premiums
Use-based premiums would discourage prevention and early treatment, thus potentially costing the system more. They also move the healthcare system closer to US-style private system, which delivers worse health outcomes and at a far higher cost.

Cost of living tax credit
Given the income supports and income tax reductions mentioned earlier, increasing this credit should not be necessary. If it were to be adjusted, it should be raised for lower and middle income earners and made even across the board.

CONCLUSIONS

The recommendations in this report include both increases and decreases in tax rates as part of an integral package of tax system reforms. This package would raise revenues, while at the same time advancing important public policy goals such as equity, health promotion, resource conservation, and environmental protection.

This package would add $23 million to general revenues in the first year and $62 million by year four (about 2%-5% of total revenues, or 9%-22% of own-source revenues). These revenues could be used for important initiatives such as preventing and treating substance addictions, home energy efficiency retrofits, increases to social assistance, job training and education, or reversing the spending cuts that were announced without public consultation in early 2008.

It would also establish and quickly grow a Territorial Trust Fund that would ensure fiscal stability for the NWT in the future when non-renewable resource revenues dwindle.