Government of Northwest Territories Gouvernement des Territoires du Nord-Ouest

NORTHWEST TERRITORIES REVENUE OPTIONS

Issued by the Honourable Robert C. McLeod
Minister of Finance

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French

Kīspin ki nitawihtīn ē nīhīyawihk ōma ācimōwin, tipwāsinān.
Cree

Tłı̨chǫ yatı k'ę̀ę̀. Dı wegodı newǫ dè, gots'o gonede.
Tłı̨chǫ

Ɂerıhtł'ís Dëne Sųłıné yatı t'a huts'elkër xa beyáyatı theɂą ɂat'e, nuwe ts'ën yółtı.
Chipewyan

Edı gondı dehgáh got'ı̨e zhatıé k'ę́ę́ edatł'éh enahddhę nıde naxets'ę́ edahłí.
South Slavey

K'áhshó got'ı̨ne xədə k'é hederı ɂedı̨htl'é yerınıwę nídé dúle.
North Slavey

Jii gwandak izhii ginjìk vat'atr'ijąhch'uu zhit yinohthan jì', diits'àt ginohkhìi.
Gwich'in

Uvanittuaq ilitchurisukupku Inuvialuktun, ququaqluta.
Inuvialuktun

ᑖᒃᑯᐊ ᑎᑎᕋᒃᑲᐃᑦ ᐱᔪᒪᒍᕕᒋᑦ ᐃᓄᒃᑎᑐᓕᕐᓯᒪᓗᑎᒃ, ᐅᕙᑦᑎᓐᓄᑦ ᐅᖄᓚᔪᓐᓇᖅᑐᑎᑦ.
Inuktitut

Hapkua titiqqat pijumagupkit Inuinnaqtun, uvaptinnut hivajarlutit.
Inuinnaqtun

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Table of Contents

Executive Summary

The Government of the Northwest Territories (GNWT) is on an unsustainable fiscal path. Over the medium term GNWT revenues are declining while expenditure pressures continue to mount. As a result, operating surpluses are quickly shrinking at the same time the GNWT needs operating surpluses to pay for infrastructure investments to address a $3 billion and growing infrastructure deficit. Borrowing is not an option because of the federally-imposed $1.3 billion borrowing limit and the need to service this debt. The choices are: increase revenues, reduce expenditures, or a combination of both.

The following paper examines the revenues the GNWT collects and provides options to generate additional revenues. All of the options presented have been considered in previous fiscal strategies but after due consideration the NWT tax system has remained relatively unchanged, usually because of concerns about the effect of increasing the tax burden on individuals and business and the resulting impact on the cost of living and on the NWT economy. If decision-makers chose to support specific revenue-raising options, further analysis would be required to ensure that decision-makers are provided with the information necessary to make a measured and balanced approach to increasing revenues that is consistent with the GNWT's long-term vision and goals.

The options are considered using the following criteria:

- their revenue-raising potential – small tax bases limit the amount that can be raised through increased taxation, even if the options would not harm the economy;
- the impact they may have on the NWT economy – the NWT's harsh climate, limited infrastructure and high transportation costs all contribute to a high cost of living and doing business, which most tax increases will exacerbate; and
- the principles of sound tax policy in order to ensure that the tax system is as predictable, fair, efficient and simple as possible.

The timing of tax increases needs to consider the current events in the global economy and the resulting implications for the NWT economy. Currently, the NWT economy is not robust due to global economic and financial uncertainty. The resource-based nature of the NWT economy makes it extremely open, which means that the NWT economy is strongly linked to the global economy and world commodity prices. Both workers and capital can easily leave the NWT when the NWT economy slows down or to another province if they are experiencing stronger economic growth.

While the GNWT's fiscal strategy will include looking at tax options, fiscal sustainability will not be achieved solely by increasing taxes on NWT residents and businesses. This would discourage business investment and economic growth, and would leave individuals and families with less disposable income at a time when costs of living are rising.

A. Introduction

The Government of the Northwest Territories (GNWT) is on an unsustainable fiscal path. Over the medium term, GNWT revenues are declining while expenditure pressures continue to mount. As a result, operating surpluses are shrinking at the same time the GNWT needs operating surpluses to pay for infrastructure investments to address a $3 billion and growing infrastructure deficit. Borrowing is not an option because of the federally-imposed $1.3 billion borrowing limit and the need to service this debt.

The choices are straight forward – raise more revenue, reduce expenditures, or a combination of both.

Increasing revenues is one option to address the fiscal challenge of not having enough revenues to address increasing demand for programs and services and to finance investments in infrastructure. However, revenue-raising options carry the risk of unintended consequences. While new revenues can be raised by increasing taxes or introducing new fees, the type of tax or fee increase can have significant consequences for individuals, families, and businesses. Without careful thought and analysis before advocating a particular revenue increase, there is an increased risk of implementing an option that can hurt the economy, discourage investment, or even push people into leaving the territory.

The following paper examines the revenues the GNWT collects and provides options to generate additional revenues. All of the options presented have been considered in previous fiscal strategies but after due consideration, the NWT tax system has remained relatively unchanged, usually because of concerns about the effect of increasing the tax burden on individuals and business.

If decision-makers are supportive of specific options, further analysis would be required. The revenue projections under these options are determined as if all other things are unchanged. Work would still need to be undertaken to test the sensitivity of the assumptions so that decision-makers are provided with the information necessary to make a measured and balanced approach to increasing revenues that is consistent with the GNWT's long-term vision and goals.

The options are considered using the following criteria:

- their revenue-raising potential – small tax bases limit the amount that can be raised through increased taxation, even if the options would not harm the economy;
- the impact they may have on the NWT economy – the NWT's harsh climate, limited infrastructure and high transportation costs all contribute to a high cost of living and doing business, which most tax increases will exacerbate; and
- the principles of sound tax policy in order to ensure that the tax system is as predictable, fair, efficient and simple as possible.

The GNWT Fiscal Situation

GNWT revenues are projected to decline by 1.7 per cent over the medium-term while expenditure pressures continue to grow by 4.1 per cent over the same period. This projection is based on the following facts:

- The majority (69 per cent) of GNWT revenues comes from the Territorial Formula Financing Grant and, therefore, growth in Territorial Formula Financing largely determines total revenue growth.

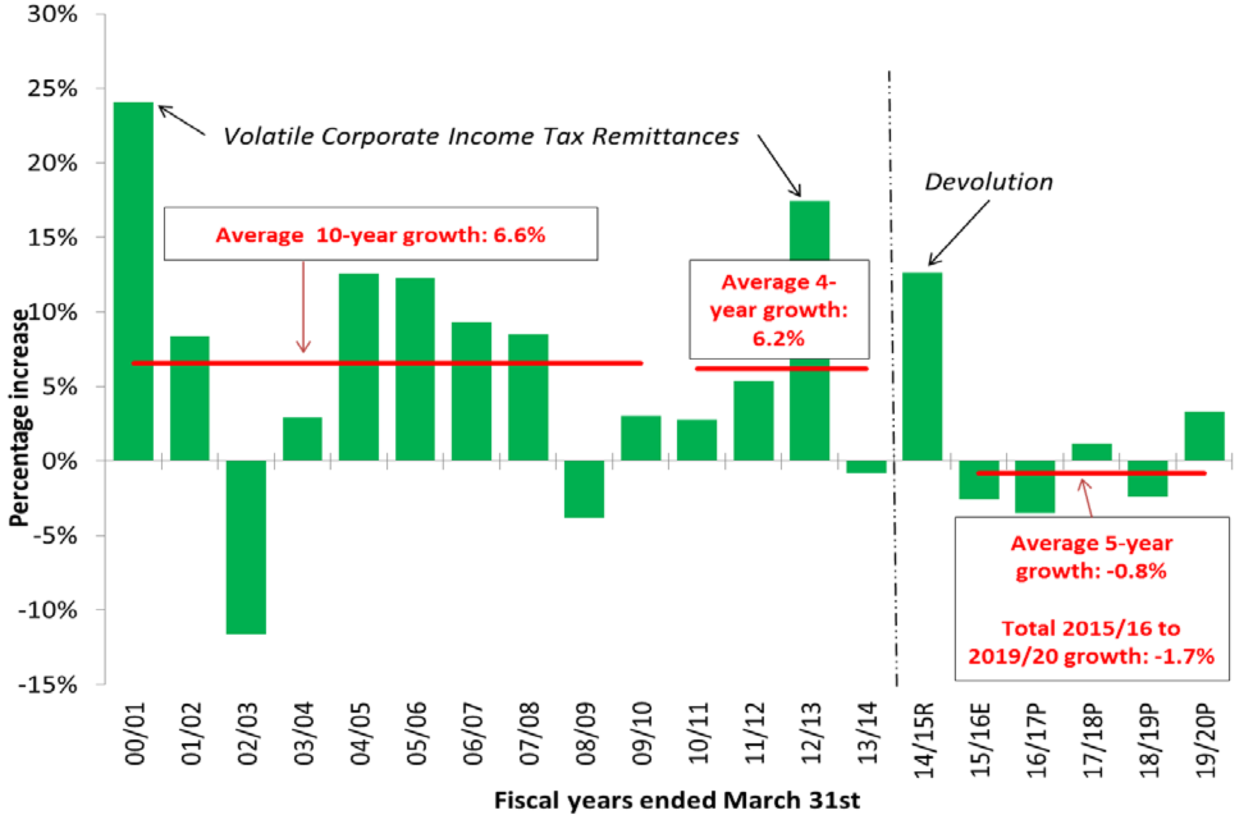
- The GNWT's tax bases are too small to fund GNWT program and service responsibilities, which is why Territorial Formula Financing is designed to cover the fiscal gap between GNWT own-source revenues and expenditure needs.

- The key variables in the Territorial Formula Financing Grant are the growth in NWT population relative to the Canadian population and the growth in provincial/local government expenditures. Growth in own-source revenues decreases Territorial Formula Financing by a corresponding but lesser amount and decreases in own-source revenues increase the Territorial Formula Financing Grant. The Grant entitlement is an estimate of the fiscal gap between what the GNWT needs to provide comparable levels of programs and services as the provinces to what it could raise at comparable levels of taxes, less a 30 per cent Economic Development Incentive discount. As economic growth shrinks the gap between expenditure need and the GNWT's ability to raise its own revenues, the Formula Financing Grant will decline but the Economic Development Incentive ensures that changes in own source revenues are only partially offset under Territorial Formula Financing.

- The slowdown in the Canadian economy means that provinces are facing slower revenue growth while addressing debt levels, providing them with few options other than to restrict expenditures. Reduced provincial/local government expenditure growth and flat NWT population growth are the main reasons for slower Territorial Formula Financing growth.

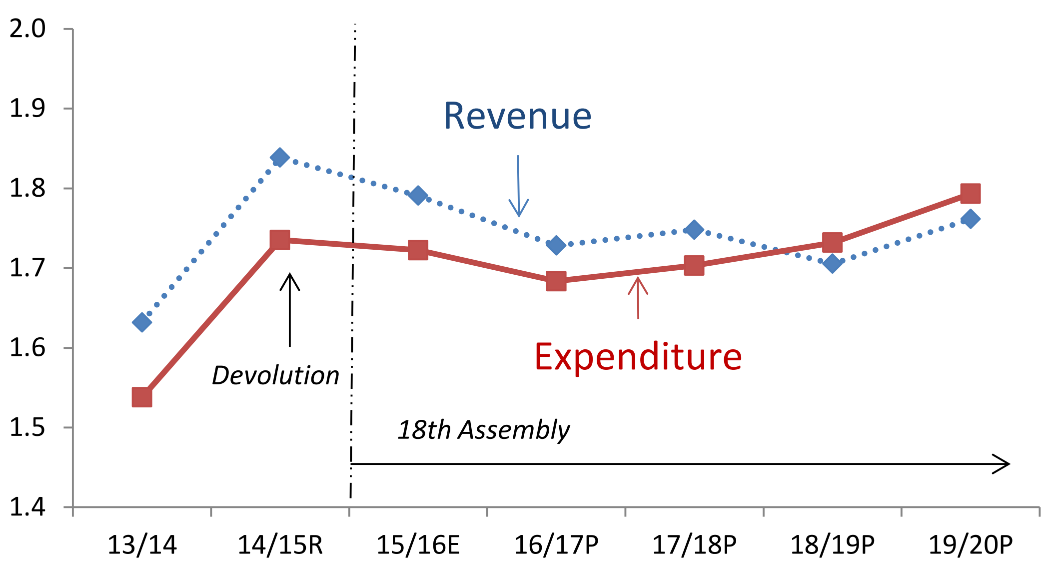
- The lower revenue projection means that there can be no expenditure growth if the GNWT's fiscal framework is to remain sustainable. Increasing expenditure growth combined with the declining revenue projection will squeeze operating surpluses. Under the current medium-term outlook (January 2016), expenditure growth is projected to increase, causing the projected surplus to fall from \$69 million in 2015-16, becoming a \$27 million deficit in 2018-19 and a \$32 million deficit by 2019-20. This means that there will be no capital investment available for the last two years of the 18th Assembly, as the *Fiscal Responsibility Policy* requires that at least half of capital investment be funded by operating surpluses. Expenditure management and/or sustained increases in revenues will be necessary to ensure operating surpluses are available to have an impact on the infrastructure deficit.

Figure 1: Revenue Performance



R: Revised; E: Main Estimate; P: Projection
Source: NWT Department of Finance

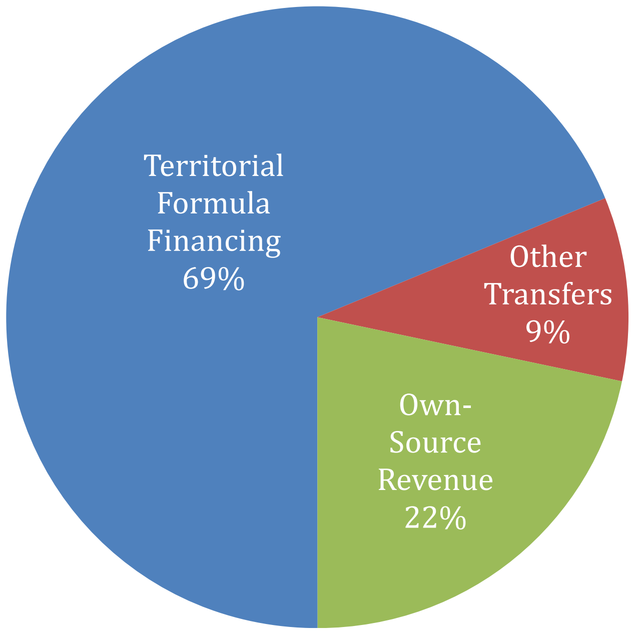
Figure 2: GNWT Fiscal Outlook ($ Billions)



R: Revised; E: Main Estimate; P: Projection
Source: NWT Department of Finance

GNWT own-source revenues are 22 per cent of total revenue, or almost $390 million in 2015-16, out of a total budget of $1.8 billion. Own-source revenues can be volatile from one year to the next, especially corporate income tax and resource revenues.

Figure 3: Shares of Total Revenue, 2015-16



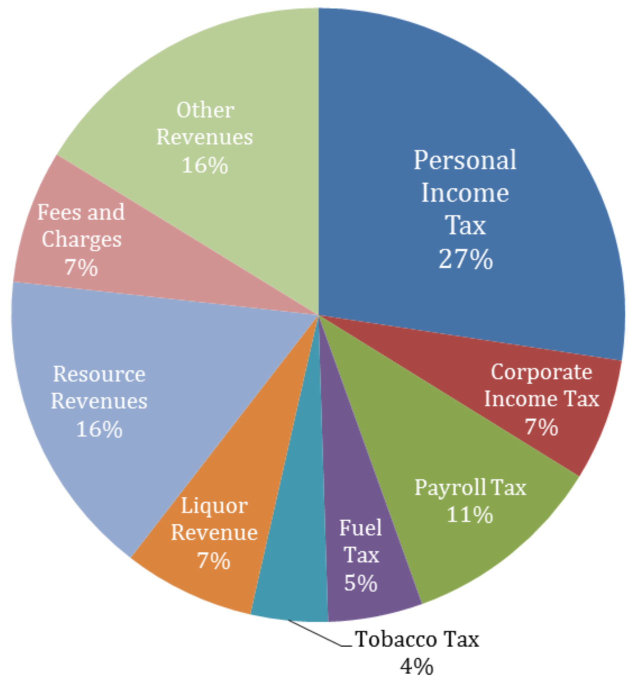
Source: NWT Department of Finance

The GNWT's own-source revenues are too small a share of total GNWT revenues for increases in tax rates to make a noticeable difference in revenue growth. On the other hand, raising taxes on people and businesses may cause revenue decline, especially if the increased taxation reduces economic activity and causes people to leave the territory. Increasing taxes will be felt disproportionately by taxpayers compared to the benefit to the GNWT's fiscal situation.

To maintain an operating surplus of at least $100 million without changing the expenditure outlook would require own-source revenues to increase by over thirty per cent. This would be equivalent to a tax increase of roughly $3,000 for every resident in the NWT. By 2018-19, maintaining a $100 million operating surplus solely through tax increases would not only remove $130 million from the local economy and reduce consumer expenditures, but it would make businesses that are unable to pass their costs onto consumers even more vulnerable. Higher taxes and fees in the territory would increase the incentive for individuals to shop in the south and online. Ultimately, the high cost of living would increase further.

Tax increases could also have an effect on recruitment and retention of NWT employees, further reducing the Territorial Formula Financing Grant.

Figure 4: Shares of Own-Source Revenue, 2015-16



Source: NWT Department of Finance

Taking advantage of room under the federally-imposed $1.3 billion borrowing limit is not a solution. Increased debt would impose higher repayments on the operating budget. The increased debt room, if it were to be totally used, would add $30 million to operating expenses for the next three decades and increase the unsustainability of the fiscal framework.

The NWT Economic Outlook

The NWT economy is feeling the effects of events in the global and Canadian economies. In particular, low commodity prices, uncertainty in the financial markets, slowing global demand and a sharply depreciating Canadian dollar are having a direct impact on the NWT economy, including reducing employment and increasing the cost of living, especially for food.

The NWT economy is dominated by the non-renewable resource sector. While all components of the economy are important, developments in the non-renewable resource sector have a more dramatic and immediate ripple effect on the rest of the economy. The mining sector has a significant impact on all other industries in the NWT through strong linkages to transportation, wholesale and retail trade, and real estate, and is directly and indirectly responsible for high-income employment. The NWT's strong overall economic performance over the past 10 years was driven by the non-renewable resource industry, both by exploration and production. However, current low commodity prices are causing investment in oil and gas industry exploration to stop and have forced the Snap Lake diamond mine to cease production, both of which have caused significant job losses. At the same time, the low Canadian dollar is causing inflation for imported products.

While the near-term outlook projects higher levels of rough diamond production, none of the plans for existing diamond mines, or those currently under construction, project production past 2031. If the Ekati mine does not develop its Jay Pipe, it may close as early as 2020. At present, there are no potential projects large enough to replace the existing diamond mines in terms of output and employment when they stop production in the medium-term and current possible projects are finding it extremely difficult to obtain financing due to weak global demand for NWT resources and general global economic uncertainty.

Economic activity, whether it is the operations of a mine or other smaller sectors such as tourism, manufacturing, commercial fishing, fur, agriculture, film and arts and crafts production, have a direct impact on employment and an indirect impact on other territorial businesses. The smaller economic sectors have room for growth but are in no position to substitute for the economic impact of a strong resource sector. Although NWT economic growth does not always get reflected in a corresponding growth in GNWT revenues because of leakages to other jurisdictions, increased economic activity does get reflected in increased income, fuel, property, and payroll tax revenue, some fees and charges, and resource royalties. However, the strongest economic link to GNWT revenues is through population growth, which increases growth in Territorial Formula Financing. A strong economy is a key factor for attracting and retaining NWT residents.

Promoting economic growth, and increasing the tax base, is important for long-run growth in GNWT revenue. Proposed actions taken under fiscal policy, whether on the expenditure or revenue side, to strengthen the GNWT's fiscal situation and restore fiscal sustainability must be evaluated on the basis of its economic implications. Any fiscal actions undertaken should, therefore, work to promote economic growth, and ought not to decrease investment, increase the cost of living or unnecessarily raise the cost of operating for NWT businesses.

Tax Policy and Objectives of the Tax System

While the main objective of taxes is to raise revenues to pay for government expenditures, the tax system is also used to achieve other objectives. For example, it is used to promote economic activity and growth, redistribute income from higher to lower income individuals, or from one region to another. Taxes can provide incentives to promote behavioural changes, such as saving for retirement or post-secondary education, and discouraging tobacco or alcohol use. Some of these objectives may compete against each other and must be carefully weighed against potential unintended consequences.

The tax system should be as predictable, fair, efficient, and simple as possible. The challenge for tax policy is to find the appropriate balance between:

- ***Expenditure needs to pay for programs and services and economic growth*** – the proper level of taxation is a critical component of good tax policy. If tax levels/rates are too low, there are not enough fiscal resources for the GNWT to pay for necessary programs and services and infrastructure, which harms economic growth as business relies on government to provide the environment that supports and promotes a healthy and skilled labour force and attracts investment. However, if tax rates are too high then businesses will not invest, will not hire people, and they will have less incentive to grow, with the result that the NWT economy suffers.

- ***Income redistribution and incentives to work and live in the NWT*** – the income tax structure currently used in all Canadian jurisdictions is designed to tax individuals based on their ability to pay so that the tax burden is less on those of lower incomes than those with higher incomes with a greater ability to pay. Each jurisdiction must find this balance based on their circumstances. The NWT, with its high cost of living and the ability of individuals to work in the NWT but live elsewhere, must be careful that higher tax burdens on higher income earners do not become a disincentive to live and work in the NWT.

- ***Businesses/industry and individuals*** – a strong NWT economy requires co-operation between industry and NWT residents. Industry requires workers to build their businesses and tax payers require industry to provide employment. Industry and residents rely on government to provide the programs and services that produce an NWT in which people want to live and work. This relationship means that individuals and industry must contribute revenues to pay for the government's expenditures that create the environment that supports a strong economy. Since investment capital is mobile and competition for business and labour is global, too high a tax burden on industry and labour will harm economic growth; on the other hand, industry and NWT residents must contribute to the government programs and services on which they rely.

Overlying consideration of the appropriate balance is how much the government desires to spend. The more government needs or wants to spend, the more revenue it needs to raise.

The following describes the objectives used by the GNWT to evaluate tax rate changes or new taxes. Some of these objectives may conflict with others. No single tax change will meet all objectives.

Taxes should raise sufficient revenues.

The main objective of the tax system is to raise revenues so that the government is able to provide essential services. Taxes should raise revenue for government in a way that is as fair, efficient and simple as possible.

Revenue raising potential needs to take into account the costs of implementing and administering a tax and other costs the tax may create for government operations.

Taxes should be fair.

A fair tax system levies taxes proportional to a taxpayer's ability to pay.

Taxpayers who have a similar ability to pay should have a similar tax burden. Those who have a greater ability to pay should bear a greater burden. Ability to pay is measured by income, adjusted to reflect varied family and personal circumstances and the costs of earning income.

The tax system should be balanced.

Governments levy taxes on a variety of bases, in part to provide a mix of tax sources that can minimize the risk of any one base declining substantially, but also to spread the tax burden across sectors of the economy and individuals. Changes to the tax system must take into account resulting shifts in the tax burden.

The tax system should be neutral.

An economically efficient tax system should influence a taxpayer's behaviour as little as possible. Decisions made based on tax considerations, rather than sound business or personal reasons, can cause distortions in the economy. However, in some cases, tax incentives may increase efficiency if they encourage activities which benefit society or activities which indirectly benefit the taxpayer.

Taxes may help promote other Government objectives.

Taxes may be used to promote economic, social or environmental goals, such as stimulating certain industries or regions, or encouraging or discouraging certain kinds of activities. For example, higher alcohol or tobacco taxes should lead to lower consumption. However, increases in tobacco taxes, for example, relative to those of other jurisdictions could increase illegal activities like smuggling and foster black market sales.

The tax system should be simple.

The tax system should be simple and allow for easy compliance. The reason for exemptions, credits or other special measures should be weighed against the complexity they add to the system. Complex legislation may be necessary, but compliance by the taxpayer should be as easy as possible.

The NWT tax system should be competitive and predictable.

A tax system must be competitive with those in other jurisdictions. Most large corporations in the NWT operate in other provinces and in other countries, and many individuals, especially those at higher income levels, are mobile and can easily move within Canada. If the tax burden is too heavy, these corporations may transfer income and taxes outside the NWT or individuals may move to a jurisdiction with a lower tax rate, reducing the government's tax base and revenues. The cost of living and doing business in the NWT is high compared to southern jurisdictions, reducing the attractiveness of the territory as a place to live and invest. Higher taxes increase this relative disadvantage.

The tax system should also be stable. Changes should be infrequent and, where possible, should be predictable to the taxpayer.

Objectives of Fees and Charges

Fees are sometimes viewed by the public as taxes; however, fees are charged to offset the cost of providing specific services to users. If a fee is excessive and does not have a reasonable relationship to the cost of the service provided, it might be considered a tax and therefore unlawful as being collected without enacted legislation.

Objectives of a Royalty System

Royalties are not taxes.

Royalties are payments for exclusive rights to exploit Crown/government property (resources) granted to the developer by the government. In the NWT, the calculation of royalty payments is based on the profits generated by each project. Royalties as payment for a resource exploitation privilege is what makes royalties fundamentally different from taxes, which are imposed on taxpayers (individuals or business) and so are compulsory payments to government to pay for government programs and services.

To the developer of a resource project, royalties tend to be viewed as taxes and this perspective clearly needs to be understood by governments in designing their royalty systems. To industry, the royalty is part of the cost of the resource extraction, similar to operating costs and taxes. To the GNWT, as owner/manager of the resource, the royalty should represent the best price it can get for the resource without compromising the viability of the purchaser to develop the resource. Industry wants to develop NWT resources to generate income and the GNWT wants resource development to provide employment, strengthen the economy and generate revenues in the form of both royalties and taxes to pay for government programs and services.

While royalties are payments made in compensation for development rights and not taxes, the considerations for designing good systems for royalty and taxation are similar. Governments take into consideration the entire fiscal system including taxes and other levies and the level of government services provided to industry when designing royalty systems since these considerations bear on how much industry is prepared to pay for the resource.

B. Current NWT Tax Regime

Limits to What the GNWT May Tax

Under the *Northwest Territories Act*, the GNWT has the legislative authority to levy direct taxes and licensing within the NWT in order to raise revenue for territorial, municipal or local purposes; however, the GNWT is not authorised to impose an indirect tax on a producer or manufacturer, nor duties on goods imported into the territory.

The GNWT is also bound by the terms of the *Tax Collection Agreement* with Canada. The three territories and all provinces, except Quebec, have signed these agreements that harmonize income tax legislation and collection, and minimize administrative costs for taxpayers and governments. Under the tax collection agreements, the Canada Revenue Agency administers and collects territorial personal and corporate income taxes on behalf of the GNWT as long as the territorial income tax legislation uses the federal definition of taxable income. The common tax base is the cornerstone of the tax collection agreements; it minimizes compliance and administrative costs for tax payers and governments.

Tax policy has economic consequences that also limit how much the GNWT may tax. Although the GNWT may have the legal authority to impose a tax, taxpayers are free to take legal measures to minimize their tax burden, including restructuring their affairs, moving to other jurisdictions, or changing their purchasing habits. These changes may affect the yield from any particular tax measure. In addition, some residents may attempt to evade tax, reducing revenues and increasing administration and compliance costs for government.

Current Tax Regime

The GNWT levies the following taxes:

- tax on individuals: personal income tax, payroll tax, and property tax;
- tax on businesses: corporate income tax and property tax; and,
- tax on consumption: fuel taxes, tobacco taxes, insurance tax.

In lieu of levying a tax on liquor, the NWT Liquor Commission applies a mark-up on alcoholic beverages through its control of distribution, prices and sales of liquor in the territory.

Table 1 shows NWT tax and liquor revenues over the past five fiscal years.

Table 1: NWT Tax and Liquor Revenues

	Five year average	2014-15	2013-14	2012-13	2011-12	2010-11
			(thousands of dollars)			
Personal income tax	96,996	110,810	89,451	105,360	94,679	84,681
Corporate income tax	60,194	31,815	81,256	108,422	22,660	56,818
Tobacco tax	16,248	16,053	15,683	15,587	17,108	16,810
Fuel tax	18,267	19,260	18,514	18,608	18,851	16,103
Payroll tax	39,948	40,250	41,245	41,619	39,662	36,965
Property tax	26,490	28,261	27,866	27,058	24,883	24,381
Insurance tax	4,574	4,676	4,645	4,763	4,505	4,283
Total taxes	262,718	251,125	278,660	321,417	222,348	240,041
Liquor revenue	24,473	25,003	24,124	25,136	24,182	23,920
Total	287,191	276,128	302,784	346,553	246,530	263,961

Table 2 compares provincial-territorial tax rates for various taxes. With the exception of tobacco and payroll tax rates, NWT tax rates are below provincial-territorial averages and the NWT does not have a sales tax. The NWT's high cost of living is the main reason that there is no sales tax and that other tax rates are kept lower than most provinces.

Table 2: Provincial-Territorial Tax Rates – as at December 2015

	Combined top marginal PIT rates[1] (%)	Retail sales tax (%)	Fuel tax: Gasoline (¢/litre)	Fuel tax: Diesel (¢/litre)	Tobacco tax ($/carton)	Payroll tax (%)	Corporate income tax: Small (%)	Corporate income tax: Large (%)
Northwest Territories	43.05	-	10.7[2]	9.1[3]	57.20	2.00	4.0	11.5
Nunavut	40.50	-	6.4	9.1	50.00	2.00	4.0	12.0
Yukon	44.00	-	6.2	7.2	42.00	-	3.0	15.0
British Columbia	45.80	7.0	21.2	22.7	47.80	-	2.5	11.0
Alberta	40.25	-	13.0	13.0	50.00	-	3.0	12.0
Saskatchewan	44.00	5.0	15.0	15.0	50.00	-	2.0	12.0
Manitoba	46.40	8.0	14.0	14.0	59.00	2.15	0.0	12.0
Ontario	49.53	8.0	14.7	14.3	27.95	1.95	4.5	11.5
Quebec	49.97	9.975	19.2	20.2	29.80	4.26	8.0	11.9
New Brunswick	54.75	8.0	15.5	21.5	38.00	-	4.0	12.0
Nova Scotia	50.00	10.0	15.5	15.4	51.04	-	3.0	16.0
Prince Edward Island	47.37	9.0	13.1	20.2	50.00	-	4.5	16.0
Newfoundland & Labrador	44.30	8.0	16.5	16.5	47.00	2.00	3.0	14.0

Notes:

1. Highest combined 2015 federal-provincial/territorial personal income tax rates including provincial surtaxes.
2. The on-highway gasoline tax rate is shown. The NWT off-highway gasoline tax rate is 6.4 ¢/litre (in practice the NWT is the only jurisdiction to tax off-road consumption - others offer rebates or exemptions).
3. The motive diesel tax rate is shown. The non-motive diesel tax rate is 3.1 ¢/litre.

Taxes on Individuals

a. Personal income tax (PIT)

Personal income tax is levied on an individual's taxable income, which, because of the *Tax Collection Agreement*, uses the same definition of taxable income as under the federal *Income Tax Act*. An individual's gross territorial income tax is determined by applying applicable tax rates to the individual's taxable income, which is calculated after allowing for deductions such as Registered Retirement Savings Plan (RRSP) contributions or the Northern Residents Deduction. A taxpayer pays net NWT income tax, which is the gross NWT tax minus territorial tax credits. A tax filer is considered a resident of the NWT for territorial personal income tax purposes if the individual lived in the territory on December 31st of a given tax year.

The NWT has a progressive income tax structure, which means that as income increases the tax burden increases. The progressive system is created by applying higher tax rates to higher levels of income, referred to as tax brackets. These tax brackets are adjusted annually by the change in the Canada Consumer Price Index (CPI).

The 2015 NWT tax rates and brackets are as follows:

- 5.9% on the first $40,484 of taxable income +
- 8.6% on the next $40,487 +
- 12.2% on the next $50,670 +
- 14.05% on the amount over $131,641

The following example shows how gross (before tax credits are deducted) NWT personal income tax is calculated for taxable income of $85,000 and $150,000. As a result of the different tax rates on different levels of income, the effective tax rate for the individual earning $85,000 is 7.5 per cent and the effective tax rate for the individual earning $150,000 is 9.75 per cent.

	Taxable income $85,000			Taxable income $150,000		
Tax bracket	Income in each bracket	Tax rate	NWT personal income tax	Income in each bracket	Tax rate	NWT personal income tax
$0-$40,484	$40,484	5.90%	$2,389	$40,484	5.90%	$2,389
$40,484-$80,971	$40,487	8.60%	$3,482	$40,487	8.60%	$3,482
$80,971-$131,641	$4,029	12.20%	$492	$50,670	12.20%	$6,182
Over $131,641	$0	14.05%	$0	$18,359	14.05%	$2,579
	$85,000	7.50%	$6,362	$150,000	9.75%	$14,632

PIT has been the highest tax revenue source for the NWT, averaging over $97 million annually over the past five years (Table 1) before accounting for two related expenditure items: the NWT child benefit and the refundable cost of living tax credit, which annually cost the GNWT about $1 million and $20 million, respectively.

b. Payroll tax

The NWT payroll tax is a 2 per cent tax on employment income. Unlike the progressive personal income tax, the payroll tax is a proportional tax because all taxpayers pay the same 2 per cent of their employment income, regardless of how much employment income they earn.

The NWT payroll tax was introduced in 1993 at one per cent tax (increased in 2005 to two per cent) in an effort to capture tax revenues from non-resident (fly in/out) workers who work in the NWT but who live elsewhere. These fly in/out workers benefit from the high wages offered in the NWT but do not contribute to GNWT personal income tax revenues that help pay for the programs and services necessary to support the businesses that hire them.

The GNWT collects an average of $40 million in payroll tax annually (Table 1), of which about $10 million is paid by non-resident workers.

Non-resident Workers

- Non-resident or “fly-in/fly-out” workers are individuals who work in one province or territory, but reside in another.
- The NWT has a significant non-resident labour force because the NWT resident workforce is too small to meet the employment needs of the NWT economy. These workers are most commonly employed in the NWT’s resource and construction industries, which account for two-thirds of total earnings paid to non-resident workers.
- Large numbers of non-resident workers represent lost potential economic activity in the NWT, and lost tax revenue to the GNWT.
- Between 2003 and 2011, non-resident workers ranged between 5,700 and 8,600 workers, accounting for roughly one third of the NWT workforce; the second highest rate (after Nunavut) in the country and significantly higher than in all provinces.
- Nearly half of non-resident employees working in the NWT claim residency in either **Alberta** or **British Columbia**.
- Between 2003 and 2011 the number of NWT residents who worked in another jurisdiction (mainly Alberta, British Columbia, and Nunavut) ranged between 1,400 and 1,900.

c. The cost of living tax credit

The refundable cost of living credit (COLTC) was introduced through the income tax system when the payroll tax was introduced. The COLTC is available to all NWT tax filers, regardless of their income sources. The credit has increased several times since 1993, with the most recent change in 2005.

The maximum COLTC is capped at $942. Low-income couples and individuals over 18 years of age are also eligible for a cost of living supplement. For couples, the minimum credit is $700 and only one person can claim the supplement. The minimum COLTC for single filers is $350.

The COLTC is calculated as follows:

Adjusted Net Income (ANI)	Credit Amount
Less than $12,000	ANI x 2.60%
$12,001 to $48,000	$312 + 1.25% x (ANI - $12,000)
$48,000 to $66,000	$762 + 1% x (ANI - $48,000)
Over $66,000	$942

The COLTC costs the GNWT about $20 million annually.

d. Comparison to other provinces and territories

Table 2 compares the combined federal and territorial top marginal tax rate to those in other provinces and territories The NWT has the third lowest combined top personal income tax rate in Canada. Figure 5 to Figure 10 compare the NWT personal income tax burden to those in other provinces and territories at three employment income levels: $40,000, $80,000 and $130,000 based on 2013 tax rate information for single individuals with no children and one-income couples with two children under six years of age. The impact of the territorial payroll tax is included in this comparison.

The comparison shows that the NWT's personal income tax burden is competitive with other jurisdictions. At the $40,000 income level, the NWT has the second lowest level of tax for a single earner and fourth for a single earner with two children. At higher income levels, the NWT moves closer to the average but generally the NWT's tax burden is below the national median. Even with changes in tax regimes since 2013, the NWT has some of the lowest personal income tax rates in the country.

Figure 5: 2013 Provincial-Territorial Personal Income Tax
Single tax filer – No children - $40,000 employment income

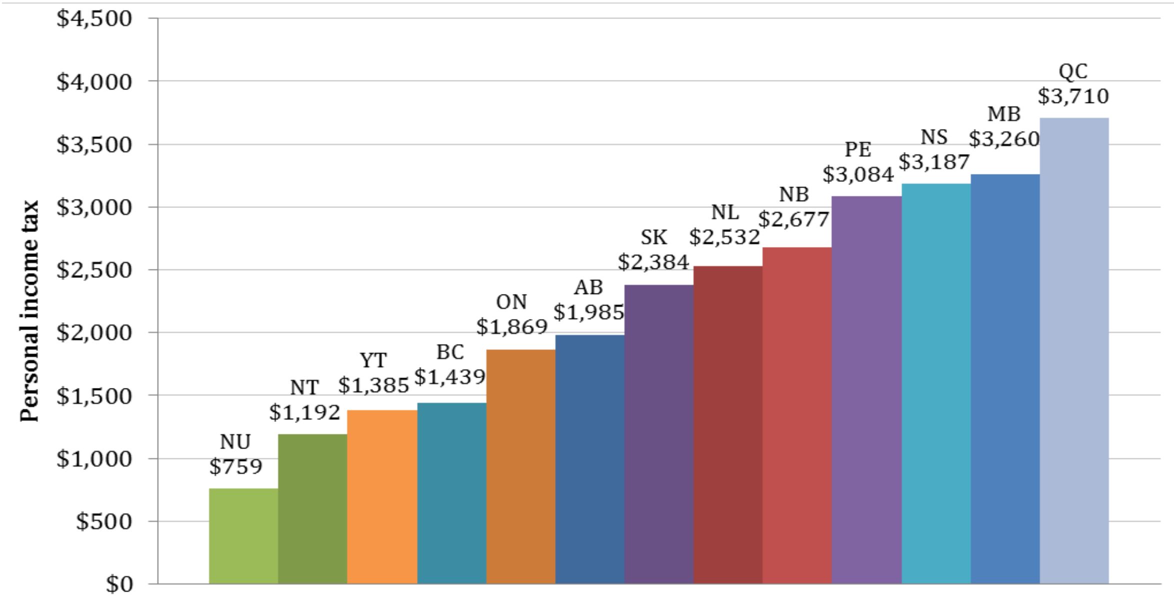


Figure 6: 2013 Provincial-Territorial Personal Income Tax
One earner couple – Two children aged under 6 years - $40,000 employment income

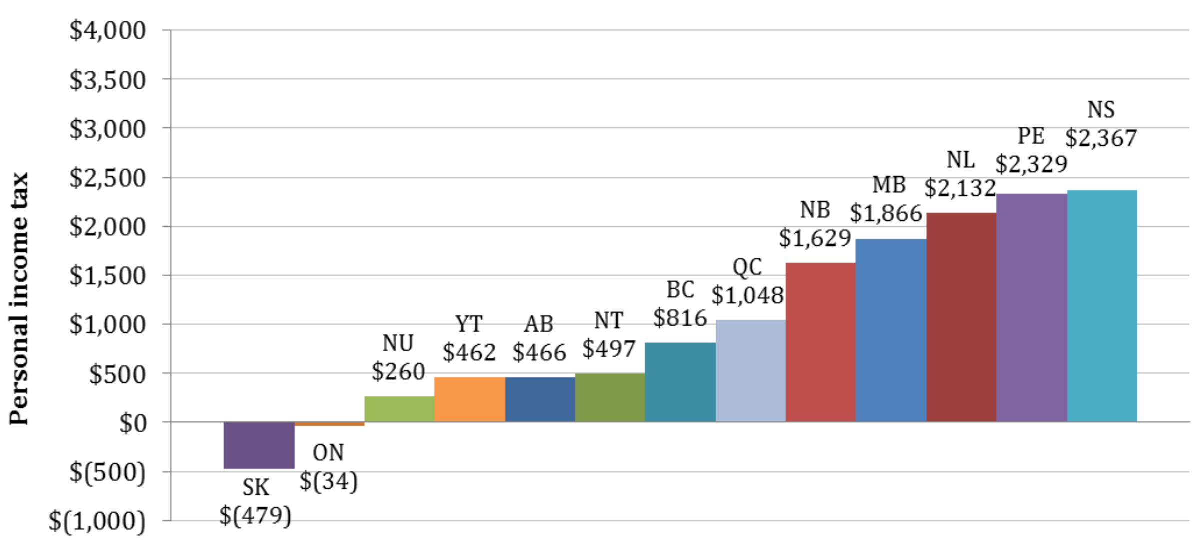


Figure 7: 2013 Provincial-Territorial Personal Income Tax
Single tax filer – No Children - $80,000 employment income

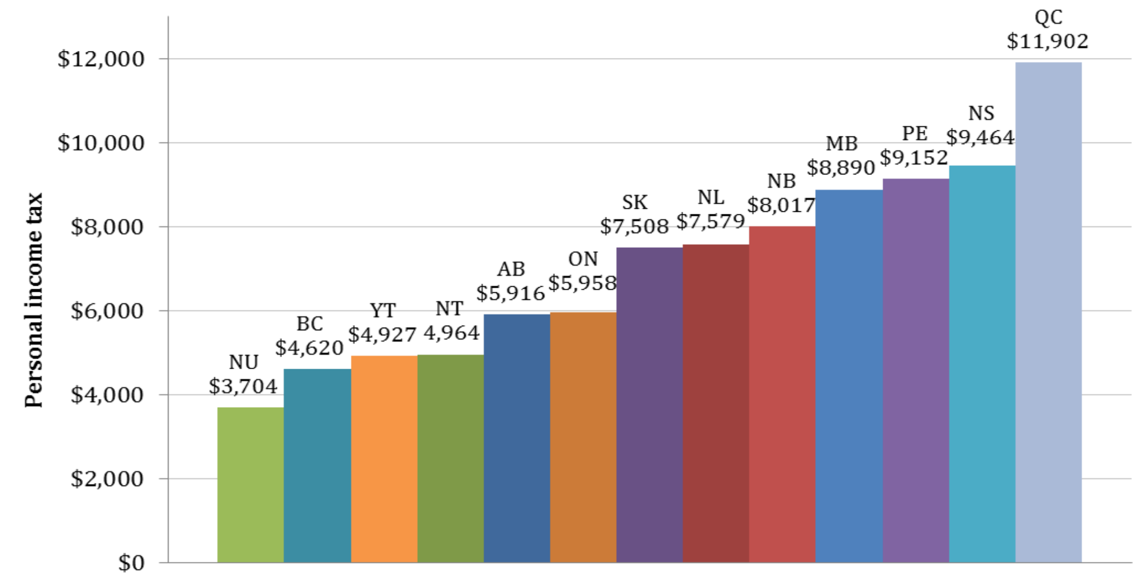


Figure 8: 2013 Provincial-Territorial Personal Income Tax
One earner couple – Two children aged under 6 years - $80,000 employment income

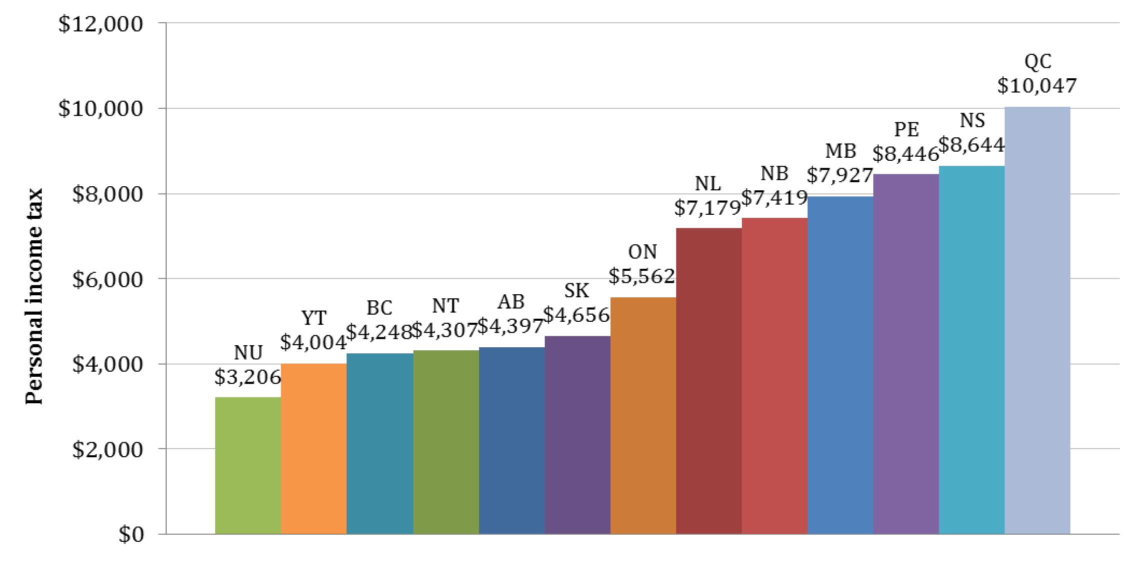


Figure 9: 2013 Provincial-Territorial Personal Income Tax
Single tax filer – No children - $130,000 employment income

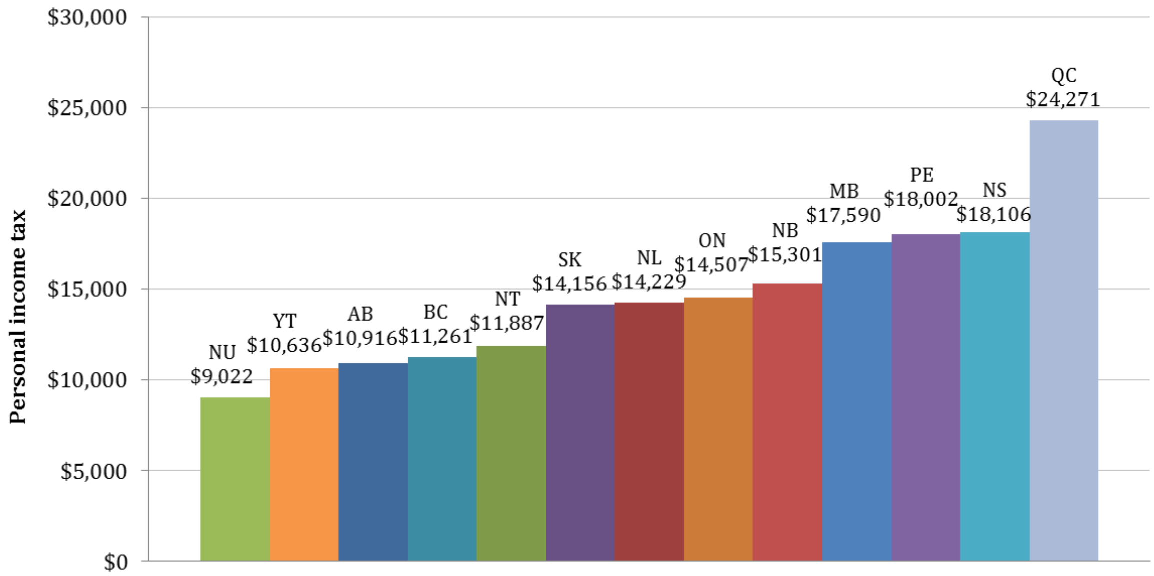
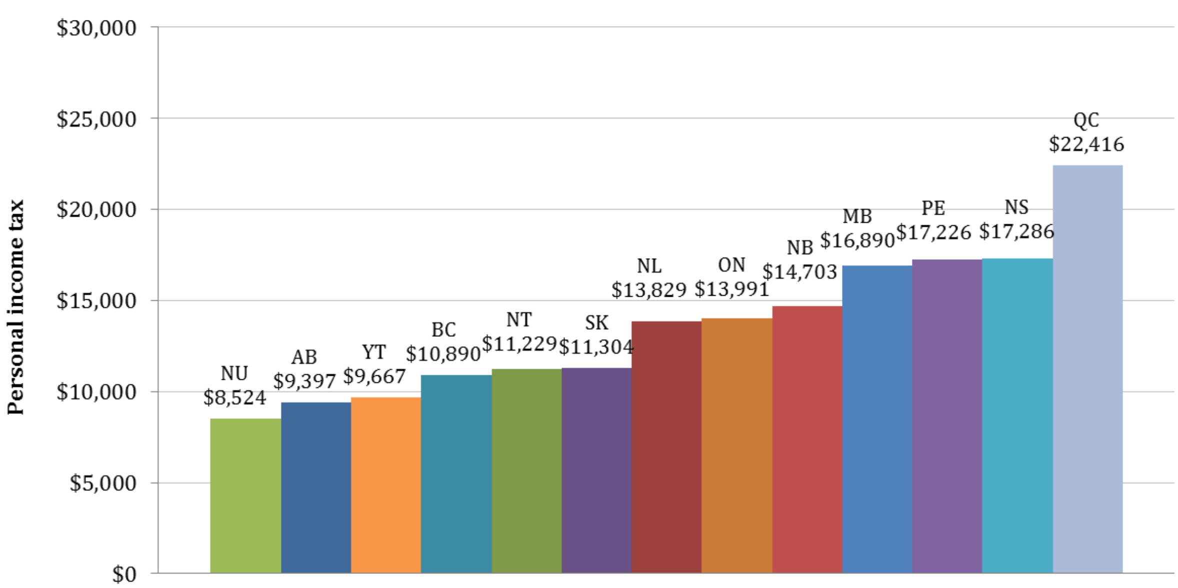


Figure 10: 2013 Provincial-Territorial Personal Income Tax
One earner couple – Two children under 6 years - $130,000 employment income



The NWT competes primarily with Alberta and Western Canada generally for skilled workers and, therefore, Alberta's personal income tax structure is of particular interest to the GNWT. The above comparison is based on the 2013 tax system. The Alberta 2015-16 Budget (October 2015) introduced graduated income tax rates over two years with the top tax rate rising from 11.25 per cent in 2015 to 15 per cent in 2016. Table 3 compares current NWT tax rates and brackets with Alberta's 2015 and 2016 graduated tax structures.

Table 3: NWT-Alberta PIT Tax Rate and Bracket Comparison

NWT		ALBERTA		
Taxable income brackets	2015 Tax Rate	Taxable income brackets	2015 Tax Rate	2016 Tax Rate
$0 to $40,484	5.90%	$0 to $125,000	10%	10%
Over $40,484 up to $80,971	8.60%	Over $125,000 up to $150,000	10.5%	12%
Over $80,971 up to $131,641	12.20%	Over $150,000 up to $200,000	10.75%	13%
Over $131,641	14.05%	Over $200,000 up to $300,000	11%	14%
		Over $300,000	11.25%	15%

Figure 11 to Figure 14 compare tax burdens under the NWT's tax structure with tax paid under Alberta's flat tax and 2016 graduated tax regimes for single filers and single earner couples earning between $100,000-$200,000 and $200,000-$400,000. The Figures show that relative to the flat rate tax regime, Alberta's graduated rates diminish the difference between the tax paid by high income Alberta and NWT tax filers, with minimal impact at low incomes below $100,000.

Figure 11: Single Tax Filer - Comparison of NWT & Alberta Flat Rate & Graduated PIT Structures: Employment income $100,000 - $200,000

Figure 12: Single Tax Filer - Comparison of NWT & Alberta Flat Rate & Graduated PIT Structures: Employment income $200,000 - $400,000

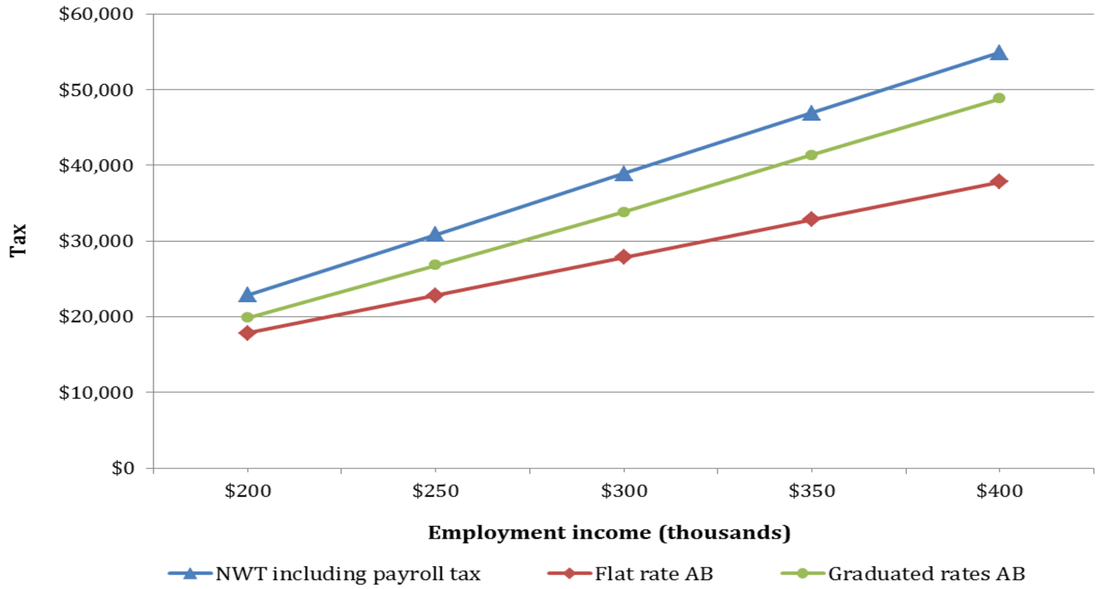
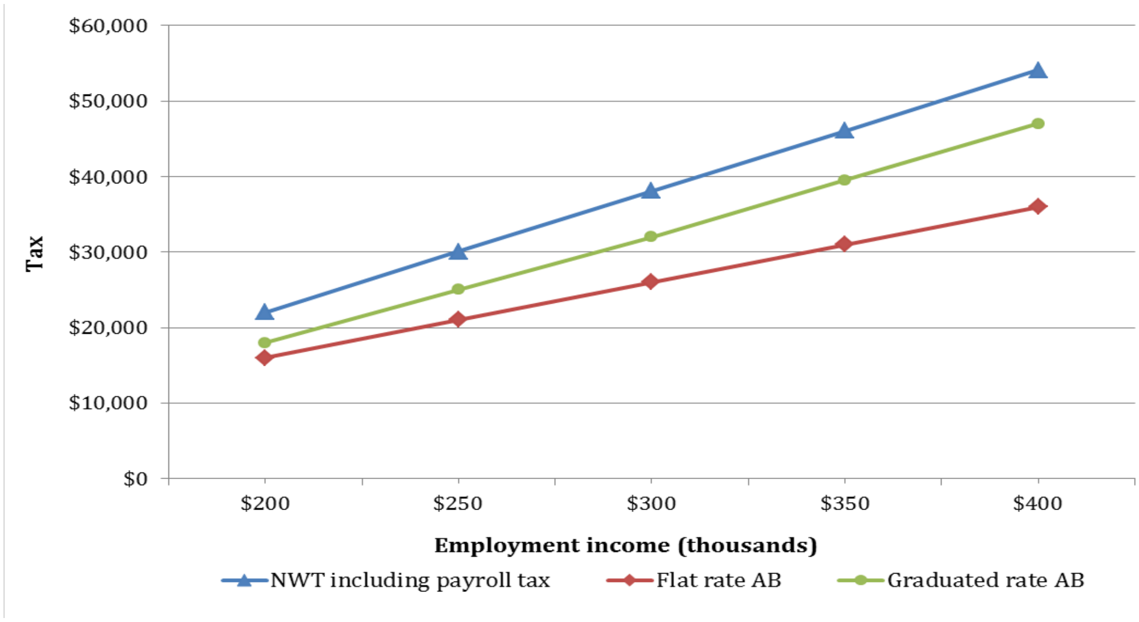


Figure 13: Single Earner Couple – Comparison of NWT & Alberta Flat Rate & Graduated PIT Structures: Employment income $100,000 - $200,000

Figure 14: Single Earner Couple – Comparison of NWT & Alberta Flat Rate & Graduated PIT Structures: Employment income $200,000 - $400,000



Taxes on Business

a. Corporate income tax (CIT)

The NWT corporate income tax structure imposes two tax rates on NWT corporate taxable income:

- a general tax rate of 11.5 per cent, and
- a small business rate of 4 per cent for Canadian controlled private corporations (CCPC) with taxable income up to $500,000.

In accordance with the *Tax Collection Agreement*, the NWT uses the same definition of corporate taxable income as the federal government.

Corporate income tax is considered a significant own-source revenue for the GNWT but its importance varies significantly year-over-year as corporate income is volatile. The NWT economy is resource-based and corporate income tax is paid mainly by a few large companies in the mining, and oil and gas sectors. The profitability of these resource companies can fluctuate significantly from year-to-year depending on factors such as operating costs and global commodity prices. From 2005-06 to 2014-15, corporate income tax averaged $60 million but ranged from $17 million to $108 million.

Despite these fluctuations, on average the large, mainly resource, companies account for 80 per cent of NWT corporate income tax revenues. The remaining 20 per cent come from Canadian controlled private corporations. About 75 per cent of NWT businesses are Canadian controlled private corporations, but 11 per cent of these businesses are subject to the general corporate tax rate, 35 per cent pay tax at the small business rate and the remaining 54 per cent do not pay any income tax. The last category includes taxable small businesses with no taxable income and exempt businesses such as incorporated charities.

If the GNWT were to offer a tax incentive to the small business sector, a small business tax rate reduction would benefit these businesses more than an increase in the business limit, but would be of no benefit to the approximately 1,000 firms that usually do not pay corporate income tax.

Table 2 compares NWT CIT rates to those in other jurisdictions. The NWT has the highest small business corporate income tax rate among the five western provinces and territories. However, the NWT general corporate tax rate is slightly below the national average.

Other Taxes

a. Fuel tax

The NWT levies fuel taxes on all fuels used in the NWT except propane, natural gas and heating fuel.

Unlike most provinces and territories where fuel tax exemptions or rebates are available for fuel used off-road, the NWT fuel tax is based on how the fuel is used regardless of where it is used. As a consequence, the NWT is one of the few jurisdictions in Canada that taxes fuel used in production as well as in transportation. The NWT on-highway gasoline tax is ad valorem (17 per cent of the prescribed retail price) and all other fuel taxes except the aviation fuel tax rate are a percentage of the on-highway gasoline tax rate. The aviation fuel tax rate is set at one cent per litre.

NWT fuel tax rates have not changed since 1997 due to concerns about the impact of higher taxes on the territorial economy. NWT gasoline and motive diesel tax rates are comparable to those in other provinces and territories (Table 2).

Current fuel tax rates are shown in Table 4.

Table 4: NWT Fuel Tax Rates

	Factor[4]	Tax per litre	2014-15 Volumes (millions/litres)	2014-15 Revenues ($ millions)
On-highway gasoline[1]		$0.107	42.38	4.53
Off-highway gasoline[2]	0.60	$0.064	5.68	0.36
Motive diesel	0.85	$0.091	97.95	8.91
Non-motive diesel[3]	0.29	$0.031	158.13	4.90
Railway diesel	1.07	$0.114	0.21	0.02
Aviation		$0.010	52.24	0.52

Notes:

1. The on-highway tax rate applies in communities served by the NWT highway system.
2. The off-highway rate applies in communities not served by NWT all-weather roads.
3. The non-motive tax rate applies to fuel used in stationary equipment such as power generation and pumps.
4. Section 2(1) of the *Petroleum Products Tax Act* sets tax rates for off-highway gasoline, motive diesel, non-motive diesel and railway diesel as the on-highway gasoline tax rate times the factor shown. The aviation fuel tax rate is set at 1¢ per litre.

b. Tobacco tax

Tobacco taxes are imposed on all tobacco products shown in Table 5. Tobacco tax rates are set by the Minister of Finance based on *Quarterly Retail Price Survey* calculations described in regulation. The Minister may choose to not raise tobacco taxes, even though the quarterly retail price survey indicates that it is possible, but if the Minister chooses to raise tobacco tax rates, then they must be raised in accordance with the results of the price survey.

The Department of Finance conducts the quarterly retail price surveys which are used to determine if a tobacco tax rate increase is warranted. Based on these surveys, all tobacco taxes could be increased; however, the cigarette tax rate has not changed from the current rate of $57.20 per carton set April 1, 2011 due to concerns about smuggling. The NWT has some of the highest taxes on tobacco products and has the second highest cigarette tax after Manitoba (Table 2). Smuggling is a real concern.

Table 5: Historical NWT Tobacco Tax Rates

	Feb 1 2014	Jul 1 2013	Apr 1 2011	Apr 1 2010	Apr 1 2009
Cigarettes					
- per cigarette	$0.286	$0.286	$0.286	$0.274	$0.268
- per carton of 200	$57.20	$57.20	$57.20	$54.80	$53.60
Loose tobacco					
- per gram	$0.266	$0.200	$0.188	$0.186	$0.192
- per 200 grams	$53.20	$40.00	$37.60	$37.20	$38.40
Cigars					
- % of suggested retail price	75	75	75	75	75

c. Property tax and school levies

The GNWT collects general property tax and education tax in non-tax based communities and the hinterland. Non-tax based communities are all NWT communities except tax-based communities of Yellowknife, Fort Smith, Fort Simpson, Hay River, Inuvik and Norman Wells. Outside Yellowknife, tax-based communities collect education tax on behalf of the GNWT. Yellowknife collects education tax on behalf of the Yellowknife school boards.

The Minister of Finance sets annual general mill rates for non-tax based communities as well as education mill rates for all communities except Yellowknife. Property tax mill rates are adjusted annually based on the change in the consumer price index for Yellowknife; however, under the New Deal for Community Governments (2005) a non-tax-based community may make a request to the Minister for a general mill rate increase as a way to raise additional revenue.

Table 6 shows 2015 property tax and education mill rates.

Table 6: 2015 Property Tax and Education Mill Rates

	2015 General mill rate	2014 General mill rate	2014-15 Tax Revenue	2014-15 Per Cent Shares
General Taxation Area				
- Class 3 (Hydrocarbons)	11.28	11.09	$90,343	0.4%
- Class 4 (Mining)	10.04	9.87	$18,337,894	87.2%
- Class 5 (Pipelines)	23.39	23.00	$1,625,158	7.7%
- Other classes	2.25	2.21	$977,362	4.6%
Total tax revenue			$21,030,758	100.0%

	Education mill rate	Education mill rate	2014-15 Tax Revenue	2014-15 Per Cent Shares
General Taxation Area	2.07	2.04	$4,853,138	67.1%
Fort Simpson	2.72	2.67	$153,997	2.1%
Fort Smith	3.90	3.83	$336,173	4.6%
Hay River	2.49	2.45	$667,388	9.2%
Inuvik	2.71	2.66	$612,627	8.5%
Norman Wells	3.33	3.27	$606,921	8.4%
Total tax revenue			$7,230,244	100.0%

d. Insurance tax

The GNWT levies a 3 per cent tax on insurance premiums and an additional 1 per cent tax on fire insurance premiums. Insurance tax rates have not changed for over twenty years but are in line with the rates charged in other provinces (Table 7). Insurance tax accounts for less than 2 per cent of total GNWT tax revenues, averaging $4.5 million over the last five years.

Table 7: 2015 Provincial/Territorial Insurance Tax Rates

Jurisdiction	Premium Tax: Life, accident and sickness	Premium Tax: Property and casualty	Fire [1] tax
Northwest Territories [2]	3%	3% or 4%	nil
Nunavut [2]	3%	3% or 4%	nil
Yukon [2]	2%	2% or 3%	nil
British Columbia [3]	2%	4% or 4.4%	Nil
Alberta [4]	2%	3%	nil
Saskatchewan	3%	4%	1%
Manitoba	2%	3%	1.25%
Ontario [5]	2%	3% or 3.5%	nil
Quebec	nil	9%	nil
New Brunswick	2%	3%	1%
Nova Scotia	3%	4%	1.25%
Prince Edward Island	3.5%	3.5%	1%
Newfoundland	4%	4%	nil

Notes:

[1] Fire tax rates are levied under Fire Prevention Act or similar legislation of each jurisdiction.

[2] An additional 1% tax on fire insurance premium in the NWT, Yukon and Nunavut.

[3] Premium tax on property is 4.4% and on others is 4%.

[4] An increase in life, accident and group premium tax to 3% and an increase to other insurance to effective April 1, 2016.

[5] Premium tax on property is 3.5% and on others is 3%.

e. Liquor mark-ups

The NWT Liquor Commission controls sales and distribution of liquor products in the territory. Liquor sales in the NWT generate about $24.5 million for the GNWT annually. Instead of a tax, prices are marked up as determined by the Minister of Finance.

Price mark-ups were increased by 10 per cent in 2009, and subsequently adjusted for inflation in 2010, 2011 and 2012 (Table 8). They have remained unchanged since 2012 due to concerns about more purchases from outside the NWT. Liquor prices in the NWT are already among the highest of provinces and territories (Table 9).

Table 8: Liquor Mark-ups

	Apr 1 2012	Apr 1 2011	Apr 1 2010	Apr 1 2009
	(mark-up/litre)			
Spirits	$29.98	$29.08	$28.59	$28.42
Wine	$8.92	$8.65	$8.51	$8.46
Beer	$2.22	$2.15	$2.11	$2.10
Coolers	$3.47	$3.37	$3.32	$3.30
Cider	$2.29	$2.22	$2.18	$2.17

Table 9: Retail Price Ranking, April 1, 2015

	Overall*		Spirits		Wine		Beer	
Jurisdiction	2015	2014	2015	2014	2015	2014	2015	2014
Northwest Territories	12	12	12	12	6	4	12	12
Nunavut	13	13	13	13	7	7	13	13
Yukon	7	10	2	5	11	11	9	10
British Columbia	3	3	4	2	4	2	2	3
Alberta	8	9	9	9	3	6	11	11
Saskatchewan	5	5	6	6	2	3	7	8
Manitoba	10	8	11	11	13	13	6	5
Ontario	1	1	5	3	1	1	1	2
Quebec	2	2	1	1	5	5	4	1
New Brunswick	4	4	3	4	10	8	3	4
Nova Scotia	9	6	10	8	8	9	8	9
Prince Edward Island	6	7	8	7	9	10	5	7
Newfoundland	11	11	7	10	12	12	10	10

* Excludes Coolers. The source: 2015 CALJ Annual Price Survey (August 2015)- Canadian Association of Liquor Jurisdictions

C. Tax Revenue Options – Changes to Tax Rates and Introducing New Taxes

This section examines options for the GNWT to generate additional tax revenues through increasing tax rates or introducing new taxes. New revenues can also be raised by increasing the size of the NWT economy and population. This strategy is not discussed in this paper, partly because increased own-source revenue due to growth in tax bases is largely offset by decreases in Territorial Formula Financing entitlements (see box), and also because this strategy is already being implemented through existing economic development strategies.

Own-source revenues from taxes and other sources will increase with economic growth, even after leakages to other jurisdictions, but a large part of these revenues is offset by a lower Territorial Formula Financing Grant. The Grant is designed to fill the gap between what the GNWT needs to provide comparable levels of programs and services as the provinces at comparable levels of taxes. Therefore, as economic growth shrinks the gap between expenditure need and the GNWT's ability to raise its own revenues, the Formula Financing Grant will decline. However, because of the Economic Development Incentive in the formula, the GNWT is able to keep 30 per cent of its own-source revenues that it could raise at National Average Tax Rates. Therefore, changes in own-source revenues are only partially offset under Territorial Formula Financing.

The revenues deducted to determine the annual Territorial Formula Financing Grant are based on what the GNWT could raise using a tax system that represents the average tax structure and rates used by the provinces. This means that the GNWT revenue policy choices do not affect Territorial Formula Financing and, therefore, changes to tax rates or the introduction or elimination of NWT taxes do not affect Territorial Formula Financing entitlements.

The options are considered using the following criteria:

- revenue-raising potential;
- impact on the NWT economy, including the need to be competitive with other jurisdictions; and
- principles of sound tax policy.

Territorial Formula Financing and Own-Source Revenues

The GNWT has received the bulk of its revenues through Territorial Formula Financing (TFF) arrangements since 1985. The TFF Grant is based on a "gap-filling" principle and theoretically measures the difference between what the GNWT would need to spend to provide comparable levels of public services as the provinces and its ability to raise its own revenues at comparable levels of taxation:

TFF Grant *equals* Expenditure Requirements *minus* Revenue-Raising Ability

The GNWT's expenditure requirements are represented by a Gross Expenditure Base (GEB) which is a proxy for the fiscal resources required to deliver public services of similar quality to those in the provinces while taking into account the higher costs and needs in the North. The Gross Expenditure Base is escalated every year by the growth in provincial/territorial-local government spending, adjusted by the rate of population growth in the NWT compared to that of Canada. The escalator ensures that the Gross Expenditure Base grows at the same rate as total provincial/territorial-local per capita government expenditures.

The GNWT's revenue-raising ability takes into account the various revenue sources that the government has at its disposal to raise revenues, including taxes and fees, and measures how much the GNWT could raise from these sources if it levied the same taxes as the provinces at national average tax rates. This revenue-raising ability is referred to as Eligible Revenues. The TFF Grant calculation is based on what the GNWT could raise in tax revenues, whether or not it chooses to do so. An Economic Development Incentive is applied to Eligible Revenues, effectively excluding 30 per cent of Eligible Revenues from the Grant calculation. This is meant to provide a fiscal incentive for the GNWT to promote economic growth. Without it, a dollar of increased tax revenue would simply be offset by an equal reduction in the Grant.

The combination of the revenues measured at national average tax rates and the Economic Development Incentive produce different rates at which each revenue source reduces the TFF Grant. Although the GNWT realizes an average net benefit from the growth of tax revenues of 30 per cent, the specific benefit depends on whether the GNWT tax rate is above or below the national average rate for a given tax base. If the GNWT lowers its tax rates below national average rates, the offset rate is more than 70 per cent, and can be more than 100 per cent if rates are significantly below the national average. The offset drops below 70 per cent when tax rates are above the national average.

Changes in NWT tax rates or types of taxes do not affect the claw back rates. This means that revenue changes caused by changes in NWT tax rates do not change TFF entitlements.

It is sometimes suggested that governments can boost their tax revenues by lowering tax rates, based on the assumption that lower tax rates will encourage greater economic activity and therefore generate additional tax revenues. Although lower tax rates generally do benefit the economy, they will not necessarily lead to enough economic growth to increase total tax revenues. Even if total tax revenues increase, however, the interaction between tax revenues and the TFF must be considered, as it is possible for the GNWT to lose more in TFF revenue than it gains in tax revenue by lowering tax rates. In other words, a tax rate decrease must be able to provide enough of a tax base increase to counter the reduced revenue effect of the tax rate decrease.

Starting April 1, 2014, the GNWT collects the resource revenues on NWT public lands. Under the Devolution Agreement, 50 per cent of resource revenue, up to a cap of 5 per cent of the TFF Gross Expenditure Base (currently $78 million), is shared with the federal government through an offset to TFF and up to 25 per cent of the remainder is shared with Aboriginal organizations that are signatories to the Devolution Agreement. The maximum the GNWT retains from resource revenues (net fiscal benefit) is 37.5 per cent, and nothing above a $78 million cap.

a. Personal income tax

As provinces struggle to address budget deficits, potential changes to personal income tax rates have come under consideration and several jurisdictions have recently targeted high income earners by adding new threshold tax brackets and tax rates at the top income levels (see Table 10). For examples:

- Alberta has abandoned their flat tax personal income tax structure and have created five tax brackets with graduated tax rates starting in 2015;
- Nova Scotia and Yukon added higher tax rate brackets but at the same time eliminated their high income surtaxes;
- Ontario added a fifth tax bracket in 2014 and continues to retain its high income surtax; and
- effective 2016, the federal government has introduced a fifth bracket rate of 33 per cent for individuals with taxable income over $200,000 and reduced the second lowest federal income tax bracket tax rate from 22 to 20.5 per cent.

The federal Liberal election platform also proposed the increasing Northern Residents Deduction maximum residency amount 33 per cent, from $16.50 to $22 per day. If the election promise to increase the Northern Residents Deduction is enacted, the combination of the federal tax measures and the Northern Residents Deduction increase will provide a net $11.4 million in tax savings annually for NWT residents. However, this federal measure will cost the GNWT $2 million in reduced income tax revenues (increasing the Northern Residents Deduction lowers the total taxable income in the NWT).

While there is no guarantee that the net $11.4 million added to NWT residents' disposable income would be spent in the NWT, at least a portion of the new funds could be expected to be spent in the NWT economy. There is also the possibility that tax savings will increase savings or result in some spending outside the NWT.

The increase in the Northern Residents Deduction may create an incentive for individuals to live and work in the NWT. **Growing the resident labour force will raise more revenues than a personal income tax increase because it will increase the Gross Expenditure Base in Territorial Formula Financing as well as increase own-source revenues.**

Table 10: Recent Federal- Provincial/Territorial Personal Income Tax Bracket Changes

	Year effective	Number of tax brackets: Previous	Number of tax brackets: Current	Previous: Top bracket tax rate	Previous: Top bracket threshold	Current: Top bracket tax rate	Current: Top bracket threshold
Alberta[1]	2016	Not applicable	5	10.00%	Not applicable	15.00%	$300,000
British Columbia	2014	5	6	14.70%	$104,754	16.80%	$151,050
New Brunswick	2015	4	6	17.84%	$127,802	25.75%	$250,000
Nova Scotia[2]	2010	4	5	17.50%	$93,000	21.00%	$150,000
Ontario[3]	2014	4	5	13.16%	$509,000	13.16%	$220,000
Yukon[4]	2015	4	5	12.76%	$136,270	15.00%	$500,000
Federal[5]	2016	4	5	29.00%	$138,586	33.00%	$200,000

Notes:

1. Before 2015 Alberta had a 10% flat tax rate regardless of taxable income level. Graduated tax rates were introduced in 2015 with a 11.25 per cent top tax rate. The top tax rate will rise to 15 per cent in 2016.
2. Prior to the 2010 tax year a surtax of 10% was applied to Nova Scotia tax exceeding $10,000. Nova Scotia's surtax was eliminated in 2010.
3. Ontario applies a surtax to high income earners. Surtax rates for 2015 are 20% of Ontario tax greater than $4,418 and an additional 36% of Ontario tax greater than $5,654.
4. Yukon's surtax was eliminated in 2015. The 2014 Yukon surtax was 5% of Yukon tax over $6,000.
5. Changes proposed in the 2015 Liberal Party election platform.

Based on the most recent complete set of tax data (2013), 1,336 of 30,229 NWT tax filers had taxable income in excess of the 2015 top tax bracket threshold of $131,641. If the NWT introduces a fifth tax bracket targeting this high income group, Table 11 shows the potential new revenues for the GNWT under different combinations of top tax brackets and tax rates, ranging from $0.9 million to $4.3 million.

Table 11: New Top NWT Personal Income Tax Bracket Potential Revenue[1]

New tax rate	New top tax bracket threshold: $150,000	$180,000	$200,000
		(millions)	
16%	$1.4	$1.0	$0.9
18%	$2.9	$2.1	$1.8
20%	$4.3	$3.2	$2.7

Note:

1. Revenue estimated using 2013 tax year data.

Whether an increase in personal income taxes for high income taxpayers would influence their decision to live in the NWT is difficult to evaluate as there are many factors influencing an individual's decision to live in the NWT. Nevertheless, a tax increase reduces the ability of NWT business to use low NWT tax rates as an incentive to attract workers who are worried about the high cost of living in the North. Further, personal income tax increases will tend to increase labour costs as workers put pressure on employers for increased wages to counter the higher taxes. However, if the Northern Residents Deduction is increased, it will offset the disincentive caused by the addition of a new top tax bracket.

b. Payroll tax

Each one percentage point increase in the payroll tax rate would generate about $20.5 million in additional revenue, assuming no change in employment as a result of the payroll tax increase. An average NWT employee would pay $680 more in annual payroll tax and, therefore, have $680 less in disposable income, which would have negative consequences for consumer spending.

Because the payroll tax is levied only on employment income, a rate increase would increase the tax burden of NWT residents earning employment income relative to those who earn other sources of income such as self-employment income, pension or investment income, which strains the principles of fairness and neutrality of the tax system (at some point, increasing payroll tax rates may provide sufficient incentive for individuals who can to turn employment into self-employment contracts).

Some of a possible payroll tax increase could be offset by an increase in the Cost of Living Tax Credit (COLTC). However, this would create two issues:

- because the COLTC applies to all NWT tax payers, a COLTC increase would give more benefit to those who do not pay payroll tax; a further violation of the principle of fairness in the tax system;

- simultaneous increases to the COLTC and the payroll tax could be seen as imposing a payroll tax targeting non-resident workers with implications for the *Tax Collection Agreement* with Canada, including a refusal to administer the COLTC.

Suggestions have been made to impose a differentiated payroll tax, with a higher rate on higher employment income. This would make the system complicated to administer for business and influence taxpayer behaviour at the wage points where the rate changes.

A higher payroll tax rate could make NWT labour recruitment more difficult or increase employers' labour costs as new employees try to negotiate higher wages to compensate for a payroll tax increase. A higher payroll tax would reduce disposable income and would result in lower consumer spending.

c. Fuel tax

As an ad valorem tax, NWT fuel tax rates, with the exception of the aviation fuel tax rate, cannot be set arbitrarily. These tax rates are based on the taxable price per litre of gasoline obtained by a quarterly price survey of retail outlets in Yellowknife and prescribed by the Minister of Finance pursuant to the Regulations of the *Petroleum Products Tax Act*. Replacing the current rate structure with a regime where the rates could be set independently of the price survey would require amendments to the legislation.

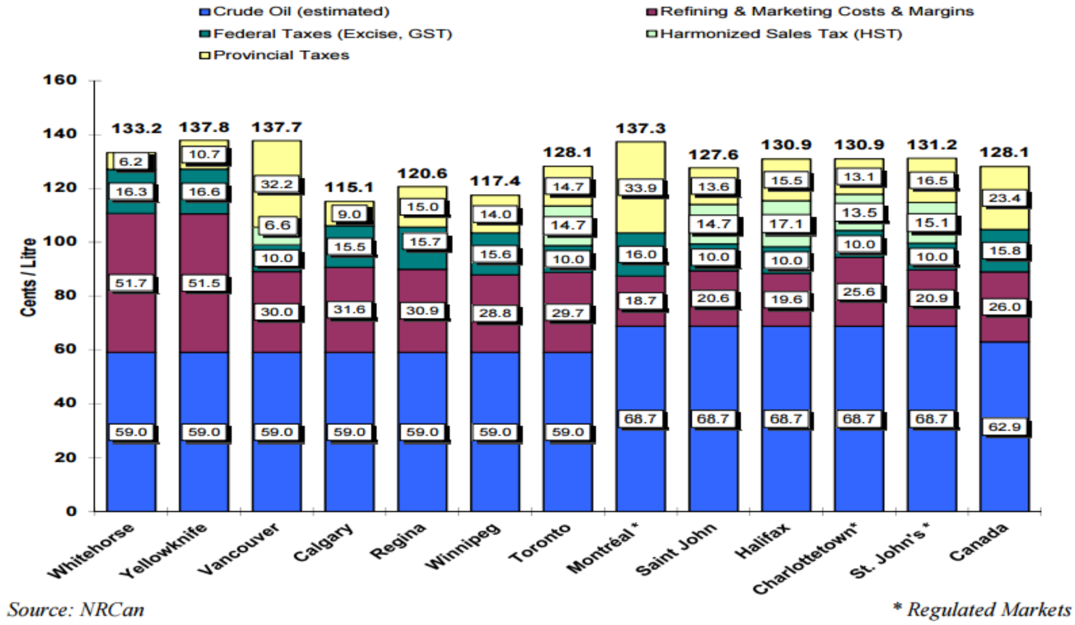
Retail prices include taxes (NWT fuel tax, federal excise tax and GST) that are paid by consumers. These taxes theoretically have no effect on a retailer's profit margin, which is determined by factors such as:

- costs of doing business such as inventory, labour, operations and maintenance;
- rate of return on investment; and
- competitiveness in the market place.

Figure 15 shows that Yellowknife has the highest retail gasoline price before taxes among 12 Canadian centres and is 30 per cent higher than the national average. High Yellowknife costs can be attributed to high business costs in the North when compared to major southern cities and the lack of competition. Yellowknife has the highest refining and marketing costs and margins (margins in Yellowknife are 56 per cent higher and in Whitehorse 43 per cent higher than the national average). The higher retail prices before taxes are an important consideration when setting NWT fuel tax rates.

Table 12 shows that raising fuel tax rates in increments of 1 cent per litre on the base gasoline rate will generate about $1.8 million in additional fuel tax revenues assuming that fuel consumption does not change as a result of the fuel tax increase. Unfortunately, determining the effect of a change in the tax rate and, therefore, the fuel price will have on demand is difficult. An increase in the fuel tax rate will most likely increase the cost of living for consumers and operating costs for business, which will likely be passed on to consumers to the extent they can without increasing online shopping – already a concern for many NWT retail businesses. Business operating costs, including fuel taxes, are deductible from corporate income tax.

Figure 15: Retail Gasoline Price Components Canadian City Comparisons



Source: Fuel Focus, Natural Resources Canada, January 23, 2015.

Table 12: Fuel Tax Increase Revenue Impact

	Current tax rates[1]	Increased tax rates						Aug 14, 2015 Survey possible tax rates [2]
On-highway gasoline tax rate increase		$0.010	$0.020	$0.030	$0.040	$0.050	$0.060	
On-highway gasoline	$0.107	$0.117	$0.127	$0.137	$0.147	$0.157	$0.167	$0.211
Off-highway gasoline	$0.064	$0.070	$0.076	$0.082	$0.088	$0.094	$0.100	$0.127
Motive diesel	$0.091	$0.099	$0.108	$0.116	$0.125	$0.133	$0.142	$0.179
Non-motive diesel	$0.031	$0.034	$0.037	$0.040	$0.043	$0.046	$0.048	$0.061
Railway diesel	$0.114	$0.125	$0.136	$0.147	$0.157	$0.168	$0.179	$0.226
Revenue (millions)	$18.7	$20.5	$22.2	$24.0	$25.7	$27.5	$29.2	$37.0
Revenue increase from current rates (millions)		$1.8	$3.5	$5.3	$7.0	$8.8	$10.5	$18.2

Note:

1. Calculations do not include aviation fuel. The aviation fuel tax rate is set at 1¢ per litre under the *Petroleum Products Tax Act.* This tax rate does not change when there is a change in the on-highway gasoline tax rate. Calculations are based on 2014-15 actual volumes.
2. Fuel tax rates based on the August 14, 2015 price survey would make the NWT gasoline tax the second highest and the motive diesel tax the fifth highest in Canada.

d. Tobacco tax

Tobacco tax is also an ad valorem tax. Tax rates for cigarettes and loose tobacco are based on their taxable price obtained from a quarterly price survey of retail outlets in Yellowknife and prescribed by the Minister of Finance pursuant to the *Tobacco Tax Regulations*. Replacing the current rate structure with one where the rates could be set independent of the price survey would require amendments to the *Tobacco Tax Act*.

Increasing tobacco tax rates to current survey rates would raise tobacco tax revenue by $2.7 million assuming consumption remains unaffected. However, tax rate increases would be expected to decrease consumption and this decline can be estimated using the price elasticity of demand. Table 13 shows that the tax revenue increase would be reduced to about $2 million under two different assumptions of the amount consumption would decline in response to tax rate increases.

Raising tobacco tax rates would likely increase smokers' attraction to e-cigarettes, which are currently unregulated and untaxed in Canada, and have unknown health implications. Of more immediate concern is that further increases to already high tobacco tax rates could increase illegal activities such as smuggling.

Table 13: Estimated Revenue Impact of Tobacco Tax Rate Increase Proposal

	Elasticity	
	Low[1]	High[2]
Cigarettes		
Revenue increase with no consumption decline	$2,677,367	$2,677,367
Revenue impact of consumption decline	$(590,101)	$(820,385)
Net revenue increase	$2,087,266	$1,856,982
Loose tobacco		
Revenue increase with no consumption decline	$123,692	$123,692
Revenue impact of consumption decline	$(26,064)	$(36,236)
Net revenue increase	$97,627	$87,456
Net total revenue increase[3]	$2,184,893	$1,944,438

Notes:

1. Elasticity of -0.41 from The Ontario Tobacco Research Unit's February 2015 study *What Effect Does Tobacco Taxation Have on Contraband? Debunking the Taxation - Contraband Tobacco Myth.*
2. Elasticity of -0.57 calculated from historical Treasury Division consumption data after a previous cigarette tax rate increase.
3. Revenues are based on 2014-15 actual consumption and the August 14, 2015 Quarterly Retail Price Survey. Survey rates would increase the cigarette tax rate by $10.80 to $68.00 per carton and the loose tobacco tax rate by $4.00 to $57.20 per 200 grams.

e. Corporate Income Tax

The NWT's 11.5 per cent general corporate income tax rate is close to the average among provinces and territories (see table 2 or below).

	NT	NU	YT	BC	AB	SK	MB	ON	QC	NB	NS	PE	NL
Large (%)	11.5	12.0	15.0	11.0	12.0	12.0	12.0	11.5	11.9	12.0	16.0	16.0	14.0
Small (%)	4.0	4.0	3.0	2.5	3.0	2.0	0.0	4.5	8.0	4.0	3.0	4.5	3.0

It is difficult to estimate what an increase in the tax rate for large corporations could raise because it would depend on the resulting behaviour from corporations. If the NWT tax rate is not competitive with other jurisdictions it could encourage companies to allocate income outside the NWT.

Corporations that operate in more than one province or territory must allocate their income according to a formula set out in the federal *Income Tax Regulations*. The allocation is based on where the corporation's employees are located (wages and salaries paid) and where sales take place (revenues). There are different formulas for some types of corporations, such as financial institutions, transportation companies or pipelines. Low tax rates may encourage companies to structure their affairs to allocate their income, particularly investment income, to that jurisdiction. This change can be accomplished relatively easily, though there would be little or no increase in economic activity or employment in the jurisdiction. Similarly, a high rate may encourage companies to allocate income outside the jurisdiction.

Based on recent levels of corporate taxable income, a one percentage point increase in the tax rate for large corporations could raise about $5 million per year in additional revenues, assuming no shift in the allocation of income to outside the NWT.

The NWT has the highest small business corporate income tax rate among the five western provinces and territories. Reducing the current small business tax rate by 1 per cent to match Alberta's current 3 per cent rate would reduce GNWT tax revenue by about $700,000 and benefit only a small number of firms, since about 55 per cent of NWT companies eligible for the small business rate typically pay no corporate income tax. Small business may be better supported through access to financing and other support programs than by reducing taxes.

Corporate tax rates are a consideration for potential NWT business investors and for the investment plans of existing businesses. An increase in corporate income tax rates would make the NWT less attractive for business and could hamper investment. Setting both corporate income tax rates is a balance between getting a fair share of revenue from industry and business and discouraging economic investment and activity. In general, that balance is achieved by remaining competitive with other jurisdictions.

f. Introduction of a territorial sales tax

The three territories currently do not have sales taxes because of concerns about the high cost of living.

Table 14 shows current Goods and Services Tax (GST) and Harmonized Sales Tax (HST) and provincial sales tax (PST) rates in Canada. Residents in Alberta and the three territories are only subject to the federal 5 per cent GST on their purchases of taxable goods and services. The HST is the combination of the GST and the PST in five participating provinces and is administered by the Canada Revenue Agency. British Columbia, Saskatchewan, Manitoba, and Quebec collect their own PST.

Under the federal *Excise Tax Act*, consumers do not pay the GST/HST when purchasing goods and services listed in Schedule V (exempt supplies) or Schedule VI (zero-rated supplies):

- Exempt supplies mean that the producer of the goods or services cannot get a refund of the GST paid on goods and services used to produce the good or service. Include in exempt supplies are health care services, course fees, and sales of used residential housing, long-term residential rentals, and bridge tolls. Exempt supplies will have some tax embedded in the price of the good or service.
- Zero-rated supplies mean producer of the goods or services does get a refund of the GST paid on goods and services used to produce the good or service. Zero-rated supplies include prescription drugs, medical devices, basic groceries, and exports.

Table 14: GST, HST, and Provincial Territorial Sales Tax

									Harmonised PST				
	NT	YT	NU	AB	BC	SK	MB	QC	ON	PE	NS	NB	NL
								(percent)					
GST	5	5	5	5	5	5	5	5	5	5	5	5	5
PST	-	-	-	-	7	5	8	9.975	8	9	10	8	8
HST	-	-	-	-	-	-	-	-	13	14	15	13	13

A territorial sales tax harmonised with the federal GST using a common tax base would be a more effective approach than a territorial sales tax because it would:

- keep compliance costs unchanged for businesses;
- minimise the GNWT's administration costs since the Canada Revenue Agency would administer and collect the tax on behalf of the GNWT; and
- would avoid sales tax that is paid on inputs to produce the final good or service being embedded in the final price because it is a value-added tax paid only by the final consumer.

The GST was reduced from 7 per cent to 6 per cent in 2006 and to the current 5 per cent in 2008. Filling this tax room with a 2 per cent territorial sales tax would generate about $20 million annually for the GNWT, based on the $50 million in GST collected from the NWT in 2013, assuming no change in consumption as a result of the tax effect on retail prices. Each additional one per cent tax rate increase would generate an extra $10 million.

The NWT HST would only affect residents and non-profit organizations, because most other businesses receive input tax credits for the tax paid on their business expenditures. **A 2 per cent HST would increase the general consumer price level by about 1.4 per cent given that 30 per cent of NWT household spending is on exempt or zero-rated goods.**

To alleviate the impact of the new territorial sales tax on residents, the NWT could provide point-of-sale rebates on specific items such as heating fuel, similar to those offered by some participating provinces. For example, Prince Edward Island established a point-of-sale rebate of the 9 per cent provincial component of the HST paid on heating fuel, children's clothing, children's shoes and books. Point-of-sale rebates would lower the sales tax revenues; for example, a rebate on heating fuel would cost the GNWT about $1.8 million, assuming a 2 per cent HST.

g. Introduction of a carbon tax

A carbon tax is a consumption tax that is levied on fuels based on the carbon content. Typically carbon taxes are intended to encourage individuals and businesses to reduce their consumption of fuels that contribute to global warming through greenhouse gas emissions by raising the price of these fuels, rather than as a revenue generator for government.

A carbon tax differs from the current NWT fuel tax in that it applies to a broader range of fuels than the current fuel tax and the carbon tax rate for each fuel type would be based on its carbon content.

A NWT carbon tax could apply to a variety of fossil fuels such as gasoline, diesel, natural gas, propane, and coal, and to fuel used in transportation, energy generation and home heating. Tax rates would be based on the per tonnage carbon dioxide equivalent emissions from the combustion of each fuel. If the objective of the carbon tax is to reduce greenhouse gas emissions, then all fuels that produce these emissions, including wood, would be subject to the carbon tax; however, if the purpose of the carbon tax is to reduce fossil fuel consumption then wood would not be taxable on the basis that it is a renewable energy source. Since the NWT only has the authority to impose direct taxation within its boundaries, fuels exported for use outside the NWT would be exempt.

A carbon tax based on a $10 per tonne of CO_2 equivalent (CO_2e) emissions[1] (the initial British Columbia rate) would produce the following carbon tax rates:

- Aviation fuel 2.46¢/litre
- Gasoline 2.22¢/litre
- Diesel 2.55¢/litre
- Jet fuel 2.61¢/litre
- Heating fuel 2.55¢/litre
- Propane 1.54¢/litre
- Natural gas 1.90¢/m3

[1] A model commissioned by the Department of Environment and Natural Resources estimates that a carbon tax of $10 per tonne of CO_2e would, over five years, reduce NWT greenhouse gas emissions by 0.7 per cent relative to the case where no carbon tax is implemented. However, greenhouse gas emissions would still rise over the same five year period regardless of the carbon tax due to increased economic activity assumed in the model.

Carbon Taxes in Canada

To date, Quebec, Alberta, and British Columbia are the only Canadian jurisdictions to have introduced a carbon tax.

On October 1, 2007, Quebec imposed a carbon tax on energy use. The tax revenues, estimated at $200 million a year, are deposited into the provincial Green Fund to finance sustainable development projects.

In 2007, Alberta also imposed a carbon tax on large industrial companies in the province (mostly oil sand companies and coal-fired electricity plants) with the introduction of the *Climate Change and Emissions Management Act.* The *Act* establishes a technology fund whose revenues from the tax, at $15 dollars per tonne of CO_2 equivalent, are used to fund projects that align with Alberta's Climate Change Strategy such as carbon capture and storage, and greening energy production. This dedicated fund is administered by the Climate Change and Emissions Management Corporation (CCEMC), an Alberta-based not-for-profit, independent corporation with its mandate established by the Climate Change and Emissions Management Fund Administration Regulation.

British Columbia implemented a broad-based, revenue-neutral carbon tax in 2008. The tax was introduced at a rate of $10 per tonne of CO_2 equivalent emissions, increased to $30 a tonne by July 2012. Its main purpose was to achieve reduction in the use of fossil fuels, rather than to raise new revenues. Therefore, to help offset the impact of this new tax, the province also introduced a number of income tax credits and tax rate reductions for residents and businesses.

Using these carbon tax rates, the GNWT would collect about $10 million in carbon tax revenues from NWT residents and businesses. About half of the tax would be paid, directly or indirectly, by individuals, and the rest by businesses, primarily in the resource sector.

As was done in British Columbia, the high costs associated with the imposition of a carbon tax could be offset through reductions in other taxes; assuming that the objective of the carbon tax is to lower greenhouse gas emissions. If the objective is to raise additional revenues, any offsetting tax measures would be counter to this objective.

If the intent of introducing a carbon tax is strictly to encourage reduced consumption of fossil fuels and not as an additional revenue source, the tax could be made revenue neutral for the GNWT. Accordingly, the revenue received through a carbon tax could flow back to NWT residents and businesses through income tax reductions and credits. These measures would offset the impacts of the new tax on the costs of living and business in the territory; however, even with offsetting tax measures, a carbon tax could not be truly cost-neutral for everybody. There would be winners and losers due to differences in consumption habits, household income, family size, community of residence, or whether the tax could be passed on. For example, a household may pay an additional $400 annually in carbon tax, but may only receive $300 in income tax reductions. Individuals and families who use less fuel will pay less tax than those who consume more. Furthermore, it is expected that the GNWT would incur higher expenditures associated with the tax, such as higher energy costs for the NWT Housing Corporation and social assistance clients, and higher freight costs on government purchases.

A carbon tax designed for the NWT must take into account the fact that the NWT is a small, open, resource-based economy and those characteristics make for a different set of consequences than would be experienced in more diverse economies such as British Columbia. NWT residents and business depend on fossil fuels for a variety of reasons:

- Harsh northern environment with long and cold winters where home heating mainly relies on diesel or propane. While use of alternatives, especially biomass, are increasing, many alternative energy sources such as wind mills, solar panels, or geothermal installations, are not financially affordable;

- Continued reliance on diesel for power generation and heating in isolated communities outside the current electricity transmission grid or where no alternatives are financially viable. For example, even biomass, the currently most viable alternative, is not an economically viable option for remote communities above the tree line such as Sachs Harbour;

- Continued reliance on diesel fuel by the transportation and resource sectors for their operations.

This dependence on fossil fuels means that introducing a carbon tax would have the following implications:

- A carbon tax will increase costs for all NWT businesses and residents, with the lowest income individuals and those in small, remote communities being relatively more burdened. While it is possible to implement a tax that is revenue-neutral at the GNWT level, it is not possible to create one that will be neutral at the level of households and businesses; at this level there will be winners and losers.

- Remote communities that are heavily reliant on carbon-based fuels will be disproportionally burdened by a carbon tax. Further, these communities, particularly those above the tree line, have limited opportunities to reduce their consumption of carbon-based fuels by making use of alternative fuels.

- By increasing the cost of fuels, a carbon tax will increase the cost of participating in traditional activities, including hunting, fishing and trapping, which are an important part of the NWT's heritage and remain important to many NWT individuals and communities.

- The easiest and least costly changes that can be made to reduce consumption of carbon-based fuels will be pursued first. As time passes, it will become more difficult to achieve further reductions, unless there are considerable technological improvements that allow for low-cost reductions.

- By itself, a carbon tax may not be enough of an incentive to reduce greenhouse gas emissions since the current high fuel costs already work as an incentive to reduce energy consumption. It is necessary that NWT residents and businesses be technically and economically able to make reductions in their emissions at affordable costs. The GNWT already supports the use of biomass as an energy source.

Implementing a carbon tax in the NWT will increase the costs of doing business within the territory and would make the NWT less competitive for businesses, compared with jurisdictions that do not have a carbon tax. Fuel-intensive industries such as exploration for and extraction of minerals, oil and gas, which represent the backbone of the NWT economy, may be especially hard hit.

h. Introduction of a hotel room tax

Most provincial governments levy a hotel tax and some provinces, such as British Columbia, Manitoba, and Prince Edward Island, also grant municipalities the authority to levy a municipal hotel room levy. In addition to the hotel tax in these jurisdictions, hotel guests may also be subject to a destination marketing fee imposed by a hotel association or similar group. Unlike a compulsory hotel tax, a destination marketing fee is an unlegislated activity based on hoteliers' voluntary participation without government involvement.

Introduction of a hotel tax has been proposed in the past to raise revenue for tourist industry investment but has not been implemented due to concerns about the negative effect on the tourism industry, especially in communities outside of Yellowknife. A hotel tax of 5 per cent of the room charge on their short-term accommodation, 28 days or less, in commercial lodging establishments having five rooms or more would generate between $3.3 and 3.5 million in gross new revenues for the GNWT after netting the amount the GNWT would pay in hotel tax for GNWT employees' travel and the cost of administering the tax.

i. Taxes on Sugary Drinks and Junk Food

Imposing a tax on sugary drinks (soda pop) or "junk" food is often proposed to increase the relative price of these products and, therefore, discourage their consumption. Sugary drinks and junk food are linked to obesity and increased levels of diabetes, which in turn are linked to poorer health and higher health care costs.

Some other countries are experimenting with these taxes and studies on these taxes suggest that if the tax rate is high enough, the increase in prices will discourage consumption. However, some studies note that the reduced consumption due to the sugary drink tax (Mexico) had only a minimal effect on reducing caloric consumption.

Since low income individuals tend to consume more sugary drinks and junk food, a junk food tax is regressive (low income individuals pay a larger share of their income for this tax than higher income earners). However, since the objective of the tax is modify social behaviour (discourage poor food choices), regressivity may not be an issue.

More consumption data is necessary to determine the amount of revenue that could be generated at different tax rates based on sugar content or caloric intake of sugary drinks.

However, it is unlikely that a sugary drink tax would generate enough revenue to cover the cost of administration for the GNWT. The sugary drink tax could be administered similar to the current tobacco tax administration but revenues generated would be minimal.

A junk food tax would be more complicated to implement and administer. Many issues would have to be addressed such as what foods would be taxed, whether restaurant foods are included and how the tax is applied; for example, based on sugar/salt/fat content.

D. Fees and Charges

The GNWT collects about $22 million annually in fees and licences, ranging from $20 for a birth certificate to hundreds of dollars for industrial permits and licences. Fees are sometimes viewed by the public as taxes; however, fees are charged to offset the cost of providing specific services to users. If a fee is excessive and does not have a reasonable relationship to the cost of the service provided, it might be considered a tax and, therefore, unlawful as being collected without enacted legislation.

In November 2008, the Department of Finance conducted a survey of all departments' fees. The survey indicated that many fees were not updated regularly – in fact, many fees had not increased since the 1990s. As a consequence, many fees had lost value after allowing for inflation. In a number of cases, departments noted that a doubling of fee rates could be justified.

The Minister of Finance announced in the 2010-11 Budget Address that, effective April 1, 2011 measures would be put in place to ensure GNWT fees keep up with inflation. Therefore, effective April 1, 2011 regulations were changed for fees that needed to "catch up" to inflation increases and thereafter a schedule was put in place to increase fees by inflation on a regular basis. Since regulatory-making authorities for most fees are set up in the individual *Acts* and are unique to the specific *Act*, changing most fees have to be made through separate amendments to each individual regulation. Consequently, department fees that generate minimal amounts of revenue are increased for inflation on a schedule greater than one year.

An exemption from an automatic increase of a specific fee on its review date is allowed if:

- the fee increase would discourage use and, therefore, compromise public safety;
- the fee increase would be uncompetitive with other jurisdictions;
- the fee is already based on market rates (for example commercial leases);
- the fee increase would be politically sensitive (for example, seen as a barrier to government accountability, such as fees for Access to Information requests);
- the cost of delivering the service has declined; or

- the regulations or corresponding *Act* are under review.

As a result of the all-department fee review in 2008, most fees and charges are now considered to be at appropriate levels and there is little room for generating additional revenue from regulatory fees without turning the fee into tax. Furthermore, increasing regulatory fees would increase the cost of doing business and the cost of living for NWT residents.

E. Resource Revenues

Effective April 1, 2014, as part of the *Northwest Territories Lands and Resources Devolution Agreement*, the GNWT collects non-renewable resource revenues from NWT public lands. Under the Agreement, the GNWT receives a "net fiscal benefit" of 50 per cent of resource revenues, subject to a cap equivalent to 5 per cent of the Territorial Formula Financing Gross Expenditure Base, which equals $78 million in 2015-16. This cap will grow at the same rate as the Gross Expenditure Base. It is not expected that the cap will be triggered in the foreseeable future. The GNWT also agreed to share up to 25 per cent of the net fiscal benefit with NWT Aboriginal organizations that are signatories to the *Devolution Agreement*. Therefore, the GNWT keeps 37.5 per cent of all resource revenues and because resource revenues are outside Territorial Formula Financing, the GNWT would also keep 37.5 per cent of any new revenues raised by an increase in royalty rates.

As the manager of the NWT non-renewable resources, the GNWT tries to capture as much revenue as possible from these sources. The GNWT does this through profit-based royalties on minerals, oil and gas and related fees and leases, in addition to taxes.

Theoretically, the government is trying to extract all the revenue that a firm earns from the resource above the minimum amount that it needs to be willing to continue to extract the resource. This is known as "economic rent", which is the surplus revenue that a firm earns from engaging in economic activity, above the production costs it incurs and is essentially the amount that a firm receives over and above the minimum amount it needs to keep it willing to stay in business.

Both tax systems and royalty structures are designed to collect as much revenue from resources as possible without stopping their development. Theoretically, the GNWT can remove through taxes all the economic rent without stopping the resource from being developed but in reality it is impossible to design a tax system that removes just the economic rent when economic conditions, including prices of inputs and outputs, can change considerably over the life span of a resource project. That is why royalties, must be used in combination with taxes to derive as much revenue as reasonably possible from NWT resources.

Mineral and diamond royalties are profit-based and calculated on a mine basis as the value of the mine's output times the royalty rate on the graduated scale shown on the table below.

Table 15: NWT Mineral Royalty Rates

Value of Output ($)	Royalty Rate applicable to portion
10,000 or less	0
In excess of 10,000 but not exceeding $5 million	5%
In excess of $5 million but not exceeding $10 million	6%
In excess of $10 million but not exceeding $15 million	7%
In excess of $15 million but not exceeding $20 million	8%
In excess of $20 million but not exceeding $25 million	9%
In excess of $25 million but not exceeding $30 million	10%
In excess of $30 million but not exceeding $35 million	11%
In excess of $35 million but not exceeding $40 million	12%
In excess of $40 million but not exceeding $45 million	13%
In excess of $45 million*	14%

*Capped at the lesser of: (1) the total amount through Sliding Scale or (2) the 13% value of Output cap

The value of output is the revenues generated by the mine minus mining and processing costs including, salaries and wages, power, transportation costs, reclamation costs and allowances (depreciation on machine and buildings, development allowance and a processing allowance if additional processing is done in the NWT).

For oil and gas, the royalty is calculated on a project basis, and the royalty payments can be taken in kind or value. Royalties are determined at a reduced rate of one per cent of gross revenue (total revenue received from the sale of petroleum produced less pipeline tolls, transportation and process allowances), with the rate increasing by one per cent every 18 months to a maximum of five per cent until capital expenditure payout occurs. After payout, the royalty rate is the maximum of five per cent of gross revenue or 30 per cent of net revenue (gross revenue less operating and capital costs and operating and capital cost adjustments).

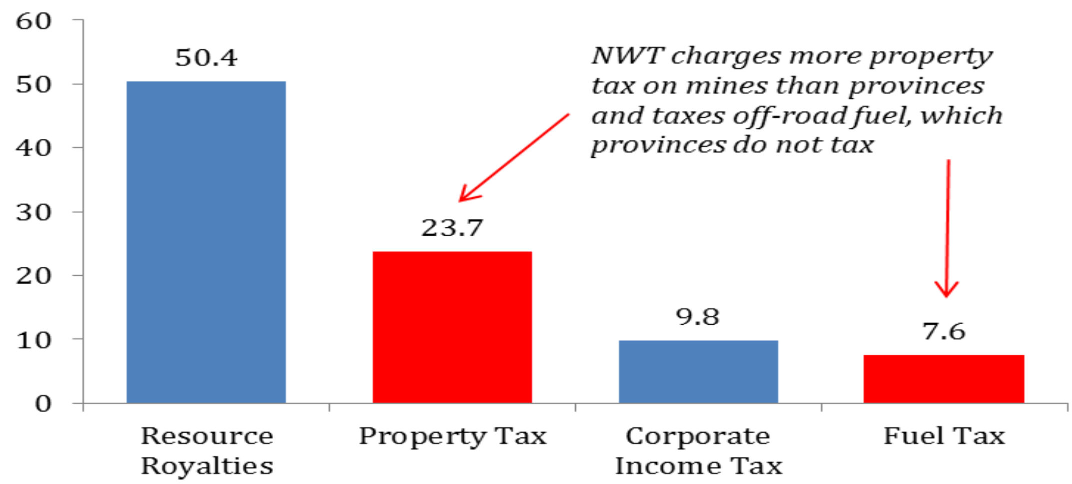
Changing the royalty structures to raise additional revenue would require careful study, taking into consideration the importance of resource development to the NWT economy and the global investment and market climate. The contributions that resource companies make to total GNWT revenues directly through property taxes, corporate income tax, and fuel taxes and indirectly through payroll and personal income tax from their employees must be considered in combination with royalties.

While other jurisdictions have similar tax structures, the NWT and Nunavut are the only Canadian jurisdictions that levy property taxes at significant levels. Mines in similar areas (remote hinterland) in provinces would not pay property taxes. Furthermore, the GNWT applies a fuel tax on off-road fuel consumption which mines do not pay in other jurisdictions (Figure 16).

Canadian mining provinces also have other advantages. For example: Quebec offers cheap electricity, good infrastructure and the ability to take equity interests in mines; and Ontario provides a 10 year exemption on the first $10 million in profits and a reduced tax rate on profits for new mines in "remote" Ontario.

Capturing the maximum resource value through taxes/royalties must be balanced with the need to remain competitive and attract further investment. The risk that a royalty increase upsets the balance and causes existing projects to close earlier than they otherwise would have or stalls new investment must be weighed against the understanding that the GNWT retains only 37.5 per cent of every new dollar raised by the increased rates. Uncertainty in the global economy, low commodity prices and exchange rate volatility are major factors in the profitability of the NWT resource sector and temper any expectation that raising royalty rates would generate significant additional resource revenues. A royalty review requires careful and thorough study, which does not lend itself to providing possible revenue options at this time.

Figure 16: NWT Royalty and Tax Revenues from Resource Companies ($ millions) Calendar Year 2014



F. Summary of Options

This paper provides a brief review of the NWT tax structure and other own-source revenue sources and presents options to increase these revenues. Table 15 summarizes the revenue that could be generated from the tax options discussed above. Depending on the tax rate chosen, revenue generated will change; however, implications for increasing the cost of living for residents and/or increase business costs will remain the same.

Table 15: Summary of Revenue Options

Current taxes	Tax rate increase	Projected tax yield (millions)	Implications
Personal income tax	New 18% top tax rate on taxable income over new $180,000 top tax bracket.	$2.1	**Pro:** Easy to implement (requires an amendment to the *NWT Income Tax Act* and Canada Revenue Agency administers). Is consistent with the progressive nature of the NWT personal income tax system. **Con:** Increasing tax burden on high-income earners may be a disincentive to attract new high-salaried professionals to the territory. Would be a rate increase on top of the new federal top tax bracket.
Payroll tax	1 percentage point rate increase to 3% tax on NWT employment income	$20.5	**Pro:** Easy to implement as it is a rate change only. **Con:** Increasing tax burden on employment income compared to other forms of personal income. Creates disincentive to attract new labour to the territory. Reduces the progressivity of the tax system.
Fuel tax	Increase rate based on Quarterly Retail Price Survey	$18.2 or $1.8 for every one cent per litre increase above current rate	**Pro:** Fuel tax rates have not increased since 1997 and, therefore, have not kept up to inflation. **Con:** Increasing the cost of living and operating costs for businesses.
Corporate income tax (General rate)	Could increase general tax rate above national average	Adding 1 percentage point to the general rate may generate $5 million but depends on corporate profitability	**Pro:** General tax rate change does not affect small business. **Con:** Revenue will depend on corporations' profitability at time of rate increase and assumptions of corporate behaviour. Will make the NWT less attractive for business investment.

Tobacco tax	Quarterly Retail Price Survey rates	$2.0	**Pro:** Increased taxes may discourage consumption. **Con:** Potential increase in illegal cigarette activity.
New taxes			
Sales tax	2% on goods and services taxed under the federal GST	$20.0	**Pro:** Harmonized sales tax would be easy to implement. Administration would be done by the Canada Revenue Agency. Large and stable revenue generating potential and can take up room vacated by the 2 percentage point reduction in GST (dropped to 6% in 2006 and 5% in 2008). **Con:** The cost of living will increase. The GNWT would have to administer any rebate program for specific goods. Residents in remote communities will be most affected because of higher prices.
Carbon tax	Based on a $10 per tonne of CO2 equivalent emissions	$10.0	**Pro:** Provide an incentive to reduce fossil fuel consumption. **Con:** Would increase the cost of living and cost of doing business, including making it more expensive for mineral exploration and mining operating costs.
Hotel room tax	5% of hotel room price	$3.3-$3.5 net of GNWT expenditures	**Pro:** Generates tax revenue with limited tax on NWT residents. **Con:** May discourage cost-conscious tourists and would increase costs for business travel.
Sugary drink tax	Based on sugar content	Consumption data not available	More work required to determine if revenue generated is worth the administrative cost.

G. Conclusion

This paper provides a brief review of the NWT tax structure and other own-source revenues and presents possible options to increase these revenues.

The main reason that the GNWT raises revenues is to provide government programs and services and make infrastructure investments that make the NWT a good place to live and do business. However, tax revenues, which are the main source of GNWT own-source revenues, are also used for other purposes such as redistributing wealth and income, promoting economic growth and encouraging certain behaviours and discouraging others. The differing tax policy objectives mean that raising rates on existing tax bases, or introducing new taxes to the NWT tax mix, is more complex than simply generating a list of potential revenue-raising options.

The key considerations when determining possible revenue-raising options are:

- **Economic impact:** no matter how carefully revenue raising measures are structured, they will likely raise the cost of living and/or the cost of doing business, with implications for the ability to attract new investment and employment, as well as for the NWT economy as a whole. The NWT's harsh climate, limited infrastructure and high transportation costs, all contribute to the high cost of living, which is reflected in the current NWT tax structure. For example, NWT fuel taxes are lower than the national average and the GNWT does not impose a sales tax. Fuel prices in Yellowknife are the highest among Canadian metropolitan areas and retail prices are on average 30 per cent higher, and prices in remote communities are even higher. Personal income tax rates are lower than the national average as well, particularly at lower income ranges, partly in recognition of the high cost of living. Corporate income taxes are close to the national average to remain competitive with other jurisdictions since the majority of NWT corporate tax payers are resource companies that make their investment decisions on a global scale.

- **Timing of tax increases:** raising taxes during uncertain economic times is not good fiscal policy**.** Governments typically try to stimulate the economy during slow or uncertain periods and resist increasing the tax burden. A continuing weak global economy will dampen demand for NWT resources, and low resource prices will hurt the overall NWT economy. Potential new mines are currently having difficulty obtaining financing. Low oil prices have caused oil and gas activity, including new drilling and exploration projects, to almost disappear. The economic dominance of the resource sector has a dramatic ripple effect on the rest of the NWT economy in relatively short order through its strong linkages to transportation, construction, wholesale and retail trade, and real estate. Current economic projections show a protracted decline in resource production and identified potential mining operations will not replace the economic activity of current operations in terms of output or employment. Resource exploration, essential for further development, is also declining. Increasing taxes on the resource sector or increasing the royalty rates carries both near and long term risk for the NWT economic outlook, which directly translates into revenue risk for the GNWT.

- **The GNWT cannot raise enough new own-source revenues to address the GNWT's fiscal sustainability problem**. GNWT own-source revenues are 22 per cent of $1.8 billion. Own-source revenues would have to increase by one-third to maintain an annual operating surplus of $100 million in each of the five years of the current fiscal framework without changing current expenditure projections. Depending on the type of new revenue, this could take over $130 million out of the local economy annually by 2018-19, reducing consumer expenditures and further increasing the already high cost of living.

Increased revenues may have a place in addressing the GNWT's need for increased operating surpluses but expenditure needs and wants must be squared with the ability to raise revenues to pay for them. The GNWT has limited flexibility on the revenue side of the budget. While the GNWT's fiscal strategy will include looking at tax options, the solution to the fiscal situation will not be realized solely by increasing taxes on NWT residents and businesses. The few revenue options that could generate significant revenues would discourage business investment and economic growth, and would leave individuals and families with less disposable income at a time when the costs of living are rising.

The negative impact on consumers and businesses must be weighed against the positive effect of increased government spending, especially given the size of the NWT tax base and its small contribution to total revenue.