



What Nova Scotians Need To Know





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A Message from the Premier

Fellow Nova Scotians:

Like all of you, I want our province to continue to grow, to rely more on its own success and to contribute to a stronger Canada.

And like every parent, I want our children to have good opportunities for a good future here at home.

The Government of Nova Scotia has been working hard to make this happen.

We posted five consecutive balanced budgets, made significant down payments on our debt, and improved our credit ratings. All of which have helped attract new jobs and new investments to our province. In fact, more Nova Scotians are working today than at any time in recent memory.

Nova Scotia's fiscal, economic, and social progress can be further secured or put in doubt, depending on how the federal government addresses the fiscal inequities that currently exist within our country: inequities that must be fully and fairly dealt with if Nova Scotia is to compete on a level playing field for new investments, new jobs, and new opportunities.

I encourage you to read on, to learn more about Nova Scotia's position, and to understand why this is such an important issue for you and your family.

A handwritten signature in black ink that reads "Rodney MacDonald".

Rodney MacDonald,
Premier of Nova Scotia

The Fiscal Imbalance in Canada: What Nova Scotians Need to Know

Introduction

All Canadians—wherever they live—have a constitutional right to receive about the same level of programs and services, at about the same level of taxation.

That's not happening right now because of what politicians and bureaucrats call a fiscal imbalance. Fiscal imbalance is caused by two things:

1. The federal government has most of the money, while the provinces have most of the responsibilities for delivering expensive programs and services like health care and education.
2. Some provinces have more revenue and resources than others.

The federal government and provinces want to fix this problem by finding a better way to redistribute your tax dollars. Governments are talking now about how to do this. Depending on the outcome, Nova Scotia could gain—or lose—significant funding.

The gain or loss will have a significant impact. Because fiscal imbalance is really about health care, education, and other essential programs and services—and the level of taxes you pay for them.

“It is encouraging that the federal government has recognized that fiscal imbalance exists at more than one level.”

**Finance Minister
Michael Baker**

What Is Fiscal Imbalance?

Fiscal imbalance exists among provinces, and between the provinces and the federal government.

Among Provinces (“Horizontal Imbalance”)

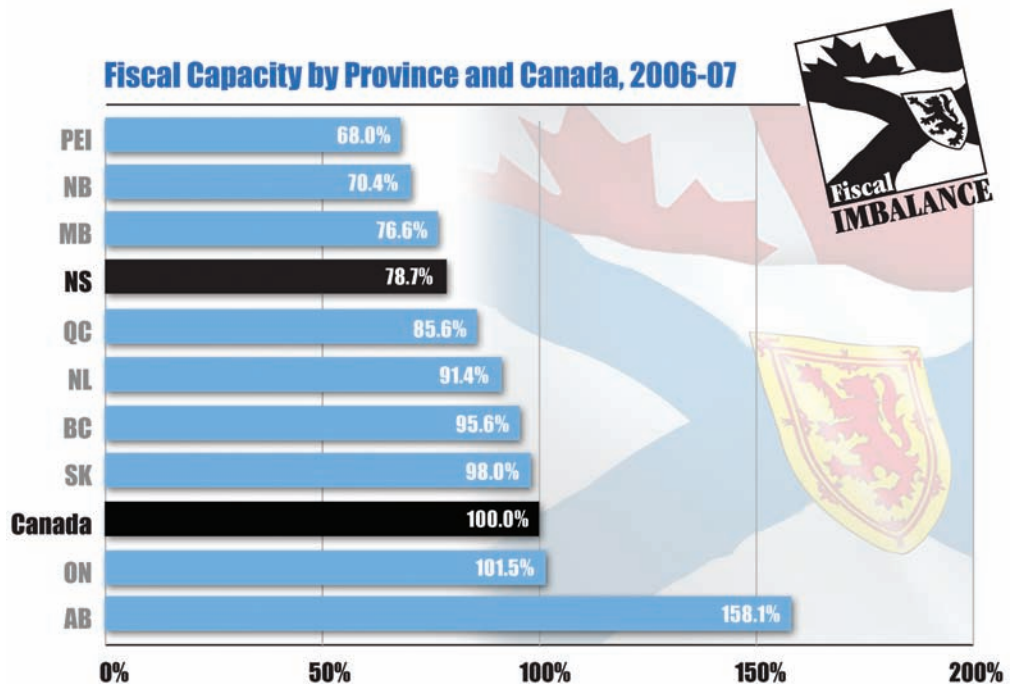
In simple terms, some provinces are richer than others. Factors—such as the strength of the provincial economy, population size, income levels, tax base, and the cost of delivering essential services—together define a province’s “richness,” or fiscal capacity.

Nova Scotia’s fiscal health has improved significantly in recent years. Yet, our fiscal capacity remains well below the national average.

Despite these differences among provinces, all Canadians have a constitutional right to receive about the same level of services at about the same level of taxation. (*Constitution Act, Sec. 36-2*)

“A small province like ours doesn’t have a huge revenue base to draw from. Fiscal imbalance must be resolved in a meaningful way to ensure sustainability of essential public programs and services.”

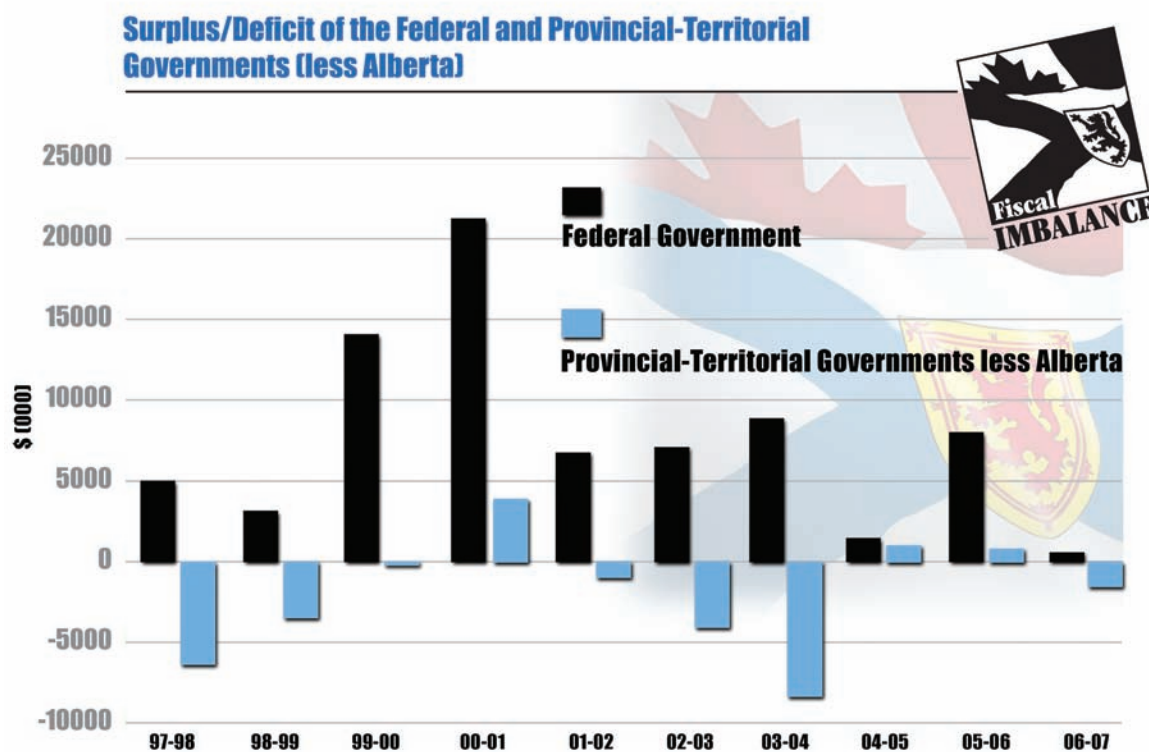
**Finance Minister
Michael Baker**



Equalization is how the federal government has tried to fulfil this constitutional responsibility to all Canadians. While equalization has helped, Nova Scotians are well aware that differences continue to exist—in terms of both the programs and services they receive and the taxes they pay.

Between the Provinces and the Federal Government (“Vertical Imbalance”)

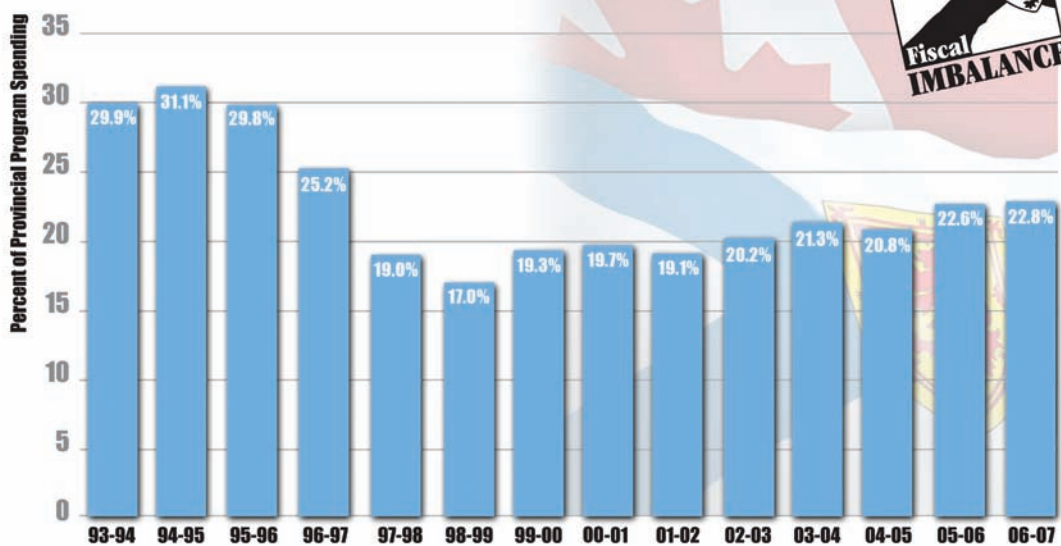
The federal government has most of the money through tax collection, while the provinces have most of the responsibilities for delivering programs and services. As a result, since 1997-98, the federal government has recorded a surplus—in some years a very sizable surplus—while provinces, collectively, have recorded deficits or small surpluses.



The federal government reallocates tax dollars to provinces through programs such as the Canada Health Transfer, the Canada Social Transfer, and Equalization. Over the past decade, however, federal transfers have declined dramatically.

The federal contribution in support of Nova Scotia's social programs has declined from about 30 per cent to about 20 per cent. In dollar terms, in 2005-06, it would have taken an additional federal investment of approximately \$240 million to obtain the proportion of federal support that existed in 1994-95. The fact that expected increases to social transfers (about 3.3 per cent annually) are being outpaced by growth in provincial expenditures (4 per cent annually) is widening the gap between what the federal government provides and what provinces need.

**Federal Contribution in Support of Nova Scotia's Social Programs
1993-94 to 2006-07**



What Is Nova Scotia's Position?

On Equalization

Ensure Adequacy

Nova Scotia's bottom line is simple. The province must receive adequate funding so Nova Scotians receive about the same level of services, at about the same tax level, as other Canadians.

Getting there is not so simple.

Step 1: The federal government must increase the amount of money available for equalization. Ensuring that provinces have the funding needed to provide a basic level of programs and services equal to the national average would require an estimated \$2-billion increase nationally.

Step 2: How this pot of money is shared among provinces—to ensure fairness and equity—must also change in a number of ways.

Move from a 5-Province to a 10-Province Standard

Equalization is intended to bring each province up to a certain standard level. That standard is set by averaging the relative wealth, or fiscal capacities, of the provinces.

Prior to the 1980s, the federal government averaged the fiscal capacities of 10 provinces. In 1982, the federal government began using 5 provinces—removing the wealthiest and poorest provinces from the calculation. This significantly reduced the costs of the program for the federal government—and has cost Nova Scotia more than \$3.3 billion since that time.

Nova Scotia believes the federal government must once again consider the circumstances in all provinces when setting the standard for equalization.

Include All Provincial Revenues in Calculating Equalization Entitlements

Nova Scotia believes that all revenue sources need to be considered when calculating what each province receives through equalization.

Provinces rich in natural resources generate revenue from those resources. That revenue needs to be accounted for when equalization benefits are calculated.

Similarly, user fees are a source of revenue for provinces, yet they are currently only partially included when calculating each province's equalization benefit. Nova Scotia believes user fees should be fully included in the equalization calculation.

Maintain Representative Tax System to Assess Fiscal Capacity

Currently, a "representative tax system" is used to measure each province's revenue potential, or fiscal capacity. Basically, the system compares a province's yield from numerous tax bases to that of the current five standard provinces, in calculating how much each province can generate in taxes.

Some provinces believe that other economic indicators, such as gross domestic product, should be used as a basis for calculating fiscal capacity. This, however, does not reflect each province's actual tax base.

Nova Scotia believes that the representative tax system should remain as the basis for calculating equalization benefits because the system is a closer reflection of every province's actual taxing practices and taxing capacity.

Remove Caps on Equalization Fund

In October 2004, the federal government announced it would increase the equalization fund by 3.5 per cent annually. However, this growth rate is not based upon measurement of fiscal differences among provinces, but rather, is an arbitrary growth rate set by the federal government.

The equalization cap must be removed so funding levels take the fiscal differences of each province into account.

On Federal Transfers

Federal transfers can broadly be defined as funding provided to provinces for specific purposes, such as health care, education, social services, and infrastructure. To ensure that the funding is adequate, the funding level must be linked to both the revenues and the real costs of delivering programs and services in each province.

For example, Nova Scotia has more seniors, an above-average rate of illnesses, the second-shortest life expectancy of all Canadians, and the largest number of persons with disabilities. While Nova Scotia has significantly increased its efforts to promote better health, results will take time. In the meantime, the province will continue to face higher health-care costs to meet the needs of Nova Scotians.

As another example, the funding Nova Scotia receives for post-secondary education does not reflect actual costs. Because of Nova Scotia's high-quality, post-secondary education schools, almost 13,000 out-of-province students are attracted to study in Nova Scotia each year. However, federal funding is linked to our population—not to the total number of students our province educates. This costs the province an estimated additional \$25 million.

Finally, the federal government provides transfers to support projects that contribute to the prosperity of the province and, in turn, the country. One of the best examples, and highest priorities for Nova Scotia, is infrastructure—in particular, funding for our roads, our ports, our information technology, and other essential building blocks that support our progress to greater prosperity. As well, the province benefits from funding agreements that support a wide range of programs and services—from child care to housing to our resource sectors.

What Are Other Provinces Saying?

All provinces agree—the fiscal imbalance must be corrected. But there are differences of opinion on how to correct the problem.

Provinces that do not receive equalization are concerned about further increases in the size of the equalization pot. However, current restrictions on the equalization program are already limiting provinces from receiving the level of financial support guaranteed under the constitution. As a result, the ability of some provinces to provide comparable levels of basic programs and services is already being threatened. If equalization funding is not increased, the differences among provinces will grow, and Canadians' constitutional right to similar programs and services at similar tax levels will be further compromised.

Provinces that are rich in natural resources believe the revenues they generate from these resources should not be included within the equalization formula. Specifically, they argue that natural resources, such as oil and gas reserves, eventually run out, so the revenues they generate cannot be used to fund programs and services.

However, natural resources generate wealth for a province—whether that money flows directly into programs or is used to reduce a province’s debt. To exclude these resources would seriously misrepresent a province’s wealth and entitle the province to equalization that would increase the inequities among provinces—the exact opposite of what equalization is intended to achieve.

Some provinces have criticized the Offshore Accord signed between the federal government and Nova Scotia. However, the accord did not take one dime away from any other province’s equalization payments. The revenues are fully accounted for within the equalization formula.

Nova Scotia and Newfoundland signed bilateral agreements with the federal government related to the Offshore Accord, and outside of equalization. This again is rooted in a constitutional obligation to further economic development in all regions.

Finally, these bilateral agreements are similar to those that exist with other provinces to support economic development. Examples include grain subsidies in the west and subsidies to the automotive and aerospace industries in central Canada.

Why Should This Matter to You?

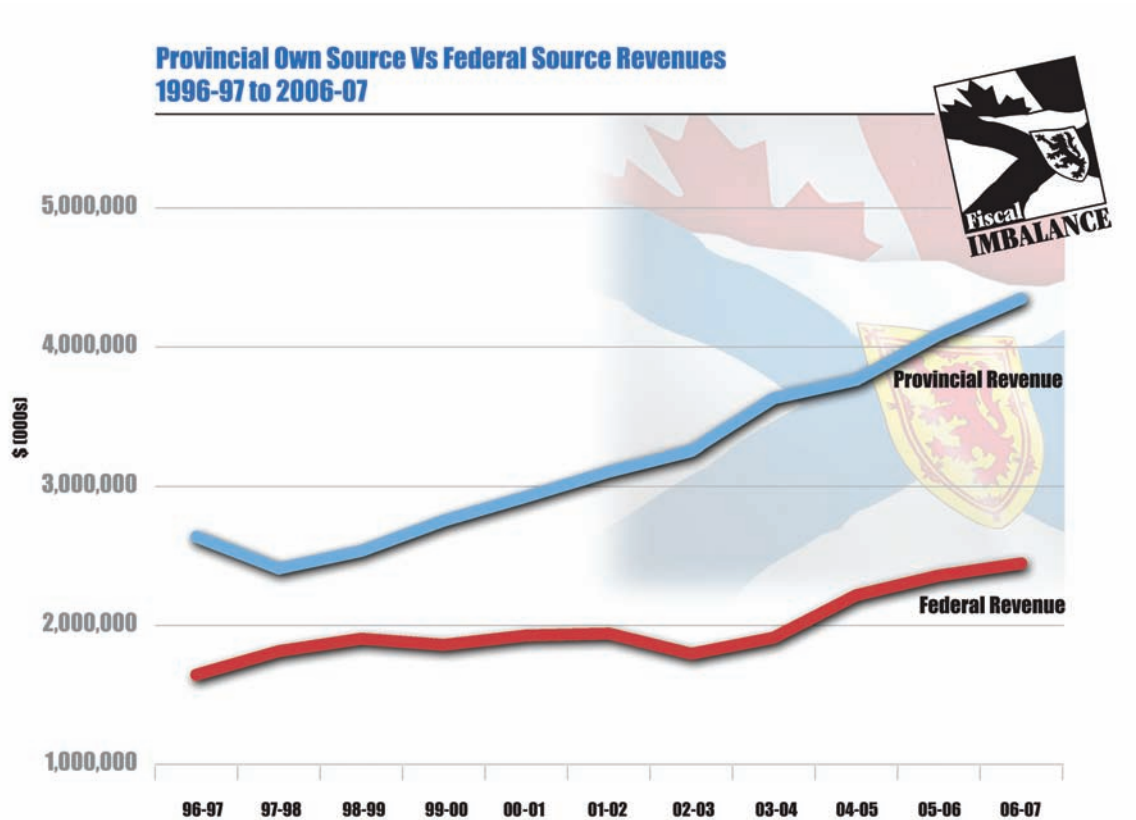
This is about the health care, education, and other programs and services you need—and the level of taxes you pay for them.

As a Nova Scotian, you have a constitutional right to receive about the same level of programs and services, while paying about the same level of taxes, as any other Canadian. This constitutional obligation is rooted in what it means to be part of the Canadian family. When we need to reach out when a natural disaster, drought, or disease strikes, Canadians from all provinces are there to do their part. And when a province benefits from greater economic prosperity, Canada is stronger and the benefits of this prosperity are shared.

In Nova Scotia, our economy is stronger than it has been in at least 10 years. This is demonstrated in our growing reliance on provincial own source revenues versus federal revenues.

“We are following through with our debt management plan. This is the last year that Nova Scotia’s debt will grow.”

**Finance Minister
Michael Baker**



Other facts that speak to Nova Scotia’s growing prosperity include:

- In 2005, Nova Scotia’s unemployment rate was at its lowest level in 30 years.
- Real personal disposable income per person in Nova Scotia has increased by 10 per cent in the last 10 years.
- We have posted five consecutive balanced budgets.
- All surpluses—and every penny from our Offshore Accord—have been applied to our debt. And this is the last year our debt will grow.
- Our international credit rating continues to improve.

But like almost all other provinces, we continue to rely on equalization—accounting for about 21 per cent of our total revenues.

The discussion among provinces, and with the federal government, could result in either a reduction or an increase in equalization for Nova Scotia in the tens, or even hundreds, of millions of dollars. For example, taking natural resources out of the equalization formula—in isolation of other changes—could cost Nova Scotia about \$200 million a year.

Even maintaining what we now receive could have a significant impact on our programs and services. Given that more than 40 per cent of the \$6.9-billion provincial budget is spent on health care—with costs growing by more than 8 per cent a year—Nova Scotia must receive adequate funding to protect the quality of health care.

Raising taxes is not an option. Nova Scotians do not earn as much money as Canadians in some of the richer provinces. Almost two-thirds of Nova Scotian taxpayers earn less than \$30,000 a year, with just 8 per cent of our taxpayers carrying almost 50 per cent of our personal income tax burden.

You Can Take Action

Contact your federal Member of Parliament today to stress the importance of this issue for you, your family, and our province.

Go to Nova Scotia's fiscal imbalance website at www.gov.ns.ca/fina/fiscal and get the contact information you need. Or call 1-800-670-4357 today.

Time is short. The federal government is committed to addressing the fiscal imbalance issue in 2007. Therefore, they must introduce new legislation on equalization by spring 2007. That makes a federal decision likely in late fall or early winter 2006.

“The results of the process are of critical importance not only to Nova Scotians, but to all Canadians. Unless these disparities are fully and fairly addressed, they could undermine the future strength and prosperity of our country.”

**Finance Minister
Michael Baker**



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