

## 2004-05 TAX INITIATIVES

The GNWT's fiscal situation requires action both to control expenditure growth and to raise additional revenues. While the GNWT is pursuing better fiscal arrangements with the federal government through Formula Financing and resource revenue sharing discussions, NWT taxpayers are also being asked to contribute a share of the growing cost of providing programs and services.

Two underlying principles of the NWT tax system are that taxes should be based on the ability to pay and that users of government services should contribute to maintaining those services. Based on these principles, the GNWT has introduced three tax initiatives as part of its goal to achieve fiscal sustainability.

The 2004-05 Budget includes the following tax initiatives:

- ◆ Effective January 1, 2004, the large Corporate Income Tax (CIT) rate will be increased from 12 per cent to 14 per cent.
- ◆ Effective July 1, 2004 the Personal Income Tax (PIT) rate on taxable income greater than \$108,101 will be increased from 13.05 per cent to 14.05 and the second highest PIT bracket rate will be increased from 11.70 per cent to 12.20 per cent.
- ◆ Effective January 1, 2005, the NWT Payroll Tax will increase from 1 per cent to 2 per cent of employment income. To reduce the effect of this change on low-income earners, the PIT rate for the lowest bracket will be decreased from 7.2 per cent to 5.9 per cent and for the second lowest bracket will be decreased from 9.9 per cent to 8.6 per cent. The Cost of Living Tax Credit (COLTC) will be increased from 1.6 per cent to 2.6 per cent of income up to \$12,000 and the minimum credit will be increased from \$250 to \$350 for singles and from \$500 to \$700 for couples. These changes will also take effect January 1, 2005.

### LARGE CORPORATE INCOME TAX RATE INITIATIVE

In July 2002, the large CIT rate was lowered from 14 to 12 per cent and the small business rate was lowered from 5 to 4 per cent to maintain the competitiveness of the NWT CIT. However, since then, changes in the interaction between the NWT tax system and the Formula Financing Grant mean that changes in tax rates must be considered. The Formula's "tax effort" factor will likely be recalculated when the Formula Financing Agreement is renewed effective April 1, 2004. The effect of changing the tax effort would create the perverse situation where the GNWT would lose revenue for every dollar in CIT collected unless it increases its CIT rate. For example, if NWT large corporate taxable income is \$100 million, at 12 per cent the GNWT would collect \$12 million in CIT. However, the Formula Financing Grant would fall by \$12.8 million – a net reduction in revenue of \$800,000. With a CIT rate of 14 per cent, the GNWT would collect \$14 million in income tax, and receive net revenue of \$1.2 million. Increasing the CIT rate to 14 per cent is necessary to ensure that the GNWT receives a net fiscal benefit from growth in the CIT base.

CIT collections fluctuate significantly from year to year in the NWT, but it is estimated that increasing the tax rate from 12 per cent to 14 per cent effective January 1, 2004 will result in approximately \$8 million in additional revenue in 2004-05.

### HIGH INCOME PERSONAL INCOME TAX CHANGE

Effective July 1, 2004, the tax rates for the top two tax brackets will increase. An increase of 0.5 percentage points to the second highest PIT tax bracket will change the marginal rate from 11.70 per cent to 12.20 per cent. This change will raise an additional \$250,000 from 3,700 NWT taxpayers. A taxpayer with a taxable income of \$88,000 will pay \$108 per year more tax, or \$4.15 per biweekly pay.

Increasing the top rate from 13.05 per cent to 14.05 per cent, combined with the impact of the second highest tax bracket increase will generate an additional \$700,000 from approximately 900 taxpayers. A taxpayer with a taxable income of \$150,000 would pay an additional \$627 per year in tax or \$24.12 biweekly.

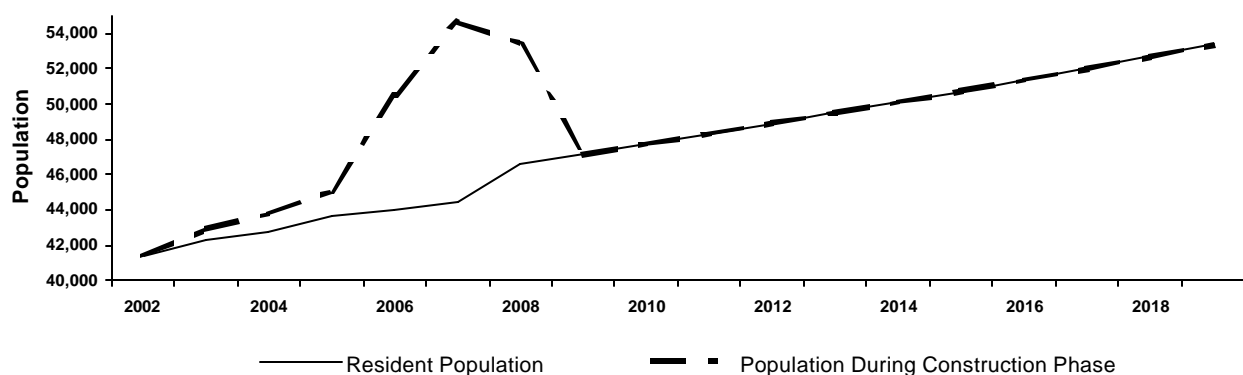
The changes will move the NWT combined top marginal rate to 43.05 per cent, still below the Canadian average of 45.68 per cent.

### PAYROLL TAX, INCOME TAX AND COST OF LIVING TAX CREDIT INITIATIVE

The Tax Collection Agreement between the GNWT and Canada specifies that most income, including employment income, is taxed in the province or territory in which the taxpayer resides on December 31. As a result, many people who work in the NWT do not pay income tax to the NWT. This is a particularly significant problem for the NWT because the nature of work schedules in the resource industries allows individuals to work in the NWT but to live and pay taxes elsewhere. Payroll Tax receipts for 2002 suggest that employment income earned in the NWT reached \$1.2 billion. However, 2002 PIT returns filed in the NWT show only \$1 billion of employment income. It is important that individuals who benefit from NWT resource development contribute toward the GNWT's increased costs caused by resource development. The GNWT introduced a Payroll Tax in 1993 to address this issue.

It is expected that the proposed Mackenzie Valley Pipeline will create almost 60,000 person years of employment over the next 30 years. Much of this will be imported labour from outside the NWT. Other resource projects, such as the construction of additional diamond mines, will add to this number. The potential impact on the NWT population of expected resource development is shown in the following chart.

*Population Impacts From Anticipated Resource Development Projects*



The GNWT receives no fiscal benefit from this huge influx of workers, either through the Formula Financing Grant or from Income Tax, as these individuals are not officially residents of the NWT. However, the GNWT must absorb the additional operational and capital costs from activities of the larger workforce. To address these pressures, the Payroll Tax will be increased by 1 per cent effective January 1, 2005.

The GNWT stands to generate significant Payroll Tax revenues from the construction phase of the proposed Mackenzie Valley Pipeline. It is estimated that labour income over a 21-year period from this project could be \$2.5 billion dollars, ranging from an annual low of \$9 million to a high of \$561 million during the construction phase.

To minimize the negative impacts of this change on lower-income NWT residents, the PIT rate for the lowest bracket will be decreased from 7.2 per cent to 5.9 per cent and the second lowest bracket will be decreased from 9.9 per cent to 8.6 per cent. Furthermore, the COLTC will be increased from 1.6 per cent to 2.6 per cent of income up to \$12,000 and the minimum credit will be increased from \$250 to \$350 for singles and from \$500 to \$700 for couples.

### *2004-05 Budget Tax Changes*

	<b>Pre-Budget Rates</b>	<b>Proposed Rate Changes</b>
<b>Corporate Income Tax</b>	12%	14%, effective January 1, 2004
<b>Payroll Tax</b>	1%	2%, effective January 1, 2005
<b>COLTC</b>		Effective January 1, 2005
\$0 to \$12,000	1.6%	2.6%
\$12,000 to \$48,000	\$192 plus 1.25% of amount exceeding \$12,000	\$312 plus 1.25% of amount exceeding \$12,000
\$48,000 to \$66,000	\$642 plus 1.00% of amount exceeding \$48,000	\$762 plus 1.00% of amount exceeding \$48,000
Over \$66,000	\$822	\$942
Single Minimum Credit	\$250	\$350
Couple Minimum Credit	\$500	\$700
<b>Personal Income Tax</b>		Effective January 1, 2005 <sup>1</sup>
\$0 to \$33,245	7.2%	5.9%
\$33,245 to \$66,492	\$2,394 plus 9.9% of the amount exceeding \$33,245	\$1,961 plus 8.6% of the amount exceeding \$33,245
\$66,492 to \$108,101	\$5,685 plus 11.7% of the amount exceeding \$66,492	\$4,820 plus 12.2% of the amount exceeding \$66,492
Over \$108,101	\$10,553 plus 13.05% of the amount exceeding \$108,101	\$9,897 plus 14.05% of the amount exceeding \$108,101

<sup>1</sup> The top two tax brackets will be increased effective July 1, 2004. Changing the top tax bracket from 13.05% to 14.05% in the middle of the 2004 year causes the 2004 rate to be 13.55% (13.05% plus half of 1%). The second highest tax bracket rate for 2004 will be 11.95% (11.7% plus half of 0.5%).

**2004 Provincial and Territorial Tax Rates as of March 17, 2004**

	Combined Top Marginal PIT rate <sup>(a)</sup> (%)	Retail Sales Tax (%)	Fuel Tax <sup>(b)</sup>		Tobacco Tax on Cigarettes (\$/carton) <sup>(c)</sup>	Payroll Tax <sup>(d)</sup> (%)	Corporate Income Tax		Capital Tax <sup>(e)</sup> (%)
			Gas (¢/litre)	Diesel (¢/litre)			Small (%)	Large (%)	
Northwest Territories	42.55	-	10.7	9.1	42.00	1.00	4.0	14.0	-
Nunavut	40.50	-	6.4	9.1	31.20	1.00	4.0	12.0	-
Yukon	42.40	-	6.2	7.2	26.40	-	6.0	15.0	-
British Columbia	43.70	7.5	14.5	15.0	35.80	-	4.5	13.5	0/3.0
Alberta	39.00	-	9.0	9.0	32.00	-	3.0 <sup>(f)</sup>	11.5 <sup>(f)</sup>	-
Saskatchewan	44.00	6.0	15.0	15.0	32.00	-	5.5	17.0	0.6/3.25
Manitoba	46.40	7.0	11.5	10.9	31.00	2.15	5.0	15.5	0.5/3.0
Ontario	46.41	8.0	14.7	14.3	19.70	1.95	5.5	14.0	0.3/0.9
Quebec	48.22	7.5	15.2	16.2	20.60	4.26	8.9	8.9	0.64/1.28
New Brunswick	46.84	8.0	14.5	16.9	23.50	-	3.0	13.0	0.3/3.0
Nova Scotia	47.69	8.0	15.5	15.4	26.04	-	5.0	16.0	0.25/3.0
Prince Edward Island	47.37	10.0	14.0	13.5	29.90	-	7.5	16.0	0/3.0
Newfoundland	48.64	8.0	16.5	16.5	30.00	2.00	5.0	14.0	0/4.0
Average <sup>(g)</sup>	45.68	6.9	14.1	14.3	24.59	1.88	5.8	12.7	

## Notes:

- (a) Combined Federal-Provincial/Territorial highest personal income tax rates in effect for the 2004 tax year.
- (b) Quebec, New Brunswick, Nova Scotia and Newfoundland apply sales tax to fuel. Most provinces have separate tax rates for on-highway and off-highway gasoline. The NWT's off-highway gasoline tax rate is 6.4 cents/litre.
- (c) Saskatchewan, Manitoba, Ontario, New Brunswick, Nova Scotia and Newfoundland apply sales tax to tobacco products.
- (d) The NWT and Nunavut levy payroll taxes on employees. Other provinces that levy payroll taxes provide exemptions for small business and/or the rates vary depending on the payroll size.
- (e) Capital tax rates are for large corporations and for financial institutions in the order shown. The tax bases are different for different types of companies.
- (f) Alberta plans to reduce small and large corporate income tax rates to 3.0 per cent and 11.5 per cent, respectively, effective April 1, 2004.
- (g) Average weighted by provincial/territorial population.