

NUNAVUT ECONOMIC FORUM

**Submission to the
House of Commons Standing Committee on Finance
Pre-Budget Consultations**

THE TAX SYSTEM THE COUNTRY NEEDS FOR A PROSPEROUS FUTURE

**Iqaluit, Nunavut
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EXECUTIVE SUMMARY

The Nunavut Economic Forum (NEF) first emerged in 1998 to identify and share information to support planning for economic development in Nunavut. The primary focus for the thirty members of the NEF is to collaborate on the implementation of the Nunavut Economic Development Strategy, which includes a broad range of recommendations to address Nunavut's economic challenges.

For the purposes of the House of Commons Standing Committee Pre-Budget Consultations for 2007 on the theme: **The Tax System the Country Needs for a Prosperous Future**, the Nunavut Economic Forum wishes to discuss the Northern Residents Deduction.

The Northern Residents Deduction has not increased since it was implemented in 1987. Since this time the Consumer Price Index has increased significantly, effectively eroding the impact and undermining the objectives of the deduction.

The effectiveness of the current Northern Residents Deduction as a measure to alleviate the high cost of living in Nunavut must be questioned when the cost of living is as much as 75% higher than the Canadian average.¹

Due to the structure of the Northern Residents Deduction lower income earners do not receive the full benefit of the deduction. As well, there are barriers to maximizing some of the benefits administered under the Canada Revenue Agency. Eligibility ceilings for these benefits based on national determinations of lower incomes do not apply in Nunavut where the cost of living is significantly higher than the Canadian average.

Due to the high cost of living, employers are required to provide wage and benefits packages that compensate for the high costs associated with daily life in Nunavut. While this is necessary, these are taxable benefits and it has the effect of increasing the amount of income tax paid by the individual.

The erosion of wages due to the high cost of living and high taxes may also have a negative effect on the overall development of the labour force. There is intense nation-wide competition for skilled employees to provide much needed expertise and skills transfer in order to build human resource capacity in Nunavut. An appropriate enhancement to the Northern Residents Deduction may be a cost effective way to help develop Nunavut's labour force.

In order to address these issues the Nunavut Economic Forum submits the following recommendations:

- 1. The Northern Residents Deduction should be increased based on the cumulative effects of inflation since 1987 and indexed going forward.**
- 2. The Northern Residents Deduction should be increased to more effectively address the high cost of living in Canada's far north.**
- 3. The Northern Residents Deduction should be further enhanced for lower income earners that do not benefit from the travel deduction and to ensure eligibility for federal programs such as the GST Tax Credit, Child Tax Benefit and the Energy Cost Benefit.**
- 4. The Northern Residents Deduction should be increased to achieve equitable tax burden for northerners that receive enhanced wage and benefits packages necessary to off-set the high cost of living.**
- 5. The Northern Residents Deduction should be viewed as one of the tools available to help facilitate the development of Nunavut's labour force which will benefit the overall economy of the territory and Canada.**



INTRODUCTION

The Nunavut Economic Forum (NEF) first emerged in 1998, when a Forum for the Strategic Planning of the Nunavut Economy was developed “to identify and share information to support planning for economic development activity in Nunavut.” The primary focus for the thirty members of the NEF is to collaborate on the implementation of the Nunavut Economic Development Strategy (Strategy).² Subtitled “Building a Foundation for the Future” the Strategy includes a broad range of recommendations to address challenges for Nunavut’s economic growth. These recommendations focus on such areas as education, infrastructure, community and resource development, tourism, the arts and the traditional economy. The Strategy was released in 2003 and has a ten-year implementation period.

The NEF also undertakes research and data collection on Nunavut’s economy and functions as a representative and advocacy group on issues related to the implementation of the Strategy. The NEF has produced such documents as Qanijjuq (Preparing for the Journey), the 2005 Nunavut Economic Outlook and the 2005 Progress Review of the Nunavut Economic Development Strategy.³

THE PURPOSE OF THIS SUBMISSION

For the purposes of the House of Commons Standing Committee Pre-Budget Consultations for 2007 on the theme: **The Tax System the Country Needs for a Prosperous Future**, the Nunavut Economic Forum wishes to discuss the Northern Residents Deduction (NRD).

THE NORTHERN RESIDENTS DEDUCTION

The NRD was introduced in 1987 and remains essentially unchanged. It is intended to provide an incentive to encourage individuals to work and live in northern and remote areas by compensating them for a higher cost of living and to make travel to southern Canada more affordable. It has two components, the residency deduction for having lived in a prescribed zone, and the travel deduction for taxable travel benefits received from employment in a prescribed zone. The residency component of the NRD is calculated based on \$15 per day for a total amount of \$5,475 or 20% of the net income, whichever is less. The travel deduction is only available to individuals that receive a taxable travel benefit from their employers, which effectively excludes many northerners from receiving the full benefit of the NRD.⁴

In a report prepared by the Parliamentary Information and Research Service in 2004 (PRB 03-52E) the rationale for special tax treatment for northern and isolated areas is discussed and includes the following justifications for the deduction: sovereignty, economic development, regional differences in wages and the cost of living, regional differences in the level of goods and services and environmental hardship. This report also includes some arguments against special tax treatment for northerners, but these arguments reveal a lack of understanding of northern communities and seem to imply that the labour force of northern Canada is exclusively made up of transient southerners.⁵

The inclusion of sovereignty and economic development as part of the justification for special tax treatment for northerners should be of particular interest to the current government, and taxation issues such as the NRD should be considered under the broader scope of developing a new *Northern Vision* as described in the Conservative Party Platform.⁶



With a renewed federal interest on the development of Canada's north, now is a good time to review the intent and value of the NRD in the context of the changing political environment, social and economic conditions, and opportunities and objectives for the far north. Now is the time to make improvements that support the broader objectives for the development and economic prosperity of northern Canada and Nunavut.

THE IMPACT OF INFLATION

The residency component of the NRD of \$15 per day for a total of \$5,475 has not increased since it was implemented in 1987. Since 1987 the cumulative rate of inflation has been 64%. With the cumulative rate of inflation applied, the deduction for 2007 would be \$24.50 per day for a total of \$8,943.⁷

The Northern Residents Deduction should be increased based on the cumulative effects of inflation since 1987 and indexed going forward.

THE HIGH COST OF LIVING

The effectiveness of the current NRD as a measure to alleviate the high cost of living in Nunavut must be questioned when the cost of living has been calculated as being as much as 75% higher than the Canadian average.⁸

The high cost of living is recognized and addressed by the Government of Canada through the salary and benefits packages provided to federal employees working in Nunavut, where the total compensation package is significantly higher than that of a comparable position in southern Canada. In a comparison prepared for a cost of doing business study, it is shown that a position with a salary and benefits package of \$88,208 in southern Canada would receive \$133,208 in Nunavut.⁹ This represents a 51% premium that is paid to the Nunavut based employee without incorporating other housing related costs which increase the total staffing budget to \$178,208. The staffing budget for Nunavut based federal employees is reflective of the high cost of living and this recognition should be extended to influence a decision to increase the NRD.

The Northern Residents Deduction should be increased to more effectively address the high cost of living in Canada's far north.

ENHANCED BENEFITS FOR LOWER INCOME EARNERS

Although tax relief is most urgently required among lower income earners to off-set the high cost of living, they are less likely to fully benefit from the NRD and in particular the travel deduction component. This is because the residency deduction is the lesser of \$5,475 or 20% of net earnings and because lower income earners are less likely to receive taxable travel benefits from an employer. An enhanced residency deduction should be considered for northerners that do not benefit from the travel deduction.

At the same time, the NRD should not be viewed exclusively as a benefit to off-set the higher cost of living. It should also be seen as a method to achieve parity for lower income earners to ensure they have access to programs such as the GST/HST Credit, the Canada Child Tax Benefit and the Energy Cost Benefit.

Eligibility ceilings based on national determinations of lower incomes do not apply in Nunavut where the cost of living is significantly higher than the Canadian average. In July 2006 the income level for a family of four where the individual would no longer receive the GST/HST Credit was \$44,430. This is just slightly above the poverty rate for a family of four in Nunavut, which is \$43,236 while the rate for Canada is \$28,824.¹⁰



If we were to apply the overall cost of living adjustment that is used by the federal government to determine the premium for living in Nunavut, the eligibility ceiling for the GST/HST Credit and similar programs should be increased by 51% to \$67,090.

Alternatively, the NRD with enhancements for lower income earners could help achieve parity with other Canadians based on poverty rates. Using the figures for poverty rates provided in the previous paragraph, this would mean that the deduction would be the difference between \$43,236 and \$28,824 or \$14,412.

The Northern Residents Deduction should be further enhanced for lower income earners that do not benefit from the travel deduction and to ensure eligibility for federal programs such as the GST Tax Credit, Child Tax Benefit and the Energy Cost Benefit.

EQUITABLE TAXATION

As discussed, employers including the Government of Canada are required to provide wage packages that compensate for the high costs associated with daily life in Nunavut. While this is necessary, these are taxable benefits and it has the effect of increasing the amount of income tax paid.

In a scenario comparing the tax burden of the Ottawa and Nunavut based federal employees whose incomes are described in the previous section we found that the additional federal tax paid by the Nunavut based employee was \$5,395. These findings are similar to those discussed in the PRB 03-52E report which indicates that a progressive tax system “may lead to unequal tax treatment.” Even with the NRD and allowable deductions for vacation travel, a Nunavut resident is paying significantly more federal income tax than a comparable counterpart in southern Canada.¹¹

The Northern Residents Deduction should be increased to achieve equitable tax burden for northerners that receive enhanced wage and benefits packages necessary to off-set the high cost of living.

NUNAVUT’S ECONOMIC DEVELOPMENT

The PRB 03-52E report includes a section that connects the NRD with economic development. The NRD is seen as a cost effective way to help attract and retain the skills required for the labour force in northern Canada. However, the landscape in which this policy is functioning has changed dramatically in the 20 years since it was implemented. There is now intense nation-wide competition for skilled labour and with the establishment of the Nunavut Government, resource and infrastructure development and increasing need for education and medical services the territory requires more human resource capacity than ever before. The ability to attract and retain the skilled labour required to meet current demands and to facilitate skills transfer to northerners is critical to Nunavut’s economic development.

The Northern Residents Deduction should be viewed as one of the tools available to help facilitate the development of Nunavut’s labour force which will benefit the overall economy of the territory and Canada.



RECOMMENDATIONS

The underlying objective of the Northern Residents Deduction is to assist in attracting skilled labour to northern and isolated communities by providing recognition for the additional costs faced by residents of these areas. In order to renew and maintain the effectiveness of the deduction in achieving its objectives, the Nunavut Economic Forum makes the following recommendations:

- 1. The Northern Residents Deduction should be increased based on the cumulative effects of inflation since 1987 and indexed going forward.**
- 2. The Northern Residents Deduction should be increased to more effectively address the high cost of living in Canada's far north.**
- 3. The Northern Residents Deduction should be further enhanced for lower income earners that do not benefit from the travel deduction and to ensure eligibility for federal programs such as the GST Tax Credit, Child Tax Benefit and the Energy Cost Benefit.**
- 4. The Northern Residents Deduction should be increased to achieve equitable tax burden for northerners that receive enhanced wage and benefits packages necessary to off-set the high cost of living.**
- 5. The Northern Residents Deduction should be viewed as one of the tools available to help facilitate the development of Nunavut's labour force which will benefit the overall economy of the territory and Canada.**

CONCLUSION

The tax system provides a mechanism to raise funds for public purposes and provide for a redistribution of wealth in order to reduce poverty and inequality for individual Canadians, specific segments of society and for geographic regions with particular development needs.

The Northern Residents Deduction is one component of the tax system intended to achieve a range of objectives for Canadians living in the north, and in particular the far north, where the cost of living is significantly higher than the Canadian average.

However, this benefit has not changed in 20 years and its effectiveness has been eroded by inflation. As well, the social, economic and political environment has changed dramatically and the need to support the development of the north has never been greater.

The Government of Canada should carefully consider the objectives of the Northern Residents Deduction and the recommendations provided in the context of developing a new "Northern Vision" and take appropriate steps to enhance the deduction to provide incentive and benefits for residents of the far north.



¹ With information from “Addressing the Cost of Living in Nunavut” Alison Rogan for the Nunavut Employees Union, April 2003

<http://www.nunavuteconomicforum.ca/public/files/library/LABOURFO/COSTOFLI.PDF>

² The Nunavut Economic Development Strategy: Building a Foundation for the Future

<http://www.nunavuteconomicforum.ca/public/strategy/index.php>

³ <http://www.nunavuteconomicforum.ca/public/index.php>

⁴ With information from the Parliamentary Information and Research Service report on the Federal Northern Residents Deduction (PRB 03-52E), Marc-Andre Pigeon, Economics Division, January 28, 2004.

<http://dsp-psd.pwgsc.gc.ca/Collection-R/LoPBdP/PRB-e/PRB0352-e.pdf>

⁵ ibid

⁶ “Stand Up For Canada” Conservative Party Platform page 18

<http://www.conservative.ca/media/20060113-Platform.pdf>

⁷ With information from the Bank of Canada Inflation Calculator

http://www.bankofcanada.ca/en/rates/inflation_calc.html

⁸ With information from “Addressing the Cost of Living in Nunavut” Alison Rogan for the Nunavut Employees Union, April 2003

<http://www.nunavuteconomicforum.ca/public/files/library/LABOURFO/COSTOFLI.PDF>

And “The Cost of Doing Business in Nunavut” Robert Higgins for Nunavut CEDO, April 2007.

<http://www.nunavuteconomicforum.ca/public/files/library/REPORTSO/Cost%20of%20Doing%20Business%20-%20Nunavut%20CEDO.pdf>

⁹ ibid

¹⁰ ibid

¹¹ Parliamentary Information and Research Service report on the Federal Northern Residents Deduction (PRB 03-52E), Marc-Andre Pigeon, Economics Division, January 28, 2004.

<http://dsp-psd.pwgsc.gc.ca/Collection-R/LoPBdP/PRB-e/PRB0352-e.pdf>