

Charting a Path for Growth



Nova Scotia Tax and Regulatory Review

November 2014

Laurel C. Broten

Lead, Nova Scotia Tax and Regulatory Review

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November 19, 2014

Honourable Diana Whalen
Minister of Finance & Treasury Board
1723 Hollis Street
Halifax, NS B3J 2N3

Dear Minister Whalen:

I am pleased to present the final report and recommendations of The Nova Scotia Tax and Regulatory Review, entitled *Charting a Path for Growth*. This report represents the culmination of nine months of consultation, study and investigation related to taxes, regulations and fees in Nova Scotia. The report and its recommendations focus on the central feature of the terms of reference: the economic growth imperative in Nova Scotia.

The work began with consultations across the province and an extensive examination of the tax, regulatory and fee environment in Nova Scotia. The review also drew on a broad array of studies and findings from local, national and international academic, government and other sources in a search for ideas and actions that could be relevant to Nova Scotia.

During the course of this review, experts, business leaders and Nova Scotians right across the province made it clear that fundamental tax changes are required to create a more competitive and ultimately more prosperous economic climate in Nova Scotia. Tax reform is necessary to lift the high personal income tax burden off Nova Scotia families in order to reduce disincentives to work and encourage entrepreneurs to emerge and to take the risks that build dynamic economies.

The essence of the tax recommendations would shift more of the burden of taxation toward consumption, and off personal and corporate income; and would tax pollution with the resulting revenue further reducing income taxes and offering income support to Nova Scotians who need it most.

The basic rationale for pollution taxation is clear. Pollution imposes costs on society that are not currently borne by the polluter. A tax ensures that the polluter accounts for these costs and, on this basis, reduces pollution at least to a level that takes into account both the costs of the pollution and the benefits of the polluting activity.

The small business tax rate would increase gradually to narrow the gap with a reduced general corporate tax rate, encouraging all businesses to grow and recognizing the important role large Nova Scotia corporations play in creating jobs and driving prosperity.

Two fundamental issues are at the centre of these recommendations: the economic prospects and the demographic realities of Nova Scotia. At present, the provincial corporate tax rate – one of the highest in Canada – is a competitive disadvantage and a barrier to economic growth. And, as Nova Scotians are repeatedly reminded, the province is aging. The result will be an overall reduction in the size of the workforce, along with the income taxes they pay.

In light of this reality, Nova Scotia requires a tax system that generates adequate resources to fund the public services Nova Scotians need, puts the Province on a sound fiscal footing and still allows the economy to grow. The product of this review seeks to balance those and other interests with a comprehensive plan for reform that shares the burdens and the benefits fairly.

The tax reform measures are based on an assumption that the government can and will hold the line on spending. The first recommendation is that Nova Scotia should freeze program spending at current levels, adjusted only for existing collective agreements. The provincial budget would be close to balance in 2015-16, and subsequent surpluses can be used to reduce personal and corporate taxes as well as cover one-time costs of transformational change.

As requested, the report also details a number of measures to reform the regulatory processes of government and suggests that regulatory change become a springboard to the transformational changes that will be needed to maintain and improve public services while containing costs.

The report recommends that the government put in place a proven structure to drive change, publicly commit to regulatory reform, and make regulatory excellence a government-wide priority, driven from the highest political level – by the Premier. The government should create mechanisms, including legislation, to sustain the regulatory modernization agenda over the long-term. A “Regulatory Modernization and Accountability Act,” following the examples of British Columbia, Saskatchewan or Ontario, will help focus departmental regulatory modernization efforts into a centralized process and structure.

A minister should be named responsible for regulatory modernization and a central office created as a single point of accountability with the authority to coordinate regulatory reform across government. Central ownership and horizontal management of regulatory reform is the proven structure to drive change.

Joint teams of government and economic sector leaders should be created to identify priority regulatory issues which, if resolved, would strengthen the sector’s success. These teams, working expeditiously, can create an inventory of regulations to be eliminated or simplified.

The report further suggests that government should introduce legislation to repeal all outdated or inefficient regulations, streamline others for more effective enforcement and ease of compliance and reduce regulatory overlap and redundancies. The target for this legislation – a multi-departmental omnibus bill – should be the Spring of 2015 – a regulatory “Spring Cleaning.”

With respect to fees, the Province must gain a much better understanding of the cost of the services it delivers and adopt a government-wide standard methodology of costing in order to position itself for future efforts directed toward full cost recovery with limited exceptions in cases where public policy determines that full cost is an unacceptable burden to pass along to Nova Scotians.

It will come as no surprise to you that the assistance of Finance and Treasury Board staff, in particular Byron Rafuse and Denise Dickson, proved invaluable in completing this work.

Finally, thank you for the opportunity to lead this review. I was privileged to speak and work with so many dedicated Nova Scotians, who share a deep commitment to our province and its future. I hope this report proves useful as you and your colleagues deliberate and decide matters that are of great importance to all Nova Scotians today and tomorrow, including my own two boys who are pleased to call Nova Scotia home.

With sincere regards,



Laurel C. Broten
Lead, Nova Scotia Tax & Regulatory Review

Laurel C. Broten, B.Sc., B.A., J.D., I.C.D.D.



Laurel C. Broten is a public policy expert, former senior Ontario cabinet minister, lawyer, legislator, and advocate. Now, president and CEO of Broten Public Policy International Inc., she provides strategic advice on complex public policy challenges, change management, and government transformation to clients in Canada and abroad.

From 2003 to 2013, Ms. Broten served the people of Ontario as Minister of Education, Minister of Children and Youth Services, Minister of the Environment, Minister of Intergovernmental

Affairs, Minister Responsible for Women's Issues, and Vice-chair of Treasury and Management Board. She oversaw the government's agenda of continuous improvement, system transformation, and sustainability, and she worked across several ministries to bring expenditures in line with the province's fiscal realities. She is an expert in results-based planning and budgetary and financial analysis.

Ms. Broten has developed and implemented a number of transformative strategies to ensure evidence-based decision making, to modernize regulatory and funding regimes, and to establish more robust accountability measures. Some of these include the development of comprehensive strategies to modernize child-care services, to improve the delivery of children's mental health services, to transform Ontario's \$1.4 billion child welfare system, to more effectively integrate internationally trained medical professionals, and to tackle bullying in Ontario schools. She was responsible for developing and leading a number of cross-ministry strategies, including Ontario's Domestic Violence Action Plan, Sexual Violence Action Plan, and Air Quality and Climate Change plans.

As Minister of Education, Ms. Broten achieved savings of more than \$2 billion over two years, while protecting the classroom experience for students and continuing to roll-out full-day kindergarten. As Minister of the Environment, she oversaw implementation of all Walkerton Inquiry recommendations and introduced Ontario's ground-breaking source water protection legislation. As Minister of Intergovernmental Affairs, Ms. Broten worked toward the development of a national strategy to modernize Canada's federal-provincial fiscal architecture.

After graduating with distinction with her *Juris Doctor* degree from the University of Western Ontario, Ms. Broten clerked at the Supreme Court of Canada for Madam Justice Claire L'Heureux-Dubé, and later practised commercial, civil, and constitutional law with three leading Canadian law firms.

Ms. Broten and her family live in Hammonds Plains, Nova Scotia.

Table of Contents

Section One: The Review	1
Introduction	1
Mandate	3
Consultation	5
Literature and Best Practice Review	6
Setting the Stage—Finances: A Nova Scotia Primer	7
Where the Money Comes From	9
Federal Transfers	10
Where the Money Goes	12
Section Two: Taxes	15
System-Wide Plan Toward Recovery and Prosperity	15
Nova Scotia Tax Levers	15
Personal income tax	15
Business taxes	16
HST	17
Motive fuel tax	17
Tobacco tax	18
Where to Start	18
Principles for a Modern Tax System	21
What is Nova Scotia to do?	23
A Comprehensive and Interconnected Pathway Forward	25
Recommendations	26
Hold the line on spending	26
Priorities for personal tax reform:	28
Reduce and simplify income taxes: Shift taxation toward consumption. . . .	28
Increase Basic Personal Amount	31
End bracket creep	32
Eliminate the “temporary” fifth tax bracket	33
Promote fairness and simplify personal income tax	
eliminate non-essential tax expenditures	34
Remove disincentive to work	35
Reform personal income tax rates	37
Competitive corporate taxes for all businesses	38
Corporate tax expenditures	42

Film Industry and Digital Media tax credits	45
The Scientific Research and Experimental Development tax credit	47
Equity Tax Credit	48
Implement a Pollution Tax	51
Maintain reform momentum	55
Additional fiscal considerations	56
Beyond taxes: Revenue innovations to invest in the future	56
Revenue integrity	57
Underground economy	58
Tax Recommendations	60
Section Three: Regulation	64
Modern Regulation – How do we get there?	64
Put in place a culture of prospective and retrospective reform	64
Acknowledge the cost and impact of regulation	65
Aspire to be better smarter regulators	67
Be cognizant of the history of regulatory reform in Nova Scotia	68
Learn lessons from others	70
Use information wisely	73
Prioritize the highest impact reforms	73
Embrace regulatory impact analysis (RIA)	74
Fully examine regional opportunities	74
Recognize the impact of regulations on individuals	76
Ultimately deliver better government	77
Make evidence-based decisions	77
Adopt continuous improvement	78
Get the best value from information and technology investments	79
Embrace customer service	80
Involve everyone in the reform agenda	80
Establish a robust and structured process to identify and develop specific regulatory reforms	81
Regulatory Reform Recommendations	82
Section Four: Fees	89
Adopt a Standard Costing of Government Services	89
Aim toward Full Cost Recovery	90
Put in place measures to increase transparency and predictability	90
Identify areas where user fees can be implemented	91
Fees Recommendations	91
Conclusion	93
List of Recommendations	95
Notes	105

Charting a Path for Growth

Nova Scotia Tax and Regulatory Review

Section One: The Review

Introduction

“The status quo in our province is not working. We are facing significant economic and fiscal challenges.”

Nova Scotia’s Minister of Finance, Diana Whalen in the *2014–15 Budget Address*.

The minister’s budget statement says it all, and not for the first time. For decades, Nova Scotians have been raising the alarm about the financial reality and economic prospects of the province. The conclusions are always the same. What we’re doing now is not working for us. We need to make some dramatic changes.

Most recently, the Nova Scotia Commission on Building our New Economy (the Ivany Commission) delivered the message in clear and convincing language. The Commission titled its final report *Now or Never*. Nova Scotians can get to work building a sustainable economic future, making government work better, and putting our collective financial house in order now, or . . . For our children and the future of this province, there can be no “or.” It must be now.

Fifteen years ago, Voluntary Planning’s Fiscal Management Task Force defined the “daunting task ahead” as nothing less than “to save Nova Scotia from itself.”

“Nova Scotia’s vision should be to gain control of its own economy in order to enhance the opportunities and well-being of all our citizens,” task force chair Allan Shaw wrote in his preliminary report to the government of the day.

Success, he said, ultimately depends “not only [on] a political will to change the way government operates but also – and equally importantly – on a public

“The future depends on what you do today.”

Mahatma Gandhi

understanding and acceptance that such changes should be made if we are to regain and maintain control of our economic destiny.”

The Voluntary Planning report recommended that all reasonable options for increasing government revenues be considered. These included user fees for non-essential services, a surtax on cigarettes and alcohol, and eliminating or reducing tax credits for businesses.¹

The Shaw task force knew then what we all should know by now: “There is no single solution that can magically and painlessly restore us to good fiscal health and economic well-being. And the fixes, whatever they are, will not be quick either.”

Fifteen years ago, the case was made for regulatory and program reform, or what the task force called “a rigorous, systematic review” of every government function to determine whether it should be delivered by government, by others, or eliminated.²

The recent New Economy commission, chaired by Acadia University President Ray Ivany, told Nova Scotians in no uncertain terms why we have to change.

The review and recommendations on taxes, regulations, and fees in this report are the product of an intensive, albeit time-compressed, investigation of current and past practices in Nova Scotia and best practices in Canada and beyond.

This report will not dwell on why change is needed. That ground is well covered. Rather, this review sought to focus on how some of government’s foundational activities – the rules and regulations it sets, the taxes it imposes, and fees it charges – can be changed to sustain economic growth and stabilize the public finances. It is a tall order. But it is **now**. **Never** is **not** an option Nova Scotians can contemplate.

The Ivany report, summarized the challenge this way:

After two decades and more of slow economic growth, and with an aging population, Nova Scotians are on the verge of a significant and prolonged decline in their standard of living, in the quality of public services and amenities and in our population base, most seriously in the rural regions of the province.

Act now, the commission implored, and Nova Scotia can reverse this decline and begin its recovery.

This review draws on a broad range of advice, research and evidence. That evidence offers government a pathway forward. Now is the time. Here’s how.

The simple truth is that the Province of Nova Scotia has struggled under a heavy fiscal burden for 30 years. Had the solutions been easy, they would have been done by now. Unfortunately, there is no magic wand to wave to modernize and strengthen the provincial economy.

But steady, long-term, disciplined management, accompanied by some bold initiatives that require brave leadership, and a lot of heavy lifting can and will change the direction of this province.

Nova Scotians have heard it all before. From a past premier who, almost 25 years ago, declared the province all but bankrupt, to economic and financial reports that cried wolf because the wolf was at the door. So what's different now? The finances are in the red and, economically, most of Nova Scotia is struggling. Heard it. What's different? One thing. It is **now**. Nova Scotians can either take up the challenges of change, or let their province slide further into debt and decline.

If government is to act, a critical barrier must be overcome. Nova Scotians have to be willing to embrace the fact, or at least accept, that tough action is required today to achieve financial stability and economic opportunity tomorrow.

Over the next two decades, Nova Scotia's labour force will decline significantly, taking with it the income tax revenue the province needs to pay health, education, and every other bill. But that doesn't mean the province has 20 years' grace.

As the Ivany Commission emphasized repeatedly, Nova Scotians must work together. The province needs a collective commitment to fiscal responsibility, to a competitive tax environment, and above all, to young and future Nova Scotians. For without change soon, our legacy to coming generations will be crippling taxes and limited economic prospects.

We can turn it around. But if we don't act now, it may be too late.

Mandate

On February 27, 2014, the new government of Nova Scotia named Laurel Broten to lead a comprehensive review of taxes, regulations, and fees in the province. The Nova Scotia Tax and Regulatory Review: Charting a Path for Growth was asked for recommendations to

- create a tax structure that will better position Nova Scotia to address its demographic, fiscal, and economic challenges; and
- evaluate regulations and fees against their impact on Nova Scotia's economic and business climate, competitive position, and the extent to which they hinder business investment, private sector employment, and economic growth.

Provincial taxes and regulations were to be examined for their ability to promote

1. an environment more conducive to investment, wealth creation, and business expansion in Nova Scotia
2. innovation, productivity gains, and entrepreneurship
3. private sector employment

"The best way to
predict your future
is to create it"

Abraham Lincoln

This review is advisory. The Minister of Finance and the Executive Council will consider its findings and recommendations as part of the normal budgetary process. The work is guided by the principles that taxes, fees, and regulations should be simple, fair, and sustainable, and that they should enhance the competitive position of businesses operating in the province.

Expanding on these principles, the terms of reference state that taxes and regulations should be understandable, compliance should be easy, and effective administration should minimize intrusion, including the collection of taxpayer information.

Equitable taxation should create “a level playing field” whereby the relative tax burden is based on the ability of individuals or businesses to pay. Noting that tax levels and rates are key considerations in business decisions, including where to invest or locate, the terms define competitive as a “tax system [that] promote(s) private sector economic development and growth and position(s) the province as an attractive choice.”

A sustainable tax system allows government to meet its obligations. “Important public services including health care, education, social services and public infrastructure should be funded at a level that maintains the standard of living expected by Nova Scotians.”

The government recognized that these can be competing values and that tradeoffs are, at times, necessary.

Given these parameters, the province set goals for tax and regulatory review and change. These goals are to explore and determine how taxes, fees, and regulations can

1. contribute to greater economic growth for the province;
2. make the province more investment ready, create greater predictability for business, and encourage private sector capital spending; and
3. increase consumer and business confidence in the economy and encourage them to build lives and businesses here.

The province drew on the report of the Nova Scotia Commission on Building the New Economy as context for the review. The Commission reported:

Two independent factors – an aging and shrinking population and very low rates of economic growth – mean that our economy today is barely able to support our current standard of living and public services, and will be much less so going forward unless we can reverse the current trends.

While economic growth will be driven from the private sector, government must ensure that the right conditions are in place. The proliferation and complexity of regulations, stability and predictability in the economic environment, and confidence are identified by business as critical factors in investment decisions. Clearly, taxes, regulations, and fees are vital elements to that determination.

Consultation

Consultation with Nova Scotians and selected experts across the province was an important and highly informative part of the extensive data gathering effort that informs the findings and recommendations of this review. Consultations began in April and continued into the summer. They took the form of roundtable discussions, targeted discussions with specific experts, and input from a range of citizens and groups, including online comments through the Tax & Regulatory Review website. Roundtable discussions were held in Halifax, Yarmouth, Lunenburg, Sydney, Truro, and Kentville. Interested and engaged citizens participated, and the review sought out discussions with representatives of various industry and other associations, chambers of commerce, think tanks, business people, the academic community, and local public leaders.

The review received 15 formal written submissions. Fourteen roundtable discussions were held, attracting about 250 Nova Scotians; another 100 responded to our call for participation online. In addition, members of the legislature were provided with information so that they could consult constituents.

The number of participants was not large, but the sense of dedication to the province and commitment to a better future was palpable.

The review's aim was to identify and understand current tax policy, regulations, and fees, and, to this end, advice and insight were broadly solicited from government departments and external stakeholders.

The scope and time frame of the Tax & Regulatory Review demanded that the ground be covered quickly. A project team from the Department of Finance and Treasury Board, the Office of Priorities and Planning, and the Department of Economic and Rural Development worked to make data and analysis available. The review researched tax policy and regulations, including studies, previous reviews, and reports from Nova Scotia, the rest of Canada, and jurisdictions around the world. The advice and assistance of public servants were invaluable; however, the findings and recommendations to follow are those of the Tax and Regulatory Review Lead – specifically, Ms. Broten.

Literature and Best Practice Review

The sheer volume of academic and practical investigation and advice related to taxation and regulation is both a blessing and a curse. This review drew on a wealth of knowledge and a broad array of studies and findings from local, national, and international sources in its search for ideas and actions that could be relevant to Nova Scotia.

“The world as we have created it is a process of our thinking. It cannot be changed without changing our thinking.”

Albert Einstein

The review had a natural and appropriate bias for Canadian studies and papers, although the Mirrlees review – named for lead author and Nobel Laureate in Economics Sir James Mirrlees – is significant for the depth and breadth of its examination of taxation. While its focus is the tax system in the UK, the final report, *Tax by Design*, offers a comprehensive analysis of the characteristics of a good tax system in an open, developed economy, and suggests coherent tax reform.

The Conference Board of Canada, the International Monetary Fund (IMF), the Organisation for Economic Co-operation and Development (OECD), federal and provincial governments, including the 2008 Select Legislative Committee review of New Brunswick’s tax system, the Canadian Federation of Independent Business (CFIB), and other professional associations have contributed insight on almost all aspects of taxation in Canada. The contributions of academic leaders and institutions have also proven invaluable. The writing and work of Saint Mary’s University Professor Barry Gorman; the Mowat Centre at the University of Toronto’s School for Public Policy and Governance; the University of Calgary’s School for Public Policy, specifically the work of Jack Mintz; and the book *Tax Is Not a Four-Letter Word: A Different Take on Taxes in Canada*, edited by Alex Himelfarb and Jordan Himelfarb, were all helpful. Others who should be noted here include Kevin Milligan, Department of Economics, University of British Columbia; Robin Boadway and Jean-Francois Tremblay, of the Mowat Centre; and the work of the Advisory Panel on Canada’s System of International Taxation, chaired by Peter Godsoe, titled *Enhancing Canada’s International Tax Advantage*.

The wealth of material related to regulatory reform and simplification was similarly voluminous and insightful. In addition to a comprehensive analysis of Nova Scotia’s experience in regulatory reform, work in Ontario, British Columbia, and Saskatchewan was thoroughly reviewed and provided valuable insight. Again, organizations such as the OECD and the CFIB offered useful information and ideas, as did KPMG’s study for the Mowat Centre entitled *Future State 2030: The global megatrends shaping governments*.

Regulatory reform cuts to the very heart of government. Governments, after all, make the rules citizens are expected to live by. Some rules come in the form of laws, but regulations invariably put the broad intent of law into practice. In the US government, the Office of Information and Regulatory Affairs in the White House is considered a centre of power. As administrator of that office during the first term of the Obama Presidency, Cass R. Sunstein’s 2013 bestseller, *Simple: The Future of Government*, was a valuable guide to the right questions to ask about regulations, and how to interpret the answers. Another book, published 20 years earlier, called *Reinventing Government, How The Entrepreneurial Spirit is Transforming the Public Sector*, by David Osborne and Ted Gaebler, retains its relevance and was a source of both inspiration and validation in the content that follows.

Setting the Stage – Finances: a Nova Scotia Primer

The 2013–14 public accounts of the province show a deficit for the fiscal year of \$679 million, on total spending of \$10.7 billion, and revenues just over \$10 billion. These numbers are so large as to be meaningless to most Nova Scotians. As is the net debt of the province, which at the end of March 2014 stood at \$14.7 billion and is likely over \$15 billion at the time of this writing (some nine months later).

Perhaps more meaningful are numbers related to individual Nova Scotians. The provincial debt per capita was \$15,655 on March 31, 2014. That means if Nova Scotians were asked, for some reason, to pay off their collective public debt, every man, woman and child would owe \$15,655. A decade ago, that number was \$13,144; 20 years ago it was \$8,789; and 30 years ago, per capita debt in Nova Scotia stood at \$2,632. Had growth in the debt kept pace with inflation over the past 30 years, the province's net debt now would be \$4.9 billion rather than \$14.7 billion, or \$5,200 per capita as opposed to \$15,655.

As the numbers suggest, there was a period during the last decade when the province's financial picture brightened, but in more recent years clouds have gathered, and Nova Scotia is again spending beyond its means.

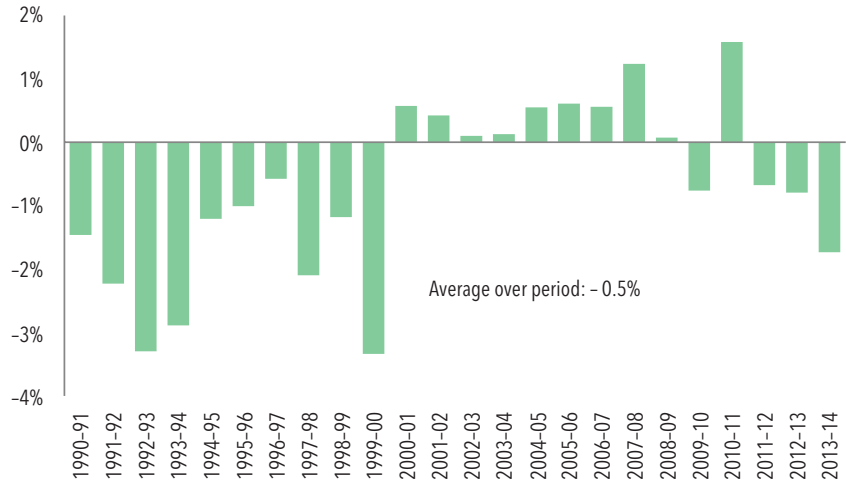
In the 2014 Speech from the Throne, the government committed to balance the budget by 2017–18. Based on the current projected spending trajectory, this would freeze debt per capita at \$17,084, and then the hard work of paying down the debt would begin. Nova Scotians must prioritize getting the debt in check; otherwise this generation is simply surrendering its responsibilities and handing a problem to our children and grandchildren that may be beyond their capacity to solve.

In fiscal 2013–14, it cost the province \$886 million to service the debt. Nova Scotia revenue lost to debt payments is among the highest in Canada.³

“(Government) should be a partner in common purpose with business, education and communities. It has to become more innovative itself in the delivery of government services, more efficient in the management of its regulatory systems and more effective in reining in the growth of its debt.”

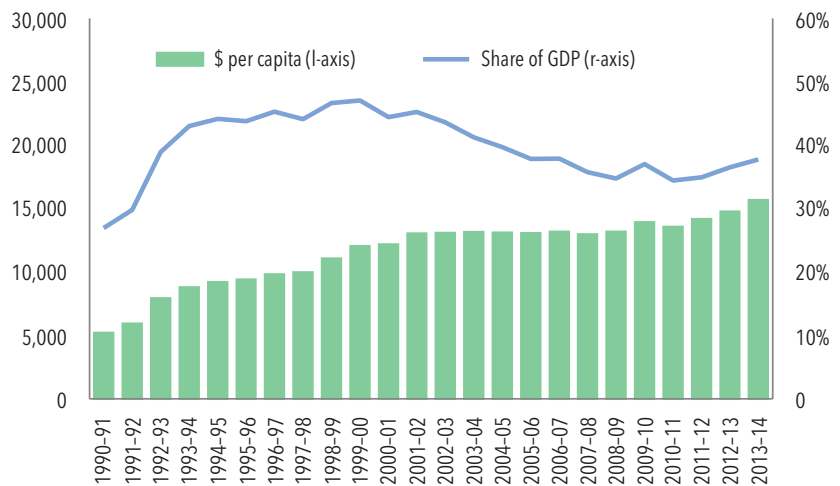
Kevin Lynch, vice-chairman,
BMO Financial Group⁴

Nova Scotia Deficits and Surpluses Share of GDP



Source: Finance Canada, *Fiscal Reference Tables, 2014*;
Statistics Canada, *CANSIM table 384-0038*

Nova Scotia Net Debt Share of GDP



Source: Finance Canada, *Fiscal Reference Tables, 2014*;
Statistics Canada, *CANSIM tables 051-0001 and 384-0038*

Where the Money Comes From

An examination of the province's revenue sources is also relevant and revealing. In the most recent complete year (2013-14), the province took in just over \$10 billion, of which \$6.6 billion, or 66 per cent, came from provincial sources. The remaining 3.4 billion, 34 per cent was from Ottawa in the form of equalization (\$1.7 billion) and other transfers mostly for health, post-secondary education and social services (\$1.67 billion).

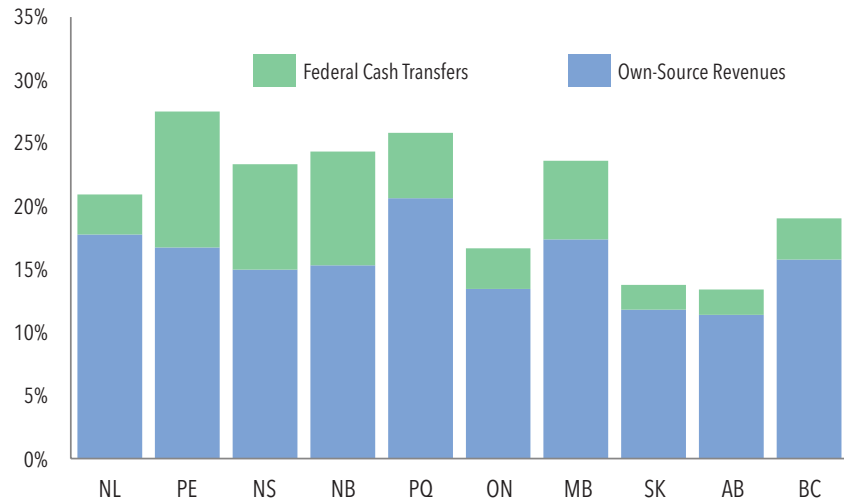
While there have been ups and downs over the past 30 years, an increased reliance on "own-source" revenues rather than on federal payments has been a fairly steady trend line and every indication from Ottawa suggests this trend will continue. In 1983-84, for example, 55 per cent of the province's revenue was from provincial sources. Ottawa contributed the other 45 per cent. By 1993-94, the split had become 62 per cent provincial, 38 federal; and a decade ago it was very close to where it is today.

Another trend line, again with peaks and valleys, but overall a fairly steady increase, has been revenue from Nova Scotians' personal income taxes. Today, personal income taxes account for roughly one-quarter of the province's revenue. A decade ago, personal income taxes accounted for about 23 per cent of revenue; 20 years ago, personal income taxes brought in 20 per cent; and in 1983-84, personal income taxes made up about 18 per cent of the government's revenues.

Corporate income tax revenues have fluctuated more widely than personal income taxes, ranging over the past two decades from slightly less than 2 per cent to more than 5 per cent of provincial revenue. In real terms, however, the trend has been a steady increase in total dollars collected. Currently, corporate income taxes bring in about \$430 million annually, while personal income taxes total more than \$2.1 billion.

Sales tax revenue has also fluctuated, as the provincial portion of the Harmonized Sales Tax (HST) was adjusted, most recently, from 8 per cent to 10 per cent on most consumer purchases. The 2013-14 public accounts show total sales tax revenue at \$2.1 billion, but that figure includes all sales-related taxes. The HST alone brought in \$1.7 billion. Since harmonization with the federal Goods and Services Tax (GST), the province has relied on the HST for between 15 and 18 per cent of its total revenue.

Provincial Revenues Share of GDP, 2013-14



Source: Finance Canada, *Fiscal Reference Tables, 2014*;
Statistics Canada, *CANSIM table 384-0038*

Federal Transfers

Funding from the national government to Nova Scotia and every other province comes primarily in three envelopes. Current federal plans present very significant fiscal challenges and risks to most provinces, Nova Scotia included. Ottawa has indicated that the rate of increase of major transfer programs will be reduced. Changes have begun or are coming to equalization, the Canada Social Transfer (CST), and, perhaps most threatening to Nova Scotia, to the Canada Health Transfer (CHT) payment.

CHT funding has transitioned to an equal per capita payment. In addition, growth in federal CHT payments – previously 6 per cent annually – will be held to 3 per cent per year or will be based on a three-year average of national GDP growth, whichever is greater, commencing in 2017-18. Over the past three years, GDP growth averaged about 3.5 per cent. The cost of health care to Nova Scotia has been increasing by 7 to 10 per cent annually for most of three decades, leaving a significant and growing gap the province alone must close.

For provinces like Nova Scotia, where population growth is flat or slow and the average age of citizens is climbing, the CHT changes are bad news. Older populations consume more health services than younger communities. Statistics Canada reports that, on average, Canadians aged one year to 64 consume the equivalent of \$4,000 in health services annually. At age 65, those costs begin to increase rapidly. By age 70, average health costs have increased to \$7,500 per person; at 75, the cost is \$10,600; and at age 80 and beyond, average health-care costs per person are \$17,000 per year.

Canada Health Transfer (CHT) Projections (\$ millions)									
Equal Per Capita Cash	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23	2023-24
Cash Plus Tax Points	902.0	947.8	979.3	1,010.3	1,041.3	1,072.4	1,102.9	1,133.3	1,164.0
Gap	924.9	971.3	1,020.3	1,071.7	1,125.7	1,182.4	1,241.8	1,304.1	1,369.6
	(22.9)	(23.5)	(41.0)	(61.4)	(84.4)	(110.0)	(138.9)	(170.8)	(205.6)

Source: Finance Canada, Statistics Canada, Conference Board of Canada, Council of the Federation Working Group on Fiscal Arrangements

Equalization, the most widely debated transfer, was entrenched in the Canadian Constitution in 1982:

Parliament and the government of Canada are committed to the principle of making equalization payments to ensure that provincial governments have sufficient revenues to provide reasonably comparable levels of public services at reasonably comparable levels of taxation.⁵

Equalization payments are unconditional. Provinces are free to use equalization funding as they see fit. That is a model found in most OECD countries; it began in Canada in 1957.

Since its inception, every province in the country has, at some point, been a recipient of equalization payments. Equalization is not an interprovincial transfer, but is funded by revenues Ottawa collects from all provinces.

Recent federal changes in equalization payments are challenging for Nova Scotia. In 2009, Ottawa modified the equalization cap. In simple terms, the old system lifted “poorer” provinces – those receiving equalization – up to a fiscal capacity on par with the least-wealthy province not receiving equalization. The new formula provides equalization at a level up to the average of all equalization-receiving provinces.

The Canadian Press, in June of this year, reported an official in the Parliamentary Budget Office as saying that equalization has become just another transfer, because “the way it is designed now, it does not equalize to any national standard.”⁶

Federal social transfer payments earmarked for post-secondary education, social assistance, and early childhood development have also been capped at 3 per cent growth annually.

The financial outcomes from these fundamental shifts in federal-provincial fiscal arrangements, the Parliamentary Budget Office says, will drive federal budget surpluses and impose difficult financial and program choices on the provinces.

In a nutshell, Nova Scotians should have no illusions that the federal government will solve our financial woes. In fact, the reality is quite the opposite.

Where the Money Goes

No review of the province's financial situation would be complete without some reference to spending. Government program spending has increased at more than twice the pace of inflation over the past 30 years. As set out above, 2013-14 provincial spending was \$10.7 billion. By contrast, in 1984, the budget of the province was \$2.8 billion. Had spending kept pace with inflation, last year's total would have been approximately \$5 billion rather than double that amount.

"There is only one taxpayer – and it's all of us."

Nova Scotian at a roundtable discussion.

This is not to suggest that government spending should track inflation. There are a multitude of other factors involved. The cost of programs, particularly health-care services, has escalated at a rate far in excess of inflation, and Nova Scotians should expect to benefit from health-care advances to the same degree as all Canadians. Health care has steadily increased its share of total program spending, from 25 per cent in the early-to-mid 1980s, to 30 per cent a decade later. By 2000, health care had become about one-third of provincial spending, and today for every dollar the province spends, more than 40 cents go to health.

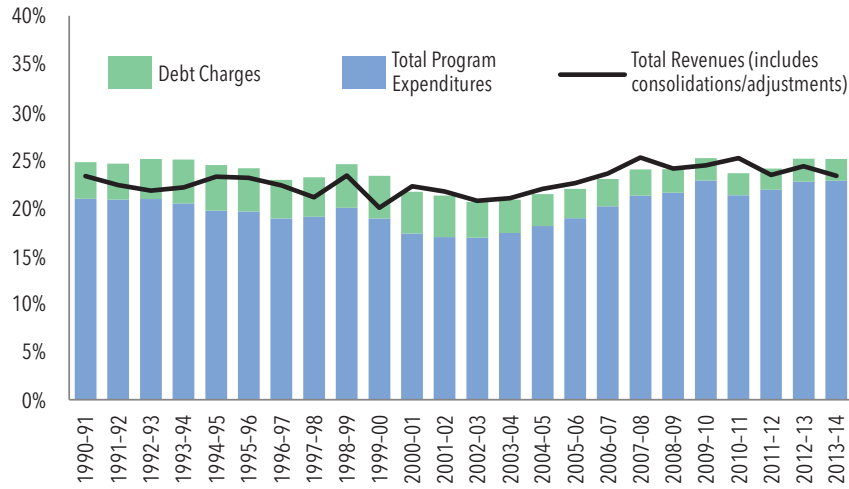
Obviously, health care is the biggest expense. Others include education (13%); community services (10%); interest on debt (8+%); labour and advanced education, which includes payments to universities and colleges (7%); and transportation and infrastructure (4%). This leaves 18 cents on the dollar for everything else: the justice system and police, natural resources, pension contributions, the environment, business and industry programs, etc.

By category, 37 per cent of total government spending pays salaries and benefits of public servants, including departmental staff, doctors, nurses, teachers, and many others. Grants to municipalities and support for individuals on income assistance, in long-term care, and with other needs take 33 per cent; goods and services required for government operations consume 15 per cent of the budget; professional fees, 3 per cent; and finally, interest on debt, at 8 per cent, rounds out spending.

Nova Scotia Provincial Spending by Category – Public Accounts Province of Nova Scotia for the Year ending March 31, 2014

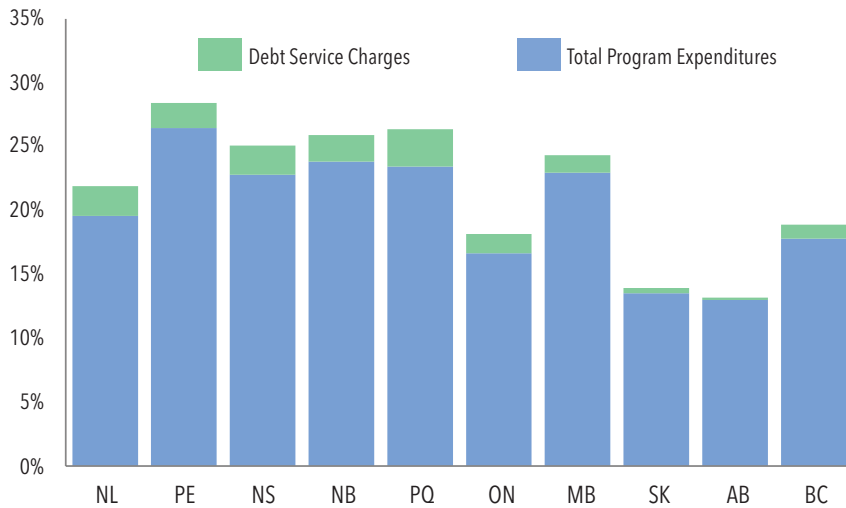
Spending Category	Amount (millions)	Percentage of Total
Grants/Subsidies	3,588.4	33%
Salaries/Benefits	3,974.5	37%
Goods & Services	1,572.6	15%
Professional	288.9	3%
Amortization	399.8	4%
Debt Servicing	886.2	8%
Other	3.6	–
Total	10,714.0	100%

Nova Scotia Program Spending vs Revenues Share of GDP



Source: Finance Canada, *Fiscal Reference Tables, 2014*;
Statistics Canada, *CANSIM table 384-0038*

Provincial Expenditures Comparison by Province Share of GDP, 2012-13



Source: Finance Canada, *Fiscal Reference Tables, 2014*;
Statistics Canada, *CANSIM table 384-0038*

"Governments need money. Modern governments need lots of money. How they get this money and whom they take it from are two of the most difficult political issues faced in any modern political economy."

Sven Steinmo,
Taxation and Democracy,
1993⁷

What has all this to do with taxes, regulations, and fees? Plenty. The most obvious connection is that Nova Scotians' taxes pay for services, programs, and debt. But as we have seen, Nova Scotians' taxes do not meet these demands. Nova Scotian governments have posted operating deficits in 20 of the last 30 years. Spending in excess of revenue is the biggest driver of the province's debt, which also includes money borrowed for capital assets. Overspending on annual operations has been compared to buying groceries on credit. We are essentially borrowing from our children, our grandchildren, and great-grandchildren to pay our expenses today. Borrowing to build for the future – investing in assets such as roads and bridges, transit infrastructure, and state of the art hospitals and schools – is entirely acceptable. Borrowing to fund programs or interest on past debt must be questioned, managed, and eventually eliminated.

Regulation and fees also enter into the equation. The former places administration costs on government and compliance costs on individuals and businesses. The latter are intended to offset costs of services and programs that are of value to the users of those programs and services. In the end, it is all connected – every expense, every tax, every fee.

Section Two: Taxes

System-wide Plan Toward Recovery and Prosperity

Why should Nova Scotians, or any citizens for that matter, care about tax policy? The answer is that no other activity of government has more direct impact on the daily lives of virtually every individual and on the operations of every business.

It is a complex topic, because our tax system has become complex. Indeed, most experts – whether academic, advisory, or in government themselves – agree. Tax systems have become too complicated. Simplifying the tax structure was a goal, or principle, of virtually every tax reform effort undertaken anywhere in recent decades, and this review is no exception.

One of the primary reasons for the complication of the tax system can be found in the way tax changes are made. Here in Nova Scotia – and Nova Scotia is not unique – changes are most frequently made to address a specific issue at a given point in time. The change could be for economic, political, compassionate, or any number of reasons. The change is made to a specific, identified tax, with insufficient regard for the whole tax “system.” Over time, new governments, new demands, new social needs, and expectations are met with new tax exemptions, increases, credits, and myriad other tweaks and revisions, each of which piles more complexity into the tax system. This review recommends a comprehensive package of system-wide reforms that recognize the interconnectedness of various tax measures and that are designed with fiscal responsibility and recovery, and economic growth and prosperity, as the driving goals.

“Tax is not a four-letter word; rather, it’s the price we pay for the country we want.”

Alex Himelfarb, *Tax is Not a Four-Letter Word: A Different Take on Taxes in Canada*.

Nova Scotia Tax Levers

Personal income tax

Every Nova Scotian with an income is required by law to file an income tax return, and for the purpose of provincial income taxes, you are a Nova Scotian if you are a resident of the province on the last day of the calendar (tax) year.

Nova Scotia has five personal income tax brackets, and an increasing tax rate is applied to that portion of taxable income that falls within each successive bracket. Personal income is taxed at 8.79 per cent, up to \$29,590. The rate in the second bracket (\$29,591 to \$59,180) – is 14.95 per cent. The rate climbs to 16.67 per cent in the third bracket, which taxes income from \$59,181 up to \$93,000. The fourth bracket, established in 2004, taxes income of \$93,001 to \$150,000 at 17.5 per cent;

"We believe that it would be best to focus on reducing corporate and personal income taxes."

Halifax Chamber of Commerce, June 2014⁸

and the fifth and final bracket, added as a temporary measure in 2010 imposes a 21 per cent tax rate on income over \$150,000.

Nova Scotia is one of three Canadian provinces that does not index tax brackets. Indexing is an adjustment made by the federal government and most provinces to protect earnings from inflation, or "bracket creep."

Indexing preserves purchasing power. Bracket creep occurs when inflation drives income into higher tax brackets, resulting in higher income taxes but no real increase in purchasing power. Tax indexing is an attempt to eliminate the potential for bracket creep by altering the tax brackets before the creep occurs.

The Basic Personal Amount is a credit against personal income taxes, for all personal income taxpayers. In Nova Scotia, this amount is \$8,481, which is at the low end compared with other Canadian provinces.

Basic Personal Amount by Jurisdiction (2014 Tax Year)										
NL	PE	NS	NB	QC	ON	MB	SK	AB	BC	FED
8,578	7,708	8,481	9,472	11,305	9,670	9,134	15,378	17,787	9,869	11,138

Source: Canada Revenue Agency, Finances Québec

Business taxes

On the business side, there are two basic tax rates: the general corporate rate is 16 per cent, and the small business rate is 3 per cent. Small businesses are taxed at 3 per cent on income up to \$350,000, and at the general corporate rate above that threshold.

A business pays taxes in Nova Scotia if it has a permanent establishment in the province. If the business is established in only one province, it pays provincial tax only in that province. However, many corporations are established in more than one province. In those cases, income is apportioned by province, and taxes are paid in each province accordingly.

Canadian policy offers businesses that operate in several provinces the option of allocating taxable income via an apportionment formula or via transfer pricing. This permits companies to engage in "income shifting" – a tax strategy that shifts more income into jurisdictions with lower corporate tax rates, and losses into jurisdictions with higher corporate rates.⁹ With the highest corporate tax in Canada, Nova Scotia's economy and revenues suffer as firms adjust their affairs to transfer taxable income to lower-taxed jurisdictions.

HST

Nova Scotia is one of five provinces – the four Atlantic provinces and Ontario – that have harmonized their sales taxes with the federal government’s GST. At 15 per cent, Nova Scotia has the highest sales tax in Canada. The federal GST is 5 per cent, and the provincial sales tax portion is 10 per cent.

The HST is a tax on the consumption of most goods and services in the province. Through agreement with the federal government, the province imposes the tax on the same goods and services as the federal GST. The province has autonomy to set the provincial portion of the tax rate, and to rebate the provincial portion of the tax.

Nova Scotia rebates the provincial portion of the HST on printed books; children’s clothing, shoes, and diapers; feminine hygiene products; and residential energy, notably heat. These are “point-of-sale” rebates, so as far as consumers are concerned, there are no provincial sales taxes on these items.

The GST is exempted from a long list of goods and services, so the provincial portion of the HST is also exempted from these items, including used residential property, residential rents, publicly-insured medical services, medical devices, publicly provided homemaker services, most educational programs, professional accreditation, tutoring, school cafeteria meals, supervision of children and disabled people, legal aid, most supplies made by charities and not-for-profit organizations, and many government-provided goods and services.

A number of other goods and services are zero-rated – the tax is zero. Zero-rated goods and services include basic groceries, commercial agricultural and fishing supplies, prescription drugs, exports, and some financial and transportation services. Removing the zero-rating on such items as groceries, as called for by many tax experts – including Jack Mintz – is entirely within the purview of the federal government.

Motive fuel tax

Nova Scotia levies a motive fuel tax on gasoline, diesel oil, and propane. The tax is charged at the wholesale level but passed through to retailers, who in turn pass it on to consumers. The rates are 15.5 cents per litre for gasoline, 15.4 cents per litre for diesel, and 7 cents per litre for propane. Aviation and marine fuel are also subject to the tax, at a rate of 2.5 and 1.1 cents per litre, respectively.

A stated purpose of the motive fuel tax is to offset the cost of highway construction and maintenance, although the revenues from the tax are generally insufficient for the purpose. The tax is also levied on fuels that power aircraft and boats, which do not use the roads.

Provincial and municipal vehicles, resource-based industrial uses, rail and commercial sea transport, and manufacturing are generally exempt from the

motive fuel tax. Tax-exempt fuel – known generally as “marked” gas – is dyed to differentiate it from taxed fuel.

In Nova Scotia, the motive fuel tax is not intended or sufficient to correct for external harm – in this case, the pollution caused by combustion of the fuel.

Many experts predict that vehicle fuel taxes will, over time, lose the ability to capture the revenue to maintain highways and roads. Fuel consumption per kilometre driven is falling and will continue to do so, possibly at an increasing rate and eventually falling close to zero, as new technologies replace gasoline and diesel. A replacement source of revenue is required.

Tobacco tax

Tobacco products are taxed by the province to deter consumption and provide additional revenues to offset, in part, the increased health costs associated with treating smokers. Nova Scotia has sought to maximize taxation in this area. Over the past decade, the provincial tax on one cigarette has increased from 8 cents to 23.5 cents.

Where to Start

“Taxes are the price
we pay for civilization.”

Oliver Wendell Holmes Jr.

Taxes can be viewed, and therefore reviewed, from many angles: the cost of compliance, the economic impact, or from a policy orientation. A policy analysis of taxation, for example, would look to answer questions like Why do we pay taxes? What types of taxes can be levied? What base and/or rate structure should be considered?¹⁰

This review draws on a broad array of advice and insight on all aspects of tax reform and seeks to match the best of that to the realities of Nova Scotia. The result is a proposed course of tax changes to meet Nova Scotia’s present and future needs in a practical and achievable way, and as set out in the mandate from government.

At its simplest, a tax is a compulsory payment made by a citizen to a government. There are, generally, two reasons why taxes are necessary. The first is to finance the expenditures of the government. The second is to accomplish a range of economic, social, and/or political objectives.¹¹

Canada’s first income tax went into effect “temporarily” in 1917 as the Income War Tax Act. It was a law captured on 11 pages including the regulations; it provided the legislative authority and general principles necessary to raise personal and corporate income taxes to help finance the First World War. It was, as is now clear, not temporary, and its present day successor, the *Canadian Income Tax Act*, runs more than 3,000 pages.¹²

It is not likely that Nova Scotia's tax system can be simplified to 11 pages, but it certainly could use a bit of housecleaning.

Arguably, tax policy is government's most pervasive influence and involvement in the economic and social lives of individual and corporate Canadians. Virtually every Canadian is affected by taxation and by changes to tax laws. Taxes, because of their effect on disposable income and the cost of living, are ultimately a significant factor in determining the standard of living.¹³

Taxation affects the daily decisions of business people and individuals, whether they are consumers, producers, savers, or investors. Barry Gorman writes in his book *Canadian Income Taxation*: "In addition to the obvious reduction of disposable income, taxation, and in particular changes to tax law, can affect taxpayers and the economy in a multitude of ways:

(a) Industry and Employment Location

Incentives offered to industry to locate in designated regions of the country, or to employees moving to a new work location, can affect the availability of employment in those regions and the mobility of workers willing to move to the designated regions.

(b) Labour Supply

Taxes affect the quantity of labour supplied. As an individual has a choice between leisure and work, and for a given amount of time is assumed to desire the maximization of his or her utility, tax rules may increase, decrease, or have no effect on the amount of labour offered. The type of occupation and the number of hours employed may also be affected by tax policy. More particularly, promotion or relocation decisions, the decision of individuals to enter or exit the workforce, or the choice between part-time versus full-time employment may be based, in part, on the tax consequences of such decisions.

(c) Utilization of Labour Versus Capital Equipment

Tax measures that reduce the effective cost of the factors of production affect the decision of the producers to employ labour or equipment in the production process. For example, a tax incentive that reduces the cost of capital equipment often results in a reduction of the labour force.

(d) Investment Decisions

Since it is the after-tax cost of an investment that is important, tax incentives that reduce the effective cost of an investment are critical to investment decision making. Where tax rules create discrepancies between investment alternatives, the final decision is often determined by the tax impact. For example, businesses may be induced to invest in new rather than used plant and equipment because tax preferences such as the investment tax credit are generally available only for new acquisitions.

(e) Type of Business Organization

The allocation of capital between the corporate and non-corporate sectors will be affected by discriminatory legislation favouring one form of business organization over another. Where tax law creates distortions between the tax cost of alternative forms, business persons will naturally choose the most favourable. The choice between operating as a proprietorship or limited company may rest on the availability of the small business deduction or potentially lower tax rates applicable to corporate income. Alternatively, smaller owner-managed businesses may remain as proprietorships where there is a likelihood of losses in the early years of the business, because annual losses are deductible against the owner's other income. These distortions lead to potential economic inefficiencies when one form of organization is chosen for the tax reasons when another would be more appropriate on economic grounds.

"Apart from questions relating to basic civil liberties, few matters affect all members of the public to the same extent as the budget policies."

Canadian Tax Journal
(April-May 1978)¹⁴

(f) Consumer Prices

The cost of goods and services is increased because of the imposition of both direct and indirect taxes on the supplier or the consumer of the good or service.

(g) Risk Taking

Taxes affect the risk and expected return of investment decisions. . . . There is a disincentive to risk if the tax system provides less reduction of taxes for losses than it requires in payments for profits – that is, (a) where losses are not fully deductible because not enough taxable income is generated or because losses are only deductible against certain gains, or (b) because marginal tax rates tax gains more than they give relief for losses.

(h) Capital Supply

Because taxes decrease the marginal utility of capital and reduce existing differentials between interest rates and the marginal efficiency of the capital, capital flows are affected by the distortions in tax rates or incentives across taxing jurisdictions. . . . Discrepancies between provincial tax rates can affect the flow of capital within the country. Finally, distortions in the tax treatment of different sectors of the economy (for example, small business and manufacturing) will tend to direct capital to the more favoured sectors and away from the more heavily taxed sectors.

(i) Savings

. . . taxation affects both the capacity and willingness to save. As taxes reduce the income flowing to the investor, the type and level of savings will be influenced by both the tax imposed on investment income and by the incentives available to certain types of savings.

(j) Economic Growth

Economic growth is fostered by the accumulation of the factors of production, the rate of technological progress, and the rate of investment in risky projects. The tax system affects growth by its effect on the accumulation of capital required to finance acquisitions and/or expansion of the productive base.

(k) Income Redistribution

Tax policies will facilitate the transfer of purchasing power among individuals and levels of government, including the *intergenerational transfer* of such power.

(l) Consumption Decisions

To the extent that taxpayers are aware that a particular expenditure is eligible for a tax preference, the nature and quantum of expenditure decisions may be influenced by the associated deduction or tax credit. Tax shelters, for example, are aggressively marketed and acquired more often for their tax preferences than as a sound commercial investment. The popularity of Registered Retirement Savings Plans (RRSPs) is no doubt partly due to the deduction granted to the annual contribution. However, it is somewhat less obvious that expenditures on, for example, donations and tuition, are incurred because of the tax credits available.

(m) Form of Financing

Taxation affects a firm's cost of capital and its method of corporate financing. Interest, the cost of debt financing, is deductible, whereas dividends, the cost of equity financing, are not. This discrepancy may distort the pattern of capital formation and influence the real rate of return of different forms of financing, as it raises the cost of issuing shares relative to long-term debt and may create liquidity problems for the firms in periods of recession or lower profits.

(n) Dividend Policy

The rate of tax, and any differentiation between distributed and undistributed profits, can affect the decisions to retain profits or distribute them to shareholders.¹⁵

As is obvious from the comprehensive nature of Professor Gorman's list, tax policy affects each and every Nova Scotian every single day, and in ways we cannot always quantify or articulate. Every government's existing tax policy is essentially the accumulation of tax decisions made in previous budgets, generally by previous governments. As a result, embedded within current tax policies are often conflicting elements as well as tax measures that are not evidence-based but may have been, or been portrayed as, a response to an issue of concern to society, the government, and taxpayers of that day.¹⁶

Our goal should be "a tax system that looks like someone designed it on purpose," said former US Treasury Secretary William Simon. Unfortunately, more often than not, the tax system can be "the product of often incoherent piecemeal changes rather than strategic design."¹⁷

The reality is that governments rarely examine taxation in a comprehensive way, and as a result, the majority of tax measures included in any budget are essentially tinkering around the edges to offer some identified group tax relief by way of new tax credits or by shifting rates or brackets.

If we truly aspire to have a tax system – a set of interacting or interdependent components acting as an integrated whole – we need to step back and assess it as a whole.

The intention of this review is to take a "big picture" view, asking what Nova Scotia needs from a tax system now and in the future, and how best it might accomplish that end.

Principles for a Modern Tax System

As has been illustrated above, the financial situation of the province is precarious. Nova Scotia has fewer than one million residents, a net debt at or approaching \$15 billion, annual deficits in the hundreds of millions, yearly payments on debt that take close to a dime from every tax dollar, and public service costs that continue to rise. For two decades, Nova Scotia's economic performance has lagged behind the rest of the country, the workforce is aging, and there aren't enough young people waiting in the wings to fill the jobs that will soon be vacated. High unemployment, particularly among the young, is sending too many of those soon-to-be essential workers west. What that means in terms of future government revenue is reduced income tax revenue at the same time that demands on services, particularly for health care, intensify.

There is no panacea. Certainly tax reform alone can't solve all the province's fiscal and economic problems. Government remedial action, however, is urgent, and changes to the tax system and regulatory regime must be a part of the resuscitation plan.

All that prompts the question, what does the province need from tax reform?

"We need to get out of our comfort zone."

Nova Scotian at roundtable discussion

"We need a more competitive tax structure – not the most, but more."

Nova Scotian at roundtable discussion

At its most basic, Nova Scotia, like every government, requires a tax system that generates adequate resources to fund the public services Nova Scotians need and expect, and to put the province on a strong fiscal footing.

The tax and regulatory system must not impede economic growth. The ability of the tax system to drive economic growth is uncertain, but taxes can certainly stunt or even kill growth.

The tax system can help make Nova Scotia a more attractive place to live, raise a family, and start or grow a business. High personal taxes can erode the quality of life of individuals and families. At the same time, quality health, public education, and other services paid for by taxes enhance life. It is a fine balance.

Tax reform should squarely address the aging demographic tsunami bearing down on Nova Scotia. Tax reform must look to the future and recognize the obligation each generation has to the next, including fiscal stability, social responsibility, and sustainability.

Qualities of a good, modern tax system:

Competitive People and business will seek out and find better economic opportunities. The tax burden imposed on them is part of the calculation.

Neutral According to the Conference Board of Canada, "an efficient tax system should have a broad, stable, neutral base. Neutrality permits the choice of investment or action to be made on the basis of market or personal considerations without influence or bias from the tax laws. Purposeful departures from neutrality will be made to discourage specific activities, like smoking, alcohol consumption, or pollution. In these cases, the tax should be set to capture the cost of harm caused by the activity."¹⁸

Simple Canadian Certified General Accountants report that the costs of compliance with personal and corporate income tax in Canada is equivalent to 2 per cent of the nation's gross domestic product.¹⁹

Balanced The tax system needs to balance divergent and sometimes conflicting objectives. The province needs revenues sufficient to provide high-quality services, while at the same time it must maintain tax rates that are competitive with other jurisdictions in Canada and abroad.

Sustainable According to the United Nations, "sustainable development . . . meets the needs of the present without compromising the ability of future generations to meet their own needs." Sustainable taxation must pass the same test.

Fair A dictionary definition of "fair" – treating equally without favouritism or discrimination – is an easy concept to grasp that becomes complicated in reference to taxation. Generally, "fair" in a modern, democratic, progressive tax structure means that those in the same economic circumstances are treated the same way.

However, in the aim of substantive rather than procedural fairness, what is fair is at times a challenging concept to universalize.

Fiscally responsible A government should not tax people more than the government requires, nor should it tax less than is required to provide services of a kind and quality the people have agreed they need.

Supportive of those in need A modern, civil, progressive society accepts its responsibility to those in need. The tax system is “progressive,” and its role extends to ensuring that advantaged citizens pay sufficient taxes to allow the state to support others.

Understandable “A tax system that people can understand is preferable to one that taxes by ‘stealth.’”²⁰ Transparency and clarity in both taxation and regulation are essential in order to promote compliance and even support.

How do we identify a good tax system when we see one? One way is to see how it stacks up against a checklist of desirable properties. The most famous is the four canons of taxation set out by Adam Smith in *The Wealth of Nations*:

- (i) The subjects of every state ought to contribute towards the support of the government, as nearly as possible, in proportion to their respective abilities . . .
- (ii) The tax which the individual is bound to pay ought to be certain and not arbitrary . . .
- (iii) Every tax ought to be levied at the time, or in the manner, in which it is most likely to be convenient for the contributor to pay it.
- (iv) Every tax ought to be so contrived as to take out of the pockets as little as possible, over and above that which it brings into the public treasury of the state.

These may be longstanding axioms of taxation, but they are not a roadmap out of trouble when it comes to the really difficult questions that arise when one objective is traded off against another.

What is Nova Scotia to do?

At virtually every income level, and for almost every family configuration, Nova Scotians pay the highest or second highest personal income taxes in Canada. The same is true of corporate income tax, where Nova Scotia compares unfavourably with every other jurisdiction save Prince Edward Island, which shares Nova Scotia’s 16 per cent corporate income tax rate. Across the country, the corporate rate is generally between 10 and 12 per cent.

In a few cases, Nova Scotia does offer more-generous specific personal income exemptions than other provinces, particularly other Atlantic provinces. However,

"The art of taxation consists of plucking the goose so as to obtain the most feathers with the least hissing."

Jean-Baptiste Colbert

"The surtax (high tax bracket) is a restraint on our ability to attract entrepreneurs and those in the knowledge sector."

Nova Scotian at roundtable discussion

the province is again at the low end of the spectrum in terms of broader income tax relief. For example, Nova Scotia's Basic Personal Amount of \$8,481 is the second lowest in Canada.

The point here is that after income taxes, Nova Scotians have less to spend than Canadians earning the same income in almost every other province. This becomes more discouraging given that Nova Scotia's economy generates the second-lowest incomes per capita in the country.

When it comes to spending, as if to add insult to injury, Nova Scotia has the highest consumption tax – the 15 per cent HST.

Nova Scotia's high taxation levels are being noticed – and not favourably. A recent CFIB comparative analysis of provincial tax systems across the country ranked Nova Scotia second-to-last. The analysis consisted of 53 indicators in five major tax areas and highlighted a number of concerns with respect to the competitiveness of Nova Scotian taxes.²¹

To be more economically competitive and in turn more sustainable in the long term, Nova Scotia must prioritize the creation of a tax system that minimizes interference with economic prosperity and encourages investment and private sector employment growth.

This review heard time and time again that both the perception and the reality of Nova Scotia as a high-tax jurisdiction must be altered in order to secure a prosperous future for Nova Scotians.

But what does that mean in terms of tax reform, and how can that be done in light of the province's challenging financial circumstances and demographic realities?

One of Nova Scotia's real and unique economic advantages may well be the number of post-secondary institutions for a province of this size. The high number of well-educated Nova Scotians is one desirable result. Another is the potential, and success, of these universities and colleges to attract students from outside the province, some of whom stay to live, work, and raise their families.

However, high taxation discourages investment and growth in the province, which in turn drives graduates elsewhere to seek wider career prospects. Once gone, they are difficult to attract back, and Nova Scotia loses much of the benefit of one of its greatest assets.

According to the OECD, high tax wedges that discourage work are a growing concern in light of labour shortages and an aging workforce in many regions. Personal savings tend to be discouraged by income taxes but are critical for sustainable growth and sound public finances. The net benefits of education are also reduced by high marginal taxation on future earned income. Tax reforms with the goal of increased efficiency – to boost savings, work, and human-capital investments – often reduce tax progressivity. However, consumption-based taxes

with better targeting of tax relief to those most in need (progressivity concentrated at the lower end of the income spectrum) could help resolve this dilemma.²²

A Comprehensive and Interconnected Pathway Forward

In designing the Nova Scotia tax system of the future, it is imperative that we collectively reimagine the tax construct governing Nova Scotia and do so in a way that is guided by the best available academic and economic advice. At the same time, we must remain cognizant of the challenges faced when seeking to drive long-term transformative change. Despite the tough journey ahead, this review seeks to provide a roadmap to do just that, with a couple of caveats: Nova Scotians accept that the comprehensive nature of the proposed reforms is necessary under this recommended plan of reform; and the government is able to hold the line on spending.

Many of the measures recommended are mutually dependent. Taken as a whole, they seek to share the burden and the benefits in a fair and balanced way. Nova Scotia simply cannot afford to take certain measures that drive taxation to a more competitive level without undertaking other measures to generate revenue from alternative sources. In setting out a comprehensive plan for reform, the review seeks to balance all the competing interests. It would be imprudent to cherry-pick more popular reforms and ignore the less palatable ones. The numbers simply won't add up. Every Nova Scotian will no doubt like some suggestions and dislike others but will hopefully, when all measures are taken as a whole, see the pathway forward and understand why it makes sense even if they don't like it. As is often the case, medicine that works can be hard to take.

The second caveat is the simple fact that it is irresponsible to reduce taxes in a meaningful way while still running deficits and accumulating debt. Accordingly, the proposals in this review are premised on essentially freezing or flatlining spending at the current level. Without flatlining overall program spending, the government has no realistic chance to make meaningful tax reductions. As set out above, this review heard over and over that spending must be brought down in order to prioritize tax reform.

To curb spending in a long-term sustainable way, spending constraint requires the transformation of government service delivery models rather than simple compression or thoughtless across-the-board cuts. Without basic, underlying reform of government systems, restraint measures, no matter how significant, tend to be temporary, as spending pressures build to drive expenditures quickly back up to previous levels and beyond.

Expenditure restraint can be guided by similar efforts undertaken over the past 20 years, to varying degrees of success, by other jurisdictions and levels of government. The national efforts of the early 1990s imposed cuts to departmental

operating budgets, grants, and contributions, with some as high as 15–25 per cent, in order to bring federal spending back to a sustainable level.

Provinces have undertaken similar efforts. Perhaps the best example for Nova Scotia is the long and difficult path taken by Premier Roy Romanow's government in Saskatchewan from 1991 to 1998. Premier Romanow's plan produced seven consecutive years of reduced or flat program spending through departmental cuts and government-wide expenditure management, including civil service wage freezes and overall down-sized government. Welfare reform also focused on increased independence and skills training. Saskatchewan balanced its budget in 1994–95, and the province is now one of Canada's economic leaders. There is no doubt that Saskatchewan has and continues to benefit from a resource boom, but getting its fiscal house in order set the stage for Saskatchewan's prosperity. This will be a critical foundational element for a strong Nova Scotia economic future as well.

Recommendations

Hold the line on spending

The Government of Nova Scotia must develop a plan to bring provincial expenses into balance. The review heard clearly that there is simply no more capacity to increase revenue from personal or corporate income tax. A more competitive tax regime is essential to the economic future of the province, but is not possible if spending continues to grow. Expenditure restraint – flatlining total program spending at today's levels over the next five years – should be a priority.

This is easier to write than to do. A detailed and thorough examination of all spending is required, along with nothing less than re-imagining and redesigning the way government serves citizens, and a change in citizens' expectations of government.

Across-the-board cuts don't last. Service delivery must be transformed and bold decisions are required to ensure that vital public services are sustainable, while action is taken to allow a strong, vibrant, and prosperous economy to grow.

Zero-based budgeting and lean management tools in the ongoing program review process will be critical to the province's success and are an essential foundation for tax reform. Departmental budgets for the 2015–16 fiscal year should be justified against a zero-based standard. Departments and programs where spending has increased significantly year-over-year should go to the top of the list for evaluation and transformation. Alternative service delivery, including regionally based models, and alternative financing models, including asset monetization, should be seriously considered. These are proven transformative strategies in other jurisdictions, where they have resulted in more modern and cost-effective service delivery to citizens.

Flatlining departmental expenses at the projected 2014–15 level, with adjustments of \$34 million to accommodate already-committed collective agreement obligations, for a total of \$8,885.6 million, with all other revenues and expenses as projected, would result in a relatively small deficit (\$23 million) in 2015–16 and surpluses of \$202.2 million in 2016–17, \$535 million in 2017–18, \$829 million in 2018–19, and \$1.1 billion in 2019–20.

Tax reform and relief must be the priority for 2016–17, but by 2017–18 significant funds should be earmarked to fund the costs associated with vigorous and durable transformation in government service delivery models, including the delivery of improved and modernized supports for low-income Nova Scotians, as discussed later in the review.

Fiscal Projections Nova Scotia Department of Finance and Treasury Board 2014–15 to 2019–20 (\$ millions)

	2014–15 Estimate	2015–16 Estimate	2016–17 Estimate	2017–18 Estimate	2018–19 Estimate	2019–20 Estimate
General Revenue Fund						
Revenue						
Ordinary Revenue	8,703.7	9,033.7	9,297.7	9,641.0	9,930.2	10,228.1
Ordinary Recoveries	522.0	516.5	518.3	519.0	519.0	519.0
Net Income Government Business Enterprises	340.4	339.0	337.2	332.9	332.9	332.9
	<u>9,566.1</u>	<u>9,889.2</u>	<u>10,153.2</u>	<u>10,492.9</u>	<u>10,782.1</u>	<u>11,080.0</u>
Expenses						
Departmental Expenses	8,851.6	8,885.6	8,885.6	8,885.6	8,885.6	8,885.6
Refundable Tax Credits	115.6	117.8	121.3	123.9	126.7	129.7
Pension Valuation Adjustment	90.5	92.2	106.4	117.6	128.5	140.5
Debt Servicing Costs	878.0	890.6	911.8	904.7	886.0	857.0
	<u>9,935.7</u>	<u>9,986.2</u>	<u>10,025.3</u>	<u>10,032.0</u>	<u>10,027.0</u>	<u>10,012.7</u>
Consolidation and Accounting Adjustments for Governmental Units	<u>90.6</u>	<u>74.1</u>	<u>74.1</u>	<u>74.1</u>	<u>74.1</u>	<u>74.1</u>
Provincial Surplus (Deficit)	<u>(279.0)</u>	<u>(22.9)</u>	<u>202.0</u>	<u>535.0</u>	<u>829.3</u>	<u>1,141.4</u>

Recommendation 1.1

Nova Scotia should freeze program spending at current levels, with adjustments for already-committed collective agreement obligations, bringing the provincial budget close to balance in 2015–16. Provincial surpluses in subsequent years should be allocated primarily to personal and corporate tax reductions and one-time costs of transformational change in government.

Priorities for personal tax reform

Reduce and simplify income taxes: Shift taxation toward consumption

Every individual Nova Scotian who pays personal income tax benefits from the Basic Personal Amount, may benefit from a variety of personal tax credits, and pays HST on most goods and services. While it has been stated before, it bears repeating – the way that these and other tax measures fit together matters, as does the balance, or lack thereof, created by the mix of taxation. The bottom line is that while tax relief is integral to economic growth and future prosperity in Nova Scotia, getting the balance right must remain at the forefront as priorities are established for tax changes.

The broadly held and prevalent view among leading economists is that shifting the burden away from income-based taxation to consumption-based taxation can have significant benefits in economic growth and job creation.²³ This shift in tax emphasis will also provide improved incentives for work and investment, which would in turn provide a boost to productivity growth.²⁴

Perhaps as important for Nova Scotia, in light of slow or no population growth and an aging population, is the “strong demographic driver for such reform,” as noted by the Conference Board of Canada:

“As more Canadians retire from the workforce or work fewer hours as they age, labour force growth will slow, as will the growth in income available for taxation. Shifting the balance of personal income taxation from earned income to consumption will become increasingly important if governments are to sustain the growth in revenues (they require) to fund government programs.”²⁵

The Conference Board and others note that income tax reductions – personal and corporate – provide significantly more encouragement to growth than do lower consumption taxes. “The research indicates that cuts to personal and corporate income taxes provide a stimulus to productivity and economic growth that is many times higher than that produced by cuts to consumption taxes.”²⁶

Recommendation 1.2

Nova Scotia should restructure its tax system to shift revenue emphasis away from high personal and corporate income taxes, toward more revenue from consumption taxes, such as the HST, while protecting poor and low-income Nova Scotians.

The arguments for, and rationale supporting, this shift respond to many of the present and future problems facing Nova Scotia's finances and economy. The erosion of the province's income tax base as the Nova Scotian workforce ages and retires can be redressed by shifting more of the tax burden off income and onto consumption.

The harsh reality is that Nova Scotia's largest single source of revenue, personal income tax, is on a long-term path to decline, unless rates are drastically increased, because of projected labour force reductions. Solving Nova Scotia's revenue woes by increasing personal income taxes on the workers that remain would be at best counterproductive to Nova Scotia's other aims and at worst disastrous to the province's future. Younger Nova Scotians are already prone to look outside the province for economic opportunities. Place an additional economic burden on them through higher income taxes in order to pay for services needed by retiring baby boomers, and their exodus is likely to escalate. Conversely, with lower income and broader consumption taxes, retired Nova Scotians will continue to share more equitably in the province's revenue requirements.

The primary argument against such a shift is that consumption taxes are regressive, and that is true. Everyone, regardless of ability to pay, buys goods and services, and in Nova Scotia, almost every transaction attracts the same 15 per cent tax.

However, the regressive aspects of a broader HST can be fully overcome by building a stronger transfer (refund) mechanism into the consumption tax system.²⁷ As well, those with more disposable income spend more, and are therefore taxed more, so there is an element of progressivity in consumption taxes. Further evidence to support the change comes from the fact that "for many people, the amount they spend in a particular year is probably a better indicator of their lifetime living standard than the level of their income in that year."²⁸

As well, consumption tax allows those with a fluctuating income to even-out expenditures and therefore taxes. Reduced personal income tax promotes increased savings from increased take-home pay, and shifting the personal tax burden to consumption from income enhances taxpayer choice.

If the logic of shifting more of the tax burden from income to consumption wins the day, the next question is, How do you make such a shift? Increase the rate or broaden the base? Given that Nova Scotia already has the highest HST in Canada, the only realistic reform is to broaden the base by eliminating provincial rebates.

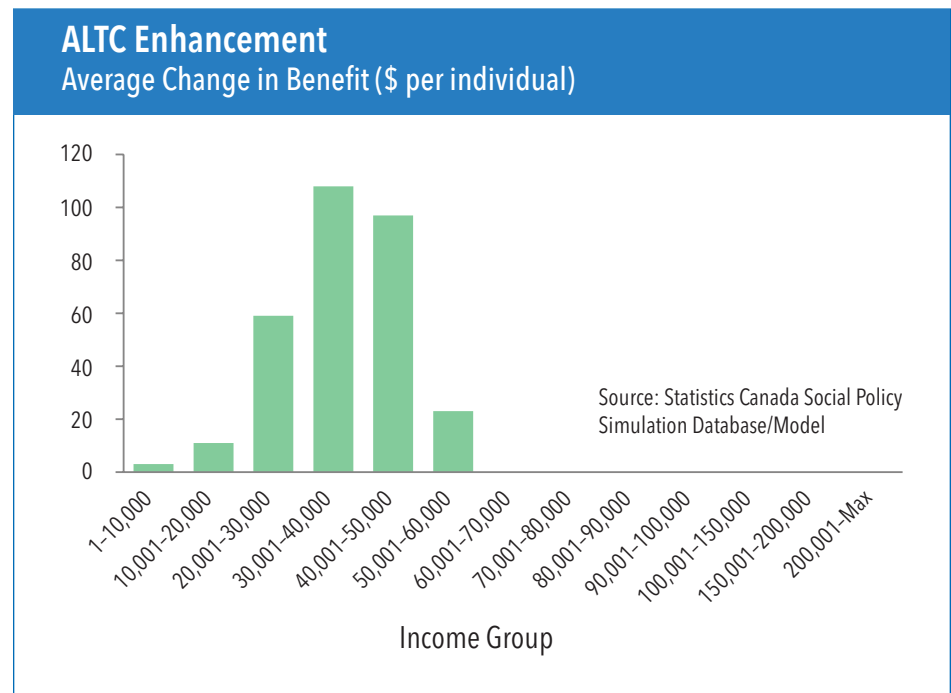
"The energy rebate makes zero sense."

Nova Scotian at roundtable discussion

As noted previously, Nova Scotia rebates the provincial portion of the HST on printed books; children's clothing, shoes, and diapers; feminine hygiene products; and home energy use through the Your Energy Rebate program, as well as a portion of the HST on first-time home purchases. Fully eliminating these exemptions would generate approximately \$128 million dollars in new revenue for the province annually.

A broader application of the HST will help to ensure that the province does not suffer the revenue decline a smaller workforce will deliver, and which Nova Scotia clearly cannot afford. And an income tax reduction along with robust targeted support at the lower income levels will, among other things, increase Nova Scotians' purchasing power and likely increase their consumption of goods and services, which is frequently discretionary.

Clearly, broadening the HST by removing these exemptions will not be popular, but the fact remains that broadening the HST will have a significant and immediate impact on provincial revenues and thereby provide the province with room to reduce personal income taxes. That reduction would begin, as set out below, with an increase in the Basic Personal Amount as well as an increase in the Affordable Living Tax Credit. An enhanced Affordable Living Tax Credit for both adults and children, as set out below, will provide Nova Scotian families with \$29.1 million in tax relief.



Recommendation 1.3

Nova Scotia should eliminate rebates for the provincial portion of the HST on printed books; children’s clothing, shoes, and diapers; feminine hygiene products; residential energy; and first-time home purchases. Nova Scotia must offset the impact of the broadened HST on low-income Nova Scotians by enhancing the Affordable Living Tax Credit and making improvements to the Heating Assistance Rebate Program (HARP).

A broadened HST base is evidence-based tax reform that advances the principles articulated earlier. It also runs headlong into the harsh political reality that the HST is a much – and frequently – hated tax, given that most consumers pay it almost every day. Conversely, income taxes, while not popular, are for most Nova Scotians deducted at source (from the paycheque) and therefore much less conspicuous. Reducing the provincial income tax, while maintaining the 15 per cent consumption tax and broadening its base to include more goods may be a hard political sell. But it is the right thing for Nova Scotia to do.

Increase Basic Personal Amount

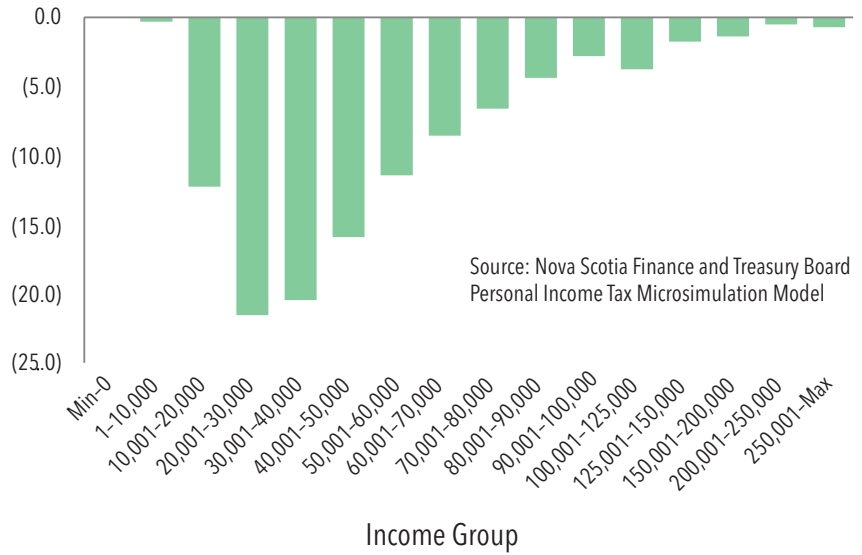
The simplest, most fair, progressive, and broad-based mechanism to reduce personal income taxes for Nova Scotians is to increase the Basic Personal Amount. This measure offers the advantages of reducing income taxes for all taxpayers, while ensuring that those with the lowest income benefit most in proportion to their income. Nova Scotia should raise the Basic Personal Amount – currently at \$8,481 – to \$11,000, moving the province from among the lowest to near the top among provinces. This measure will provide tax relief to every working Nova Scotian and is a good and important place to start along a tax reform journey.

Support for such a measure can be found in *Tax by Design*, by James Mirrlees, who suggests that the “simplest way to achieve progressivity in an income tax is to have a tax-free allowance (Basic Personal Amount) before taxes start to be payable . . . income tax can be made more progressive by increasing the tax-free allowance.”²⁹

Similarly, the Nova Scotia basic dependent amount should be increased, consistent with the increase in the Basic Personal Amount, although this measure will need to be phased in as the province’s finances allow, but should begin with a cost of living increase to the dependant amount. The recommendation will provide \$112 million in annual tax relief to Nova Scotians.

BPA Increase to \$11,000

Tax Change Among Income Groups (\$ millions)



Recommendation 1.4

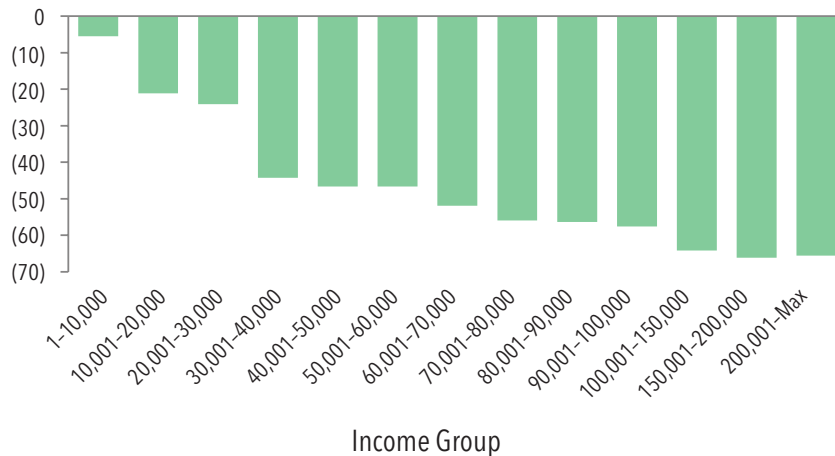
The province should reduce personal income taxes by increasing the Basic Personal Amount to \$11,000 and increase the Dependent Amount by the cost of living.

End bracket creep

Nova Scotia must stop the taxation slide caused by bracket creep – the lack of indexation of the tax brackets. Nova Scotia is one of only three provinces that does not index its tax brackets to annual inflation. This amounts to what Mirrlees refers to as tax by stealth. This needs to change to further both fairness and transparency in the system.

New brackets created as a result of this report must have a built-in cost-of-living adjustment clause, and if new brackets are not created, existing brackets should be indexed. This measure will provide \$20 million in tax relief to Nova Scotians in 2015-16.

Indexation of Income Tax Brackets at 1.2 per cent Average Change in Tax



Source: Nova Scotia Finance and Treasury Board
Personal Income Tax Microsimulation Model

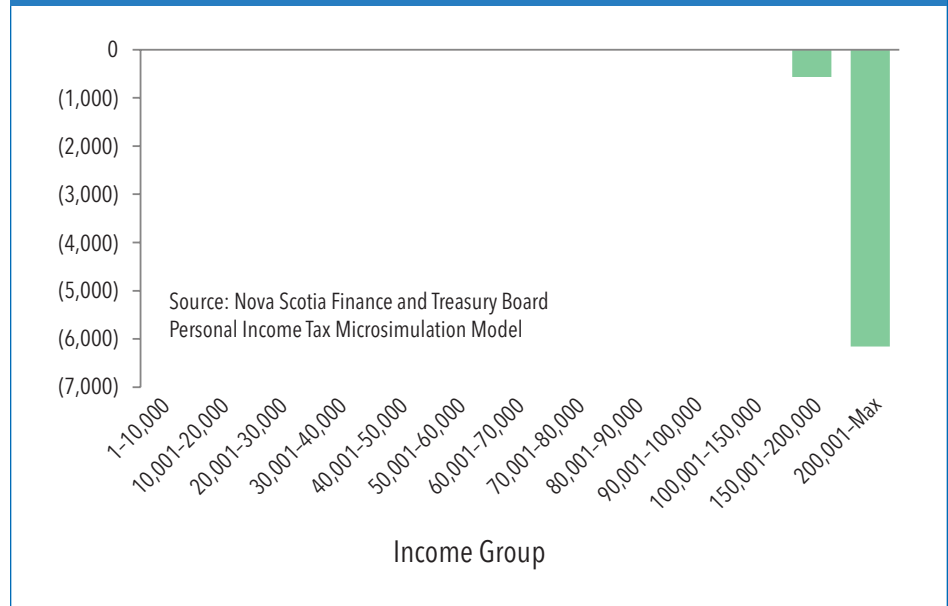
Recommendation 1.5

Personal income tax should have a built-in cost-of-living adjustment to eliminate so-called bracket creep.

Eliminate the “temporary” fifth tax bracket

Nova Scotia has Canada’s highest tax threshold as a result of the fifth bracket beginning at \$150,000, with a marginal tax rate of 21 per cent. When this measure was put in place it was said to be temporary, but so far there is no end in sight. As the Ivany Commission emphasized, innovation and risk taking hold vital keys to a prosperous economic future in Nova Scotia. The OECD points out that high top marginal tax rates reduce the payoff for risk taking, so reducing them should boost entrepreneurship and innovative activity in the economy.³⁰ A boost to entrepreneurship – rewarding risk-takers, dreamers, doers, and builders – is exactly what Nova Scotia needs, and another emphasis of the Ivany report. Nova Scotia needs more people who will stay here or come here to create jobs, strengthen the economy, and build a prosperous future. An important way to do that is to rebalance the risk-reward imperative. This recommendation will provide \$36 million in annual tax relief to Nova Scotians.

Eliminate 5th Tax Bracket: Average Change in Tax (\$ per individual)



Recommendation 1.6

The highest income bracket, 21 per cent on income over \$150,000, should be eliminated.

Promote fairness and simplify personal income tax: eliminate non-essential tax expenditures

The term “tax expenditure” refers to any form of incentive, preference, or relief granted through the tax system to a defined group of taxpayers, in the form of deductions, exemptions, credits, or deferrals. Tax expenditures are generally intended to relieve some hardship, encourage or assist certain activity, or provide an incentive or subsidy to those in special circumstances or need. These tax preferences are expenditures in the sense that revenues are less than they would otherwise be if the preference did not exist.³¹

The effect of tax expenditures does not end with revenue losses – critics often claim that revenues could remain constant, and tax rates reduced, if tax expenditures were eliminated – but extends to reduced progressivity and reduced equity in the tax system. Tax expenditures are “vertically inequitable” because savings are generally greater for higher-income taxpayers, and “horizontally inequitable” because taxpayers with equal incomes pay different amounts of taxes when one can use a preference and another cannot. Tax expenditures also increase the complexity of the tax system.³²

While they are generally enacted for legitimate and well-founded reasons, tax expenditures frequently disrupt the principles of an ideal tax system. Simplicity, ease of administration and compliance (efficiency), neutrality, and fairness are frequent losers when tax expenditures roll out. Conversely, these positive taxation characteristics are advanced when tax credits and other exemptions are eliminated.

Nova Scotia should keep only those income tax credits and exemptions that serve public policy priorities and provide demonstrated value for money. Evidence shows that most tax credits have little or no effect in motivating behaviour, which is frequently their purpose. In many cases they merely compensate or reward taxpayers for behaviour they intended anyway – with or without the credit.

To this end, Nova Scotia should eliminate the Volunteer credits and Healthy Living tax credit, which were put in place presumably as a result of political motivation rather than sound public policy.

The Volunteer tax credits are refundable, so they are worth \$500 to volunteer firefighters and search-and-rescue volunteers. The Healthy Living credit is non-refundable and allows taxpayers to claim a maximum of \$500 against the registration costs of children 17 and under in sports and other athletic activities. Tax savings from a maximum claim would amount to \$44. Any added tax burden as a result of the elimination of this credit would be more than offset by the increase in the Basic Personal Amount, as set out above.

In addition, the Seniors provincial income tax refund and the age credit are virtually redundant. The province should eliminate the Seniors provincial income tax refund, as it will be more than offset by the increased Basic Personal Amount, and the age credit is of greater benefit. This will simplify personal income tax compliance for seniors and administration for the province.

The revenue impact of these measures is over \$5 million annually.

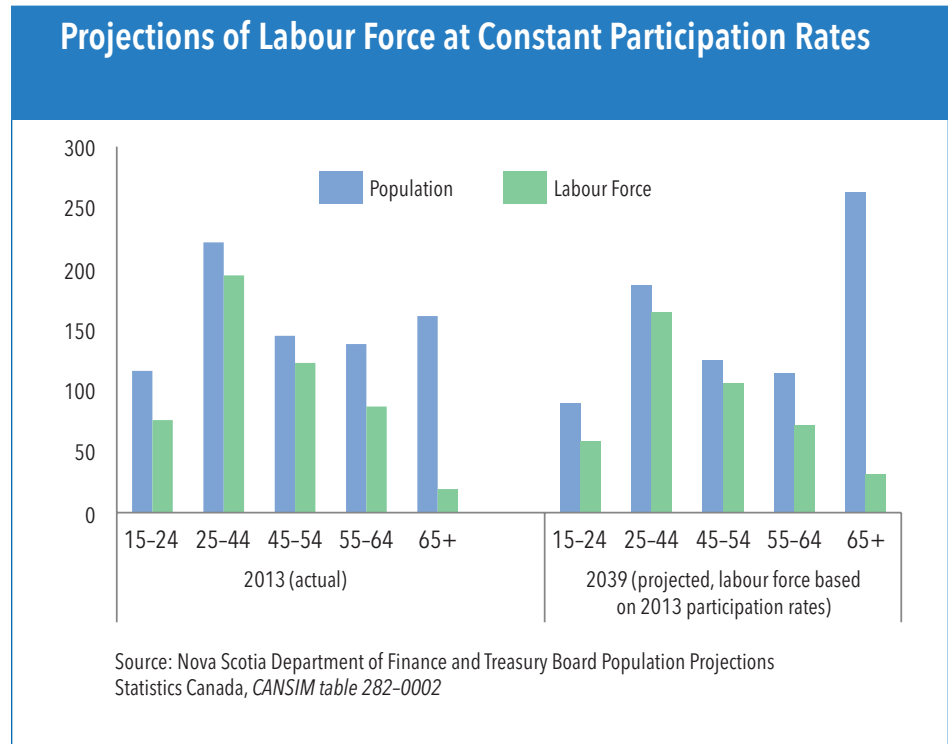
Recommendation 1.7

The Volunteer tax credits and the Healthy Living tax credit should be eliminated, as should the Seniors provincial income tax refund.

Remove disincentive to work

Another priority for Nova Scotia is to increase workforce participation, particularly among marginalized groups. Nova Scotia suffers the second-lowest overall labour force participation rate in the country (63.4 per cent, compared to the national average 66.4 per cent), and the rate for historically disadvantaged groups is lower.

As highlighted in the Ivany Commission report: “Opening up our workplaces to greater participation by minority and disadvantaged people, and building job skills and entrepreneurship among these groups, are critical objectives for social and economic progress in Nova Scotia.”



Government’s role in advancing this objective is, among other things, to ensure that the tax system does not create disincentives to work for anyone, particularly under-represented groups who are desperately required in the provincial workforce.

The province needs to remove every barrier to work it can and remove disincentives to entrepreneurial risk taking and the high-paying opportunities that attract highly educated people.

Low-income earners require more support to stay in or enter the workforce. Taking home more of their pay provides that incentive, and an increased threshold for the Basic Personal Amount achieves that goal.

As noted by the OECD, strong work disincentives afflict people eligible for social assistance, who face high marginal effective tax rates as benefits are withdrawn with earned or pension income. Low or negative returns for paid work for vulnerable groups – notably aboriginals, the disabled, high-school drop-outs, new immigrants, lone parents, and unattached males aged 45–64 – can keep them in relative poverty over a lifetime and prevent important virtuous cycles for the economy as a whole from getting underway.³³

To get people engaged in the workforce, the Department of Community Services must work with the Department of Finance, and seek out additional expertise if necessary, to redesign an income support system that positively interacts with the tax system to lower barriers and offer incentives for people to enter and stay in the workforce rather than penalizing them if they do.

Coordination of the social support and tax systems and the establishment of a steady marginal effective tax rate across the lower income spectrum are critical in this regard. Further insight may be found in the 2008 *Australia's Future Tax System* review as well the Government of Ontario's 2012 Review of Social Assistance, *Brighter Prospects: Transforming Social Assistance in Ontario*.³⁴

In order to accomplish this goal, funds should be earmarked for investment in low-income supports for the working poor and in particular for poor families with children, including an expansion of the Nova Scotia Child Benefit.

As the Conference Board of Canada notes, a simplified personal income tax system would also create the conditions that would allow for a cost-effective guaranteed annual income (GAI) delivered through the income tax system. While outside the scope of this review, it is a conversation that Nova Scotians should be having.

Recommendation 1.8

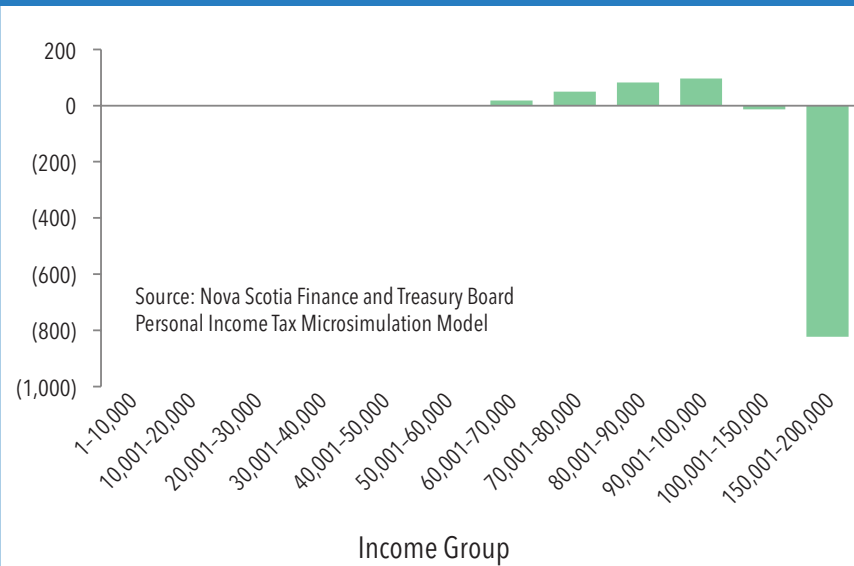
The Department of Community Services should redesign its income support systems with a goal of eliminating all disincentives to work. Income support and income taxes need to work in concert to ensure that low-income Nova Scotians are not financially disadvantaged by going to work. A portion of available 2017-18 transformation funds should be earmarked for investment in low-income supports for the working poor and in particular for poor families with children, including an expansion of the Nova Scotia Child Benefit, as part of this robust effort.

Reform personal income tax rates

Nova Scotia's personal income tax rates should be reduced over time, as funds become available, as spending targets are met, as new tax revenue becomes available, and as transformation of government reduces costs and captures previously untapped revenue sources. As a priority, efforts should be made to flatten the steep taxation curve of tax rates and simplify the rate structure by collapsing the two upper brackets. The targeted preferred rate for the new upper bracket would be 17 per cent. (Current rates are 16.67% and 17.5%.) This measure will provide \$36 million in tax relief to Nova Scotians.

Flattening Tax Bracket: Change in Tax

Average Change in Tax (\$ per individual)



Recommendation 1.9

Nova Scotia's personal income tax rates should be reduced over time. Efforts should be made to flatten the steep taxation curve and simplify the rate structure by collapsing the two upper brackets. The targeted preferred rate for the new upper bracket would be 17 per cent. (Current rates are 16.67% and 17.5%.)

Competitive corporate taxes for all businesses

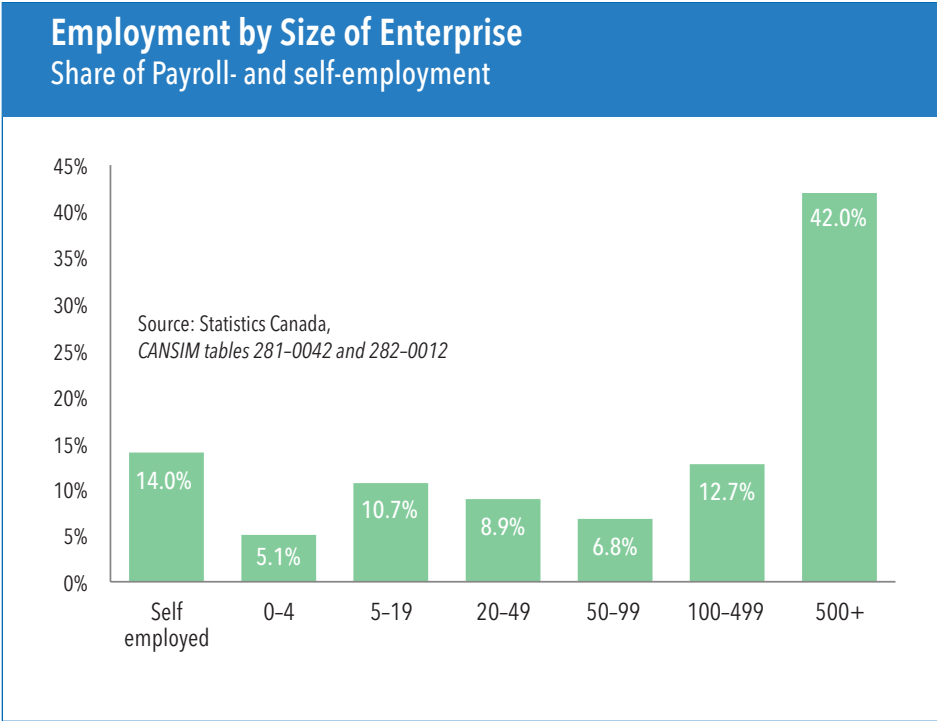
Although one should not underestimate the importance of personal taxation and the positive impact that a reduction in personal income taxes will have on the overall non-discretionary tax burden of Nova Scotians, the province needs to focus hard on its corporate tax structure. Having the highest provincial corporate tax rate in Canada puts Nova Scotia at a distinct competitive disadvantage.

Corporate tax is levied on the income earned by all corporations operating in Canada. Corporate income is subject to federal tax as well as tax at a rate set by each province. For corporations that operate in more than one province, income is generally allocated among provinces based on the proportion of their payrolls and their sales in each province. This is referred to as formula apportionment.

As noted previously, corporations retain some discretion regarding this allocation by organizing themselves into separate subsidiaries. Those that choose to do so are not required to consolidate the accounts of their subsidiaries for tax purposes. Subsidiaries operating in different provinces are taxed at the corporate tax rate applicable in each province. As Jack Mintz and Michael Smart observe, corporations may be able to shift profits from subsidiaries in high-tax provinces to those in low-tax provinces using transfer pricing or other financial planning techniques.³⁵

Corporations operating in Nova Scotia and elsewhere have incentives to shift profits outside the province, given that Nova Scotia’s corporate income tax rate is the highest among provinces. The 16 per cent general corporate rate has been in effect since 1991, and a reduction will almost certainly lead to more taxable income being allocated to Nova Scotia.

One of the objectives the government wants to pursue, and asked for from this review, is ideas to improve Nova Scotia’s competitive position. Nova Scotia and Prince Edward Island share the highest corporate tax rates among provinces. However, at 3 per cent, Nova Scotia is at the lower end of the scale in taxing small business. In fact, the largest business tax expenditure provided by the province is the small business rate. The estimated annual costs of small business tax relief has ranged from \$128 million to almost \$200 million since 2008. In addition, Nova Scotia’s New Small Business Tax Holiday effectively eliminates the corporate income tax for the first three taxation years of new small businesses following their incorporation. The tax holiday does not exist in any other Canadian jurisdiction.



Again, in this area, solid tax policy and traditional government decision making are not fully aligned. The term small business tends to generate images of the mom-and-pop store, the corner garage, or the little tech start-up. Those images are accurate, but they don't paint the complete picture.

On the other hand, high "corporate" taxes seem justified in the minds of many, who see companies paying these taxes as faceless "big, bad corporations" rather than the significant Nova Scotian employers that they in fact are.

The small business sector is important insofar as it creates jobs, generates wealth, and contributes to innovation. Small firms provide work for their owners, at least, and contribute to local economies. They carry out functions that it would not be economical for large firms to carry out, and some of them have spillover effects that help to develop markets. The attributes of small firms need to be recognized but not overstated.³⁶ "The term 'small business' is sometimes used as a proxy for other characteristics which governments may wish to target through the tax system, such as new firms, 'entrepreneurship,' growth and job creation. Using size as a means of targeting these groups is inaccurate because size does not relate directly to these characteristics."³⁷

One evidence-based rationale for providing tax relief to small firms is that tax reductions are important in countering the inherent disadvantages of being small, which come primarily from tax and regulatory compliance costs.³⁸

In this regard, evidence is consistent across jurisdictions that the costs of complying with tax and regulatory burdens fall disproportionately on small business with fewer staff and less expertise and time to devote to understanding and complying with these burdens than larger corporations. Economies of scale and methods of organization used by larger firms are not available to smaller firms. This is a problem that can and should be addressed by comprehensive regulatory relief and reform – as discussed in the regulatory reform section of this review – as well as a slight beneficial adjustment to the taxation levels, but not so large as to be distortive.

Professor David Storey, OBE, co-author of *Small Business and Entrepreneurship*, has shown that most small firms do not grow, and a "handy rule of thumb" is that over any 10-year period, in almost any open economic jurisdiction, 4 per cent of small businesses will create 50 per cent of the jobs in the sector.³⁹

According to Jack Mintz,

In contradiction to the widely held view that small business tax concessions encourage growth, such small business tax relief could actually be antithetical to growth by creating a "taxation wall". First it could result in the breakup of companies into smaller, less efficient-sized units in order to take advantage of tax benefits even if there are economic gains to growing in size. Second, it could encourage individuals to create small corporations in order to reduce their personal tax liabilities rather than grow companies.

And third, it could lead to a “threshold effect” that holds back small business from growing beyond the official definition of “smallness,” regardless of the criteria for measuring size.⁴⁰

Jack Mintz chaired the federal Technical Committee on Business Taxation, which found that more than 80 per cent of small businesses (that claimed the small business tax deduction) earn less than \$100,000 annually.

Rather than encourage economic growth, advantageous tax treatment may encourage small business owners to keep their businesses small – the unintended consequence Mintz calls “the threshold effect.” He also notes that small business tax incentives “undermine the neutrality of the overall tax system and the tax goals of simplification, economic efficiency and fairness.”⁴¹ Mintz accordingly concludes that “in the interest of fairness, business taxes are best levied at similar rates across business activities while varying personal tax rates to accomplish fairness objectives.”⁴²

OECD surveys have also found small business tax breaks to be a serious distortion, reducing firms’ incentives to grow to the optimal size for economies of scale while also creating opportunities for personal and corporate tax avoidance. The research and evidence suggests strongly that reducing corporate income tax would produce far more growth benefits than reducing taxes for small businesses.

Finally, it is interesting to note that the UK has acted on the advice it received in the Mirrlees review. The UK has sped up its previously announced tax reduction plan. Instead of reducing the company tax rate to 22 per cent in 2014, the government will reduce the rate to 21 per cent in 2014 and to 20 per cent by 2015. With its current 20 per cent Corporation Tax (CIT) rate for small business unchanged, the UK will effectively unify the existing two-tier CIT rates by 2015.⁴³

The Nova Scotia economy requires growth and job creation. Nova Scotia needs to remove the tax incentive for businesses to stay small, and get out of the way and allow large enterprises and employers to grow. Nova Scotia needs to reform its small business and corporate tax structure to ensure that it encourages, rather than creates barriers to, growth, and it needs to advance this reform in an incremental revenue-neutral manner as set out below.

Corporate Income Tax Changes (\$ millions)

	Threshold 500K	15.5G/4S	15G/5S	14.5G/6S	14G/7S	13.5G/8S
Small Rate Gain	3.9	11.6	27.0	42.3	57.7	73.1
General Rate Loss	(18.0)	(24.1)	(37.3)	(50.4)	(63.6)	(76.8)
Total	(14.1)	(12.5)	(10.3)	(8.1)	(5.9)	(3.7)

Source: Nova Scotia Department of Finance and Treasury Board

Recommendation 1.10

The province should raise the small business tax threshold to \$500,000 from the current \$350,000, and it should incrementally over the next five years raise the small business tax rate to 8 per cent from the current 3 per cent. The increased revenue should be used to gradually lower the general corporate income tax rate, which at 16 per cent is the highest in Canada, to 13.5 per cent.

As well, Nova Scotia's New Small Business Tax Holiday, which effectively eliminates the corporate income tax for the first three taxation years of new small businesses following their incorporation, has not been widely used, does not exist in any other Canadian jurisdiction, does not have any evidentiary basis of support, and should, for tax simplification reasons, be eliminated.

Recommendation 1.11

The New Small Business Tax Holiday should be eliminated.

Corporate tax expenditures

The tax system is a blunt instrument for economic development. Corporate tax expenditures are designed to provide an incentive or subsidy to specific industries. But, as noted in the Economist, July 2013: "Loopholes for some mean higher tax rates for everyone else."⁴⁴

Nova Scotia must take a balanced approach to business supports and fiscal sustainability in order to make Nova Scotia a destination of choice for foreign and domestic private sector investment and to strengthen the whole of the provincial economy. The government should recognize that Nova Scotia can be a more competitive jurisdiction for business by making investments in a broad range of areas, such as public infrastructure, skills training, and reduced taxes, to name a few. Tax expenditures and incentives are business supports that are often attempts to make something sustainable that isn't, that draw resources away from other areas of possible government investment, and that require the imposition of an increased tax burden on others.

There is a significant body of academic and economic literature that can provide good advice with respect to the considerations surrounding tax incentives, in particular from the OECD and the IMF.⁴⁵

Preferential tax regimes make tax administration more complicated and “once implemented, these systems generate significant benefits for the recipients who become powerful lobbyists making their modification extremely difficult. Even if these benefits are temporary, there are strong incentives to maintain them. Tax incentives tend to have non-transparent costs which make their estimation difficult and increasing their social costs, underrating their impact in terms of foregone revenue.”⁴⁶

Nonetheless, “tax expenditures remain the most popular measure to promote investment in both developing and industrialised countries.”⁴⁷

The OECD has set out a succinct summary of best practices to use when implementing targeted tax credits:

When justifiable and applied, there seems to be a consensus that incentives should be targeted in scope and length. A first condition is that incentives should be directed toward activities that while not originally feasible without them are viable after benefits expire. Second, since these schemes impose fiscal costs and administrative burdens, they should not be indefinite. Third, the targeting mechanism should be explicit from the start and ideally be included in the budget process. Monitoring, qualifying and disclosing information regarding tax expenditures associated with these incentives is also an important factor . . .

Rigorous evaluation, transparency, and recognition that “once a system creates a precedent there is considerable pressure for additional ones to emerge” are key considerations.⁴⁸

Similar advice was advanced by the Ontario (Drummond) Commission on the Reform of Ontario Public Service, which noted that subsidy programs can distort business decisions, are “susceptible to stakeholder lobbying which can result in an economically inefficient allocation of funds,” and “the outcomes of these programs are often vague and difficult to measure, preventing thorough analysis.”⁴⁹

The Millier Dickinson Blais Review of Business Development Assistance tools, an appendix to the Traves Report, also provides a review of best practices when it comes to economic development incentives.

In line with the recommendations from the Drummond Commission, the Province of Nova Scotia should make departments responsible and accountable for tax expenditures that align with their respective program areas. As per Drummond: “Ministries should initially be provided with the means to fund the tax expenditures (i.e., a net zero impact for the ministries), but after that they will have to manage the pooled envelope of tax expenditures and direct business support programs to meet budgetary targets. This will provide an incentive to tighten inefficient tax expenditures as the ministries responsible for the tax expenditures will have the ability to reform tax expenditures when seeking potential savings.”⁵⁰

What Don Drummond was pointing out is that there is often less accountability for tax expenditures than direct spending programs. Tax expenditures are less transparent and can be amended or increased by regulation without any legislative review. As a result, governments do not have to justify tax expenditures to the same degree as direct expenditures.

In his report to government, Dr. Traves said tax credits should be held to the same standard as all business incentive programs and should be reviewed every five years to “assess the benefits they deliver in support of the achievement of provincial economic goals.”⁵¹

Charting a new direction on tax expenditures will be critical to Nova Scotia’s future economic prosperity and its ability to maintain a solid tax base, but it will be particularly challenging given the seemingly insatiable demand for more tax credits in areas such as sound recording, book publishing, apprenticeship training and co-operative education, to name a few.

Going forward, all expenditures and programs to support business should be treated the same way, regardless of whether they are tax expenditures or direct expenditures. The government should publish a report detailing all tax expenditures and their estimated cost. Corporate tax expenditures should be regularly reviewed and analyzed using the same parameters as any other business support initiative. Business tax credits should be targeted in scope and limited in length.

Recommendation 1.12

Corporate tax expenditures should be analyzed using the same parameters as any other business support initiative. That includes cost-benefit analysis to determine if they are meeting their public policy objectives, determining their effectiveness and efficiency in creating incremental economic activity and jobs, and measuring their impact on the broader economy.

All business tax credits should be targeted in scope and of limited duration; only those that demonstrate success through a mandatory, comprehensive evaluation should be extended.

Sponsoring departments should have budgetary accountability for corporate tax expenditures.

The province should ensure greater transparency in business support programs by publishing annually a list of direct business support programs and any related spending, including companies receiving direct financial support and the quantum of that support.

Film Industry and Digital Media tax credits

The government's recent decision to renew the Film Industry and Digital Media tax credits through 2020 demonstrates its commitment to both industries. It also provides an opportunity for the province and the sectors to work toward embedding the best-practice recommendations set out in this report. In the short term, the province should make adjustments to both tax credits to remedy longstanding administrative and processing issues identified by the industries and to better align Nova Scotia's credits with other provincial credits.

The Film Industry Tax Credit is a refundable corporate income tax credit that was designed to encourage filmmaking in Nova Scotia and generate employment for Nova Scotians in the industry. Film and Creative Industries Nova Scotia, a Crown corporation, administers the credit in conjunction with the Department of Finance and Treasury Board. The credit costs the province about \$22 million a year in foregone revenue.

The base credit pays 50 per cent of eligible salaries. Two additional bonuses are also offered: a 10 per cent eligible geographic area (EGA) bonus if at least 50 per cent of the production is filmed outside the Halifax Regional Municipality, and a 5 per cent frequent filming bonus (FFB) if three films are produced by the same company within a two-year period. Collectively, these measures can bring the value of the credit up to 65 per cent. Historically, there was a production cost cap, but the cap was removed in 2010 to enhance the program.

Along with a long-term commitment, the industry has been seeking clear and concise guidelines and a streamlined application process. To address concerns about tax credit administration, the government should consider aligning its credit with another province. The Ontario Film and Television Tax Credit and OFTTC Guidelines were held up as exemplary, as was the Ontario online application process; they should be used as examples of best practices to guide Nova Scotia reforms. Film and Creative Industries Nova Scotia should assume sole responsibility for the administration of the Nova Scotia tax credit. Nova Scotia's Film Industry Tax Credit is considered to be one of the most generous in the country. Significant differences and anomalies, compared with other provinces, should be corrected:

- The FFB is one such anomaly and should be eliminated. This would help bring Nova Scotia's maximum credit rate in line with Ontario, British Columbia, and Quebec. Except for documentaries, out-of-province filming should not qualify for the tax credit.
- The EGA bonus should be pro-rated and the province should consider pushing the radius further from HRM to encourage filming in rural areas.
- Definitions of residency should also be aligned with tax credits in other provinces.
- Allowing eligibility for writers' fees and rentals would also be in keeping with the practice in other jurisdictions.

"The province needs better expertise internally."

Nova Scotian at roundtable discussion

“Industry changes quickly. How can government ever keep pace?”

Nova Scotian at roundtable discussion

The Digital Media Tax Credit (DMTC) was introduced in 2007. It was designed to encourage employment of skilled Nova Scotians and build the sector by providing a refundable corporate income tax credit for digital media corporations. The cost of the DMTC has grown from \$1.66 million in 2008 to \$5.3 million in 2012.

The credit is the lesser of the cost of eligible labour or total production costs. The base rate is 50 per cent of eligible labour or 25 per cent of total production costs. An EGA bonus of up to 10 per cent of eligible labour or 5 per cent of total production costs is available for work outside the Halifax Regional Municipality. In addition, a credit is available on a maximum \$100,000 in eligible marketing and distribution costs.

A digital media product must be “interactive” to qualify for the credit. The user must interact with the product, exercising control, receiving feedback – not simply being a spectator. The product must be completed within a three-year period.

The current eligibility is narrowly defined as interactive digital media content, and the constantly evolving sector is seeking a broader definition of eligible activities. Expanding the base of eligibility may not be possible given the fiscal realities of the province. The term “interactive,” however, is highly subjective and lacks clarity.

With the government’s commitment to the sector, the province and the industry must now work to develop strategies that will allow the industry to expand and grow, while giving certainty to the province with regard to expenditures.

The review heard this sector’s concern about processing delays for credits as well as frustration that the Department of Finance and Treasury Board does not have the expertise to evaluate interactive material. The industry noted that it must be nimble and build on its ability to move into simulation, and the definition of “interactive” cannot be left to interpretation.

As with the Film Industry Tax Credit, the province should seek to better align its Digital Media Tax Credit with the convergence of sectors within the creative economy.

Specific changes that should be considered are as follows:

- Use industry-led expertise to determine eligibility.
- Eliminate the \$100,000 Marketing & Distribution allowance, as this is more closely aligned with video games and does not reflect activities of the broader sector.
- Funding received from government and government agencies should be deemed “government assistance” and not eligible for the tax credit.

From both the film and digital sectors, the review heard that “certainty and long-term planning” are needed in order for Nova Scotia to fully benefit and to spur the growth of the industries. With the government’s committed support through 2020, it will be important for administrative and regulatory issues and uncertainties to be resolved, while balancing the province’s challenging fiscal realities.

Recommendation 1.13

The regulatory framework and detailed elements of both the Nova Scotia Film Tax Credit and the Digital Media Tax Credit should be better aligned with similar tax measures in other Canadian jurisdictions.

Film and Creative Industries Nova Scotia should be solely responsible for the administration of both tax credits.

Industry and the province should use the period leading up to the sunset of the two credits in 2020 to determine the most effective tools to help grow the creative economy in Nova Scotia and transition the tax credits to departmental expenditure programs that are transparent, accountable, and focused on economic growth.

The Scientific Research and Experimental Development tax credit

According to the OECD:

R&D credits are a prominent example of a justifiable tax subsidy, one that is widely used in OECD countries on the premise that R&D provides benefits to society at large (knowledge spill overs) beyond those to the individual firm undertaking the investment. They are a priori more efficient than research grants, which are administratively costly and may involve government picking winners, though basic research usually taking place within the private or non-profit university sector may require a grants approach.⁵²

At 15 per cent, Nova Scotia's Research and Development tax credit ranks in the middle of the pack across Canada. The review received a good deal of support and positive feedback for this credit, which is relatively modest and plays to a potential provincial strength given the university population. However, one issue of concern raised repeatedly by Nova Scotian industry representatives was what they saw as regional differences in the application of the Scientific Research and Experimental Development (SR&ED) tax credit by the CRA. The province should take a leadership role, working with affected Nova Scotian industries, other Atlantic provinces, and the CRA to resolve this longstanding area of concern.

“Nova Scotia does one thing right: the Equity Tax Credit.”

Nova Scotian at roundtable discussion

Recommendation 1.14

The province should work with the federal government and the CRA to respond to concerns raised by industry that the current SR&ED tax credit is not administered consistently across the country.

Equity Tax Credit

The Equity Tax Credit was introduced in 1994 after public consultation confirmed that the lack of equity capital financing for small and medium-sized businesses was hindering growth and success and that more than \$600 million per year was leaving the province in RRSP investments.

To encourage Nova Scotians to invest in Nova Scotia and supply needed equity capital, the Equity Tax Credit (ETC) program was introduced. This approach was thought to have several advantages over traditional direct government investment in businesses. First, businesses would actively pursue equity capital, and reliance on debt and traditional government financing would be reduced. Second, equity partners would provide personal contact and guidance to businesses that government could not. Third, investment decisions would now rest with investors and business people who would aim to optimize returns through efficient use of their capital.

The ETC was designed to help Nova Scotia small businesses, co-operatives, and community economic development initiatives obtain equity financing by offering a personal income tax credit to individuals investing in eligible businesses. The ETC has been extended to December 31, 2022.

For investments made before January 1, 2010, the tax credit is calculated at 30 per cent to a maximum annual investment of \$50,000 (or a maximum annual credit of \$15,000). For investments after December 31, 2009, the tax credit is 35 per cent to a maximum annual investment of \$50,000 (a maximum annual credit of \$17,500). The tax credit is not refundable but may be carried forward for seven years or carried back three years, and the investment must be held for five years. The provisions of the ETC program, including labour and innovation tax credits, were recognized as best practices by Millier Dickinson Blais in a provincial business support review.⁵³

To comply with the Securities Act, businesses using the general ETC are limited to selling shares as exempt issues (non-public), while Community Economic Development Funds (CEDIF) can be sold to the public.

CEDIFs are a subset of the ETC program, and the maximum tax credit is the same as other ETCs. If the CEDIF is held for 10 years, the investor may be eligible for an additional 20 per cent credit, and if the investment is held for 15 years the investor may be eligible for an additional 10 per cent credit.

Although CEDIF created a direct Nova Scotia Registered Retirement Savings Plan investment, many of the assets are illiquid and therefore pose a challenge when the investor must move from the RRSP to a RRIF.

To ensure that Nova Scotian taxpayers are getting best value from their investments, a number of issues must be resolved. CEDIFs, for example, cannot be allowed to offer additional benefits to investors such as golf club memberships; there cannot be any double dipping (i.e., taking advantage of both CEDIF and another provincial tax credit, such as the Film or Digital Media credits); and the required investment by CEDIFs of 64 per cent of what they raise in the community should be increased.

The ETC and the CEDIF were designed as broad-based initiatives to enable small and medium-sized businesses to raise equity capital, and they have succeeded in this regard.

The review heard calls to raise the investment limit consistent with recommendations from the Donald Savoie report. Given the province's challenging economic circumstances, as well as this review's recommendations to put in place a stronger and more robust accountability process with regard to tax credits, it is recommended that the government consider doubling the ETC limit to \$100,000 and include preferred shares and debentures but limit its application to strategically defined high-growth sectors, such as information technology and clean technology, to be defined by regulation.

Recommendation 1.15

The province should consider doubling the annual limit for eligible ETC investments to \$100,000 from the current \$50,000. Consideration should be given to targeting the ETC to strategically defined high-growth sectors, such as information technology and clean technology, to be defined by regulation. As well, eligibility requirements must be re-examined to ensure that Nova Scotians are receiving best value from these tax credits.

In light of the ETC success and Nova Scotians' expressed desire to invest in the province, Nova Scotia should further examine the pooled investment approach that has been successful in Quebec and/or, in the alternative, develop a mechanism whereby pooled investment funds can be eligible for the ETC.

As well, the Nova Scotia government should pursue a conversation with other provinces in the region about expansion of the ETC to a regional tax credit, such as the Atlantic Gateway Capital Credit, which has been championed by 4Front Atlantic, as part of a larger regional harmonization strategy.

Recommendation 1.16

Nova Scotia should pursue interest across the region for expansion of the ETC to a regional tax credit as part of a larger regional harmonization strategy. The province should also consider allowing pooled investment funds to be eligible for the ETC.

Using the tax system as incentive for business creation, growth, and economic development is a common approach in many jurisdictions. The reality, however, is that the tax system is a blunt instrument for this purpose, and incentives are often being used to seek to sustain businesses and commercial enterprises that are, in fact, unsustainable. Nevertheless, there are many innovative economic development and job creation efforts that are tax-based and are being attempted in other jurisdictions. They include:

- Economic Diversification and Growth Enterprise (EDGE), Newfoundland and Labrador
- Ontario Commercialization Tax Credit
- Manitoba's Enterprise Zones
- Municipal tax abatement in Saskatoon and Regina
- Tax holiday for large incremental projects in Quebec
- The State of New York's Start-Up New York tax-free zones

As viable as these economic tools may prove to be, the current priority for Nova Scotia has to be to get its fundamental foundation pieces right – priorities like a reduction in the corporate tax rate and taking a much less interventionist approach to business regulations.

While Nova Scotia focuses on the basic elements of its economy, a more substantive, evidence-based analysis as to the real impact of these diverse efforts will no doubt become available with respect to the many programs being attempted in other jurisdictions. Nova Scotia will benefit from this body of evidence to ground any future conversations. Right now, Nova Scotia has to get back to basics and focus its plan for jobs and prosperity on a more competitive tax regime as a whole, rather than pinning its economic development aspirations on one-off silver-bullet tax expenditures.

Implement a Pollution Tax

Pollution has historically been regarded as a cost of production borne not by the polluter but by others, in the form of a damaged environment (ranging from noxious odours to impaired health to changes in climate). Pollution taxation aims to ensure that polluters face the true cost of their activities by charging them for the damages their activity causes the environment and others.

Pollution taxes are excise taxes on environmental pollutants or on goods whose use produces such pollutants. Economic theory suggests that taxes on polluting emissions will reduce environmental harm in the least costly manner, by encouraging changes in behaviour by those industries and households that can reduce their pollution.

From Mirrlees:

A good tax system will not just limit negative effects on efficiency. It will also promote economic welfare by dealing with externalities which arise when one person or organization does not take account of the effects of their actions on others. Taxes can affect this behaviour by altering the incentives for certain sorts of behaviour, most notably when polluting activity is taxed to reduce the total amount of pollution.⁵⁴

Former federal Liberal leader Stephane Dion knows better than most that a carbon tax, while good public policy, makes for challenging politics. In his article *Carbon Taxes: Can a Good Policy Become Good Politics?* Dion says carbon tax revenue should, in part, reduce personal or business income taxes, thus enabling governments to “tax what you burn, not what you earn.”⁵⁵

Support for a pollution tax spans the political spectrum, is almost as prevalent among economists as it is among ecologists, and flows enthusiastically from organizations such as the Rand Corporation, the Brookings Institution, the Canada West Foundation, the Canadian Council of Chief Executives, the Conference Board of Canada, OECD, and most recently Canada’s Ecofiscal Commission.⁵⁶

In fact, according to an IMF 2014 report, countries rely too much on general income, payroll, and consumption taxes for their fiscal objectives, and too little from taxes on energy use. The report makes the case for a tax shift and stresses that energy tax reform need not be about raising new revenues. Rather, reform could focus on restructuring the tax system away from taxes that are likely to be most harmful for efficiency and growth, such as income taxes, and toward carefully designed taxes on energy – smarter taxes rather than higher taxes.

Getting energy prices right involves extending motor fuel taxes, which are already well established and easily administered in many countries, to other fossil fuel products, such as coal and natural gas, or their emissions, and aligning the rates of these taxes with environmental damage.⁵⁷

“All taxes discourage something. Why not discourage bad things like pollution rather than good things like working?”

Lawrence Summers

Pricing Pollution is better than taxing income

"Whatever a government's overall fiscal situation, whether it is seeking to increase or decrease its overall level or taxation, the logic of ecofiscal policies offers a genuine opportunity. User fees and pollution taxes can always be used as a substitute for more distortionary and growth-retarding taxes. Shifting away from income taxes and toward pollution taxes can generate significant economic and environmental benefits."⁶⁴

Canada's Ecofiscal Commission

Dion notes that in most nations today, polluters can emit carbon for free:

Putting a price on carbon emissions is an eminently logical way to force polluters to take the environmental cost of their operations into account and to reduce their GHG (greenhouse gas) emissions. If carbon emissions were priced in our economy, consumers and businesses would have a powerful incentive to choose goods and services with lower carbon content, and to invest in proven or innovative energy saving and emission reducing technologies. It would be in their own interest to curb their carbon emissions, thus reducing their tax burden.⁵⁸

The basic rationale for environmental taxation is clear. Pollution imposes costs on society that are not borne by the polluter. Imposing a tax ensures that the polluter accounts for these wider costs when deciding how much to pollute. On this basis, a reasonable goal is to reduce pollution to a level that takes into account both the costs of the pollution and the benefits of the polluting activity. Taxes have been viewed to be more effective than regulation as a way to achieve this.⁵⁹

As put succinctly in Mirrlees, "If the government restricts pollution without raising revenue (which it can recycle) it risks losing much of the welfare gain associated with improved environmental performance . . ."⁶⁰

Nova Scotia's Environmental Goals and Sustainable Prosperity Act clearly recognizes the strong connection between economic and environmental goals. Building on this foundation and according to the Ecofiscal Commission:

Ecofiscal tools (such as carbon pricing) make markets work better by establishing a price for actions that result in environmental damage. They incorporate the costs of the environmental damage into market prices, thus improving market signals. Firms and households respond to these signals by finding innovative and cost-effective ways to reduce pollution.^{61/62}

Following such an approach, the province of British Columbia in 2006 introduced its carbon tax on the emission of three greenhouse gases (GHGs) – CO₂, CH₄, and N₂O – that are produced by fossil fuel combustion. The tax is a critical component of that province's goal of reducing greenhouse gas emissions by 33 per cent by 2020, estimated as equivalent to removing almost 800,000 cars from the road every year.

The BC model has drawn international attention. OECD Secretary General Angel Gurría said in a speech in October 2013, "The implementation of British Columbia's carbon tax is as near as we have to a textbook case."⁶³

BC's tax is a volumetric-based tax and was phased in. The tax rates vary across fuel types according to the level of GHG emission per unit of fuel (GHGs other than CO₂ are converted into CO₂ equivalents). The rates set are roughly aligned with various international environmental studies on the social cost of carbon emissions and

generally established at an average price of about \$43 per tonne of CO2 equivalent, but with a wide standard deviation of \$83 per tonne.

In BC, the tax rate rose by \$5 per tonne of emission each year, starting in 2008 at \$10 per tonne, to a final rate of \$30 per tonne in July 2012. This approach provided some certainty and afforded individuals and corporations time to make adjustments. This is the suggested approach for Nova Scotia.

A report by Sustainable Prosperity entitled *BC's Carbon Tax Shift After Five Years* has concluded that the BC Carbon Tax policy has been a success. The report pointed to a 17.4 per cent per capita reduction in consumption in all taxable fuel types, while BC's economic growth kept pace with or surpassed most provinces over the same period.

By law, the BC government must return all carbon tax revenue to the province through the reduction of personal and corporate taxes. The carbon revenue cannot fund any government programs, and the government is required to publish an annual plan to that effect. Specific tax measures implemented in 2008 to return the carbon revenue included

- introduction of Low Income Climate Action Tax Credit
- 2 per cent reduction in the bottom two PIT rates in 2008, followed by a 5 per cent reduction in 2009
- 1 per cent reduction in both the CIT and small business CIT in 2008.

Recognizing the regressive aspects of the tax, BC provided a refundable Low Income Climate Action Tax Credit to help offset the impact on low-income families. Following BC's lead, a Nova Scotia pollution tax should also be legislated to be revenue neutral, with revenues returned to Nova Scotia taxpayers through PIT and CIT reductions. A tax credit to mitigate the impact on low-income Nova Scotians should also be designed, and enhancements to the Heating Assistance Rebate Program should be put in place to build on those reforms set out earlier in this review.

A pollution tax is a "pigouvian" tax, named for British Economist Arthur Pigou, who 100 years ago proposed to tax "negative externalities" – that is, the social costs not reflected in the market cost of a product or activity. High taxes on alcohol and tobacco are typical pigouvian taxes, designed to recover the social costs of these products; dissuade consumers from consuming, or at least abusing, them; and encourage healthier choices. When it comes to carbon emissions, a negative externality is precisely what children worldwide will face when they have to deal with climate changes caused by the greenhouse gases emitted at no cost by previous generations.

A Nova Scotia pollution tax can play a key role in shifting the tax balance in Nova Scotia. Indeed, thanks to its carbon tax revenue, British Columbia has lowered its corporate tax to among the lowest in the G8, and personal income tax rates for those earning less than \$119,000 annually are now the lowest in Canada.

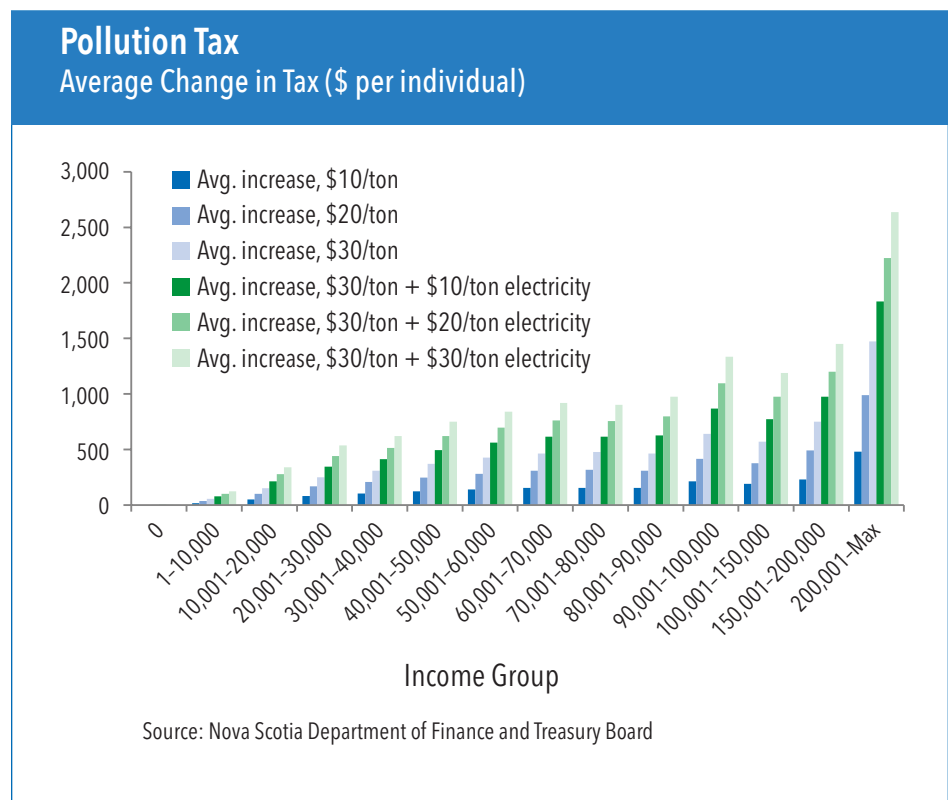
We need a better fiscal system, not higher taxes

"An effective and efficient Canadian fiscal system for the 21st century will promote innovation and growth while reducing pollution and environmental damage. This requires redesigning our current fiscal system, but it need not increase Canadians' overall tax burden or the size of government."⁶⁵

Canada's Ecofiscal Commission

If Nova Scotia were to adopt a fossil fuel tax modelled after British Columbia's, Nova Scotia could increase gross provincial revenue by as much as \$430 million per year. If electricity generation were excluded for the first five years in recognition of the current government-imposed 2020 renewable targets, the revenue generated would be approximately \$227 million by 2019 and roughly \$430 million following a second proposed five-year phase-in to 2025-26, although carbon emission should see significant reduction once renewable targets have been met. By adopting BC's revenue-neutral approach, the entirety of these funds would be directed to tax relief. BC's journey should provide a roadmap for Nova Scotia.

Given the reality of climate change, the global community must squarely face the consequences, and any jurisdiction truly looking to build a tax regime for the future would be naïve not to drive revenue-neutral tax reform in this direction. Following BC's lead, Nova Scotia should design and implement a pollution tax regime and provide generous support to low-income families as well as overall corporate and personal tax relief in line with the revenue generated.



Recommendation 1.17

Nova Scotia should phase in the implementation of a pollution tax regime over the next 10 years. The tax should be revenue neutral to the province, with all available revenue earmarked to provide generous support to low-income families as well as overall corporate and personal income tax relief.

Maintain reform momentum

Tax reform should not be a one-time event or a once-in-a-generation endeavour. Taxation is a critical function of government and should be subject to continuous assessment. New Zealand's Tax Working Group model – which includes government, academic experts, and tax professionals in an ongoing collaborative review of tax policy – would serve the province well.

Recommendation 1.18

The province should establish a Nova Scotia Tax Working Group – including government, academic experts, and tax professionals – to review tax policy and options and make recommendations to government on an ongoing basis.

As set out from the outset, a good tax system is predictable, stable, sustainable, fair, and progressive, and it contributes to the greatest extent possible to the economic and social welfare of the province. In order to advance and consolidate the objectives it articulated in establishing this review, the government should legislate a 10-year agenda of tax reform, so Nova Scotians and the province's business community understand and can plan for their financial future in Nova Scotia. This will also ensure that the province maintains a tax system that retains the desired principles and characteristics and delivers the revenues required for quality public services in the future. The chart on the next page provides an example of the tax reform proposed by this review over the next five years.

Recommendation 1.19

The province should legislate a 10-year tax reform agenda, which commits to a series of incremental yearly tax reforms as provided for in this review, in order to provide certainty and predictability to Nova Scotian citizens and businesses as well as to ensure that all measures to which the government commits as a result of this review are brought into effect.

Illustration of Potential Fiscal Impacts of Tax and Regulatory Review Recommendations (\$ millions)

	2015-16	2016-17	2017-18	2018-19	2019-20
Freeze Expenditures	0.0	202.0	535.0	829.3	1,141.4
Eliminate HST Rebates	128.0	128.0	128.0	128.0	128.0
Enhance ALTC	(29.1)	(29.1)	(29.1)	(29.1)	(29.1)
Increase BPA to \$11,000	(112.0)	(112.0)	(112.0)	(112.0)	(112.0)
HARP Enhancements	(7.0)	(7.0)	(7.0)	(7.0)	(7.0)
Indexation (@ 1.2 per cent)	(20.4)	(40.8)	(61.2)	(81.6)	(102.0)
Remove 5th PIT Bracket	(36.4)	(36.4)	(36.4)	(36.4)	(36.4)
Eliminate Volunteer Credits	3.9	3.9	3.9	3.9	3.9
Eliminate Healthy Living Credits	1.2	1.2	1.2	1.2	1.2
Remove tax refund for GIS recipients	–	–	–	–	–
Combine 3rd and 4th PIT Brackets		(36.1)	(36.1)	(36.1)	(36.1)
Enhance NSCB		(44.0)	(44.0)	(44.0)	(44.0)
Raise Small Business Rate by 1 per cent/year	11.6	27.0	42.3	57.7	73.1
Reduce General Rate by 0.5 per cent/year	(24.1)	(37.3)	(50.4)	(63.6)	(76.8)
Eliminate New Small Business Tax Holiday	0.1	0.1	0.1	0.1	0.1
FITC/DMTC Changes	(TBD)	(TBD)	(TBD)	(TBD)	(TBD)
Increase ETC Investment Limit	TBD	TBD	TBD	TBD	TBD
Pollution Tax (Electricity not included)	74.7	112.1	149.5	186.9	223.9
Further decrease CIT Rate by 2 per cent		(54.0)	(54.0)	(54.0)	(54.0)
Further decrease PIT Rate by 1 per cent			(220.0)	(220.0)	(220.0)
Priority Transformational investments/ Tax Relief/Debt Reduction		(77.0)	(209.0)	(523.0)	(854.0)
	(9.5)	0.6	0.8	0.3	0.2

Additional fiscal considerations

During the course of the consultations, three topics emerged repeatedly, which, while not strictly within the scope of the review, are related to taxation and the financial management of the province. These three topics – asset monetization, effective collections, and the underground economy – are discussed below, with a recommendation related to each.

Beyond taxes: Revenue innovations to invest in the future

Don't pay for everything with tax revenue. In fact, free up tax revenue.

This review heard from stakeholders that Nova Scotians' investment dollars and pension holdings should be invested in Nova Scotia. Calls for local investment of pension and other funds are heard, in greater and lesser volume, across the country. As pointed out by Michael Fenn, a former Ontario deputy minister, public

sector pensions are increasingly invested outside Canada, and “the lack of domestic investment opportunities in infrastructure and government business enterprises is a missed opportunity for the Canadian economy and for all Canadians.”⁶⁶

In an insightful paper for the Mowat Centre called *Recycling Ontario's Assets: A New Framework for Managing Public Finances*, Fenn explores innovative approaches to public asset management and monetization, highlighting the Australian “asset recycling” experience, whereby capital assets are sold or “recycled” with the proceeds reinvested by the government in new infrastructure – a process often referred to as asset monetization. Pension and other funds are frequent investors in recycled assets.

Fenn notes that “our current prosperity and quality of life stand on the shoulders of past investments and past visionaries” who, in the post-war decades, built Canada. That infrastructure is at the end of its life, and with no public appetite for higher taxes or increased debt, public asset monetization is a way to support future prosperity. It is a model that should be considered in Nova Scotia.

Recommendation 1.20

The government should undertake a full inventory of Nova Scotia's public assets, including intangible assets (e.g., data), followed by a well-qualified assessment to determine how best to enhance their public value. Public value should be understood as protection of the public interest, revenue maximization, and improved services to citizens.⁶⁷

The first essential step in public asset recycling for investment is asset management, beginning with an inventory of all public assets – tangible and intangible – followed by a realistic assessment of value. Fenn provides a step-by-step guide.

Fenn's ideas include the creation of an infrastructure investment fund, where government could invest funds raised through asset monetization for later reinvestment in new infrastructure. As a related benefit, the development of such a fund could also foreshadow a new approach for investing the gains from offshore resources – as Norway does with North Sea oil revenues and Alberta with oil and gas royalties.

At present, Nova Scotia's royalty regime lacks transparency and consistency across most sectors. Although addressing royalties is beyond the scope of this review, stakeholders said it is critically important for the province to develop a modern royalty regime that harnesses the benefit of resource development for future generations. A comprehensive review of Nova Scotia's royalty regime should be a priority in preparation for future offshore potential or any other resource-based expansions.

Revenue integrity

There is no doubt that a simplified tax system is a critical element for an improved economic climate, but so too is improved integrity in the revenues of the province. Nova Scotia is losing too much money to unpaid fines, fees, taxes, and other outstanding bills. If the province is to meet its fiscal obligations and maintain the credibility of its tax system, it must address the problem of revenue integrity. In this case, the lack of integrity does not suggest anything nefarious, but the results are the same – Nova Scotians' money is going missing.

The government must be more aggressive and coordinated in the pursuit of those who owe the province money. It needs to move to a centralized, coordinated, and more-robust corporate receivables initiative that builds on the shared-services model and the recent move of the collections unit to the new Department of Internal Services.⁶⁸ The problem seems aggravated by a decentralized model of collections and divergent operating systems. Government write-offs over the past five years ranged from a low of \$6 million to a high of \$38 million. In the past two years, \$10.5 million and \$12 million were written off, respectively.

Nova Scotia needs a revenue management system that is streamlined and simple, focuses on customer service, and optimizes value for taxpayers. The province may again look to BC for a model that has been designed to maximize revenue collection within the principles of fairness and equity, integrate revenue streams from across government, improve the cost effectiveness of government collection methods, increase multi-channel service delivery, improve customer service, and maintain the government's high standard of privacy and security protection.

To kick-start this process, government should implement a cash and revenue management project, eliminate the interdepartmental collections fee charged by the collections group, and, with limited exceptions such as student loans, systematically roll all collections into the centralized structure.

Recommendation 1.21

Provincial debt collection should be better coordinated across government, and collections enforcement activities centralized.

Underground economy

On a similar note, the underground economy presents an enormous challenge. Underground economic activities create an unfair advantage for businesses that do not pay their fair share of taxes

The underground economy takes many forms. Statistics Canada divides it into three categories: hidden, illegal, and informal.

The hidden sector is the most prevalent and is defined as economic activity that is productive and legal, but deliberately concealed from public authorities in order to avoid taxation and mandatory payments such as employment insurance as well as legal requirements such as minimum wages and health and safety standards. It includes economic activity that is both under-reported and unreported, such as undeclared tips, under-the-table building and construction activities, hidden rent, and skimming, which is under-reported revenue or over-reported expenditures.

The illegal sector includes trade in unlicensed tobacco and alcohol, as well as revenue from activities such as prostitution and illegal drugs. There are generally two revenue streams in these activities: smuggling/distribution and retail sales.

The informal sector of the underground economy, while almost as widespread as the hidden sector, does not generate nearly the income. The informal sector often includes home-based child care and other private household services, such as cleaning and personal care services, and the direct sale of agricultural and some other products.

The underground economy is particularly prevalent where cash transactions are common, such as the hospitality industry, automotive repairs, and construction, including home renovations. The underground economy exists because consumers believe they are getting a cost "break" and providers are pocketing a larger profit by avoiding taxes and other legal requirements.

Concern about the underground economy comes from across society. Legitimate businesses must compete on an uneven playing field, health and safety concerns are heightened in situations where workers have little or no protection, and consumers may be liable for work-related incidents and have no recourse for shoddy or incomplete work. According to Statistics Canada, the underground economy in Canada was estimated at 2.3 per cent of GDP in 2011. At that rate, in Nova Scotia the underground economy is worth almost \$900 million; and the province is losing more than \$100 million a year in taxes.

The federal government collects most of the province's taxes, so collaboration between Nova Scotia and Ottawa is essential to tackle the problem. Enhanced tax compliance strategies should be canvassed with the federal government at the earliest opportunity. A public awareness campaign should also be considered, reminding Nova Scotians that we are all hurt when taxes are evaded.

Recommendation 1.22

Working with the federal government, Nova Scotia should redouble efforts aimed at making sure that every Nova Scotian is paying his or her fair share for public services. This could include a strategy to combat the underground economy, broader and stronger penalties for non-compliance with the tax laws, and a public awareness campaign highlighting the social costs and risks of the cash economy.

Tax Recommendations

Recommendation 1.1 – Hold the line on spending

Nova Scotia should freeze program spending at current levels, with adjustments for already-committed collective agreement obligations, bringing the provincial budget close to balance in 2015–16. Provincial surpluses in subsequent years should be allocated primarily to personal and corporate tax reductions and one-time costs of transformational change in government.

Recommendation 1.2 – Shift taxation toward consumption

Nova Scotia should restructure its tax system to shift revenue emphasis away from high personal and corporate income taxes, toward more revenue from consumption taxes such as HST, while protecting poor and low-income Nova Scotians.

Recommendation 1.3 – Broaden consumption taxes

Nova Scotia should eliminate rebates for the provincial portion of the HST on printed books; children’s clothing, shoes, and diapers; feminine hygiene products; residential energy; and first-time home purchases. Nova Scotia must offset the impact of a broader HST base with increases to the Affordable Living Tax Credit and reforms to the Heating Assistance Rebate Program (HARP).

Recommendation 1.4 – Reduce Personal Income Tax (PIT)

The province should reduce personal income taxes by increasing the Basic Personal Amount to \$11,000 and increasing the Dependent Amount by the cost of living.

Recommendation 1.5 – Eliminate bracket creep

PIT should have a built-in cost-of-living adjustment to eliminate so-called bracket creep.

Recommendation 1.6 - Eliminate the top bracket

The highest income bracket, 21 per cent on income over \$150,000, should be eliminated.

Recommendation 1.7 - Eliminate and simplify personal income credits

The Volunteer tax credits and the Healthy Living tax credit should be eliminated, as should the Seniors provincial income tax refund.

Recommendation 1.8 - Eliminate disincentives to work

The Department of Community Services should redesign its income support systems with a goal of eliminating all disincentives to work. Income support and income taxes need to work in concert to ensure that low-income Nova Scotians are not financially disadvantaged by going to work. A significant portion of 2017–18 transformation funds should be earmarked for investment in low-income supports for the working poor – in particular for poor families with children – including an expansion of the Nova Scotia Child Benefit.

Recommendation 1.9 - Reform rates and simplify the PIT

Nova Scotia's personal income tax rates should be reduced over time. Efforts should be made to flatten the steep taxation curve and simplify the rate structure by collapsing the two upper brackets. The targeted preferred rate for the new upper bracket would be 17 per cent. (Current rates are 16.67% and 17.5%.)

Recommendation 1.10 - Revise Corporate and Small Business taxes and remove barriers to growth

The province should raise the small business tax threshold to \$500,000 from the current \$350,000 and should over the next five years incrementally raise the small business tax rate to 8 per cent from the current 3 per cent. The increased revenue should be used to gradually lower the general corporate income tax rate, which at 16 per cent is the highest in Canada, to 13.5 per cent in an incremental revenue-neutral tax reform measure.

Recommendation 1.11 - Eliminate the New Small Business Tax Holiday

The New Small Business Tax Holiday should be eliminated.

Recommendation 1.12 - Change the approach to corporate tax expenditures

- Corporate tax expenditures should be analyzed within the same parameters as any other business support initiative. That includes cost-benefit analysis

to determine if they are meeting their public policy objectives, determining their effectiveness and efficiency in creating incremental economic activity and jobs, and assessing their impact on the broader economy.

- All business tax credits should be targeted in scope and of limited duration; only those that demonstrate success through a mandatory, comprehensive evaluation should be extended.
- Sponsoring departments should have budgetary accountability for corporate tax expenditures.
- The province should ensure greater transparency in business support programs by publishing annually a list of direct business support programs and any related spending, including companies receiving direct financial support and the quantum of that support.

Recommendation 1.13 – Reform the Film and Digital tax credits

- The regulatory framework and detailed elements of both the Nova Scotia Film Tax Credit and Digital Media Tax Credit should be better aligned with similar tax measures in other Canadian jurisdictions.
- Film and Creative Industries Nova Scotia should be solely responsible for the administration of both tax credits.
- Industry and the province should use the period leading up to the sunset of the two credits in 2020 to determine the most effective tools to help grow the creative economy in Nova Scotia and transition the tax credits to departmental expenditure programs that are transparent, accountable, and focused on economic growth.

Recommendation 1.14 – Ensure that Nova Scotia businesses fully benefit from SR&ED tax credit

The province should work with the federal government and the CRA to respond to concerns raised by industry that the current SR&ED tax credit is not administered consistently across the country.

Recommendation 1.15 – Reform the Equity Tax Credit

The province should consider doubling the annual limit for eligible ETC investments to \$100,000 from the current \$50,000. Consideration should be given to targeting the ETC to strategically defined high-growth sectors, such as information technology and clean technology, to be defined by regulation. As well, eligibility requirements must be critically re-examined to ensure that Nova Scotians are receiving best value from these tax credits.

Recommendation 1.16 - Pursue a regional and/or pooled equity tax credit

Nova Scotia should pursue interest across the region for expansion of the ETC to a regional tax credit as part of a larger regional harmonization strategy. The province should also consider allowing pooled investment funds to be eligible for the ETC.

Recommendation 1.17 - Put in place a Pollution Tax regime

Nova Scotia should phase in the implementation of a pollution tax regime over the next 10 years. The tax should be revenue neutral to the province, with all available revenue earmarked to provide generous support to low-income families as well as overall corporate and personal income tax relief.

Recommendation 1.18 - Establish a Tax Working Group

The province should establish a Nova Scotia Tax Working Group – including government, academic experts, and tax professionals – to review tax policy and options and make recommendations to government on an ongoing basis.

Recommendation 1.19 - Legislate a 10-year tax agenda

The province should legislate a 10-year tax reform agenda, which commits to a series of incremental yearly tax reforms as provided for in this review, in order to provide certainty and predictability to Nova Scotian citizens and business.

Recommendation 1.20 - Secure full value for public assets

The government should undertake a full inventory of Nova Scotia's public assets, including intangible assets (e.g., data), followed by a well-qualified assessment to determine how best to enhance their public value. Public value should be understood as protecting the public interest, revenue maximization, and improved services to citizens.⁶⁹

Recommendation 1.21 - Coordinate collections

Provincial debt collection should be better coordinated across government, and collections enforcement activities centralized.

Recommendation 1.22 - Tackle the underground economy

Working with the federal government, Nova Scotia should redouble efforts aimed at making sure that every Nova Scotian is paying his or her fair share for public services. This could include a strategy to combat the underground economy, broader and stronger penalties for non-compliance with the tax laws, and a public awareness campaign highlighting the social costs and risks of the cash economy.

Section Three: Regulation

Modern Regulation— How Do We Get There?

Put in place a culture of prospective and retrospective reform

"... governments can be much better and do much better, it they make people's lives easier and get rid of unnecessary complexity"

Simple: The Future of Government by Cass Sunstein, 2012

Good regulation is essential for economies to function efficiently and to meet important social and environmental goals. Achieving good regulation is a demanding task that is never completed. This review will not dwell in detail on the question of why government regulation needs attention, improvement, and modernization. The answer, simply if not succinctly put, is to make dealing with government easier, faster, less expensive, less frequent, and more transparent.

Reference will be made to jurisdictions where good work has been done to further these aims. There is a wealth of evidence from academic and other sources that bolsters the case for better government through regulatory reform. Many of these sources, and the experience in leading jurisdictions, point a direction for Nova Scotia.

The fact is, governments regulate. Many argue that they over-regulate. Still others advocate for more regulation. This review avoids the ideological divide between "big" and "small" government. The reality is, governments have a responsibility to protect the citizens for whom they work from an array of risks. They have an equal responsibility to serve those same citizens effectively and efficiently. For government, these two imperatives come into daily conflict, and that conflict will frequently manifest itself in the question To regulate or not to regulate?

The right choice, at the risk of being trite, can be summed up as "regulate when necessary, but don't necessarily regulate." Most governments, and Nova Scotia's is no exception, need to get better at regulation – better at understanding the full impact of regulations, better at determining the costs and benefits in economic and human terms, better at regulatory impact analysis (RIA), and much better at drafting clear regulations in language that the citizens and businesses that are affected and must comply will understand.

Governments need to discover the alternatives to regulations, including the subtle or not-so-subtle "nudge" that can be effective in changing behaviour for the better.⁷⁰

There is no doubt that regulations are required when less-prescriptive means of protecting citizens are not options. That said, the regulatory authority must always be used wisely, and government must fulfill its ongoing responsibility to look back and revise or eliminate regulations that have lost their effectiveness or do not meet

appropriate service or efficiency standards. Likewise, government must look forward to anticipate future regulatory improvements and the potential for modernization.

How – the operative question of this review – do governments go about determining what regulations are working and which have outlived whatever usefulness they once had? Much of what follows responds to that crucial question. And, as Cass Sunstein, author of the best sellers *Nudge* and *Simple: The Future of Government*, writes in the latter, “a key question is whether particular rules should be revised, simplified, strengthened or eliminated in light of what we learn about what those rules are actually doing.” The regulator’s job is not done once even the most fully analyzed, vetted, and tested regulation is enacted. Governments need to track the regulation’s impact in the real world, be flexible, and correct previously undetected issues, even if that means lifting the regulation and heading back to the drawing board.

According to MIT economist Michael Greenstone, former chief economist at the US Council of Economic Advisers, “the single greatest problem with the current system is that most regulations are subject to cost-benefit analysis only in advance of their implementation. This is the point when the least is known and any analysis must rest on many unverifiable and potentially controversial assumptions.”⁷¹

In January 2011, focusing directly on the issue of regulatory simplification, President Barack Obama called for a government-wide “retrospective analysis” and required agencies to produce, in short order (120 days), preliminary plans for such an analysis. The plans to streamline and eliminate many regulatory requirements were made public for commentary. Those plans were finalized within 80 days. The US federal government is enormous. That it could get that job done in 200 days sets the bar high.

Obama’s instruction to “weed out regulations that aren’t contributing to the health and public safety of our people”⁷² should be an exemplar for Nova Scotian efforts. Government needs to concentrate on health, safety, and consumer and environmental protection. Otherwise, get out of the way. Focus also allows government to direct scarce resources to meaningful uses.

Regulatory excellence comes from the integration of a core culture of retrospective analysis in which departments demonstrate a willingness and readiness to improve and simplify the rules they have created. Successful and well-functioning Nova Scotia organizations are flexible, and they adapt to changing realities and new information becoming available. Their government must follow their lead.

Acknowledge the cost and impact of regulation

The need for regulatory reform has been highlighted by numerous stakeholders, business organizations, and government leaders for well over a decade. In fact, the current Nova Scotia government’s 2013 platform committed to:

“The secret of change is to focus all of your energy, not on fighting the old, but on building the new.”

Socrates

create a fair and competitive environment for business by engaging in a responsible comprehensive review of taxes, regulations and fees, guided by principles of simplicity and fairness. All regulations will be tested for their efficiency and effectiveness. Regulations that protect Nova Scotians will be strengthened, wasteful and redundant regulations will be cut.

The issue is not if Nova Scotia needs regulatory reform but rather how to deliver regulatory reform in a cost-effective, sustainable, and comprehensive way.

In 2011, Canadian small and medium-sized firms spent on average 36 hours per year and a total of approximately \$4.76 billion complying with regulations.⁷³ Using GDP share as a proxy, the cost to Nova Scotian small and medium-sized businesses for regulatory compliance can be estimated at \$119 million annually.

Regulatory burden is particularly hard on small enterprises. The CFIB's 2010 report *Prosperity Restricted by Red Tape* says businesses with fewer than five employees pay five times more per employee in compliance costs than do larger businesses.⁷⁴

The CFIB has estimated the annual "red tape" cost to Nova Scotians at \$747 million (2013), which was 1.9 per cent of the provincial GDP.⁷⁵ For a province of fewer than one million people, in financial peril and economic torpor, that's too much.

As stated throughout, this review is about **How**. Why has been established many times, most recently by the Ivany Commission. "Why change?" The answer is a given in Nova Scotia: If we go on as we are, the future won't be any better and will almost certainly be worse than the present.

The OECD notes that by negatively affecting economic performance, excessive and ineffective regulation lowers living standards, reduces consumer choice, slows down job creation, and hampers the development of healthy communities.⁷⁶

Nova Scotia has a limited number of levers available to initiate, accelerate, and support economic growth. The fiscal position of the province precludes massive public spending to attract and expand economic opportunities. The province does have a highly skilled workforce, but it also has an aging population, and at present, much youthful talent and energy is heading for greener economic pastures. Many of those young people would stay, and new Nova Scotians would move in, if the province could offer greater economic promise.

A modern regulatory environment is key to an economically prosperous future. As William Eggers writes in *Government 2.0*, "The cost of doing business in a given jurisdiction is one of the most important factors influencing a company's location choice – and the jobs and the tax revenues that go with it. Cities and states that provide a climate congenial to wealth creation will flourish; those that don't will languish."⁷⁷

Governments need hard evidence to know for themselves, and to prove to others, that they are providing a climate congenial to job creation and economic prosperity.

Anecdotal evidence that programs are working and that spending is effective isn't good enough.

Given the \$700-million-plus yearly cost of compliance, the regulatory burden associated with doing business in Nova Scotia requires action. This is not to suggest that the province should become a regulation-free wild east. Rather, this province should set its sights on being the most efficient (and cost-effective) creator and manager of regulations in the country, if not the world.

Aspire to be better, smarter regulators

The best-regulated environments have the laws and regulations in place to protect the health and welfare of both the natural environment and citizens from unscrupulous practices. Those regulations are straightforward and have undergone RIA. They have been subjected, before enactment, to the wisdom of the citizenry. Compliance requires a minimum of time, money, and effort. Once regulations are enacted, their real world effects are monitored for unanticipated negative consequences, which are then corrected.

KPMG International's 2013 report for the Mowat Centre, *The Future State 2030: Global Mega Trends Shaping Governments*, states that current characteristics of typical regulatory regimes include "regulation that is frequently cumbersome, out of date, or fails to adapt to a rapidly changing *raison d'être*." Future characteristics of leading regulatory jurisdictions look very different: "Regulation is robust, necessary, sufficient and able to anticipate emerging global and national regulatory needs."⁷⁸

Those are fairly accurate descriptions of where Nova Scotia is, and where it needs to be. The goal is leaner, smarter, more effective, more transparent regulation – easy to understand and to comply with.

The OECD's Council on Regulatory Policy and Governance offered in 2012 its best advice: Governments should conduct systematic program reviews of their stock of significant regulations against clearly defined policy goals, including consideration of costs and benefits, to ensure that regulations remain up to date, cost justified, cost effective, and consistent, and that they deliver intended policy objectives. Further, the OECD said that governments should regularly publish reports on the performance of regulatory policy and reform programs. The reviews must identify and eliminate or replace regulations that are obsolete, insufficient, or inefficient.⁷⁹

Smart regulations will protect and advance the public interest and promote a fair and competitive market economy; they are evidence-based, accessible, understandable, and responsive.⁸⁰

Smart regulatory design advances the efficiency and effectiveness of regulation by determining that the benefits of regulation justify its costs and that regulation is timely, creates or enhances policy coherence, and minimizes overlap inside government as well as for those entities being regulated.⁸¹

"We try to solve all our problems with more regulations. It has to stop."

Nova Scotian at roundtable discussion

“Interfacing with the Nova Scotia government is painful.”

Nova Scotian at roundtable discussion

Be cognizant of the history of regulatory reform in Nova Scotia

Nova Scotian governments going back almost two decades have recognized that the regulatory regime in the province is out of hand; it needs reform and a revisionary housecleaning.

Since 2000, there have been three distinct initiatives to improve the regulatory environment for Nova Scotian businesses and individuals. Not coincidentally, since 2000, preceding the current administration, there have been three governments (two Conservative; one NDP) guiding these undertakings. It is worthwhile to learn from these efforts.

The most obvious lesson is that, for a variety of reasons, they lost steam. The province is therefore once again looking for ways to cut red tape, lift the burden of regulation, improve administration, streamline bureaucracy, and become more user-friendly. That all these euphemisms and more can be and are applied to the same process suggests a broadly held opinion that the province suffers from over-regulation, regulatory inefficiency, or worst, ineffective regulation.

Previous efforts – beginning with the Red Tape Reduction Task Force in 2000, continuing through the Better Regulation Initiative (BRI) launched in 2005, and on to Better Business in 2010 – all took aim at inefficient regulatory administration and ineffective regulation.

The task force approach in 2000 was directed from the Treasury and Policy Board by a small dedicated secretariat. It combed through 150 laws and more regulations looking for opportunities to streamline or eliminate them. In its final report, the task force said elimination of regulations that have outlived their usefulness, duplicate other regulations, or are simply unnecessary should become routine government business.

Following up on the task force, in 2005 the province embarked on a broad government-wide BRI with a five-year mandate. It is not entirely clear why a five-year horizon was established rather than an enduring internal business practice, as the previous task force had suggested. Nevertheless, having measured positive results, the BRI is generally regarded as a success.

The BRI created a coordinators committee, which reached across government’s regulatory structure, and a steering committee of senior officials, chaired by the deputy minister of Treasury and Policy Board. Annual reports on progress added the merits of transparency and accountability.

The Business Registry Initiative claims some impressive accomplishments, including an overall 20 per cent reduction in the administrative burden that regulations place on Nova Scotian business, and first-time-ever performance standards: a 10 day turnaround for government-issued permits and licences.

The BRI trained regulatory compliance officials; collected federal, provincial and municipal demands on businesses in one place – an online application called BizPal; and developed a corporate (government-wide) regulatory management policy that all departments were expected to implement. Departmental implementation rates are not available.

The policy framework built around the BRI provided departments and agencies with a reference on when and how to enact regulations, and when to look for other solutions.

The BRI policy statement says government committed to

- “regulate in a way that contributes to a prosperous business climate and ensures that citizens, communities and the environment are well protected . . .
- “make it easier to do business in Nova Scotia, to help business comply with regulation, to improve the quality of regulations and to report and demonstrate progress.
- (“Regulate) . . . only when it is demonstrated that government intervention is warranted and other options fail to demonstrate they will address the issue.”

The BRI included alternatives to regulation designed to influence (rather than “govern”) behaviour and generally require less direct government involvement, including economic tools, such as grants and loans, or persuasive tools such as education, information and awareness campaigns, codes, and standards.

Nova Scotia’s BRI policy also provided a step-by-step guide to apply the principles of good regulation. The process included a clear definition of the problem; analysis to prove regulation is warranted; transparency, including consultation with those affected; a cost/benefit assessment; measures to minimize regulatory impact on “a fair and competitive market” and to ensure that regulations are easy to understand, accessible, and enforceable; and ongoing review.

In 2010, the BRI was replaced by an initiative called Better Business, and unfortunately, many of the critical aspects of BRI fell by the wayside. These included a database called the Administrative Reduction Tracking System (ARTS), which tracked all business-related regulations and quantified the paperwork imposed by each. It was this system that enabled the government to measure and claim a 20 per cent reduction in administrative burden on business. As well, the continued use of policy guidelines and BRI methodology became inconsistent across departments and fell out of use.

Better Business reorganized the previous effort into three parts: Regulatory Excellence, Service Excellence, and Compliance Excellence. In the reorganization, the big change – and mistake – was the new government’s decision to decentralize authority and accountability for various aspects of regulatory reform to “line” departments. Service Excellence, led from Service Nova Scotia and Municipal Affairs, was intended to improve service delivery standards, integrate business services,

and continue to make tangible improvements to forms, applications, and processes. The Compliance Excellence effort was entrusted to a new Department of Labour and Advanced Education, which was charged with “levelling the playing field” for business by ensuring consistent compliance requirements, improved coordination among government inspectors and regulators, and better and more collaboration with business and other stakeholders. Regulatory Excellence remained with a central agency, Treasury and Policy Board, and focused on government-wide reforms and process improvements.

By December 2013, officials reported that regulatory reform had stagnated. Many departments were regulating in “silos,” and regulatory management tools were inconsistently applied. The results: missed opportunities, increased costs of compliance for businesses, the potential for negative impacts on industry and the economy as a whole, a public perception that government is not coordinated, and an overarching and powerful perception that regulatory reform was not a priority.

To their credit, each of the previous initiatives recognized regulatory weaknesses and attempted to address them. Why the efforts lost momentum is easy to understand given the nature of government. Governments change, and with new ministers around the cabinet table come new priorities, or at least new perspectives, on existing priorities. While that is a big part of the answer, it doesn’t tell the whole story. Cabinets and ministers make regulations, but administration and enforcement lies with the permanent government – the bureaucracy. As with many large organizations, the bureaucracy tends toward risk aversion, and the existence of regulations is, for the most part, a lower-risk option than their elimination.

Somewhat discouragingly, during this review, the level of co-operation and enthusiasm from departments was inconsistent. Some actively demonstrated a desire to look for new ways, while others clearly indicated that they believe there is no real need to change processes or approaches to regulatory design or enforcement – that everything was fine and that nothing ever could or would change. For any new regulatory reform to be successful, departmental officials and line ministry personnel must believe that the government is serious about driving regulatory reform and making bold changes.

An understanding of recent Nova Scotia history in regulatory reform – what worked and what didn’t – will be key to ensuring that the mistakes from the past are not repeated and that previous good work can be built upon.

Learn lessons from others

Effective regulation is easy to say and hard to do. It takes sustained effort, consistent attention, and leadership. Regulatory modernization must be driven by leadership across government, and it must be deep and wide in order to embed a whole-of-government commitment.

The good news is that Nova Scotia has the advantage of learning from its own past, and from the experience of others. The province can and should garner insights from demonstrated success in a number of jurisdiction, including British Columbia, Ontario, and Saskatchewan. And it can and should take the best advice from organizations like the OECD, CFIB, and chambers of commerce.

The goal of British Columbia's Regulatory Reform Initiative is "enhancing the lives of all British Columbians by eliminating unnecessary red tape, and minimizing the time and cost for citizens and businesses to access government services or comply with regulatory requirements."⁸²

Since 2001, BC has focused on the development of comprehensive strategies to improve regulatory systems on four fronts:

1. Measuring progress: Reducing and capping the number of regulatory requirements, while maintaining those that protect public health, safety, and the environment.
2. Red tape reduction: Reducing red tape through streamlining, clarifying, and simplifying regulatory requirements and related business processes to reduce the time and cost of compliance and accessing government information and services.
3. Open government and citizen engagement: Establishing a policy of open government and open information to expand access to government information and provide opportunities for citizens to participate in finding solutions.
4. Partnerships: Working with federal, provincial, and local governments to reduce duplication and establish coordinated and efficient processes.

In BC, the government's central regulatory agency is not a gatekeeper or the regulation police, but a facilitator. The key role of the office is to help staff in other departments evaluate whether additional regulation is the right approach, or if non-mandatory, non-regulatory alternatives are possible. Training for staff assigned to regulatory reform in each department is another function, as is offering workshops on plain language, cost-benefit analysis, and outcome-based regulation, to name a few.

Lessons can also be learned from south of the border, where efforts have been made to ensure that modern regulations work in concert with social norms, helping to save lives and money, and to increase compliance with the law, while retaining the certainty that sometimes regulations are not necessary at all.

For example, rather than pass laws or regulations against litter, the state of Texas launched "Don't mess with Texas," a public awareness campaign to reduce litter on highways. In its first year, the campaign resulted in a 29 per cent reduction in litter, and over six years there was a 72 per cent reduction in visible roadside litter. This happened not through mandates, threats, or coercion, but through a creative nudge.⁸³

As Sunstein notes in *Simple*, some non-regulatory “nudges” are more effective when they are clearly identified as such. The pathway to change behaviour must be obvious to people, and any advice or tips must be clear and actionable, and avoid ambiguity, he writes.

Quality advice in the realm of regulation is readily available here in Nova Scotia. Dalhousie law professors William Lahey and Meinhard Doelle have contributed significant insight, particularly on the question of third-party certification and its relationship to regulation. Writing about the often controversial aquaculture industry in Nova Scotia, Doelle and Lahey say:

“Consistent with the goals of maximizing value while minimizing risk and negative social and environmental impacts, we feel strongly that certification with third-party certification bodies that offer industry leading standards and practices should be encouraged. At the same time, we do not feel that it would be appropriate to formally link the regulatory process in a significant way to third-party certification. Rather, the regulatory process should stand on its own, while supporting and rewarding where appropriate efforts by operators to demonstrate leadership through third-party certification that involves industry leading standards and practices.”⁸⁴

Advancing a related but distinct view, Roger Martin, then Dean of the University of Toronto Rotman School of Management, noted that there is an opportunity for a new generation of corporate leaders “to promote the notion that by working together as industries, and by enrolling the support of civil society and government, they can extend and enhance the benefits of economic activity.” Corporate leaders can earn the “social licence” to operate by adopting high standards and organizing widespread industry co-operation, relieving themselves of the burden of regulation, and relieving taxpayers and governments the costs of regulation.⁸⁵

In this vein, Nova Scotia’s regulating departments should continually examine the feasibility of a shift away from provincially established regulatory models to globally recognized ones, such as the Forest Stewardship Council, Marine Stewardship Council, Carbon Disclosure Project, and Extractive Industries Transparency Initiative, especially considering Nova Scotia’s small home market and increasing focus on exports.

While governments alone have the power of regulation, industry and business can clearly lead when they take it upon themselves to set and meet standards at, or superior to, levels imposed by regulators. And so it must be firmly stated that businesses, regulated industries, and corporate leaders have a clear role to play as governments take action to modernize regulation. They can choose to be in the driver’s seat or at the back of the bus.

Use information wisely

One frustration frequently repeated during the course of the review was “Why does the government need to ask us for the same information over and over again?” This problem is not unique to Nova Scotia. In most jurisdictions, the problem of administrative burden is aggravated by the continued use of antiquated means to provide, receive, and process information from businesses. Regulatory agencies have not maximized the use and benefits of information and communication technologies.

Perhaps the best example of a simplified information system can be found in Britain’s “Tell Us Once” service. Good to its name, Tell Us Once, is designed to relieve businesses of onerous and repetitive demands for information. The initiative is expected to save £260 million over the next 10 years.⁸⁶

Learning from this success, provincial departments, agencies, and regulatory authorities should immediately work to harmonize reporting obligations and definitions related to information demands on business. The province can significantly improve its access to reliable information and alleviate a significant burden on businesses through better internal information sharing.

Quality information is useful in other ways, sometimes even as an alternative to regulation. As Sunstein states in *Simple*, “Disclosure of information is a low-cost, high-impact regulatory tool.”⁸⁷ Public disclosure of information such as industrial emissions has often been used to promote accountability and change behaviour. But key to success, according to Sunstein, is ensuring that the disclosure is “concrete, straightforward, simple, meaningful, timely and salient.”

Nova Scotia does not need to reinvent the wheel of effective regulatory practices. Learn from others, make use of national or international standards and guidelines, and right-size the processes for Nova Scotia. Regulatory reform is about better government, not about more government.

Prioritize the highest-impact reforms

As the province begins a review of existing regulations – aimed at eliminating the ineffective, simplifying the onerous, collapsing redundancies, and throwing away the stale-dated – deciding how to start could present problems or produce paralysis. Again, look to the experience of others, and follow a well-worn path.

British Columbia focused on highest-impact regulations in order to achieve early success in reducing the overall regulatory burden. Economic sector representatives and individual Nova Scotians have identified burdensome regulations for years. Many of those regulations may be necessary, but if they are drawing numerous complaints, they must be revisited to determine how to reduce the burden that is the genesis of most complaints.

“Prioritize helping businesses comply. Don’t just post regulations on a website and tell business owners: ‘you should have known.’”

Nova Scotian at roundtable discussion

Embrace regulatory impact analysis

Regulatory impact assessments (RIA) are widely used to measure the benefits and costs (financial, social, and other) of new or amended regulations. These tests allow decision makers to relate the need for a regulation to the assessed risks, costs, and benefits and to compare the effectiveness of non-regulatory alternatives. RIA will assess a regulation's impact on a range of economic factors, including trade, investment, and labour mobility. A pragmatic and realistic approach dictates that the resources invested in regulatory impact assessment increase with the potential impact of the regulation.

RIA should address, at a minimum, the regulation's administrative costs, costs of compliance, and benefits. Existing regulations should be subjected to a modified RIA process, with high-impact regulations receiving more rigorous analysis than lower-impact regulations.

In Ontario, a practical guide to assessing the costs and benefits of regulatory proposals provides a useful step-by-step guide to prepare both preliminary regulatory impact analyses and full regulatory impact analyses.

RIA is an essential tool to ensure the quality of new regulations. A well-functioning RIA system will promote coherent public policy by making transparent the tradeoffs inherent in regulatory proposals, identifying who is likely to benefit from the distribution of impacts of regulation, and how risk reduction in one area may create risks for another area of government policy. RIA improves the use of evidence in policy making and reduces the incidence of regulatory failure arising from regulating where there is no case for doing so, or failing to regulate when there is a clear need.

RIA ensures that regulatory proposals and existing regulations are subject to a transparent, publicly accountable, and rigorous analysis to determine if they are the minimum means of meeting the stated objectives.

Regulatory design, RIA, and compliance assurance are mature processes in jurisdictions leading the way in regulatory reform. British Columbia and Ontario are cited as Canadian examples of advanced regulatory regimes. Internationally, the Netherlands stands out for its integrated risk-based compliance system. All of these jurisdictions provide a solid foundation for Nova Scotia reforms in the months and years ahead.⁸⁸

Fully examine regional opportunities

Regional harmonization is another area that is critical and that could vastly expand the economic and fiscal benefits of regulatory reform.

There is a long history of regional co-operation and collaboration in the Maritime provinces and in Atlantic Canada, but there is no doubt that much more can and should be done. In 2007, APEC hosted a roundtable to discuss ways to harmonize and improve regulatory efficiency. Areas identified as key included transportation, securities, energy,

and food industries. In May 2011, when the Council of Atlantic Premiers agreed to strengthen regional collaboration, regulatory reform was not highlighted.

The 2013 4Front Atlantic Conference and a number of reviews and conversations advanced by APEC have championed a “New East Partnership” to be modelled after the New West Partnership. The New West Partnership Trade Agreement (NWPTA) is an accord among the governments of British Columbia, Alberta, and Saskatchewan that has created Canada’s largest barrier-free interprovincial market.

Under the NWPTA, British Columbia, Alberta, and Saskatchewan were the first jurisdictions in Canada to commit to full mutual recognition or reconciliation of their rules affecting trade, investment, and labour mobility. They removed barriers to the free movement of goods, services, investment, and people. The NWPTA built on the Trade, Investment and Labour Mobility Agreement (TILMA) between British Columbia and Alberta. The NWPTA came into effect July 1, 2010, and has been fully implemented since July 1, 2013.

British Columbia, Alberta, and Saskatchewan have also committed to the following:

- Avoid measures that restrict or impair trade between or through their territories, or investment or labour mobility between them.
- Treat businesses, investors, and workers of the provinces as favourably as they treat their own.
- Recognize or otherwise reconcile unnecessary differences in their standards and regulations.
- Be fully transparent, and notify the others of any proposed measure that is covered by the Agreement. The objective is to ensure that new measures do not create new impediments.
- Honour an enforceable dispute resolution mechanism that is accessible by governments, businesses, workers and investors in order to ensure that each province lives up to its commitments.

Some of the benefits of the NWPTA that would also benefit the Atlantic provinces include the following:

- Labour mobility
Labour mobility provisions allow certified workers to practise their occupation in the three provinces without being subject to additional exams or training requirements.
- Business registration
Businesses registrants in one province are able to seamlessly register in the other provinces at the same time as their original incorporation. All residency requirements are removed.

- Streamlined regulations
Unnecessary differences in business standards and regulations are eliminated.
- Enhanced competitiveness
Allowing goods, services, capital and workers to flow freely across the provincial borders boosts trade, makes it easier for businesses to expand into the other provinces, and lowers costs for businesses and taxpayers.
- Best value for public spending
Open procurement policies with low thresholds help ensure best value for tax dollars. This also creates more opportunities for small and medium-sized businesses to bid on public contracts.⁸⁹

Nova Scotia should champion a New East Partnership – modelled after the New West Partnership. This province should also provide leadership nationally, and champion a federal-provincial-territorial forum on regulatory reform through the Agreement on Internal Trade Regulatory Harmonization Working Group because there is much to coordinate and to work on together right across the country.

Atlantic Canada, or at least the Maritime provinces, should coordinate regulatory reform activities and business information requirements to benefit regional business and encourage regional growth of businesses. Business could gain access to a larger market at less cost, and harmonization could include a single business registry and a single securities regulator with common securities regulations and a wide range of common regulatory standards and requirements, including transportation and agriculture. The recent Atlantic Workforce Partnership demonstrates what can be accomplished when focused attention is given to regional regulatory reform.

Recognize the impact of regulations on individuals

Although much of this review has been focused on the impact of regulations on businesses, it is critical to acknowledge the burdens imposed by regulations on every Nova Scotian, in terms of quality of life and productivity, to name but two. The old adage “time is money” rings true for individual citizens just as it does for businesses. Time has to be taken away from work or family to make application for government benefits or renew licences and registrations. In fact, the CFIB’s 2014 report *Impact of Regulation on Canadian Individuals* estimates that, excluding personal income tax, the value of time spent complying with government regulations is nearly \$1.1 billion.⁹⁰

Second only to preparing, filing, and paying income taxes, Canadians identified applying for or renewing government-issued documents – such as driver’s licence, vehicle registration, health cards, birth/death certificates – as the most burdensome

regulatory procedures they face in terms of time and money. Nearly half of Canadians agree that excessive regulations add significant stress to their lives. This reality makes it incumbent on government to think about the negative impact of government requirements and undertake a risk-based, evidence-based review of the requirements it imposes on individuals. A good starting point for such a review is the area of drivers' licences, vehicle registration, permitting, and inspection, which in Nova Scotia impose a burden on families for which there does not appear to be strong and convincing evidence of safer roads and fewer accidents as a result. One possible reform would be to eliminate the requirement for vehicle safety inspections every two years and on every vehicle coming into the province. Rather, safety inspections could be required at the time of resale.

Nova Scotia should also follow the lead of the federal government, which received a great deal of positive response simply by extending the length of time for passport renewal. If the length of time between renewal of provincial vehicle registrations, licences, and other required documents were doubled – unless there is a compelling case otherwise – the burden imposed on Nova Scotia by those regulations would be cut in half.

Each and every regulation, including those directed at individuals, should rest on evidentiary footing. Each should be subjected to a cost-benefit analysis. Each should be analyzed for redundancy internally and across jurisdictions. Many regulations should be subject to a "reverse onus" test: "We are getting rid of it unless it can be proven to be necessary." Government-wide efforts to focus on risk and the impact of regulations in relation to identified risk will improve the quality of life for Nova Scotians.

Ultimately deliver better government

Nova Scotians and businesses in the province are aware that government can work better. Business people understand, for example, that their customers won't be customers for long if they have to call multiple outlets to get a question answered. Businesses of all sizes and in every sector across this province are constantly looking to improve their processes, their services, their products, and ultimately their bottom line. In recent years, Nova Scotia has made some strides but has a way to go.

Make evidence-based decisions

Regulatory decisions – indeed any government decision – should be supported by evidence. The province should only fund programs that can show solid evidence of success. This is critical given Nova Scotia's fiscal reality but should be government as usual in the 21st century.

In an article titled *Government by Design: Four Principles for a Better Public Sector*, written by Diana Farrell and Andrew Goodman of McKinsey & Company, public sector leaders are called on to favour the rational and the analytical over the purely

ideological, and to be willing to abandon tools and techniques that no longer work.⁹¹ The four principles at the core of the recommended approach:

1. Use better evidence for decision making.
2. Engage and empower citizens.
3. Invest in expertise and skill-building.
4. Collaborate with the private and social sectors.

Better evidence in decision making will include analysis of relevant, credible data – benchmarking Nova Scotia’s performance against that of successful comparative jurisdictions and engaging stakeholders as well as public servants close to the decision. With a body of robust evidence before it, government will be in a better position to design and improve regulatory interventions.

Lessons should certainly be learned from the United Kingdom’s Behavioural Insights team, which uses randomized control trials to test the impact of regulatory and other changes government is considering. Controlled trials have long been a *modus operandi* in health care, particularly drug trials. Importing that methodology into government decision-making processes is catching on in a number of jurisdictions and should be examined as a useful tool for Nova Scotia.

Adopt continuous improvement

Equally as important would be a decision by government to adopt a program of continuous improvement for the public service.

It is inefficient to run an industrial process in such a way that only a product is produced. A process should be operated in such a way as to produce not only a product but also gain information on how to improve the product.

–Box and Draper, *Evolutionary Operation*⁹²

The institutional methodology insights of George Box and Norman Draper are not confined to industrial processes. Indeed, whether the outcome of the process is a product, service, or decision, successful individuals and organizations will gather data throughout in order to continuously improve both the process and the outcome.

“Lean” practices have evolved to become a program of continuous improvement in all kinds of organizations worldwide.

At its core, the lean approach focuses on customer/client value by improving processes to reduce waste and eliminate inefficiencies. Lean is a continuous improvement philosophy that includes value stream mapping and is designed to improve operational efficiencies and find savings. Regardless of the setting in which lean thinking is used, the application of lean is based on five defining principles:

1. Specify value – Define value from a customer’s perspective. Learn what a customer values, and how their experience could be improved to support the best outcome.
2. Identify value stream – Evaluate how all the steps of a process or procedure should be organized to deliver a seamless customer experience; eliminate any steps that do not directly contribute to achieving that goal.
3. Flow without interruptions – Whenever possible, eliminate waste between steps of a process so that a product or service is delivered as efficiently as possible.
4. Customer “pulls” services – Allow the customer to receive or request products or services if and when needed; do not push a product or service that a customer is not ready to receive.
5. Pursue perfection – Continuously adapt to an ever-changing environment and customer needs in order to deliver a product or service of the highest possible quality.⁹³

The most successful lean initiatives are systematic, implemented by employees coached by organization leaders, and consistent with an organization’s mission and strategy, rather than a reaction to a specific condition or event. Taking this approach, the application of lean principles contributes to the creation of an organizational culture in which continuous improvement is the rule and not the exception.

In government, it will be critical to develop in-house expertise in lean process to drive lean initiatives and to coach and train colleagues. By training a core government “lean team” of Treasury Board and key senior officials across government departments, the province could kick-start its program review and generate a new and consistent approach to government transformation and service delivery. Governments around the world are rethinking and re-imagining the way public services are delivered and sustained. A number of governments have fully instituted lean management and are benefiting from early success and public sector engagement.

Get the best value from information and technology investments

In regulatory reform, as in most other initiatives, the government needs to get better at using the assets it has. Nova Scotia has invested millions, possibly hundreds of millions of dollars in information and communications technology. Few in government will claim the province is getting the value it should from its investments. Information technology is more than a tool of regulatory reform; it can be an enabler.

Research conducted by the federal Treasury Board and Employment and Social Development Canada found that in-person transactions cost \$28.80, compared to only 13 cents for the online equivalent. A 2011 study in the UK concluded

that online transactions are up to 50 times cheaper to conduct than in-person transactions.⁹⁴ However, e-government initiatives frequently fall short of cost savings expectations, especially if they do not remove duplicate paper-based or in-person service, or if they fail to appropriately consider those factors in cost recovery.

Governments won't begin to optimize the value of their information and technology investments until they are used much more effectively to engage and empower citizens. In the area of regulatory reform, the question that we must ask is whether "new technology and citizen participation can unleash an era of participatory regulation, where citizens and other stakeholder groups play an active role in designing and enforcing regulations. The idea is that just about every area of regulation today – from air to water quality and food safety and financial services – could benefit from having a larger crowd of informed and empowered individuals helping to protect the public interest"⁹⁵ "Regulatory agencies would need to open up, rethink old processes, and supply the tools and data that citizens would need to contribute meaningfully,"⁹⁶ but it certainly can be done. In fact, it is already happening in some jurisdictions, notably the US Environmental Protection Agency, which has opened its rule-making processes to the public.

Some may question the public's ability to help regulatory bodies better monitor and enforce regulations, but a number of regulatory agencies around the world have been convinced, and so too should Nova Scotia.

Embrace customer service

Embrace customer service – provide easily accessible information such as checklists and information videos to facilitate compliance. Put in place navigation support; a 1-800 line, for example, where questions can be answered so that businesses can understand what is expected of them and can more easily comply with regulation. Finally, consider following the lead of other government entities, such as the US Department of Labor, which has embraced electronic expert advisory systems – available 24 hours a day because they are automated – to provide easily understandable information in a customized step-by-step format, setting out what businesses need to do to comply.⁹⁷

Involve everyone in the reform agenda

Smart organizations also look to employees, who know best how to improve systems and understand what bugs clients and stakeholders. The provincial government needs to get better at engaging provincial public servants, asking employees and citizens what they would do to improve operations.

When it comes to regulatory reform, the people of Nova Scotia don't need to be convinced. The skeptics are mostly in government. As succinctly put by the Mowat Centre,

The greatest challenge in transforming government is not designing new processes or business models. There are many options available. The greatest challenge is creating the institutional culture necessary for new service delivery models to succeed.⁹⁸

As a result, early achievements must be highlighted and recognized government-wide to help government prove to itself regulatory reform works. A Premier's award for Regulatory Reform Excellence could be launched to further this aim.

Establish a robust and structured process to identify and develop specific regulatory reforms

In order to fully drive regulatory reform down to the specifics, the Government of Nova Scotia needs to establish a robust and structured process whereby departments and sector representatives engage in a time-limited, facilitated consultation where areas of priority reform are identified by the sector and suggested responses are brought forward by the department responsible.

A model that can easily be replicated in Nova Scotia has been well tested in Ontario, where ministries and business leaders engaged in an intensive, 60-day effort to establish a joint understanding of five top priorities for regulatory reform. Thereafter, ministries were expected to address these priorities or deliver alternative solutions acceptable to the sector. The co-operative effort delivered results.

Although this review did hear specific areas of suggested reform from a number of sectors and industries, as well as from a few departments, the lack of authority embodied within an external-to-government review process did not allow for a brokered negotiation process to take place between sectors/industries and departments. Based on what was heard in consultations, however, the first economic sectors should include the agriculture and agri-food industries, hospitality, medical technology, and tourism. As well, there should be a focus on small owner-operated businesses such as convenience stores and bed and breakfast accommodations. If frequency of mentions is an indicator, the Workers' Compensation Board is also near the top of businesses' list of agencies that need a look.

Other priority areas for examination, as heard during consultations, should include

- Nova Scotia Liquor Control Act
- the Tourism Accommodation Act and the Innkeepers Act
- Department of Transportation and Infrastructure Renewal regulations – specifically licences for bike trailers, road speeds, tires, and weight restrictions

“Gas regulations in Nova Scotia are the stupidest thing I’ve ever heard.”

Nova Scotian at roundtable discussion

The Department of Environment was another significant focus of commentary during the consultations. The Department should be given priority for implementation of lean practices to streamline its processes. Environment should undertake a systematic review and examine best practices across Canada with regard to risk-based approval processes and international standards, as well as bundling approvals, sequencing of approvals, guaranteed time for processing, and improved customer interaction.

The Department of Natural Resources should be acknowledged for its positive engagement with this review process. Areas of priority examination such as land use could be prioritized in collaboration with sector and industry stakeholders. An examination of the possibility of consolidating the various statutes under which forest land in Nova Scotia can be designated as a protected wilderness area, nature reserve or special place, into a single integrated statute – in order to standardize legislative conservation terms, processes, and administrative responsibilities; clarify the different levels of conservation protection that apply to different conservation designations; and eliminate inconsistencies and unnecessary differences – should be established as a priority reform and undertaken in a timely and structured process.

Nova Scotia’s Utility and Review Board (UARB) was a heated topic of discussion throughout the review, and the province should reconsider the areas of responsibility delegated to the UARB, whose mandate is broader than most other provincial review boards. Petroleum Products Pricing, Halifax bridge tolls, and public passenger busing, for example, are inconsistent with the regulatory scope imposed in many other jurisdictions and should be reviewed by way of cost-benefit, risk-based impact analysis.

The Registry of Regulations and its association with the Office of the Legislative Counsel could be reassessed in an effort to simplify and streamline processes and find efficiencies. Regulations are generally made by delegated officials under the authority of a provincial statute. In Nova Scotia, the Office of the Legislative Counsel is responsible for statutes, and the Registry of Regulations is the central government office responsible for Nova Scotia’s regulations. Could Nova Scotia be better served by a single, unified entity? This certainly deserves a good hard look.

Regulatory Reform Recommendations

Recommendation 2.1 – Put in place a proven structure to drive change

- Publicly commit to regulatory reform at the highest political level. Regulatory excellence must be a government-wide priority driven from the top, by the Premier.

- Name a minister responsible for regulatory modernization and create a single point of accountability with the authority to coordinate regulatory reform government-wide.
- Create a central unit (Office of Regulatory Modernization) to work across government, with oversight authority and responsibility to implement consistent regulatory management government-wide and to drive the sectoral agenda by working with line departments.
- Find and name champions of change in every department.

Central ownership and horizontal management of regulatory reform is the proven structure to drive change across government. Sustained regulatory reform requires strong political leadership. In fact, without such political support, regulatory initiatives are often reduced to a few sectors or one-time regulatory reductions that are easily reversed. Strong political leadership is absolutely essential to overcome resistance and bureaucratic inertia and to prevent a backlash from aggrieved interests.⁹⁹

Recommendation 2.2 – Create mechanisms, including legislation, to sustain the regulatory modernization agenda over the long term

- Enshrine in law a lasting commitment to regulatory modernization by introducing a “Regulatory Modernization and Accountability Act,” following the examples of BC, Saskatchewan, and Ontario. The bill will help focus departmental regulatory modernization efforts into a centralized process and structure.
- Build a centre of expertise in the Office of Regulatory Modernization.
- Develop and broaden in-house expertise in continuous improvement methodology and business mapping. Build on skills already housed in Service Nova Scotia.
- Adopt and apply “Lean practices” as a government-wide methodology to support a culture of continuous improvement. (Recommendation 2.13)
- Get assistance or create partnerships with the federal government and/or other provinces to train staff in essential skills, such as regulatory impact assessment, and draw on the best practices from across Canada and beyond.
- Be clear. Use plain and consistent language in regulations. Put a process in place to ensure that government information and regulations go through a clear language lens.
- The functions of the Registry of Regulations and the Legislative Counsel office that are related to regulations should be integrated and their expertise combined.

“Government should be an ally, not an obstacle.”

Nova Scotian at roundtable discussion

“The answer is speed. Make government work at the speed of business – not the other way around.”

Nova Scotian at roundtable discussion

Recommendation 2.3 – Know where you are going with regulatory modernization

- Set a target for regulatory reform; include a time frame and make it public. (BC's was a 30 per cent reduction in regulatory requirements over three years.)
- Constrain the proliferation of regulations by committing to a zero net increase in regulatory burden, measured against a baseline to be established.
- Establish and launch a three-year plan to deregulate – eliminate ineffective, outdated, or inefficient existing regulations.

Recommendation 2.4 – Create a roadmap to drive change

- Develop a revised Provincial Regulatory Policy, Regulatory Management Policy Guide, and Regulatory Management Training Program by updating and improving previous efforts and incorporating lessons learned from other jurisdictions, to help drive the reform agenda across government.
- Establish a Regulatory Policy Checklist – the federal government and British Columbia provide good examples.
- Adopt a Regulator's Code of Practice to promote a consistent level of service excellence. Ontario's Code of Practice could be modified for Nova Scotia and would provide a good starting point.
- Create cross-departmental/sector teams to identify priority regulatory issues, which if resolved would strengthen each economic sector's success. Create an inventory of regulations to be eliminated or simplified. Determine which regulations should be changed, which can be discarded, which are unenforceable and outdated. Establish a short time frame and expedite this work.
- Mandate departmental engagement with affected citizens and businesses during the development of new regulations rather than conducting consultations after the initial work is completed by departments.

These immediate measures would be led by the Office of Regulatory Modernization, under direction of the Minister Responsible for Regulatory Modernization.

Recommendation 2.5 – Measure progress

- Develop meaningful measures of the overall regulatory burden.
- Establish the baseline from which to measure success. Where is the province today? Create an inventory of active regulations.
- Regularly expand and update measures of regulatory burden and incorporate a regulatory impact analysis into the regulatory process.

Jurisdictions at the leading edge of regulatory reform – the United Kingdom, Australia, Ontario, and BC – have moved well beyond counting proxy indicators of

regulatory efficiency, and now measure direct financial and other burden reductions on business. This example must be followed by Nova Scotia.

Recommendation 2.6 – Give regulatory reform a public profile, report progress

- Produce an annual report detailing the regulatory state in Nova Scotia.
- Create an online registry to ensure that regulatory proposals are published and posted for comment for a minimum of 45 days prior to becoming effective. Encourage business to participate in the regulatory development process and ask for public comment on existing and proposed regulations.
- Make regulation predictable. In addition to seeking advance input and collecting evidence to support evaluation and re-evaluation, the province should enact new regulations on a regular, predetermined schedule, such as twice annually – January 1 and July 1, or two other equally appropriate dates.

Recommendation 2.7 – Make information gathering and government forms simple

Public institutions at every level require people to fill out complex forms before they receive service, benefits, licences, permits, etc. The question must be asked whether all of this information and all of these forms are really necessary?

- The government should direct all departments, agencies, boards, and authorities to test any new forms to gauge the burden they will impose in the real world, and then figure out how to make them simpler. Existing forms should be subjected to the same process as they are renewed.
- Nova Scotia should establish an inventory of information burden. Departments need to work together so businesses and individuals are not asked for the same information, in a variety of forms, many times.
- There should be consistent training on how to simplify forms. Use technology to auto-populate and combine forms where it makes sense.
- The province should move to a true one-window service for all businesses. It needs to redesign web architecture to simplify access to online services for business.
- Nova Scotia should fully adopt the National Business Number program as the standard identifier in order to simplify access to information, permits, etc. The province should provide business with a “tell us once” approach to government interactions. The one-stop-shop service offerings should include directions on how to meet regulatory requirements.
- The province should reinstate the measurement of turnaround times for licences, permits, application processing and completion.

Recommendation 2.8 – Better coordinate inspections

Better coordination of provincial inspection activities and improved information sharing among departments with inspectors will reduce administrative costs and business disruptions.

- Shift the primary initial focus of inspection from enforcement to education, and escalate enforcement for repeat offenders.
- Inspections and compliance audits should be risk-based. The focus of regulators and inspectors should be greatest in those areas where the risks to society are the greatest, and licensing requirements in low-risk areas should be simplified.

Recommendation 2.9 – Do some spring cleaning

- The government should commit to tabling legislation to repeal outdated or inefficient regulations, streamline regulations for more effective enforcement and compliance, and reduce regulatory overlap and redundancies. The target for this legislation should be the spring of 2015 – a regulatory “spring cleaning” – in the form of a multi-departmental omnibus bill that would focus on the efforts of departments. During the development of this legislation, each department would work with stakeholders to identify priority areas of reform that can be undertaken immediately.

Recommendation 2.10 – Drive ongoing reform

- Establish a mandatory review policy that gives structure to, and defines a process for, the regular and ongoing review of legislation and regulations.

For example, in Ontario high-impact regulations undergo mandatory review every 10 years and low-impact regulations every 15 years.

Recommendation 2.11 – Consider alternatives to regulation

- In all cases, as regulations are considered, assess the effectiveness and appropriateness of alternative, non-regulatory, non-mandatory measures.

Nova Scotians, whether the general public, advocates for particular causes, or elected representatives, need to be better informed about regulations, regulatory changes, and, in particular, alternatives to regulation that can be used to protect the public.

Recommendation 2.12 – Make evidence-based decisions

Regulatory decisions must be based on the best available data, analysis, and testing rather than ideological inclination or emotional reaction to events or incidents.

- Regulations must be monitored for their impact in the real world, and unforeseen problems or onerous compliance issues corrected.

- The province should consider field testing regulations before enactment.
- The province should investigate partnering with the university sector to discover sophisticated and reliable methodology to collect regulatory evidence and perform assessments.

Recommendation 2.13 – Adopt a “Lean Practices” continuous improvement process

- The government needs a program of continuous improvement, essential to the provision of quality public services – including effective and efficient regulation – as well as cost containment. Lean practices are proven to promote continuous improvement. A core central group and key senior officials across government should be trained in “lean.”

Recommendation 2.14 – Take advantage of new information technology, an engaged citizenry, and public service

E-government and regulatory reform are a natural fit. In fact, technology is a significant enabler of a great deal of regulatory reform and simplification and can be an essential tool in engaging and motivating citizens in the process.

- Provincial departments, agencies, and regulatory authorities should immediately harmonize reporting obligations and definitions related to the information demands placed on businesses.

The province can significantly improve its access to reliable information and alleviate a significant burden on businesses through better internal information sharing.

- The province should use information technology as the foundation for vastly increased efforts at engaging and empowering citizens to participate in the regulatory or broader governance processes. It should also reach out to public sector employees beyond the senior management level for input and advice.

Recommendation 2.15 – Recognize the burden on small business

Small business is more heavily burdened than larger organizations by regulatory compliance costs. Accordingly, government must make additional, specific efforts to lift the regulatory burden from small business.

- The province should minimize the number of businesses affected by broad-reaching regulations by increasing the threshold to exclude small business as well as any sectors for which the regulations are redundant, unnecessary, or inappropriate.
- The province should ensure proportionality in procedural requirements so that the process requirements are proportional to the impact of the regulation.

- Nova Scotia should examine and adapt an approach similar to the BC Small Business Accord, which sets out principles, actions, and best practices with regard to small business.

Recommendation 2.16 – Pursue regional regulatory harmonization as well as multilevel government coordination

- Nova Scotia should seek agreement among the Maritime provinces to establish a joint secretariat and provincial negotiating teams with clear goals, guidelines, and timelines to negotiate a New East Partnership Agreement modelled after the New West Partnership Agreement. Regulatory and standards harmonization should be the priority, with an early focus on transportation, securities, agriculture, and business regulation. A firm deadline for the successful conclusion, or termination, of this effort should be established.
- The province should establish a working group with federal and municipal representatives and affected stakeholders in specific sectors to identify overlap in regulatory and information demands across the three levels of government and propose remedies that eliminate that burden on citizens and businesses.

Section Four: Fees

Adopt a Standard Costing of Government Services

As noted at the outset of this report, 15 years ago, Voluntary Planning's Fiscal Management Task Force said government needed to consider charging user fees for non-essential services. As a general principle, government user fees should reflect the cost of providing the service.

In October 1998, the "Eurig Estate" decision of the Supreme Court of Canada determined that government user fees must be for cost recovery only. In that case, the Court ruled that probate fees bore no relationship to the cost of providing the service and that such a fee constituted a tax and like any other tax must be introduced and approved by the legislature.

Consistent with the court decision in Eurig, the Government of Nova Scotia takes steps to ensure user fees do not exceed the cost. However, there has been little effort to ensure that fees actually reflect the cost of the service. The starting point for any such effort – or in fact any informed conversation about the appropriate quantum of a fee for a government service – will require the province to gain a much better understanding of the cost of the services it delivers and to adopt a government-wide standard methodology of costing.

The Treasury Board of Canada's *Guide to Costing* is a helpful template. The seven-step process used by the Government of Canada should be adopted in Nova Scotia, government-wide.

Recommendation 3.1

Each department should be required to complete a standard cost analysis associated with all fees. During this review, fees should be frozen.

Once standard methodology is in place and the review is complete, the fee freeze can be lifted.

Aim toward Full Cost Recovery

Recommendation 3.2

In the future, full cost recovery should be the basis of fees. Exceptions are limited, but required in cases where public policy determines that full cost is an unacceptable burden to pass along.

When full costing information is available, there is little doubt that some program efficiencies will be identified and can be realized. This should result in the reduction of some fees, or their elimination should the fee prove too costly to administer. Processes will be identified that can be improved and made leaner in order to bring the service delivery costs more in line with an appropriate fee level.

Departments should be directed to reduce actual costs of individual fees and work together in an effort to bundle charges (fees) for an “event” – e.g., opening a restaurant. Service Nova Scotia should facilitate the work required to bundle fees and should have authority to ensure that this happens across government.

Put in Place Measures to Increase Transparency and Predictability

In response to Eurig, the government of Alberta launched a complete review of user fees. The Fees, Charges and Review Committee issued its final report in June 2000. A number of the recommendations from that review are relevant to an examination of fees in Nova Scotia.

Recommendation 3.3

Fees should be periodically reviewed, and information with regard to fees – including an account of the cost of the service – should be made available to the public.

To ensure and increase accountability and transparency, any proposed charges to fees should be introduced during the annual budget process.

Systems redevelopment costs required for fee-based government services should be included in the fee and spread over the life of the system.

Information with respect to charges, fees, and systems operations should be included in departmental annual expense reports and in public reporting.

Identify Areas Where User Fees Can Be Implemented

The recommendation of the Voluntary Planning Task Force remains as relevant today as it was 15 years ago. During its program review, the province should determine which services it provides meet the criteria for a user fee. When considering or developing a new service, the appropriateness of the application of a user fee should be considered.

Recommendation 3.4

The government, during its program review, should identify services that meet the criteria for application of a user fee, and following a cost analysis, the appropriate fee should be applied. Fees should be applied to new services, where appropriate, when they are initiated.

Fees Recommendations

Recommendation 3.1 – Adopt standard costing analysis

- Each department should be required to complete a standard cost analysis associated with all fees. During this review, fees should be frozen.

Recommendation 3.2 – Aim toward full cost recovery

- In the future, full cost recovery should be the basis of fees. Exceptions are limited, but required in cases where public policy determines that full cost is an unacceptable burden to pass along.
- Departments should be directed to reduce actual costs of individual fees and work together in an effort to bundle charges (fees) for an “event” – e.g., opening a restaurant. Service Nova Scotia should facilitate the work required to bundle fees and should have authority to ensure that this happens across government.

Recommendation 3.3 – Put in place measures to increase transparency and predictability

- Fees should be periodically reviewed, and information with regard to fees – including an account of the cost of the service – should be made available to the public.
- To ensure and increase accountability and transparency, any proposed charges to fees should be introduced during the annual budget process.

- Systems redevelopment costs required for fee-based government services should be included in the fee and spread over the life of the system.
- Information with respect to charges, fees and systems operations should be included in departmental annual expense reports and in public reporting.

Recommendation 3.4 – Identify areas where user fees can be implemented

- The government, during its program review, should identify services that meet the criteria for application of a user fee, and following a cost analysis, the appropriate fee should be applied. Fees should be applied to new services, where appropriate, when they are initiated.

Conclusion

In Nova Scotia, we have the benefit of an economic vision articulated by the Ivany Commission on Nova Scotia's economic future:

Nova Scotia is a dynamic and creative province, with skilled and ambitious people and an entrepreneurial spirit. We are capable of taking bold measures and risks, and of coming together as a unified community to build a better future. We are welcoming of newcomers to Nova Scotia, supportive of our disadvantaged citizens, committed to our students and youth, and champions of our entrepreneurs and businesses. We believe in education, skills and innovation, and we compete and win globally. Nova Scotians have a shared commitment to investing in our people and growing our one economy to build a unified, progressive, innovative, and change-oriented society. Nova Scotia is a small province, but it has tremendous assets – most notably, the capabilities of its people and their spirit and determination to make this province the best place in the world to start and grow a business, live and work, and raise a family.

Nova Scotia can get there, but as the Commission makes so clear, not without significant and fundamental changes.

At its core, this report is founded on a very few inescapable realities: the population makeup of the province is aging; the economy is struggling; and public services cost more than we pay. Those circumstances demand change. This report offers how.

This report is based on a fundamental premise that continuing down the road we are currently travelling will continue to negatively impact Nova Scotians – financially, economically, and socially – for years to come.

Nova Scotians cannot expect younger, numerically smaller generations of income earners to carry a heavier income tax burden than did their more numerous predecessors. They simply cannot, and will seek out opportunity elsewhere. They will have little choice.

A shift in revenue emphasis from income to consumption and pollution can arrest, even reverse, the coming download of tax burden on younger Nova Scotians.

Conventional wisdom has always been that income taxes are progressive and consumption taxes regressive. Convention wisdom won't save Nova Scotia. It is time to turn such thinking around. The regressive nature of consumption taxes can be corrected. Nor is it progressive to shift the tax burden – and the debt load that exacerbates the problem – from many older established citizens to fewer, younger Nova Scotians who are trying to establish their careers, their families, and their lives.

Without fundamental change to our tax structure, that's what will happen – there is no other road to travel.

But if we are willing to accept change, Nova Scotia's prospects will brighten dramatically.

The review and recommendations above draw heavily on the insight of leading experts and positive experiences in other jurisdictions. While this is reassuring, common sense will take us to the same place. It did during consultations with Nova Scotians.

Nova Scotia needs to be more attractive to business, and that means lower corporate taxes and a more efficient regulatory environment. The province needs to be an inviting place for entrepreneurial risk-takers, dreamers, and innovators.

This province has to shift its reality and how others perceive us. A difficult, but honest, commitment to fiscal responsibility, and taxing consumption and pollution rather than a primary dependence on income tax, will take us there. The collective fortitude to tighten the public purse strings, not for a year or two but until we are paying fully for the services we need, will set the province's direction squarely toward fiscal stability and growing economic opportunities.

Taxing pollution is not only the way of the future, it sends a loud message that the people of Nova Scotia are ready to meet that future head on and are no longer prepared to leave a mess for children and grandchildren to clean up once we are gone.

This report asks a great deal of government. The recommendations, as has been said, will not be popular. Everyone will find something they dislike. But fair-minded Nova Scotians will also find a hard truth. Without public support, the recommendations in this report will remain just that – recommendations.

So the report asks more of Nova Scotians. It asks us all to step up and take up the collective challenge before us. "Change will not come if we wait for some other person, or if we wait for some other time. We are the ones we've been waiting for. We are the change that we seek." That was a rallying cry from Barak Obama. Even if the results may have fallen short of the promise in his Presidency, it is the sentiment backed up with real and meaningful action that Nova Scotia needs, and if it is realized today, our province will already be on the way to a better tomorrow.

While travelling across Nova Scotia, talking to citizens, I heard the resolve of Nova Scotians. I also saw, once again, the beauty and good that is Nova Scotia. I thought about a parent and child standing on the shore, somewhere along the thousands of kilometres of coast, or beside one of the hundreds of pristine lakes. The child doesn't wait, but plunges into the water, fearlessly. Does the parent do the same, or hold back, apprehensive about the water's temperature? A moment of decision, of truth.

We are, all of us, at a moment of decision. The truth is undeniable. We will take the risk, and there will be some short-term discomfort, maybe even a shock. But in the long run, we will be better for it, and our children will respect us and thank us for it.

List of Recommendations

Taxes

Recommendation 1.1 – Hold the line on spending

- Nova Scotia should freeze program spending at current levels, with adjustments for already-committed collective agreement obligations, bringing the provincial budget close to balance in 2015–16. Provincial surpluses in subsequent years should be allocated primarily to personal and corporate tax reductions and one-time costs of transformational change in government.

Recommendation 1.2 – Shift taxation toward consumption

- Nova Scotia should restructure its tax system to shift revenue emphasis away from high personal and corporate income taxes, toward more revenue from consumption taxes such as HST, while protecting poor and low-income Nova Scotians.

Recommendation 1.3 – Broaden consumption taxes

- Nova Scotia should eliminate rebates for the provincial portion of the HST on printed books; children’s clothing, shoes, and diapers; feminine hygiene products; residential energy; and first-time home purchases. Nova Scotia must offset the impact of a broader HST base with increases to the Affordable Living Tax Credit and reforms to the Heating Assistance Rebate Program (HARP).

Recommendation 1.4 – Reduce Personal Income Tax (PIT)

- The province should reduce personal income taxes by increasing the Basic Personal Amount to \$11,000 and increasing the Dependent Amount by the cost of living.

Recommendation 1.5 – Eliminate bracket creep

- PIT should have a built-in cost-of-living adjustment to eliminate so-called bracket creep.

Recommendation 1.6 – Eliminate the top bracket

- The highest income bracket, 21 per cent on income over \$150,000, should be eliminated.

Recommendation 1.7 – Eliminate and simplify personal income credits

- The Volunteer tax credits and the Healthy Living tax credit should be eliminated, as should the Seniors provincial income tax refund.

Recommendation 1.8 – Eliminate disincentives to work

- The Department of Community Services should redesign its income support systems with a goal of eliminating all disincentives to work. Income support and income taxes need to work in concert to ensure that low-income Nova Scotians are not financially disadvantaged by going to work. A significant portion of 2017–18 transformation funds should be earmarked for investment in low-income supports for the working poor – in particular for poor families with children – including an expansion of the Nova Scotia Child Benefit.

Recommendation 1.9 – Reform rates and simplify the PIT

- Nova Scotia's personal income tax rates should be reduced over time. Efforts should be made to flatten the steep taxation curve and simplify the rate structure by collapsing the two upper brackets. The targeted preferred rate for the new upper bracket would be 17 per cent. (Current rates are 16.67% and 17.5%.)

Recommendation 1.10 – Revise Corporate and Small Business taxes and remove barriers to growth

- The province should raise the small business tax threshold to \$500,000 from the current \$350,000 and should over the next five years incrementally raise the small business tax rate to 8 per cent from the current 3 per cent. The increased revenue should be used to gradually lower the general corporate income tax rate, which at 16 per cent is the highest in Canada, to 13.5 per cent in an incremental revenue-neutral tax reform measure.

Recommendation 1.11 – Eliminate the New Small Business tax holiday

- The New Small Business Tax Holiday should be eliminated.

Recommendation 1.12 – Change the approach to corporate tax expenditures

- Corporate tax expenditures should be analyzed within the same parameters as any other business support initiative. That includes cost-benefit analysis to determine if they are meeting their public policy objectives, determining their effectiveness and efficiency in creating incremental economic activity and jobs, and assessing their impact on the broader economy.
- All business tax credits should be targeted in scope and of limited duration; only those that demonstrate success through a mandatory, comprehensive evaluation should be extended.
- Sponsoring departments should have budgetary accountability for corporate tax expenditures.

- The province should ensure greater transparency in business support programs by publishing annually a list of direct business support programs and any related spending, including companies receiving direct financial support and the quantum of that support.

Recommendation 1.13 – Reform the Film and Digital tax credits

- The regulatory framework and detailed elements of both the Nova Scotia Film Tax Credit and Digital Media Tax Credit should be better aligned with similar tax measures in other Canadian jurisdictions.
- Film and Creative Industries Nova Scotia should be solely responsible for the administration of both tax credits.
- Industry and the province should use the period leading up to the sunset of the two credits in 2020 to determine the most effective tools to help grow the creative economy in Nova Scotia and transition the tax credits to departmental expenditure programs that are transparent, accountable, and focused on economic growth.

Recommendation 1.14 – Ensure that Nova Scotia businesses fully benefit from SR&ED tax credit

- The province should work with the federal government and the CRA to respond to concerns raised by industry that the current SR&ED tax credit is not administered consistently across the country.

Recommendation 1.15 – Reform the Equity tax credit

- The province should consider doubling the annual limit for eligible ETC investments to \$100,000 from the current \$50,000. Consideration should be given to targeting the ETC to strategically defined high-growth sectors, such as information technology and clean technology, to be defined by regulation. As well, eligibility requirements must be critically re-examined to ensure that Nova Scotians are receiving best value from these tax credits.

Recommendation 1.16 – Pursue a regional and/or pooled equity tax credit

- Nova Scotia should pursue interest across the region for expansion of the ETC to a regional tax credit as part of a larger regional harmonization strategy. The province should also consider allowing pooled investment funds to be eligible for the ETC.

Recommendation 1.17 – Put in place a pollution tax regime

- Nova Scotia should phase in the implementation of a pollution tax regime over the next 10 years. The tax should be revenue neutral to the province, with all available revenue earmarked to provide generous support to low-income families as well as overall corporate and personal income tax relief.

Recommendation 1.18 – Establish a tax working group

- The province should establish a Nova Scotia Tax Working Group – including government, academic experts, and tax professionals – to review tax policy and options and make recommendations to government on an ongoing basis.

Recommendation 1.19 – Legislate a 10-year tax agenda

- The province should legislate a 10-year tax reform agenda, which commits to a series of incremental yearly tax reforms as provided for in this review, in order to provide certainty and predictability to Nova Scotian citizens and business.

Recommendation 1.20 – Secure full value for public assets

- The government should undertake a full inventory of Nova Scotia's public assets, including intangible assets (e.g., data), followed by a well-qualified assessment to determine how best to enhance their public value. Public value should be understood as protecting the public interest, revenue maximization, and improved services to citizens.

Recommendation 1.21 – Coordinate collections

- Provincial debt collection should be better coordinated across government, and collections enforcement activities centralized.

Recommendation 1.22 – Tackle the underground economy

- Working with the federal government, Nova Scotia should redouble efforts aimed at making sure that every Nova Scotian is paying his or her fair share for public services. This could include a strategy to combat the underground economy, broader and stronger penalties for non-compliance with the tax laws, and a public awareness campaign highlighting the social costs and risks of the cash economy.

Regulations

Recommendation 2.1 – Put in place a proven structure to drive change

- Publicly commit to regulatory reform at the highest political level. Regulatory excellence must be a government-wide priority driven from the top, by the Premier.
- Name a minister responsible for regulatory modernization and create a single point of accountability with the authority to coordinate regulatory reform government-wide.
- Create a central unit (Office of Regulatory Modernization) to work across government, with oversight authority and responsibility to implement consistent regulatory management government-wide and to drive the sectoral agenda by working with line departments.
- Find and name champions of change in every department.

Recommendation 2.2 – Create mechanisms, including legislation, to sustain the regulatory modernization agenda over the long term

- Enshrine in law a lasting commitment to regulatory modernization by introducing a “Regulatory Modernization and Accountability Act,” following the examples of BC, Saskatchewan, and Ontario. The bill will help focus departmental regulatory modernization efforts into a centralized process and structure.
- Build a centre of expertise in the Office of Regulatory Modernization.
- Develop and broaden in-house expertise in continuous improvement methodology and business mapping. Build on skills already housed in Service Nova Scotia.
- Adopt and apply “Lean practices” as a government-wide methodology to support a culture of continuous improvement. (Recommendation 2.13)
- Get assistance or create partnerships with the federal government and/or other provinces to train staff in essential skills, such as regulatory impact assessment, and draw on the best practices from across Canada and beyond.
- Be clear. Use plain and consistent language in regulations. Put a process in place to ensure that government information and regulations go through a plain language lens.
- The functions of the Registry of Regulations and the Legislative Counsel office that are related to regulations should be integrated and their expertise combined.

Recommendation 2.3 – Know where you are going with regulatory modernization

- Set a target for regulatory reform; include a time frame and make it public. (BC's was a 30 per cent reduction in regulatory requirements over three years.)
- Constrain the proliferation of regulations by committing to a zero net increase in regulatory burden, measured against a baseline to be established.
- Establish and launch a three-year plan to deregulate – eliminate ineffective, outdated, or inefficient existing regulations.

Recommendation 2.4 – Create a roadmap to drive change

- Develop a revised Provincial Regulatory Policy, Regulatory Management Policy Guide, and Regulatory Management Training Program by updating and improving previous efforts and incorporating lessons learned from other jurisdictions, to help drive the reform agenda across government.
- Establish a Regulatory Policy Checklist – the federal government and British Columbia provide good examples.
- Adopt a Regulator's Code of Practice to promote a consistent level of service excellence. Ontario's Code of Practice could be modified for Nova Scotia and would provide a good starting point.
- Create cross-departmental/sector teams to identify priority regulatory issues, which if resolved would strengthen each economic sector's success. Create an inventory of regulations to be eliminated or simplified. Determine which regulations should be changed, which can be discarded, which are unenforceable and outdated. Establish a short time frame and expedite this work.
- Mandate departmental engagement with affected citizens and businesses during the development of new regulations rather than conducting consultations after the initial work is completed by departments.

Recommendation 2.5 – Measure progress

- Develop meaningful measures of the overall regulatory burden.
- Establish the baseline from which to measure success. Where is the province today? Create an inventory of active regulations.
- Regularly expand and update measures of regulatory burden and incorporate a regulatory impact analysis into the regulatory process.

Recommendation 2.6 - Give regulatory reform a public profile, report progress

- Produce an annual report detailing the regulatory state in Nova Scotia.
- Create an online registry to ensure that regulatory proposals are published and posted for comment for a minimum of 45 days prior to becoming effective. Encourage business to participate in the regulatory development process and ask for public comment on existing and proposed regulations.
- Make regulation predictable. In addition to seeking advance input and collecting evidence to support evaluation and re-evaluation, the province should enact new regulations on a regular, predetermined schedule, such as twice annually – January 1 and July 1, or two other equally appropriate dates.

Recommendation 2.7 - Make information gathering and government forms simple

- The government should direct all departments, agencies, boards, and authorities to test any new forms to gauge the burden they will impose in the real world, and then figure out how to make them simpler. Existing forms should be subjected to the same process as they are renewed.
- Nova Scotia should establish an inventory of information burden. Departments need to work together so businesses and individuals are not asked for the same information, in a variety of forms, many times.
- There should be consistent training on how to simplify forms. Use technology to auto-populate and combine forms where it makes sense.
- The province should move to a true one-window service for all businesses. It needs to redesign web architecture to simplify access to online services for business.
- Nova Scotia should fully adopt the National Business Number program as the standard identifier in order to simplify access to information, permits, etc. The province should provide business with a “tell us once” approach to government interactions. The one-stop-shop service offerings should include directions on how to meet regulatory requirements.
- The province should reinstate the measurement of turnaround times for licences, permits, application processing and completion.

Recommendation 2.8 – Better coordinate inspections

- Shift the primary initial focus of inspection from enforcement to education, and escalate enforcement for repeat offenders.
- Inspections and compliance audits should be risk-based. The focus of regulators and inspectors should be greatest in those areas where the risks to society are the greatest, and licensing requirements in low-risk areas should be simplified.

Recommendation 2.9 – Do some spring cleaning

- The government should commit to tabling legislation to repeal outdated or inefficient regulations, streamline regulations for more effective enforcement and compliance, and reduce regulatory overlap and redundancies. The target for this legislation should be the spring of 2015 – a regulatory “spring cleaning” – in the form of a multi-departmental omnibus bill that would focus on the efforts of departments. During the development of this legislation, each department would work with stakeholders to identify priority areas of reform that can be undertaken immediately.

Recommendation 2.10 – Drive ongoing reform

- Establish a mandatory review policy that gives structure to, and defines a process for, the regular and ongoing review of legislation and regulations.

Recommendation 2.11 – Consider alternatives to regulation

- In all cases, as regulations are considered, assess the effectiveness and appropriateness of alternative, non-regulatory, non-mandatory measures.

Recommendation 2.12 – Make evidence-based decisions

- Regulations must be monitored for their impact in the real world, and unforeseen problems or onerous compliance issues corrected.
- The province should consider field testing regulations before enactment.
- The province should investigate partnering with the university sector to discover sophisticated and reliable methodology to collect regulatory evidence and perform assessments.

Recommendation 2.13 – Adopt a “Lean Practices” continuous improvement process

- The government needs a program of continuous improvement, essential to the provision of quality public services – including effective and efficient regulation – as well as cost containment. Lean practices are proven to promote continuous improvement. A core central group and key senior officials across government should be trained in “lean.”

Recommendation 2.14 - Take advantage of new information technology, an engaged citizenry, and public service

- Provincial departments, agencies, and regulatory authorities should immediately harmonize reporting obligations and definitions related to the information demands placed on businesses.
- The province should use information technology as the foundation for vastly increased efforts at engaging and empowering citizens to participate in the regulatory or broader governance processes. It should also reach out to public sector employees beyond the senior management level for input and advice.

Recommendation 2.15 - Recognize the burden on small business

- The province should minimize the number of businesses affected by broad-reaching regulations by increasing the threshold to exclude small business as well as any sectors for which the regulations are redundant, unnecessary, or inappropriate.
- The province should ensure proportionality in procedural requirements so that the process requirements are proportional to the impact of the regulation.
- Nova Scotia should examine and adapt an approach similar to the BC Small Business Accord, which sets out principles, actions, and best practices with regard to small business.

Recommendation 2.16 - Pursue regional regulatory harmonization as well as multilevel government coordination

- Nova Scotia should seek agreement among the Maritime provinces to establish a joint secretariat and provincial negotiating teams with clear goals, guidelines, and timelines to negotiate a New East Partnership Agreement modelled after the New West Partnership Agreement. Regulatory and standards harmonization should be the priority, with an early focus on transportation, securities, agriculture, and business regulation. A firm deadline for the successful conclusion, or termination, of this effort should be established.
- The province should establish a working group with federal and municipal representatives and affected stakeholders in specific sectors to identify overlap in regulatory and information demands across the three levels of government and propose remedies that eliminate that burden on citizens and businesses.

Fees

Recommendation 3.1 – Adopt standard costing analysis

- Each department should be required to complete a standard cost analysis associated with all fees. During this review, fees should be frozen.

Recommendation 3.2 – Aim toward full cost recovery

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Notes

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