2.17 Tax Expenditures

Introduction

Programs offered by the Province are normally outlined in the Estimates and approved by the Members of the House of Assembly as part of the annual budgetary approval process. However, the Province offers a number of programs which use various tax revenues that are not part of this annual budgetary approval process. These deductions and exclusions reduce tax revenue otherwise due the Province and are commonly referred to as tax expenditures. Tax expenditures could be defined as foregone tax revenues, due to special exemptions, deductions, rate reductions, rebates, credits and deferrals that reduce the amount of tax that would otherwise be payable.

Tax expenditures in our Province are used to provide financial assistance to certain groups of taxpayers or to provide economic incentives to encourage specific program initiatives. Tax expenditure programs have comparable economic impacts as direct spending programs and affect the financial position of the Province in a similar manner. However, tax expenditure programs and direct expenditure programs are not presented to the House of Assembly in the same way in the annual budgetary approval process. The Estimates provide detailed information on direct expenditure programs to the line item category level of expenditure and related revenue classifications. However, information included on current account revenues in statements and exhibits shows the net amounts for each revenue classification only. There is no information provided on foregone tax revenues.

Scope and Objectives

We performed a review of tax expenditure programs in place for the fiscal year 31 March 2004.

The objectives of our review were to:

- Identify the various tax expenditure programs in our Province and, where possible, obtain an estimate of the annual cost to the Province of the various tax expenditures; and
- Examine and assess the processes in place for the approval, monitoring, evaluation and reporting of Provincial tax expenditure programs.

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Conclusions

The Province offers a significant number of tax expenditure programs; however, details of the impact of the various tax expenditure programs are not provided to Members of the House of Assembly as part of the annual budget approval process. We identified approximately $215.5 million of foregone revenue resulting from these tax expenditure programs. Tax expenditures affect the financial position of the Province in the same way as direct expenditures under normal spending programs. Reporting tax expenditures to the House of Assembly would provide information that the Members require in order to hold Government accountable.

There is currently no process in place to formally set target objectives for tax expenditure programs which would facilitate the measurement and monitoring of the results of the programs against desired objectives. As a result, no information is provided to the House of Assembly on the effectiveness of these programs.

Findings and Recommendations

Reporting Tax Expenditure Programs

Based upon discussion with officials of the Department of Finance and a review of available information, we identified various tax credits, benefits and rebates related to programs administered by the Department. Where possible, we obtained the latest available estimate of the annual cost to the Province of the various tax expenditures. We identified these items in such tax categories as personal income tax, corporation income tax, gasoline tax, health and post secondary education tax, provincial sales tax and tobacco tax.

A summary of Provincial tax credits, benefits and rebates with annual cost estimates identified during our review is contained in Figure 1.

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Figure 1

Estimated Annual Impact of Tax Credits, Benefits and Rebates ($ Millions)

Tax Category	Estimated Annual Impact	
Personal Income Tax credits, benefits and rebates		
Non-refundable tax credit block:		
Basic personal amount	37.7	
Age amount	9.7	
Spouse or common law partner	14.8	
Eligible dependent	6.0	
Infirm dependents amount	0.1	
CPP contributions	19.0	
EI premiums	10.7	
Pension income amount	3.6	
Caregiver amount	1.0	
Disability amount	1.7	
Disability amount transfers	1.6	
Interest on student loans	1.3	
Tuition/education amounts	7.4	
Tuition/education amounts transfers	6.8	
Transfers from spouse or common- law partner	2.7	
Medical expenses	5.7	
Charitable donations	10.2	
Total - non-refundable tax credit block	140.0	*2001 tax year - final*
Other tax credits:		
Dividend tax credit	5.0	
Overseas employment tax credit	1.4	
Foreign tax credit	1.2	
Direct equity tax	0.2	
Political contributions tax credit	0.1	
Total - Other tax credits	7.9	*2001 tax year- final*

Figure 1 (cont.)

Benefits and rebates:		
Newfoundland and Labrador child benefit	8.2	
Low income HST credit	6.0	
Low income seniors benefit	7.5	
Home heating fuel rebate	1.1	
Total - benefits and rebates	22.8	*2004 fiscal year - actual*
Total - Personal Income tax credits, benefits and rebates	**170.7**	
Corporation Income tax credits:		
Scientific research and education tax credit	2.8	
Film and video tax credit	1.0	
Foreign tax credit and political contributions tax credit	0.1	
Manufacturing and processing tax credit	10.6	
Small business tax rate	17.2	
Total - Corporation Income tax credits	**31.7**	*2001 tax year - preliminary*
Other Provincial taxes:		
Gasoline tax rebate	1.2	*2004 fiscal year*
Gasoline tax exemption	8.8	*2003 fiscal year*
EDGE refund	1.3	*2001 tax year - final*
Sales tax rebate - Labrador home construction	0.5	*2004 fiscal year*
Tobacco tax - Labrador border zone rebate	1.3	*2004 fiscal year*
Financial corporations capital tax	0.0	
HAPSET	Not available	
Exemptions relating to the Provincial component of HST	Not available	
Total - Other Provincial taxes	**13.1**	
Grand total of tax expenditures	**215.5**	

Source: Department of Finance

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As the Figure indicates, tax expenditure programs cost the Province $215.5 million and represent a significant amount of foregone revenue.

Members of the House of Assembly would initially be aware of various programs as a result of the legislation being approved in the House of Assembly. Where a tax expenditure initiative is new, the budget document may provide an estimate of the amount of revenue foregone in the initial year of implementation. However, details of the impact of the various tax expenditure programs are not provided to Members of the House of Assembly as part of the annual budget approval process.

Three Canadian jurisdictions - Saskatchewan, British Columbia and the Government of Canada do disclose details of their major tax expenditure programs in their budget documentation.

Figure 1 shows that although there are small business exemptions available under the Financial Corporations Capital Tax, there are currently no amounts shown for businesses in the Province which fall into the small business category. Therefore, officials should consider whether this program is achieving what was originally intended.

We selected the following tax expenditure programs to assess the processes in place for the approval, monitoring, evaluation and reporting of the program:

- Economic Diversification and Growth Enterprises (EDGE) Program;
- Film and Video Industry Tax Credit;
- Gas Tax rebates and exemptions; and
- Corporate Income Tax credits for small business, manufacturing and processing, and research and development.

Our review indicated that there is currently no process in place to formally set target objectives for these programs which would facilitate the measurement and monitoring of the results of the programs against desired objectives. For each program we were informed that, although results are tracked on an ongoing basis, internal program reviews occur only on an ad hoc basis. As a result, no information is provided to the House of Assembly on the effectiveness of these programs. We were informed that there is a planned accountability framework under review at the Newfoundland and Labrador Film Development Board, which administers the Film and Video Industry Tax Credit. The framework is intended to include established objectives against which actual performance could be measured and reported.

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Recommendations

The Department of Finance should determine all of the Province's tax expenditure programs, compile information on each of the programs and provide the information to Treasury Board Secretariat for inclusion in the Government's annual budget to the House of Assembly.

The department responsible for a tax expenditure program should establish a process to set target objectives which would facilitate the measurement and monitoring of the results of the programs against the desired objectives. Resulting performance against these objectives should be periodically reported to the House of Assembly.

Department's Response

Figure 1, which purports to be a table of tax expenditures, includes a number of credits and deductions which the Department considers to be part of the core tax system and should not be classified as tax expenditures.

The Department of Finance agrees that publication of an annual report of tax credits, deductions, benefits and rebates will help to achieve greater accountability and transparency. Additionally, while the effectiveness of tax expenditure programs are reviewed on an ad hoc *basis, the Department of Finance, in consultation with relevant line departments, will consider means to formalize this process.*