

May 25, 2023

Hon. Chrystia Freeland
Deputy Prime Minister and Minister of Finance
Government of Canada
90 Elgin Street
Ottawa, ON K1A 0G5

Re: **Equalization Program**

Dear Deputy Prime Minister Freeland:

Thank you for your May 15, 2023 response to my letter regarding the Equalization Program in which I had requested that the fiscal capacity cap be removed from the Equalization formula and that the cost of delivering public services be taken into account in Equalization.

Our government would like to acknowledge the technical changes to the program that were announced in the 2023 Federal Budget may have some benefit to Newfoundland and Labrador in future years. However, these changes do not address the significant concerns that our province has with the program, as outlined in my letter to you in January of this year as well as in our Premier's letter to you in May 2023.

Your response to the removal of the fiscal capacity cap states that it is following a recommendation in the 2006 Expert Panel on Equalization and Territorial Formula Financing. While this document recommended the application of the fiscal capacity cap, it also acknowledged that there were concerns with its implementation. Specifically, the report acknowledged that the inclusion of 100% resource revenues in the cap overstates fiscal capacity because it does not adequately take into account public expenditures associated with resource development and management. Without taking into account these costs, provinces with resource revenue are treated inequitably from those without. Due to data availability issues at the time, this concern was not addressed in the formula. Despite the report's documented issues with the fiscal capacity cap and the data availability issues that prevented the cap from being applied equitably, neither have been re-assessed over the nearly 20 years since the report was developed. In addition, Federal Finance has acknowledged that the fiscal capacity cap can create inconsistent resource revenue inclusion rates in the formula. The varying overall effective resource revenue inclusion rates between provinces results in further inequity.

While I am in agreement that no province receiving Equalization should have a resulting greater fiscal capacity than a non-recipient province, this is only effective if the program is being fair in its calculation. The fiscal capacity cap is currently being applied despite it overstating the fiscal capacity associated with resource revenue. Considering this, along with the other strong reasons the report cites for excluding resource revenue entirely, I request that the fiscal capacity cap be removed entirely.

It is important to note that it is not only Newfoundland and Labrador that has raised concerns with the fiscal capacity cap. Concerns were raised by our province along with others both at the FPT Finance Ministers' meeting in February 2023 and via direct correspondence to you over recent months.

The other issue of concern is our request that Equalization be adjusted to take into account the cost of delivering services. While I would have preferred this to be addressed in the current renewal, I appreciate that it is on the table to be considered for future renewals. Integrating the variable cost of delivering public services is feasible as shown by other countries having incorporated it into their 'equalization' programs. While past efforts to examine this issue have not progressed due to data availability issues, this should be re-examined often as new data and methodologies becoming accessible. To this point, it is noteworthy that the Federal Government has already committed to working with Indigenous groups on incorporating expenditure need into the fiscal policy for Indigenous self-government. Further, we have found instances of Federal Government's work on developing indicators for proximity to services as well as approaches to adjust program funding to account for remoteness. Given how important it is to not only consider fiscal capacity but also the cost to deliver services when ensuring that provinces have sufficient revenues to provide "reasonably comparable levels of public services at reasonable comparable levels of taxation," I request that this work be kept as a standing issue and strongly encourage that we not wait until the next renewal to assess ways in which to incorporate this into the program.

Unfortunately, Newfoundlanders and Labradorians will continue to be disadvantaged until these improvements to the program are made. I look forward to an opportunity to discuss this matter. I am hopeful that we can work together to ensure the Equalization program is implemented in a manner that is fair and equitable to all provinces.

Sincerely,

The Honourable Siobhan Coady
Deputy Premier
Minister of Finance
President of Treasury Board
Minister Responsible for the Public Service Commission
Minister Responsible for the Newfoundland and Labrador Liquor Corporation
MHA for St. John's West