



2008 Provincial Pre-Budget Submission

November 30, 2007



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Executive Summary

The Calgary Chamber of Commerce represents over 3,200 Calgary based businesses. The Chamber seeks to raise the consciousness and quality of public discourse on key policy issues confronting its members and stakeholders, through informed discussion grounded in fact and reasoned analysis.

The Calgary Chamber of Commerce accepts that the 'Alberta Advantage' exists in some respects, but recognizes there is room for improvement. The Calgary Chamber puts forth the following recommendations for government consideration on behalf of its members, the small, medium and large enterprises that are directly affected by the financial planning and spending decisions of the province.

Attracting the Next Wave of Young Talent Through a Competitive Tax Regime

1. Adopt broad-based personal income tax cuts through one of two methods:
 - [1] Increasing the basic personal exemption amount from \$15,435 to \$18,000; or
 - [2] Lowering the current flat tax rate from 10 per cent to 9 per cent.
2. Accelerate the implementation timelines for raising the small business threshold to \$500,000 to 2008 and eliminate or reduce the small business tax beginning in 2008.

Realizing Cost-efficiencies in Alberta Government Programs through Controlled Expenditure Policies

3. Adopt a bandwidth approach to government spending, by targeting expenditure increases within a range delimited by population and inflation growth, and real GDP and inflation growth.

Securing the Alberta Advantage for Future Generations through a Principled Approach to Saving

4. Adopt a vision for the future prosperity of the province, which clearly articulates how resource revenues and the provincial fiscal management framework directly contribute to this vision. As part of this vision, the Chamber recommends that government adopt a principled approach to saving and investing Alberta's natural resource wealth to build on the natural endowments that form Alberta's comparative advantage to secure the future prosperity of all Albertans. The Chamber further recommends that government adopt a multi-year approach to provincial expenditure policies – one that anticipates and responds to program and infrastructure demands over the short, medium and long run.
5. Structure the Heritage Savings and Trust Fund (HSTF) as a true 'trust fund', in which the net income earned on the capital invested is added to the fund rather than automatically transferred into general revenues. The Chamber further recommends that government commit to investing a long-term average of 35 per cent of non-renewable resource revenue in the HSTF and other endowments annually, and that this threshold be legislatively entrenched in the Alberta Heritage Savings Trust Fund Act (AHSTFA), subject to change through binding referendum and consultation with the Board of the Alberta Investment Management Corporation.



6. Adopt a 10 per cent proportion (rather than absolute) rule for annual resource revenue allocations to the Sustainability Fund, to help protect from the volatility of natural resource dependence, and to fund capital projects to help manage growth pressures.
7. Adopt a formula-based approach for setting the Sustainability Fund minimum amount (using economic forecasting) to ensure sufficient funding exists to cover shortfalls due to volatile energy prices.
8. Raise the priority of energy research in the province and create a new endowment called the Alberta Heritage Energy Research Fund (AHERF) under a similar framework as the Alberta Heritage Foundation for Medical Research, and that the AHERF be provided an endowment similar to those of the other research funds, currently at around \$1 billion.
9. Fortify the endowment and special purpose funds with surplus revenues produced in future budgets, automatically committing a proportion to the various endowment funds.
10. That the *Access to the Future Fund* be targeted towards addressing two or three issues that clearly restrict access to post-secondary education, rather than the carte-blanche approach that currently exists.



I. Introduction

The Calgary Chamber of Commerce represents over 3,200 Calgary based businesses. The Chamber seeks to raise the consciousness and quality of public discourse on key policy issues confronting its members and stakeholders, through informed discussion grounded in fact and reasoned analysis.

The Calgary Chamber puts forth this submission on behalf of its members, the small, medium and large enterprises that are directly impacted by the financial planning and spending decisions of the province.

Alberta attracts internationally recognized dignitaries and business leaders due to its reputation as a source of entrepreneurialism and innovation. As the number of global head offices in the province continues to rise, the province is emerging as a leader on the world stage. This is significant for both business and government and, if Alberta is to compete successfully as a global player, it must become 'the best' jurisdiction in Canada in which to live, work, and do business.

The Calgary Chamber of Commerce accepts that the 'Alberta Advantage' exists in some respects, but recognizes there is room for improvement. This pre-budget submission is structured based on three objectives that should be the bedrock of any globally competitive provincial budget:

- (1) Attracting the next wave of young talent through a competitive tax regime;
- (2) Realizing cost-efficiencies in Alberta government programs and institutions through controlled expenditure policies; and
- (3) Securing the Alberta advantage to the benefit of future generations through a principled approach to saving and investing.

II. Discussion

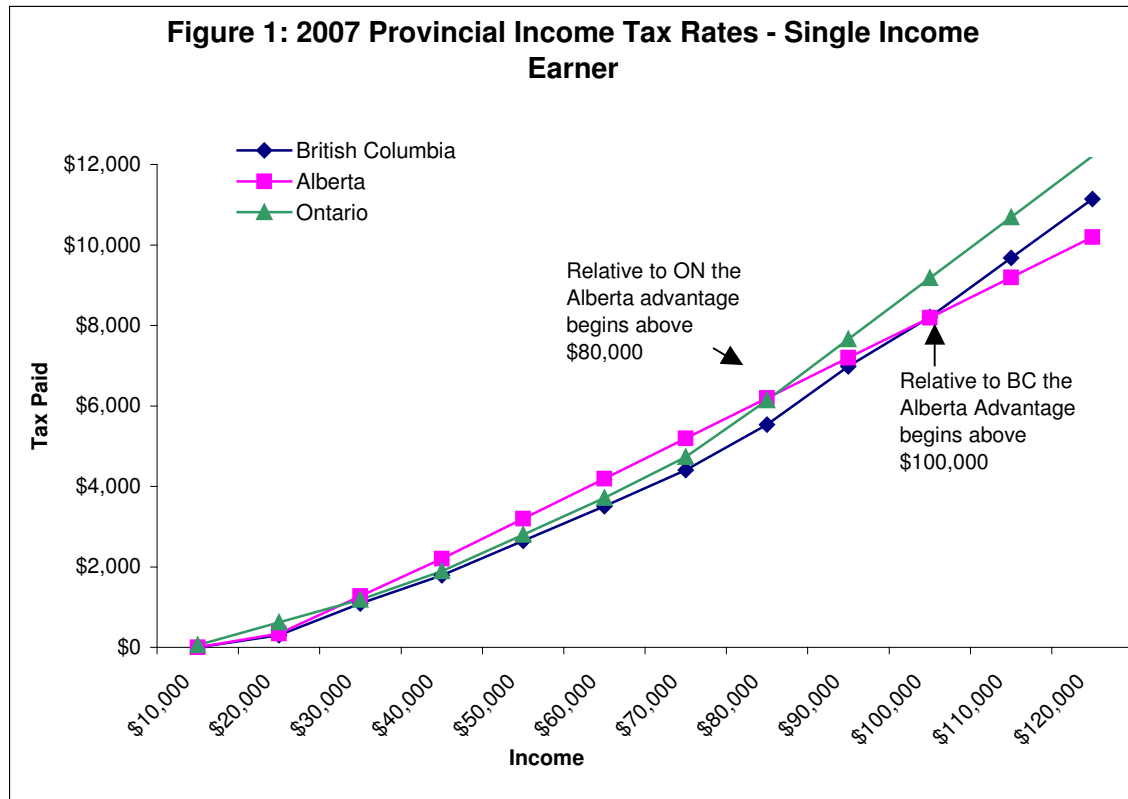
1. Attracting the Next Wave of Young Talent Through a Competitive Tax Regime

In a 2007 survey, Chamber members identified labour shortages and high levels of taxation as major priorities to be addressed.

Through generous personal exemption thresholds and child tax credits, Alberta's personal income tax system is one of the most advantageous in Canada for Alberta families with children. The absence of a provincial sales tax is also of great benefit to all Albertans. While the Chamber appreciates the government's commitment to families and applauds its no sales tax policy, in order for Alberta to attract the next wave of highly mobile, highly skilled young talent, the province's personal income tax regime for individuals needs to be more competitive relative to neighbouring jurisdictions.

In 2007, Alberta's single income earner tax rate was substantially less competitive than both Ontario and British Columbia. Individuals earning between \$20,000 and \$80,000 in Alberta paid more income tax than individuals in Ontario, and individuals earning between \$20,000 and just

over \$100,000 in Alberta paid more than individuals in British Columbia (Figure 1).¹ According to the Chamber's 2008 pre-budget membership survey, the average salaries of over 77% of Chamber members fall within this income range.



Source: Statistics Canada, Alberta Finance

From a tax-to-earnings perspective, Alberta is, therefore, less competitive than both British Columbia and Ontario for the majority of individual income earners. With Alberta forecasted to experience a labour shortage of 100,000 by 2016 (Alberta Employment, Immigration and Industry 2006:5), an effective means by which the government can help attract the next wave of new talent is with broad-based personal income tax reductions for individuals – particularly in relation to British Columbia, with whom Alberta has entered into the Trade Investment and Labour Mobility Agreement (TILMA).

Alberta is the only Canadian jurisdiction that applies a proportional flat income tax rate for all income levels – ensuring fair treatment regardless of employment income. However, Alberta also boasts the highest basic personal exemption amount (\$15,435) and, therefore, exhibits one of the most progressive average tax rates in the country (as income increases, the average tax rate also increases).

In order to preserve the favourable distributional attributes of Alberta's personal income tax regime while improving upon our competitive position within the Alberta-British Columbia economic trading block, the Chamber recommends that government adopt broad-based tax cuts through one of two methods:

¹ It should be noted that 2007 individual income earner tax rates in Alberta, British Columbia and Ontario are all more competitive than those in Saskatchewan at all income levels.



- [1] Increasing the basic personal exemption amount from \$15,435 to \$18,000; or
 [2] Lowering the current flat tax rate from 10 per cent to 9 per cent.

Increasing the basic personal exemption amount from \$15,435 to \$18,000

Increasing the basic personal exemption amount to \$18,000 will improve our competitive position relative to BC and Ontario by narrowing the Alberta-BC tax gap for all personal income levels, and reclaiming the Alberta advantage outright for income levels up to \$30,000 and those levels above \$90,000 (Table 1). The Alberta-BC tax differential would decrease from a high of \$788 to \$532 for an income of \$70,000.

Raising the personal exemption amount would improve the progressiveness of Alberta's tax regime by increasing average taxes with income. The benefits of this option would accrue largely to lower income earners in Alberta, especially employees in the service and hospitality industries.

With the total number of people employed in Alberta estimated at 1,977,100 (Statistics Canada 2007), the Chamber calculates that this proposed change would cost government \$507 million, or 1.4 per cent of 2007-08 government revenues.

Lowering the current flat tax rate from 10 to 9 per cent

Lowering the current flat tax rate would similarly improve Alberta's competitive position relative to BC and Ontario for all income levels. However, the benefit will accrue largely to higher income earners (Table 1). Under this option, Alberta regains its competitive tax position over BC for incomes above \$90,000, and the Alberta-BC tax differential would decrease from a high of \$788 to \$269 for an income of \$70,000.

The Chamber estimates that this proposed change would cost government \$732 million, representing approximately 2.1 per cent of 2007-08 government revenues based on personal income tax revenues of \$7,318 billion, as outlined in Government's 2007 budget (Alberta Finance 2007:46).

Table 1: Taxes Paid – Individual Income Earners					
Income Level	Existing Taxes			Proposed Alberta	
	Ontario	British Columbia	Alberta	Option 1 Increasing Basic Personal to \$18,000	Option 2 Decreasing Flat Tax to 9%
\$10,000	\$57	\$0	\$0	\$0	\$0
\$20,000	\$621	\$304	\$339	\$82	\$305
\$30,000	\$1,186	\$1,090	\$1,271	\$1,015	\$1,144
\$40,000	\$1,890	\$1,787	\$2,204	\$1,947	\$1,983
\$50,000	\$2,798	\$2,646	\$3,193	\$2,937	\$2,874
\$60,000	\$3,713	\$3,511	\$4,193	\$3,937	\$3,774
\$70,000	\$4,734	\$4,405	\$5,193	\$4,937	\$4,674
\$80,000	\$6,138	\$5,535	\$6,193	\$5,937	\$5,574
\$90,000	\$7,656	\$6,985	\$7,193	\$6,937	\$6,474
\$100,000	\$9,174	\$8,204	\$8,193	\$7,937	\$7,374
\$110,000	\$10,691	\$9,674	\$9,193	\$8,937	\$8,274
\$120,000	\$12,209	\$11,144	\$10,193	\$9,937	\$9,174

Bold text indicates a favorable tax burden relative to British Columbia and Ontario.



Small Business Tax

The Chamber applauds the raising of the small business threshold to \$500,000 by 2009 but also recognizes that other jurisdictions are making small business ownership more attractive. Alberta must take further action to be a leader in small business tax reform. Small business tax cuts are being contemplated in both Manitoba and Prince Edward Island, and Manitoba's Premier has promised to end taxation on small business. It is important for the Alberta government to continue to maintain a competitive small business tax environment relative to competing jurisdictions. Therefore, the Chamber recommends that the provincial government accelerate the timelines for raising the small business threshold to \$500,000 from 2009 to 2008, and eliminate or reduce the small business tax, beginning in 2008.

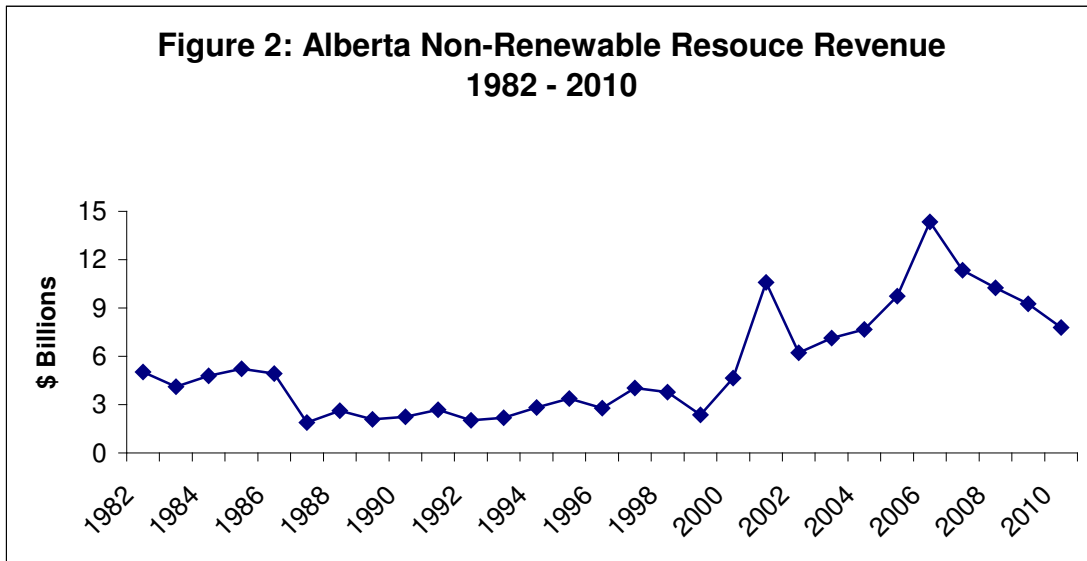
2. Realizing Cost-efficiencies in Alberta Government Programs and Institutions through Controlled Expenditure Policies

Alberta has benefited significantly from the development of its natural resources. Non-renewable resource revenues have contributed at least 30 per cent of total provincial government revenues since 2001, and were as high as 40 per cent in 2005-06.

On average, however, provincial government expenditures have increased beyond the rate of inflation and population growth since 1982 and, in budget 2007, increased by a further 17 per cent – well above the combined rate of inflation and population growth (8 per cent). Per capita government spending in Alberta is the highest of any provincial government (Canadian Taxpayers Federation 2008:10).

However, the government's continued reliance on non-renewable resource revenue for current consumption creates an unsustainable and unhealthy dependence on volatile revenue sources, and distorts incentives to maintain or improve efficiencies in program delivery. It is estimated that the proportion of resource revenue required for government to meet long-term spending obligations between 2001 and 2005 was 55 per cent, up from 44 per cent between 1995 and 2000 (Kneebone, 2005:37). In the absence of non-renewable resource revenues, the government would have been confronted with budgetary deficits every year since 1995 (Alberta Chambers of Commerce and Certified General Accountants Association of Alberta (ACC), 2006:22) and in the event of a sudden forward decline in energy prices, would be challenged to maintain current program and service expenditures without increasing corporate and personal taxes, which represent approximately 30 per cent of total provincial government revenues.

Of further concern, the Alberta Government's non-renewable resource revenues have recently declined from a high of \$14.3 billion in 2006, to approximately \$10.3 billion for the 2007-08 fiscal year, and are forecast to fall further, to \$7.8 billion, in 2010 (Figure 2).



Source: Government of Alberta

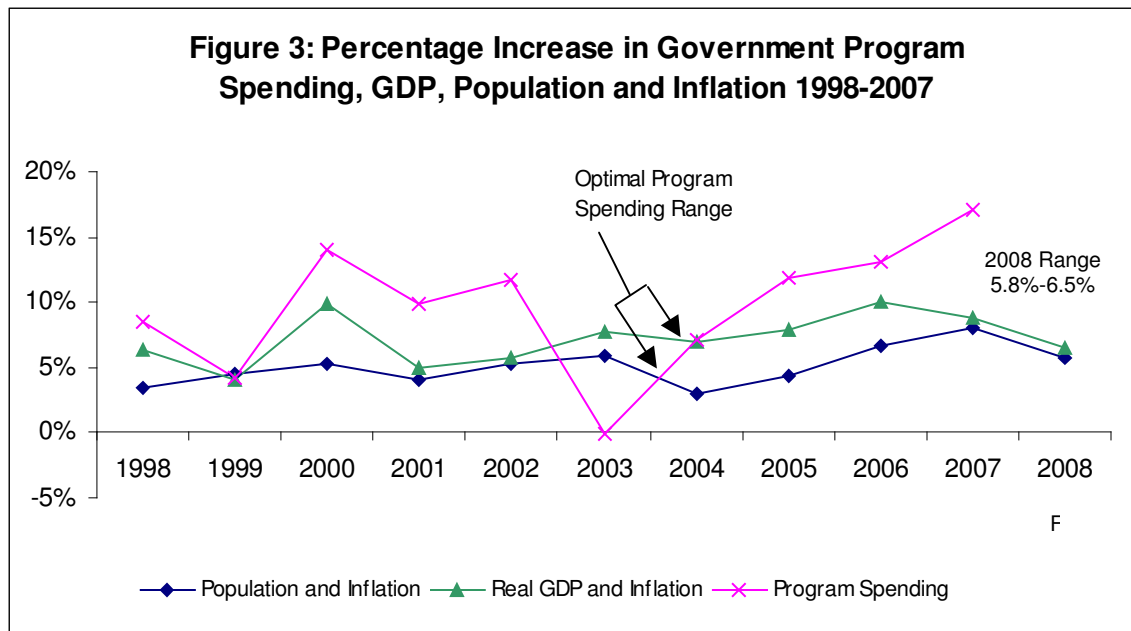
In its 2007 pre-budget submission survey, the Chamber canvassed its membership on the issue of government spending and fiscal management, and found that nearly 60 per cent believe the provincial government is spending unsustainably.

While the Calgary Chamber of Commerce recognizes the importance of maintaining and expanding Alberta's infrastructure to cope with high levels of growth, the message from Calgary business is clear, government needs to control spending. The Chamber, therefore, encourages government to adopt a more sustainable and prudent approach to program expenditures and, in its 2007 pre-budget submission, recommended that government limit program spending increases in line with inflation and population growth.

However, maintaining spending in line with population and inflation growth alone does not necessarily allow government to respond to pressures associated with economic growth, as economic expansions can occur in the absence of population growth and often impose significant strains public services and infrastructure.

Consequently, the Chamber recommends that government adopt a bandwidth approach to government spending, by targeting expenditure increases within a range delineated by population and inflation growth, and real GDP and inflation growth (Figure 3).² For 2008 this range is between 5.8 and 6.5 per cent. This is an ambitious objective, as government has exceeded this target in 7 of the last 10 years; however, it is an objective worth achieving, as nearly 70% of Chamber members indicated that government should manage spending by basing yearly increases on reasonable growth in the economy.

²Real GDP plus CPI inflation is used rather than nominal GDP because nominal GDP presents too volatile of a target for government budgeting purposes.



Source: Alberta Finance and Statistics Canada

3. Securing the Alberta Advantage to the Benefit of Future Generations Through a Principled Approach to Saving and Investing

In its submission to the Alberta Financial Investment Planning and Advisory Commission (FIPAC) the Chamber recommended that government adopt a vision for the future prosperity of the province, which clearly articulates how resource revenues and the provincial fiscal management framework directly contribute to this vision. As part of this vision, the Chamber recommends that government adopt a principled approach to saving and investing Alberta's natural resource wealth; to build on the natural endowments that form Alberta's comparative advantage to secure the future prosperity of all Albertans.³ The Chamber further recommends that government adopt a multi-year approach to provincial budgeting policies – one that anticipates and responds to program and infrastructure demands over the short medium and long run.

The Alberta Heritage Savings Trust Fund

The Alberta Chambers of Commerce and Certified General Accountants Association of Alberta, through their Vision 2020 research, estimate Alberta could deposit between 30 and 40 per cent of all non-renewable resource revenue per year into the *Alberta Heritage Savings Trust Fund* (HSTF) without cuts in current program spending. Other studies, such as the research of the Canada West Foundation (Kneebone, 2006:48), suggest that a 50 per cent savings model is feasible provided there is a binding "effort by government to control the gap between long-term expenditures and tax revenues."

In a recent survey of its membership on the issue of non-renewable resource revenue, the Calgary Chamber of Commerce found that nearly 92 per cent of members believe the provincial

³ The full submission can be viewed at www.calgarychamber.com or [http://www.calgarychamber.com/abcalcoc/doc.nsf/files/B7FA58234EFB99F98725738B006818C5/\\$file/CalgaryChamberFI PAC-Submission.pdf](http://www.calgarychamber.com/abcalcoc/doc.nsf/files/B7FA58234EFB99F98725738B006818C5/$file/CalgaryChamberFI PAC-Submission.pdf)



government should save at least one-third of all non-renewable resource revenues, and 46 per cent believe that savings should be 50 per cent or higher. The Chamber estimates that the HSTF would be valued at over \$128 billion today had the government deposited 35 per cent of non-renewable resource revenue into the HSTF every year since 1976, at 5 per cent interest compounded annually, with the net revenue reinvested.

Consequently, the Chamber recommends that government structure the HSTF as a true 'trust fund', in which the net income earned on the capital invested is added to the fund rather than automatically transferred to the General Revenue Fund. The Chamber further recommends that government commit to investing a long term average of 35 per cent of non-renewable resource revenues in the HSTF and other endowments annually, and that this threshold be legislatively entrenched in the *Alberta Heritage Trust Fund Act* (AHSTFA). Any proposed changes to this threshold, the rules governing the withdraw of net income, or investment objectives, should be subject both to consultation with the Board of the Alberta Investment Management Corporation, and elector assent (through binding referendum provisions such as those contained in the *Alberta Taxpayer Protection Act* and/or the *Constitutional Referendum Act*).

Sustainability Fund and Capital Account

In 2003, the government created the Sustainability Fund under the *Fiscal Responsibility Act* to help "ensure that government spending doesn't rise and fall with volatile energy prices." (Alberta Legislative Assembly, 2003:3). Under the *Act*, \$5.3 billion of all non-renewable resource revenues can be used for general government purposes, but any excess must be transferred to the Sustainability Fund. If actual non-renewable resource revenue is less than \$5.3 billion in any given year, the difference may be allocated from the Alberta Sustainability Fund to the General Revenue Fund.

The Chamber recognizes the importance of protecting the province from the volatility of our natural resource dependence as well as funding capital projects to help manage our growth pressures, and endorses the concept of the Sustainability Fund. However, the Chamber also recognizes and supports the need for a principled approach to the fiscal management of our resource revenues.

It is estimated that the proportion of resource revenue required for government to meet long-term spending obligations between 2001 and 2005 was 55 per cent (Kneebone, 2005:37). If government were to invest 35 per cent of resource revenue into the HSTF and other endowments as recommended above, then 10 per cent of annual resource revenues would be available for allocation to the Sustainability Fund without significantly impacting government program expenditures.⁴ The Chamber, therefore, recommends that government adopt a 10 per cent proportion (rather than absolute) rule for annual resource revenue allocations to the Sustainability Fund.

The uncertainty surrounding world energy markets creates challenges for governments in anticipating future resource revenues. According to the *Fiscal Responsibility Act*, when resource revenues exceed \$5.3 billion at least \$2.5 billion must be held in the Sustainability Fund in anticipation of emergencies, disasters, rebates, First Nation settlements and budget shortfalls. However, such an arbitrary threshold is not necessarily responsive to market conditions and future revenue shortfalls.

⁴ It should be noted the proportion of resource revenue required for government to meet long-term spending obligations increased from 44 per cent between 1995 – 2000, to 55 per cent between 2000 and 2005 (Kneebone 2006:42), an indication that a 55 per cent government dependence benchmark is a generous assumption.



Consequently, rather than establishing a minimum threshold for the Fund, the Chamber recommends that the government adopt a formula-based approach for setting the Sustainability Fund minimum amount, in part, based on economic forecasting techniques. A formula based approach will help ensure sufficient funding exists to cover budget shortfalls in response to volatile energy prices and economic trends that impact Alberta's resource revenues.

The *Fiscal Responsibility Act* has been amended in each of the last three years, with the government spending limit increasing from \$3.5 billion in 2003-04 to \$5.3 billion in 2006-07. In addition to adopting formula based approaches for establishing Fund allocations and thresholds, and in accordance with a principled approach to savings and investment, the Chamber recommends that any subsequent threshold and allocation changes to the Sustainability Fund be subject to consultation with the Board of the Alberta Investment Management Corporation.

Various Endowments

The Calgary Chamber of Commerce strongly supports the contribution that the endowment funds of the Alberta Heritage Savings and Trust Fund bring to Albertans. The funds now include the: Alberta Heritage Medical Research Endowment Fund (AHMREF), Alberta Heritage Science and Engineering Endowment Fund (AHSEEF, or Ingenuity Fund), Alberta Heritage Scholarship Fund (AHSF), and the Access to the Future Fund (AFF).

The purposes of AHMREF, AHSEEF and AHSF are sufficiently clear and have produced successful results over their respective lifetimes. However, the Chamber contends that the mandate of the Access to the Future Fund is overly broad and in need of refinement. Under the current legislation the criteria for payouts are far too general and will result in the depletion of the fund without more concrete restrictions, such as targeting access to underrepresented segments of the population, or resolving infrastructure issues that force post-secondary institutions to turn away qualified students. The Chamber recommends that the fund be focused on addressing two or three issues that clearly restrict access to post-secondary education, rather than the existing carte-blanche approach

The current savings mechanisms of the various funds are also insufficient. The savings mechanisms referred to in the terms of reference are no more than ceilings over which the funds cannot grow. For example, the Access to the Future Fund has a limit of \$3 billion and the AHMREF has an annual contribution limit of \$500 million. As it stands, there are no provisions in the legislation for minimum deposits made to these funds. As these funds are a product of resource wealth the Calgary Chamber of Commerce recommends that they be fortified with surplus revenues produced in future budgets, whereby government automatically commit a proportion of future budget surpluses to the various endowment funds – similar to the government's in year surplus allocation policy of committing one third to savings and investments (Alberta Finance 2007:8).

The Heritage Fund and its endowments are also designed to ensure the long-term prosperity of the Province of Alberta. In addition to its entrepreneurial spirit, Alberta's current prosperity is based on resource wealth and the energy sector. A fund should therefore be established to attract the best and brightest researchers on energy related issues, including alternative energy sources, to secure Alberta's position as one of the world's leading energy producers for generations to come.

The Alberta Government has already identified energy research as a priority. In 2006 when it established the \$200 million dollar Energy Innovation Fund and, under the auspices of the Alberta Science and Research Authority, created the Alberta Energy Research Institute. The Institute, which started as the *Alberta Oilsands Technology and Research Authority* (AOSTRA), is charged



with managing energy research in the province, and is considered one of the reasons that Alberta's oil sands were developed so successfully (Mansell and Schlenker, 2006:50).

Several research institutes have commented on the need for significant investment in energy research going forward. The Canada West Foundation listed among various investment ideas that the government pursue "aggressive research and development on the clean use of fossil fuels," and a "sustainable energy program of research and demonstration projects to ensure that, no matter what the energy future might be, Albertans would be at the front of the pack" (Gibbins and Roach, 2006:17).

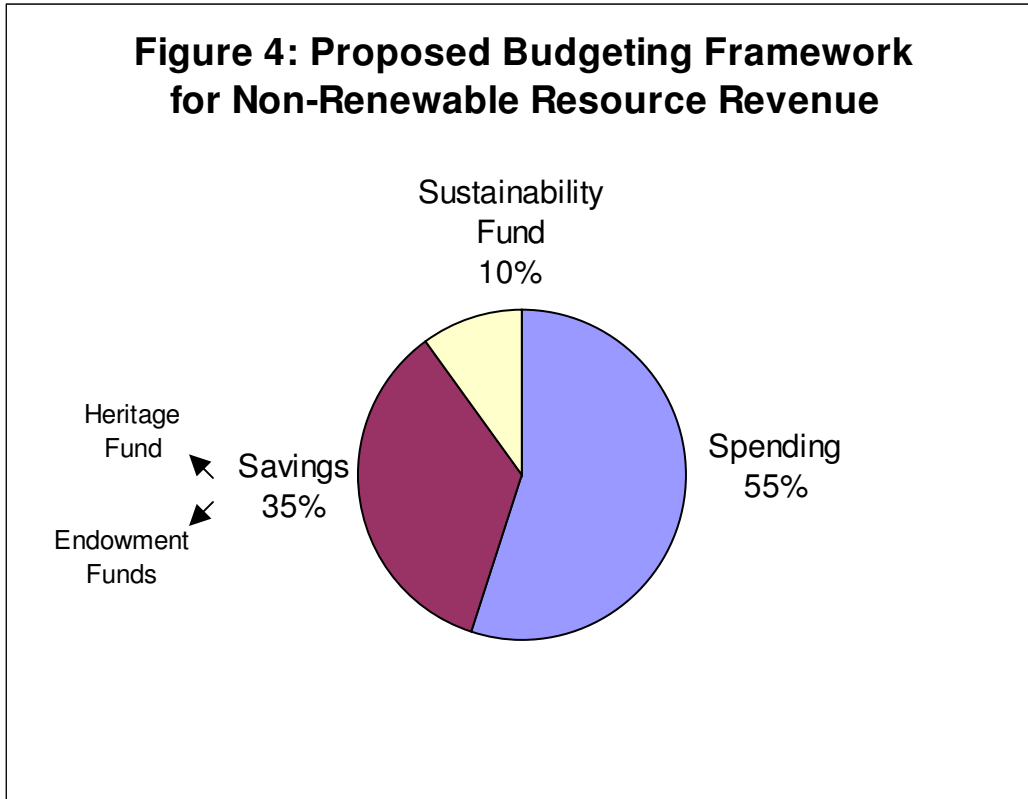
While it is unclear whether the province and industry have provided sufficient support for energy research, relative to other Canadian industries, the oil and gas sector stands to gain substantially from increased investment in research and development (R&D) activities. The level of R&D investment by the Canadian oil and gas sector is small given the size of the industry, and it is estimated that the sector spends approximately \$0.78 for every \$100 of GDP generated, which is one sixth the level of R&D invested by Canada's manufacturing sector (\$4.80 for every \$100 of GDP) (FERENCE, Weicker and Co., 2007).

The Institute for Sustainable Energy, Environment, and Economy (ISEEE) noted that research and investment in the energy sector is about one-third of what it was in the early 1980s and that it will be a "significant task" to bring R&D investment back to levels consistent with the magnitude of the energy opportunities and challenges in the province (Mansell and Schlenker, 2006:50-51).

The Chamber, therefore, recommends that government raise the priority of energy research, and create a new endowment called the *Alberta Heritage Energy Research Fund* (AHERF) under a similar framework to the *Alberta Heritage Foundation for Medical Research*, an arms length body with an appointed multi-stakeholder board of directors that manages the strategic direction of the Fund. The energy research currently taking place under the support of the Ingenuity Fund and the Energy Innovation Fund can then be transferred to the Alberta Heritage Energy Fund, freeing up resources for other, non-oil and gas related research avenues, and contribute to the diversification of research programs in the province.

If Alberta were serious about the "significant task" of increasing energy R&D investment in the province, and securing its future a global player in the energy sector, then AHERF would require an endowment similar to those of the other research funds, currently sitting at around \$1 billion.

A summary of the Chamber's proposed resource wealth allocations is presented in Figure 4.



As Albertans, we should all be aware of the fact that resource revenues are both volatile and finite. For government to spend revenues drawn from our natural resource base is both irresponsible and unsustainable. Government must focus on saving much higher levels of resource revenues and investing them wisely in Alberta's future.



III. Summary of Recommendations

The Calgary Chamber puts forth the following recommendations for government consideration on behalf of its members, the small, medium and large enterprises that are directly impacted by the financial planning and spending decisions of the province.

Attracting the Next Wave of Young Talent Through a Competitive Tax Regime

1. Adopt broad-based personal income tax cuts through one of two methods: [1] increasing the basic personal exemption amount from \$15,435 to \$18,000 or [2] lowering the current flat tax rate from 10 per cent to 9 per cent.
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