



STANDING COMMITTEE ON GOVERNMENT OPERATIONS

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TUESDAY, AUGUST 27, 2024 10:00 AM
DET'ANCHOGH KÚÉ - EAGLE ROOM - YELLOWKNIFE, NT

AGENDA

1. Prayer
2. Review and Adoption of Agenda
3. Declarations of Conflict of Interest
4. In-Camera Matters:
 - a. Disaster Financial Assistance Arrangements Internal Briefing with the Honourable Vince McKay, Minister of Municipal and Community Affairs
 - b. Heritage Fund Internal Briefing
5. Public Matters
 - a. Heritage Fund Public briefing from the the Honourable Caroline Wawzonek, Minister of Finance
6. In-Camera Matters:
 - a. Debrief
7. New Business
8. Deferred Business
9. Date and Time of Next Meeting: Wednesday August 28th 10:00 AM
10. Adjournment



The NWT Heritage Fund Presentation to the Standing Committee on Government Operations

August 27, 2024

Government of
Northwest Territories



Intergenerational Fairness and Resource Revenues

- Non-renewable resources are assets that belong to all residents of the NWT. They are one-time in nature.
- Development and extraction turns those physical assets into revenue and depletes the “inventory” of what’s in the ground.
- If it is spent immediately, only today’s population benefits from it, creating an issue of intergeneration inequity.
- The GNWT has chosen to spread the benefits between today and tomorrow’s generations through two channels on the assets side:
 1. Capital investment and debt repayment
 2. Saving and financial investment: **the NWT Heritage Fund**



When a government is fortunate enough to have resource revenues, it has an issue of intergenerational fairness. Those resources are one-time in nature and should those that live today get all of their benefit from that revenue or should those benefits be spread to future generations as well? Today’s population could have the best or most amount of doctors, nurses, teachers, and civil servants and hospitals and schools, but tomorrow’s generation may not have the means to maintain staffing levels or maintain those buildings. The impact of resource revenues could be a blip over time.

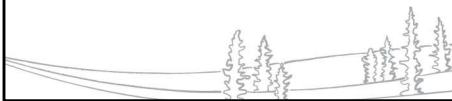
When we extract and sell those resources, the inventory of what’s available is depleted. In terms of our balance sheet, our stock of natural wealth has decreased. When we convert them into dollars, the question then becomes what to do with that money. If we spend it immediately, it has become operating spending. When resource revenue runs out, spending will have to come down as well. It is a temporary arrangement with temporary results. It also creates a volatility within an operating budget as prices go up and down in global markets, another challenge with the benefits of resource revenues.

However, when it is dedicated to the balance sheet to improve assets, the stock of financial wealth increases. The GNWT chose to keep that money out of operating and convert the resource assets into financial and capital assets. When put towards legacy capital, future generations can benefit from the economic spinoffs of that infrastructure as it helps build and develop the economy. Debt repayment prevents interest charges, saving money and reducing the debt burden for both today and tomorrow’s generations. This presentation is about the Heritage Fund, the savings and financial investment mechanism for the GNWT to

convert one-time resource assets into perpetual financial assets that benefit several generations.

The NWT Heritage Fund

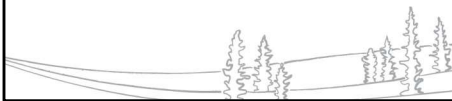
- The Fund's purpose is to save some non-renewable resource revenues for future generations.
 - Non-renewable revenue is also directed to capital investments for legacy infrastructure and debt repayment.
- The Fund is being built up by retaining both contributions and income generated for the first 20 years as principal with no withdrawals allowed.
- Withdrawals can start in 2032/33, subject to limits:
 - maximum of 5% of the year-end balance and the principal is never removed.
- After 2032/33, annual deposits are still considered principal.
- Governed by [Northwest Territories Heritage Fund Act](#) and [Regulations](#)



The NWT Heritage Fund was designed to ensure that a portion of the benefits of today's resource extraction will be saved for the benefit of future generations. There is an initial 20-year lock-up of the Fund's balance (principal and earnings), starting from 2012 when the Fund was established, and allowing deposits and prohibiting withdrawals gives the Fund a head start to build up the principal to a point where it can start generating significant amounts of income in the future. The principal of the Fund can never be withdrawn, so as to ensure perpetual benefits. Starting in 2033, withdrawals from the Fund's earnings will be permitted, so long as the annual withdrawal does not exceed 5% of the Fund's year-end balance.

NWT Heritage Fund Contributions

- Each Legislative Assembly approves the contribution to the Fund through the annual budget.
- Under the *Northwest Territories Lands and Resources Devolution Agreement* the GNWT keeps 50% of resource revenues called the Net Fiscal Benefit and shares 25% of the Net Fiscal Benefit with Indigenous government signatories.
- Since *Devolution*, the annual Heritage Fund contribution has been 25% of the Net Fiscal Benefit after sharing with Indigenous governments signatories.



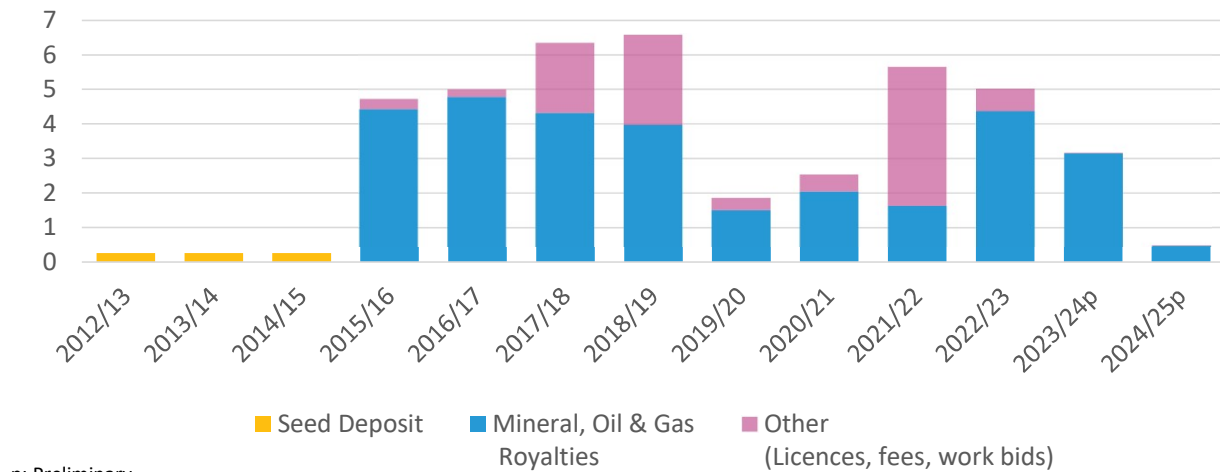
Heritage Fund contributions are made annually. There's space made for them as appropriations in each budget and they are examined and approved by the Assembly every year.

Between the federal government and the territorial government, each keep half of the resource revenues after land claim amounts are removed. The GNWT's half is called the Net Fiscal Benefit and it is subject to a cap. The cap is sufficiently large enough and growing that we have never triggered it and don't expect to hit it in the projection. The GNWT shares 25% of the Net Fiscal Benefit with Indigenous governments that have signed the Devolution agreement.

Since devolution in 2014, a quarter of the remaining Net Fiscal Benefit after sharing with Indigenous government signatories is dedicated to the Heritage Fund as a contribution through the annual budget process.

Contribution History

Heritage Fund Contributions (millions of dollars)



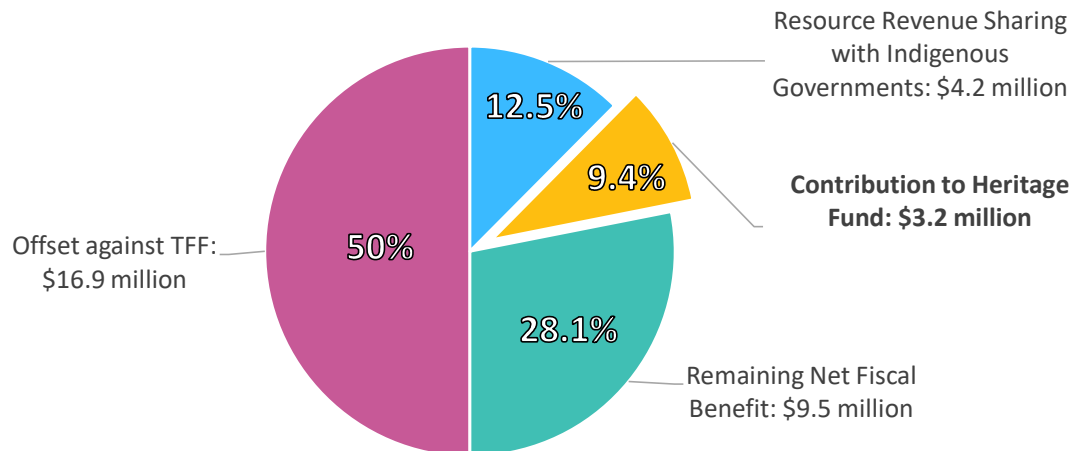
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The Heritage Fund contributions vary depending on the amount of resource revenues received in a year. The first three years were before devolution and seed money of \$250,000 were added annually, which triggered the 20-year countdown until money could be withdrawn from the fund in 2032. Total contributions since devolution are \$40.9 million.

2017/18, 2018/19 and 2021/22 are high due to receiving returned work bids. Work bids are forfeited deposits that companies pay prior to doing any investment. They had bid on certain places to work for oil development. Having these work bids returned shows that companies find it more economical to lose their bid deposits and not put any more capital at risk in our oil fields. They propped up resource revenues in those years but were one-time revenues rather than resource revenues from non-renewable resource development.

Mechanics: Net Fiscal Benefit Allocation

Resource Revenue: \$33.7 million (2022/23)



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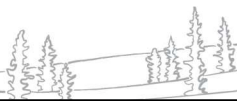
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Here's an overview example of how resource revenues are shared. Half the pie goes to the federal government but that isn't a direct payment. Instead, Canada reduces the amount transferred to us under Territorial Formula Financing and they do it two years later. This lag results in it becoming an interest-free loan for two years, but that means we need to manage our cash to bear in mind repayment down the line.

The other half is the GNWT's Net Fiscal Benefit. Regarding what we do with it, the first step is Resource Revenue Sharing to allocate a quarter of it to Indigenous governments, represented by the blue slice. Then, the yellow slice represents a quarter of the remaining Net Fiscal Benefit. The turquoise slice is what remains after Resource Revenue Sharing and the Heritage Fund contribution. This leftover portion is dedicated to capital and debt repayment. Nothing goes to operating expenses. The Heritage Fund, capital investment and debt repayment all improve the balance sheet and this strategy spreads the benefits of today's economic development of resources to future generations.

Management and Reporting

- The Fund has been managed by CIBC Wood Gundy since April 2019.
- The Fund's investment strategy in the *Act* is to maximize long-term returns without undue risk. The *Regulations* impose several conditions on investments:
 - Acceptable issuers are generally Canadian governments and banks and allowed investments are fixed income (short-term paper, bonds) that meet strict credit quality standards.
 - Equities (stocks/shares) are limited to a maximum of 25% of the portfolio value.
 - Maximums are set so that no single investment can dominate the Fund.
- The financial statements of the Fund are published annually and show the earnings and contributions made during the year, the balance of the Fund, and the change in net assets from the previous year to the current year. ([Public Accounts 2022/23](#), pp. 196-210)



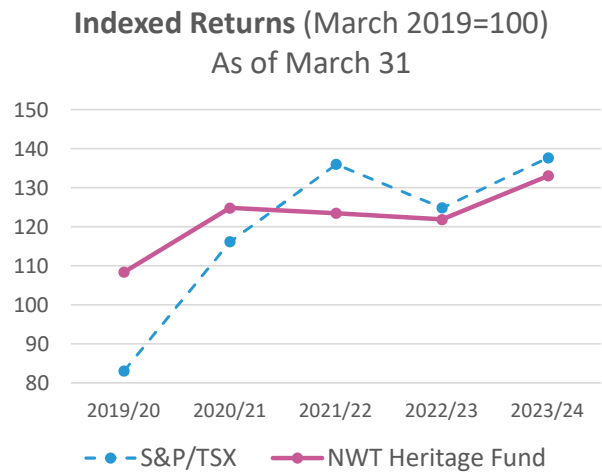
The Department of Finance internally reviewed the Heritage Fund after five years and enlisted CIBC Wood Gundy to manage it to improve returns. The regulations were adjusted slightly to help achieve the Fund's investment strategy, which is maximize returns without taking unnecessary risk. The types of investments are mainly fixed income, which are the safest investments, especially with the strict credit quality thresholds we require, with a 25% maximum exposure to equities to help increase returns.

There are limits to how big any investment can be so it would not dominate the Fund and put the Fund at risk. No single federal or PT government or its entities can have more than \$10M of the Fund. No single bank or municipal government can have more than \$5M invested. The Heritage Fund is structured to be of the highest standard of credit, thoroughly diverse, and a safe place for long-term investment.

The GNWT reports results regularly with the rest of the GNWT's annual reports. You can find the Heritage Fund report in Volume III of the Public Accounts.

Heritage Fund Performance

- Since moving to independent management, **Heritage Fund compounded annual returns are 5.9%** compared to 6.4% for the TSX.
 - Heritage Fund adjusted for deposits (removed).
 - Less volatile than TSX due to focus on fixed income and limited exposure to stocks.



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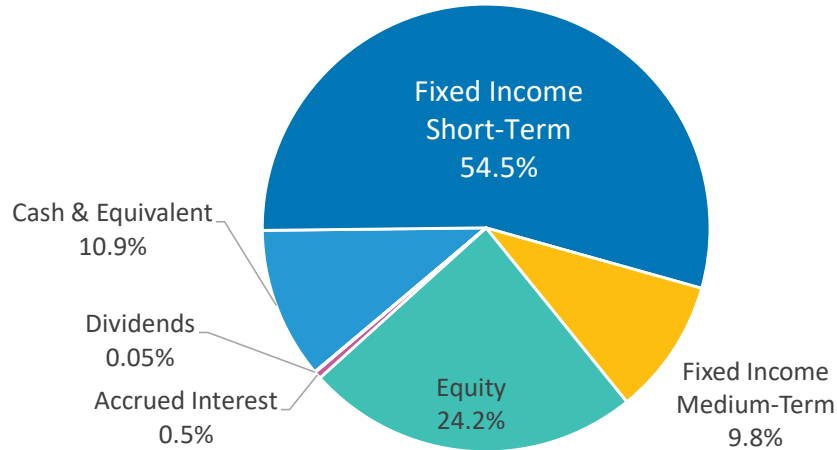
The performance of the Heritage Fund since management was handed to professionals reflects the investment strategy to maximize returns and avoid undue risk of loss.

This slide shows that the Fund is growing as designed, especially compared to the Canadian equities market reflected by the TSX. The growth in the Fund is steady and has less volatility than stocks. The Heritage Fund avoided the severe drop in 2020 due to the pandemic and its lockdowns, remained steady, and increased to such a point where its performance has not been too far from the stock index since 2019 at 5.9% annual returns for the Fund and 6.4% for the TSX. We can expect to be outperformed by the stock market but considering that it hasn't been far behind and has been insulated from those market swings validates the GNWT's approach.

This return doesn't include the annual deposits into the Heritage Fund so that the Fund's performance is measured on its own for a proper analysis.

Current Value: \$48 million

Composition as of March 31, 2024



The unaudited market value at the end of 2023/24 was \$48.3 million, with three quarters of the fund in fixed income investments or cash and a quarter of it in equities. If equities ever grows above its allowed 25 per cent share, the investment manager rebalances the fund to bring it back within regulations to manage its risk.

Heritage Fund Projection

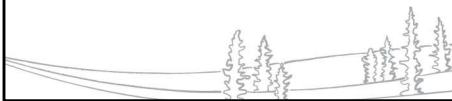
- With continued contributions, investment income and modest return assumptions, the Fund could grow to \$74 million over the next five years, representing compounded annual growth of 8%.
- Projections over 24/25 to 28/29:
 - Contributions +\$12 million, income +\$14 million



Our latest projections estimate that the Fund could increase to \$74 million over the next five years, somewhat evenly split between income earned within the Fund itself and through regular contributions from projected resource revenues.

Legislated 10-Year Reviews

- The *Act* requires a review by the Legislative Assembly every ten years.
- It must include operations of the *Act* and recommendations on spending with public input, oversight, or any amendments.
- The first review is due in the 20th Legislative Assembly.



The Act contains a provision to have the Heritage Fund reviewed in the first session after every ten years. A review will require a look at the operations of the *Act* along with any other recommendations for amendments that may come up. When the Fund can withdraw and spend, that spending will require public input. Amendments can also be made on oversight and management or other administrative issues.

The Legislative Assembly has started the process for the *Act*'s first review.

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