

confederation which poses a very severe problem. As quoted in *The Globe and Mail* of December 3, 1980, in the first week of the last election campaign, he said:

We must face the fact that the federal government is not as able as it should be to manage the national economy, to help overcome regional disparities and to conduct major national policies.

There has grown up a serious fiscal imbalance not only among the provinces, but between the federal and provincial levels of government.

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That fact has also been borne out at some length by the Economic Council of Canada in its 1979 report, which is called, appropriately enough, "Two Cheers for the Eighties". The Economic Council Report for last year—it seems almost prescient in terms of what we are facing now—points out, for example, that projections of surpluses and deficits are extremely sensitive to the projected path of the economy in assumptions about government actions. It goes on to say:

But the persistence of the federal deficit and the Alberta surplus are very clear consequences of the current fiscal structure. This situation stands in marked contrast to the one that prevailed up to 1974, when the revenue-generating powers of the federal government made possible a central distribution system to finance nation-wide policies and to supplement revenues of the provinces with a relatively low revenue base, while leaving the federal government enough room for fiscal management of the economy and programs for economic development.

The issues this development raises are political rather than economic, although the way in which they are resolved will have a bearing on the nature of economic management in the country. The federal government is in a poor position to continue to play its major role in economic management, equalization of provincial revenues, and the conduct of major national policies. In most areas of economic policy, achieving national objectives will require extensive provincial participation, or these objectives may never be met. There is an urgent need for more co-operation. In the longer run, the fiscal structure of the federation will have to be rebalanced and better institutional arrangements will have to be developed to cope with the challenge of interdependence between the federal and provincial governments.

To describe as briefly as possible the problem caused by the exponential growth in resource revenue in the three resource-rich provinces of British Columbia, Alberta and Saskatchewan, and the impact these revenues have had on the principle of equalization, let me say that the principle of equalization has been that the federal government will attempt to bring up all the provinces to a common level of service and a common level of revenue, based on the 29 factors that are taken into account in calculating the revenue base of each province. The fundamental difficulty with the resource question is that the federal government has been obliged—although it is trying to get out of it—to attempt to bring up the have-not provinces to the level of the have provinces without having access to the revenues which would make such redistribution fully possible. That is precisely the nature of the fiscal imbalance in which we find ourselves. The federal government has been expected until the present time—this is the cause of the fiscal squeeze in which it finds itself—to redistribute wealth without having full access to the revenues which are the basis upon which the equalization will take place.

The system of equalization has attempted to take this problem into account in a number of ways. It is a major problem because the growth in revenue from natural gas and oil has been exponentially higher than any other form of

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revenue one can think of. For example, there is no comparison between the growth in revenue which has taken place from sales tax or from income tax or corporate tax at the provincial level, and the growth in resource revenue. The system has tried to accommodate this fact by, first of all, saying, "We will take out 50 per cent of the resource revenues right off the bat. The provinces can skim that right off. We will not include that in the revenue base". The other way they have done it is to say that only one-third of all equalization can be based on that resource base. There is a one-third cap on the calculation of the over-all amount allowed to be calculated when one looks at the revenue of the provinces of Alberta, Saskatchewan, and so on. In a sense, this is the first shift away from the principle of equalization. It is a very understandable shift because it appears to accommodate two things. First of all, it allows the federal government to get around the dilemma of having to spend money it does not have.

An hon. Member: They can do that anyway.

Mr. Rae: It is an attempt to do that, although it has not been quite successful, as we have seen. The second thing it does is to allow the provinces to establish heritage funds. They are not permanent—it is important to remember this because we are talking about a depleting resource, not a resource which is renewable. The three producing provinces have established heritage funds so as to create a capital base which will allow them to diversify away from a reliance on non-renewable resources and give them an assurance that, in the long run, they will be able to deal with the long-term economic needs of the citizens of their provinces. I think those two principles are very important. If there are people in the country who begrudge Alberta the concept of a heritage fund or who begrudge Saskatchewan its heritage fund, I think they are mistaken because it is terribly important that provinces be able to develop capital funds so as to move away from dependence from a resource base that is very narrow so they can diversify their economies.

The bill before us further accommodates those principles because again it takes out in an aspect of the oil and gas revenues from the base and in this way further protects the provincial heritage funds. Moreover, it further guarantees that the federal government will not be required to spend money which it says it does not have.

When these things happen, somebody always loses. So who loses? The answer is very simple. It is not the federal government, because it is not making equalization payments—we have taken that out of the revenue calculations. And it is not the producing provinces because we have said to them, "We will not put that in the calculation, so you are okay too". The people who lose as a result of this are the have-not provinces. It is not the federal government that is losing, and I can understand the position of the federal government trying to protect itself. The problems that have been caused in the last six or seven years have a great deal to do with fiscal imbalances which are structural in nature. Some of them have to do with mismanagement and incompetence as well, but others