



CANADIAN WEEKLY BULLETIN

INFORMATION DIVISION · DEPARTMENT OF EXTERNAL AFFAIRS · OTTAWA, CANADA

Vol. 21 No. 39

September 28, 1966

CONTENTS

Federal-Provincial Economic Policy	1
Medical Aid to Vietnam	3
Visit of President of Senegal	3
Canada-Japan Export Controls	3
Cattle Mission from Peru	4

FEDERAL-PROVINCIAL ECONOMIC POLICY

The following is part of a statement by the Minister of Finance, Mr. Mitchell W. Sharp, to the Tax Structure Committee in Ottawa on September 14:

...It is evident to us that the federalism of the future must recognize, even more than the federalism of the past, that intergovernmental arrangements must serve the two purposes which concerned the Fathers of Confederation. One was to establish a federal system which would define the roles of the federal and the provincial governments in the management of the public affairs of Canada. The other purpose was to provide the means for promoting the social and cultural development of our two societies, a goal which has come to include the cultivation of the enriching heritages that have come to us from other lands. In this twofold purpose lies the uniqueness both of the spirit of Canadian federalism and of the intergovernmental arrangements which our system calls for.

FEDERAL, PROVINCIAL ROLES CHANGE

It will be equally self-evident, I think, that the economic and social developments of our first century have changed substantially the roles both of the federal and the provincial governments, and the inter-relationship between these roles. The Depression, the war and then the years of reconstruction taught governments everywhere that they must assume the new and difficult task of managing their economies, in the interest both of full employment and balanced economic growth, and the Federal Government assumed the primary responsibility for this role in Canada. These years taught us, too, that Canadians everywhere want and expect certain basic government services wherever they live, and that they expect

their federal and provincial governments to find the methods by which this can be achieved.

It was during these years, too, that the role of the provinces was similarly enlarged, by the expectations imposed upon them by the people of the provinces, by the technological changes and urban developments which created new needs, and by the renewed realization of provincial potential by provincial politicians. So the responsibilities of provincial governments grew both in scale and in scope, involving programmes in the fields of health and welfare, education, urban development, transportation, and resource and economic development.

Out of these developments emerged still another and a different role for the Federal Government, and new interpretations of the role of the provinces. The Federal Government assumed the responsibility for ensuring that the poorer provinces should, through a system of equalization payments, be put in a position to finance their new and heavier responsibilities. The provincial governments, in turn, exercised both their taxing and spending powers in such a way and on such a scale as to increase, in practical terms, both their fiscal powers and their influence over the nation's economy. In the process of these changes, many of the programmes of the federal and the provincial governments, each of them acting within its own constitutional domain, have come to overlap, with the consequent need for harmonization of government plans and programmes.

These are the forces the federalism of the future must accommodate. We must somehow fashion machinery which will permit a strong Federal Government to accomplish the economic and social responsibilities which properly belong to it, but without impairing

the fiscal freedom and responsibility of the provinces. We must, on the other hand, fashion machinery which will strengthen the ability of the provinces to provide the greatly expanded and improved public services which are expected of them, but without at the same time hobbling the Federal Government or forcing it to have different laws for different parts of Canada — differences which might have the effect of obscuring or weakening its proper role as a government which governs all Canadians and protects equally the interests of all of them....

PRINCIPLES GUIDING FISCAL ARRANGEMENTS

Any general appreciation of the objectives of federalism in Canada, such as this, must lead to a statement of the guiding principles which flow from it, if it is to be useful in discussions such as those we are about to begin. The following then, are the principles by which we believe we should be guided in trying to develop a system of federal-provincial fiscal arrangements which will be consistent with the federalism of the future:

(1) The fiscal arrangements should give both the federal and provincial governments access to fiscal resources sufficient to discharge their responsibilities under the constitution.

(2) They should provide that each government should be accountable to its own electors for its taxing and spending decisions and should make these decisions with due regard for their effect on other governments.

(3) The fiscal arrangements should, through a system of equalization grants, enable each province to provide an adequate level of public services without resort to rates of taxation substantially higher than those of other provinces.

(4) They should give to the Federal Government sufficient fiscal power to discharge its economic and monetary responsibilities, as well as to pay its bills. In particular, they should retain for Federal Government a sufficient part of the income tax field in all provinces — both personal and corporate — to enable it to use variations in the weight and form of that tax for economic purposes and to achieve a reasonable degree of equity in the incidence of taxation across Canada.

(5) They should lead to uniform intergovernmental arrangements and the uniform application of federal laws in all provinces.

(6) The fiscal arrangements should seek to provide machinery for harmonizing the policies and the priorities of the federal and provincial governments....

A NEW EQUALIZATION FORMULA

Equalization arrangements are one of the four central features of federal-provincial fiscal relations. They represent one of the dividends of Canadian unity, designed as they are to enable all Canadians to enjoy an adequate level of provincial public services. Where circumstances — whether natural or man-made — have channelled a larger than average share of the nation's wealth into certain sections of the country, there should be a redistribution of that wealth so that all provinces are able to provide to their citizens a reasonably comparable level of basic services,

without resorting to unduly burdensome levels of taxation.

To accomplish this goal, and in the spirit of the principles I spoke of earlier, we have concluded that we must undertake a fundamental reform in our equalization arrangements. We should seek in the future to measure the whole revenue or fiscal capacity of the provinces — to develop a comprehensive "prosperity index", if you will — in place of the partial measure now in use. Instead of selecting certain taxes and equalizing them to the level of the top two provinces, we should take into account all of a province's revenues and equalize them to the national average. This would be a good deal more expensive to the Federal Treasury, but far more equitable. Secondly, the arrangements should be sensitive to the revenue requirements of the provinces, taken together — that is, they should grow as provincial responsibilities increase — and they should be equally responsible to changes in the tax capacity of individual provinces. Finally, to develop a formula that meets these requirements, we must take into account objective factors only, recognizing at the same time the need to deal with any special problems which may arise in the transition from the present to the new arrangement.

The formula being proposed is designed to meet all of these requirements. It would provide that any province in which average provincial tax rates (not its own tax rates) would yield less revenue *per capita* than the yield in Canada as a whole would be entitled to an equalization payment. The payments would be arrived at in this way. We would determine what it is the provinces generally tax — in technical terms the tax base for each revenue source — and the average level of the rates or levels which the provinces generally impose. Then we would apply this average tax level to the tax base in each province — again the incomes or sales or resource production which provinces generally tax — to find out whether the *per capita* yield in that province is below the national average. If the total yield of all provincial revenues, calculated in this way, were to yield less than the national average in any province the Federal Government would make up the difference in equalization payment. The proposed formula is estimated to cost the Federal Treasury about \$490 million, about \$140 million more than the present one....

The transitional arrangements proposed would provide that any province which stood to receive less under the new formula than under the old, would have its payments reduced gradually, resulting presumably in the decline in equalization payments being largely offset by increases in other revenues....

SHARED-COST PROGRAMMES

...Most Canadians would agree that shared-cost programmes, such as hospital insurance and old age and unemployed assistance, have contributed greatly toward social advances across Canada. Most Canadians will expect the Federal Government to retain some vehicle for bringing about new country-wide social and economic advances in the future.

At the same time we must recognize that the continuous and cumulative use of shared-cost programmes in fields of jurisdiction which are primarily pro-

MEDICAL AID TO VIETNAM

Mr. Paul Martin, Secretary of State for External Affairs, recently announced that 165,000 Saigon school children would soon be immunized against poliomyelitis with oral vaccine supplied under Canada's External Aid programme.

The immunization has been undertaken by the Vietnamese Ministry of Health as a pilot project in a planned campaign to protect all Vietnamese children from six months to 12 years against a disease which ranks with tuberculosis and malaria as a serious health problem in southeast Asia.

In Canada, following intensive vaccination programmes, the disease has been virtually eradicated. Complete eradication of the disease in Canada is considered by medical authorities to be a reasonable goal.

Mr. Martin's announcement marked the latest development in Canada's programme of medical aid to Vietnam, to which more than \$1 million has been allocated this year. Canada recently shipped the first of ten pre-packaged emergency hospital units for integration into South Vietnam's provincial hospitals system, and work began on a tuberculosis clinic at Quang Ngai.

Mr. Martin said that, while the Canadian programme of assistance in Vietnam had grown considerably in the past three years, "one cannot minimize the difficulties of mounting quickly a large and effective programme in the circumstances which now prevail in that country".

Since 1953, Canada has allocated almost \$6 million to development assistance in Vietnam. A total of 339 students has been brought to Canada and 183 of them, the largest trainee group from any country, are now studying in academic and technical training institutes, working mainly in the French language.

VISIT OF PRESIDENT OF SENEGAL

Recently, at the invitation of His Excellency the Governor General of Canada, the President of the Republic of Senegal, His Excellency Léopold Sédar Senghor, paid a state visit to Canada. During his stay in Ottawa, from September 19 to 21, discussions were held between the leaders of the two countries and their respective ministers, which emphasized the close bonds linking Senegal and Canada — stemming from the importance of the French language and culture in their national life.

CANADIAN ASSISTANCE

The two Governments examined the bilateral links that had developed since the establishment of diplomatic relations. In order to assist Senegal to meet shortages caused by recent drought, the Canadian Government offered up to \$500,000 in Canadian foodstuffs. The two Governments agreed to allow their experts to study ways and means of developing still wider co-operation, particularly in the areas of technical and educational exchanges. Senegal is

one of the French-speaking countries in Africa where Canada hopes to proceed with certain capital assistance programmes. During the visit, representatives of the two countries signed, on behalf of their respective governments, a memorandum of understanding defining the responsibilities of the Canadian and Senegalese Governments with regard to Canadian personnel serving in Senegal under the auspices of the External Aid Office.

AREAS OF AGREEMENT

The two Governments were in full agreement on the need for vigorous support of the United Nations and on the need to strengthen the capacity of that organization to act effectively for the maintenance of peace and security. Both Governments also agreed that raising the standard of living in developing countries of the world is an urgent and vital problem in which all countries must co-operate in seeking an appropriate solution.

A *tour d'horizon* of international problems led the Senegalese and Canadian leaders to reaffirm their belief that international disputes should be settled through negotiation in the spirit of the United Nations Charter. They also restated their common determination to strive for peaceful solutions consonant with respect for human rights and international law.

The two Governments agreed on the desirability of developing closer links and more numerous exchanges, particularly in the cultural and professional fields, amongst those countries for which the French language and culture are, in varying degrees, an integral part of their national heritage. They discussed the need for increasing these links and exchanges through a wide and balanced framework which would take account of the structures and particular problems of all those countries that have a claim to membership in the community of French-speaking peoples.

CANADA-JAPAN EXPORT CONTROLS

Mr. Mitchell Sharp, Minister of Finance, recently announced the results of the consultations that had been in progress since January between the Canadian and Japanese Governments concerning the quotas the Japanese Government is applying on the export of certain products to Canada for 1966. Mr. Sharp said that the restraint levels provided generally for orderly increases in exports of these products over the 1965 levels. For the most part, the rates of increase are not greater than the expected rates of growth in the Canadian market for the individual products.

The Minister stated that, last year and earlier this year, representations had been received seeking new quotas to cover the export of all man-made fibre fabrics from Japan. It had been decided not to seek quotas but there had been a number of discussions with the Japanese authorities concerning the development of their trade in these products, and efforts were being made to ensure that these would be marketed without disrupting Canadian industry. More recently, the Canadian producers renewed their

representations. Accordingly, Mr. Sharp has asked that the Canadian market situation again be reviewed.

TV IMPORTS

Towards the end of last year Canadian producers of television sets expressed their concern that, with the capacity of patent protection in June 1966, Japanese exports of television sets to Canada might accelerate at a very rapid rate and damage their industry. The Government has decided not to seek an export quota but to alert the Japanese Government to the worries expressed by the Canadian industry and to ask that the Japanese authorities take such steps as might be necessary to ensure that their exports of this product were marketed in an orderly fashion.

Mr. Sharp noted that, in the late 1950s and earlier 1960s, total restraints covered more than a third of Canada's imports from Japan. Today, notwithstanding that the restraint levels have been increased in every year since 1961, the restraints cover only 10-15 per cent of Japanese goods, owing to Japan's efforts to diversify into less sensitive products and to Canada's ability to agree to the removal of certain quotas.

In each of the last few years, a number of products have been freed from restraint. This year, three additional products have been removed from quota. These are: elastic webbing, ladies' fabric dress gloves and transistor radios. Mr. Sharp stated that this was consistent with the Government's policy of not asking for the maintenance of restraints when disruption to Canadian markets is no longer threatened. The Minister expressed the hope that the Japanese Government would recognize this as an indication of the willingness of the Canadian Government to work toward an orderly expansion of trade between the two countries. He also noted that no new products had been placed under quota this year.

* * * *

CATTLE MISSION FROM PERU

Six livestock specialists from Peru arrived in Canada recently to study various breeds of Canadian dairy cattle.

The trade mission, which is sponsored by the Department of Trade and Commerce, is intended to bring together men involved in the Peruvian livestock-improvement programme and Canadian breeders who have developed high-quality seed stock. A tour of Canadian breeding establishments has been planned by the Department with the assistance of the Ayrshire Breeders' Association of Canada, the Canadian Guernsey Breeders' Association, the Canadian Jersey Cattle Club, the Holstein-Friesian Association of Canada and the federal Department of Agriculture.

Canadian dairy cattle have been successfully introduced into Peru, and Canadian breeders hope to demonstrate that the Peruvian industry can profit from further imports. The excellent health of Canadian cattle, as well as their proven productive ability and desirable type, will be demonstrated.

Five members of the mission are leading dairy-men from various areas of Peru. The sixth is a bank representative, who is responsible for technical advice in the handling of World Bank funds allocated for Peru's agricultural programme.

* * * *

FEDERAL-PROVINCIAL ECONOMIC POLICY

(Continued from P. 2)

vincial would result in a greater and greater proportion of provincial budgets being devoted to programmes whose costs are shared by the Federal Government, leading to a continuing influence on provincial decision-making. The result would be to reduce the fiscal responsibility of the provinces, and to hamper them in establishing their own priorities.

We must recognize too that the provinces have more and more wanted to assume full responsibility for initiating and operating their own programmes, and that their ability to do so has grown demonstrably since the War. This has been especially true of Quebec, whose particular social and cultural goals have been a continuing and dominant influence on its approach to federal-provincial relations....

In discussing the proposed new approach I would differentiate between social and economic programmes.

SOCIAL MEASURES

With regard to the first of these categories (social measures), it is our view that, in respect of the three large and continuing programmes which come under provincial jurisdiction, federal conditions should be withdrawn as soon as full provincial responsibility for them can be established. I refer to hospital insurance, the Canada Assistance Plan, and the continuing portion of National Health grants. We are considering doing this in two stages.

First, the Federal Government would invite the provinces to take the first step towards greater fiscal independence and responsibility by accepting a new form of compensation in respect of these programmes, effective January 1, 1967. This compensation would be made up of three components: the "transfer" of 17 points of the individual income tax to the provinces; the associated equalization of these 17 points up to the national average under the general equalization formula; and an adjustment grant to each province which would bring its total compensation up to the federal share of the actual costs of the three programmes.

The tax transfer would take the form of a reduction in the federal personal income tax and a corresponding increase in the provincial tax. Assuming all provinces took this action, the increase in provincial revenues would automatically enter into the general equalization formula, resulting in an equalization of this tax transfer. The third element in the compensation is an adjustment payment, a programme equalization payment, which would be equal to the difference between the federal share of the actual year-by-year cost of each province of the three shared-cost programmes, and the value to that province of the tax transfer and associated equalization.

It will be evident that this arrangement would not achieve full provincial responsibility for the social measures, since the total compensation to each province would continue to be based upon the actual cost of standard programmes. This would make it necessary to continue the shared-cost programmes in their present form, in order to determine the programme costs. The second step, therefore, would be to make the federal compensation wholly independent of programme costs, or unconditional. This would be accomplished by escalating the adjustment payments, after a given date, on an objective basis unrelated to programme costs. After this date the provinces' compensation in respect of these three programmes would increase quite independently of — and almost certainly more rapidly than — programme costs, on the formula we will propose. I am suggesting that this second step be taken on April 1, 1970.

...As to portability and programme standards, we are proposing a general intergovernmental agreement that would contain three provisions. First, all governments would agree to continue the intergovernmental machinery that has been developed for the purpose of reviewing programme developments and discussing programme improvements, and to continue to participate in these consultations. Secondly, the Federal Government would undertake to continue to provide technical assistance, to any province that wants it, for the purpose of maintaining and improving programme standards. Thirdly, the provinces would agree to maintain uniform residence requirements in respect of all health and social security measures where benefits to individuals and families are involved.

We recognize that the cost of this latter provision falls unevenly upon the different provinces: those provinces in which the "in-migration" of people exceeds "out-migration" are assuming a net burden. In recognition of this fact, the Federal Government proposes to offer annual "portability grants" which would be paid to any province maintaining the agreed residence rules and in which net in-migration is occurring. The grants would be equivalent to the amount of net in-migration for the year multiplied by the *per capita* cost of the programmes in question.

I have one other proposal to make concerning federal-provincial social measures. The arrangements I have described apply to the major and established continuing programmes. There are, in addition to these a number of smaller programmes, most of which form a part of the health grants programme and the Canada Assistance Plan, which are made up largely of a series of individual projects. These research and demonstration projects, as they have come to be known, are individual projects in respect of which federal support is non-continuing, and which are designed to determine technological soundness or the feasibility or desirability of new approaches and new ideas. They are designed to contribute knowledge and experience to the whole of Canada, and they do not, because of their size and their short-term nature, result in any significant federal influence over provincial decision-making. For these reasons the Federal Government proposes to continue to support research and demonstration projects....

ECONOMIC MEASURES

...The shared-cost programmes in this category cover a wide spectrum. They range from a variety of agricultural programmes and the ARDA agreements, to the Trans-Canada Highway and Roads to Resources, to water-conservation projects, and to the combating of unemployment through the Municipal Winter Works Programme and the training of the unemployed...

The guiding principle in the Federal Government's approach to this category of programme might be stated in this way: while the provincial governments undoubtedly have an interest in stable and balanced economic growth, and are increasingly embarking upon their own programmes for this purpose, and while it is certainly true that the provinces have control over their own resources, the Federal Government must continue to accept an overriding responsibility for employment, economic stability, and economic development in Canada.

It follows that it should continue to be free to engage in federal-provincial measures as well as its own tax, expenditure and credit measures, in order to accomplish this general objective. The Federal Government proposes, therefore, to continue to employ shared-cost programmes for economic purposes, and to offer them on the same basis to all provinces....

EDUCATION

The federal-provincial programmes in the general field of education are the subject of particular interest and controversy. It is generally recognized that expenditures on education are growing more rapidly than any others, and that educational programmes are far from being settled in their form or stable in their trend. We are conscious of the pressure the provinces are under. At the same time provincial governments, educational institutions and students have been pressing the Federal Government to take further action in this field. It is known, of course, that present federal-provincial programmes in the field of education, including the technical and vocational training agreements and university grants, are under review both by the federal and provincial governments.

I am able to announce that the Federal Government proposes to increase its financial assistance in respect of post-secondary education. The form that assistance should take, however, and its relationship to federal-provincial affairs generally, is a matter requiring the most careful and thoughtful consideration. That is why the Prime Minister suggested that there should be a special conference on this subject. At that time we will present the Federal Government's views.

JOINT USE OF TAX FIELDS

The major element of federal-provincial fiscal relations, by far the most important one in the post-war period, is the division and use of tax fields by the federal and provincial governments. What this has come to mean to most of us is periodic federal-provincial disputes over what share of personal income tax should be federal and what share provincial. We have come to the conclusion that it is time to try to recast this whole question of tax-sharing in broader and more comprehensive terms....

An examination of the tax sources now being used by the provinces reveals that these governments do, in fact, have access to revenue fields capable of yielding the required revenues. The real question is not whether they have access to such sources but rather whether there are practical considerations making it difficult for them to use their taxing powers. Under the constitution the provinces have access to the income-tax fields, both personal and corporate, just as the Federal Government has. Indeed, their use of these fields has risen substantially since the war: from 5 per cent of personal income tax 15 years ago to 25 per cent now, and from a tenth of the corporation income tax to about a quarter today. They are now levying taxes on commodities at the consumers level, while the Federal Government levies such taxes at the manufacturers' level. As I have indicated earlier, the provinces now collect some 40 per cent of all commodity taxes imposed in Canada, including nearly 40 per cent of the general sales taxes, some 50 per cent of liquor taxes, and virtually 100 per cent of gasoline tax. The provinces have full access as well to the asset-tax field; they and their municipalities now receive close to 100 per cent of all the property taxes collected, and 75 per cent of estate taxes or succession duties. The provinces also have access to resource revenues, as does the Federal Government; indeed provincial resource revenues now represent close to 100 per cent of the revenues from this source. Only the customs duties can be said to be exclusively collected by the Federal Government....

TWO FALLACIES

The conventional approach to this problem, during the post-war period, has been to argue that the Federal Government should reduce its taxes so as to give the provinces more "tax room".... The proposition that the Federal Government should reduce its taxes to ease increases in provincial levies must, in circumstances such as those I have described, be based on the assumption that Parliament is appropriating money for purposes less important than those being served by provincial expenditures. That governments should reduce expenditures is a proper subject for argument - taxpayers make it regularly, and apply it equally to federal, provincial and municipal governments. But we cannot accept as a general principle that federal expenditures are less important than provincial ones. The principle that *does* call for recognition is a different one: namely, that both Parliament and provincial legislatures must accept

their financial responsibilities and that each should look to its own electors for direction as to what money should be raised and how it should be spent....

The second convention of federal-provincial fiscal relations that must be questioned is that there is some particular share of income tax and estate taxes and succession duties, the so-called "shared taxes", which is rightly federal or rightly provincial. The fact is that both have constitutional rights in these fields.

What we must share now is the responsibility for the total taxes imposed on Canadians, taking into account what each other is doing. We must find ways of harmonizing federal and provincial tax actions, to ensure that the interests of the taxpayers of Canada are protected, both in the way and the extent to which the several tax fields are used. This must include the determination of what taxes tend to have national as opposed to provincial characteristics. The corporation tax is one of these, because corporation profits may be earned elsewhere than in the province where the head office is located and profits recorded.... There are also compelling reasons for the Federal Government to maintain a substantial position in the personal income tax field. This is the principal tax by which equity is achieved between the rich and poor across the nation. This implies that a substantial share of this tax should continue to flow to the national government. This tax, too, is one of the central instruments for regulating total demand in the economy, and Canadian Governments must not allow total federal income taxes to be abated so much that they can no longer be used for this purpose....

INTERGOVERNMENTAL LIAISON

The fiscal arrangements proposed by the Government of Canada combine into a consistent whole. They recognize as a fact of Canadian federalism that there are and must be both strong provincial governments and a strong Federal Government. Their purpose is a reform in fiscal arrangements under which both levels of government will have, in as balanced a way as possible, the fiscal strength they require, and the responsibility that must go with it. They provide a system of unconditional and automatic equalization payments to give meaning to fiscal freedom in the poorer provinces. They provide for the retention and the exercise by the Federal Government of those taxing and spending powers that are necessary to the proper management of the Canadian economy....
