Monetary Policy

Monetary policy seeks to regulate the supply of money and credit in the economy as a whole. It must be co-ordinated with fiscal policy in such a way that the two complement each other in stabilizing the economy. As with fiscal policy, there is no question that the federal government possesses the constitutional authority to pursue these goals. The federal government has authority, under section 91 of the Constitution Act, 1867, over currency and coinage, banking, the incorporation of banks, and the issue of paper money and legal tender. With these instruments, it is able to influence, at least to some degree, interest rates and the exchange rate. The growing activity of the so-called "near-banks" (that is, the provincially chartered trust and loan companies and credit unions) affects the ability of the central bank to influence the supply of money. Parliament concluded, however, when it revised the Bank Act in 1980, that this situation did not pose a significant problem for monetary policy. Similarly, as major borrowers of funds in international markets, provinces can influence the exchange rate; yet again, the main instruments of control lie in federal hands. The issues for federalism, then, are economic and political rather than constitutional.

An important political issue related to monetary policy has been the demand by some provinces for a regionally differentiated policy. The fact is, however, that the mobility of capital within the economic union does not permit interregional variation in interest rates. Moreover, as Commissioners have already noted, we do not believe that macro-economic policy is an appropriate instrument for pursuing regional development. In any event, recent experience has shown that a small open economy such as Canada's cannot follow a monetary policy which is isolated from the world financial system. The constraint is international, not domestic.

Incomes Policies

Incomes policies are intended to moderate the rate of inflation by controlling price increases and increases in wages and salaries. In Chapter 3, Commissioners argued against the adoption of a permanent incomes policy in Canada. We do not believe that such a policy is consistent with the flexibility and adaptability required in a rapidly changing world. Moreover, since the regulation of labour, property and civil rights – all of which are affected by incomes policy – lies largely within provincial jurisdiction, a permanent incomes policy would redistribute the powers and responsibilities of both orders of government. If temporary controls become necessary on an emergency basis, however, the federal power has the authority to impose them under the "Peace, Order, and good Government" clause. This authority was clearly affirmed in the 1975 Inflation Reference Case.

While Commissioners do not advocate a permanent incomes policy, there are two approaches to the issue that would not suffer from the constitutional objections that face permanent wage and price controls: a tax-based incomes policy (TIP), or a policy, like the recent "Six-and-Five" program, that applies only to federal employees and employers falling within federal labour

jurisdiction. A TIP would certainly require federal-provincial consultation, since it would involve important changes in federal tax law with major implications for the provinces. Indeed, it would require provincial acquiescence, if not full-fledged support, since the provincial governments could issue regulations or modify their taxes in such a way as to neutralize the federal tax incentives that are supposed to make the program work. The use of a Six-and-Five type approach to incomes policy, whether on a permanent or temporary basis, avoids the thorny question of the division of powers by confining federal regulations to those employers and employees over which it has jurisdiction. This group does not constitute a majority of employers and employees, but it is large enough so that an incomes policy that applied to it could have a significant affect on the economy and serve as a demonstration for the provinces and for the private actors whom they regulate. The federal government could further extend the range of a policy of this type by making conformity to these restraints a condition of some or all of its procurement contracts.

Finally, provincial governments have also promoted restraint. As with the federal Six-and-Five program, they have recently concentrated on restraining public sector wage increases and on controlling provincially regulated prices. The provincial programs have varied considerably in response to local conditions and the political and economic objectives of each government. In several provinces, such as British Columbia, Quebec and Newfoundland, they have produced vigorous internal conflict. This variation is again consistent with Commissioners' emphasis on the advantages of federalism in allowing for variety and experiment, and on diffusing conflict widely. These differences in approach, however, took place within a broad common framework which was the product of the common conditions within which provinces and the federal government found themselves.

Labour Market Restructuring: Gain Sharing

Commissioners view change in the structure of labour markets as perhaps the best way of reducing the high levels of structural unemployment that fiscal and monetary policies appear incapable of altering. Many factors affect the functioning of labour markets. Effective information channels can link workers to changing employment opportunities. Mobility grants can facilitate this matching process. Education and training can ensure the right mix of skills in the work-force.

Intervention in the wage-setting process is another factor that can affect labour markets. It can take the form of minimum wage policies, tax and other incentives designed to influence labour and management in bargaining, and regulations covering labour relations, such as those relating to union certification and the right to strike. Most of these factors fall primarily within provincial jurisdiction. Does this fact limit the capacity of the federal government to act and, more generally, impede effective policy?

Commissioners' chief recommendation with respect to labour markets in Part III was the use of federal tax incentives to encourage the private sector to determine wage levels, to some extent, by the employer's market gains. We

believe that the federal government, operating in its own jurisdiction, can pursue such an objective through the tax system. We do not expect such action to generate serious inter-regional or intergovernmental tensions.

Finally, as Canada tries out new approaches to finding answers for these questions, the variety and experimentation that federalism allows again offers an important advantage. Provincial labour laws have a great deal in common: common origins in federal wartime labour-relations legislation: and similarities in the economic and political forces at work. There are also significant variations from province to province. British Columbia, Saskatchewan, Ontario and Quebec have made important innovations, many of them the subject of controversy. In recent years, in several jurisdictions, policies favourable to organized labour have given way to a more restrictive approach, particularly with respect to the public sector. The point here is not whether individuals approve or disapprove of such changes, but the possibility for variety and experiment. Labour/management relations are indeed a national concern, but it does not follow that provincial regulation is inappropriate as a means to deal with it.

Infrastructural Development

Transportation and communication networks link the citizens spread out across our vast nation, facilitating the exchange of goods, services and ideas among them. Financial institutions discharge an important function in matching investment funds with Canadian needs and opportunities. These sorts of material and symbolic ties have helped to build the Canadian nation as witness the vital contribution of the Canadian Pacific Railway. All these networks are essential, not only to the economic health of Confederation, but also to the maintenance of the political unity that is the ultimate rationale for the existence of the economic union. Economically and politically, they are essential to making a living reality of the concept of economic union.

Transportation

Canada must develop a coherent regulatory regime encompassing all the major forms of transportation that knit the country together: railways, highways and trucking, Great Lakes and ocean shipping, and aeronautics. Canada's Constitution does not expressly confer jurisdiction over a general category of transportation. However, section 92(10) of the Constitution Act, 1867 placed navigation and shipping, railways, canals and telegraphs in federal jurisdiction, and gave the federal government power to declare other works and undertakings running beyond provincial boundaries within its purview.

The courts have interpreted the "Peace, Order, and good Government" clause of section 91 as granting constitutional authority for federal regulation of the aeronautics industry. The federal government now has clear jurisdiction over the whole of that sector. Clearly established jurisdiction is not always enough, however, as the authors of one research study made for this Commission have suggested.[6] They concluded that provincial ownership or

share holding in important regional airlines has frustrated federal attempts to use airline regulation as an instrument of national economic development. This is at least part of the reason, they argue, for recent federal moves toward deregulation of airlines.

The constitutional problem associated with federal regulation of railways and trucking is rather different. Judicial interpretation of subsections (*a*) and (*b*) of section 92(10) has resulted in the assigning of federal jurisdiction over the regulation of interprovincial undertakings of these kinds and of provincial jurisdiction over intra-provincial undertakings. The federal share of this split jurisdiction has gradually widened as the courts have held that transportation units which perform both interprovincial and intra-provincial functions fall under exclusive federal jurisdiction. The federal government also has jurisdiction over undertakings connected to, or forming part of, a broader interprovincial undertaking.

This approach has granted the federal government sufficient jurisdictional latitude to implement national transportation policies in these sectors, and in the railway sector it appears to have used this authority appropriately. The same cannot be said, however, with respect to the trucking sector, where, under Part III of the National Transportation Act, the federal government has delegated its powers to license and regulate to provincial regulatory agencies. This delegation has resulted in ten different sets of trucking-industry regulations, each formulated by two orders of government. The consequent arrangement is expensive to administer and confusing in its effects. At the time of writing, the governments of Canada are engaged in discussions with the intent of harmonizing these regulations, and agreement seems within reach. If that does not happen, serious consideration should be given to consolidating responsibility for interprovincial trucking under federal jurisdiction.

Communications

Electronic communication links are as vital to the Canadian economic union as were railways in the past. The aims of federal policy with respect to communications parallel those already identified for transportation. So does the constitutional status of federal regulation, which the courts have interpreted as giving the federal government exclusive jurisdiction over radio communication in its various forms, including radio, television, cable television, microwave and satellite.

The jurisdictional situation with respect to telephones and related forms of telecommunications is, however, unique. The courts have recognized neither the type of split jurisdiction that applies to trucking nor the exclusive jurisdiction of one order of government. Instead, a patchwork of jurisdictions has gradually evolved. Canada's two largest telephone companies and two specialized domestic common carriers fall within federal jurisdiction. Seven major provincial carriers and a host of smaller companies come under provincial regulation. To cap it all, no one regulates Telecom Canada, an association of the ten principal carriers that co-ordinates the operation of Canada's only national, public, switched-telephone network.

This jurisdictional patchwork has made it difficult to develop a national telecommunications policy, and this failure, in turn, has hindered the creation of alternative national networks and services. By international standards, Canada has an advanced and effective telecommunications system. As befits a country where the conquering of distance is a fundamental challenge, Canada has pioneered a number of important technological advances in telecommunications. We are in danger, however, of failing to keep up with the adoption of new facilities, and of falling behind the United States. Hence it is important that we clarify jurisdiction and roles.

Federal attempts to develop and pursue a comprehensive national policy on telephones and telecommunications began in 1968. At the same time, provinces were also exploring the part played by communications in economic development and culture. By the 1970s, they were seeking greater constitutional authority in the field. These conflicting objectives gave rise to bitter federal-provincial conflicts and very little effective action, as distinctions between content and hardware or between inter- and intra-provincial communications broke down under the impact of rapid technological change. Canadians must change this situation.

Three possible directions for change exist. First, the federal government might assert jurisdiction over the entire telecommunications sector. This action would bring the provincially regulated telephone companies, along with Telecom Canada, under federal regulation, but it would be very difficult. Several provinces actually own their telephone companies, and there are many aspects of services within a province that are the legitimate concern of provincial governments; these include, for example, services to remote areas and integration of cable and telephone services.

A second possible solution would be to formalize concurrent jurisdiction, with federal paramountcy. This arrangement would allow the federal government to regulate those aspects of telecommunications that are essential to interprovincial and international services and to maintenance of an effective nation-wide, telecommunications system. Provinces would retain the authority to regulate with respect to local dimensions. Such concurrency would provide a high degree of flexibility in responding to technological changes. Shared jurisdiction of this sort, however, does have dangers as American experience has shown: intrastate and interstate services use the same facilities so that separate state and federal regulation of local and interstate rates is both difficult and expensive to manage.

The third option would be joint regulation. Under this arrangement, both federal and provincial governments would delegate their regulatory authority to a common federal-provincial regulatory agency. This adjustment would involve a major change in the role and composition of the existing Canadian Radio-Television and Telecommunications Commission, either by shifting some of its responsibilities to a new body or by involving provinces in CRTC appointments and procedures. While such an arrangement might overcome some of the problems of two-tier regulation, it would lessen flexibility and reduce the responsibility and accountability of both orders of government.

On balance, concurrent jurisdiction with federal paramountcy is Commissioners' preferred option, since it meets the key objectives of ensuring

a nation-wide network for communication flows of all kinds and of showing sensitivity to provincial interests.

Financial Institutions

Just as our transportation and communications systems create a vital link between buyers and sellers, and between producers and consumers, so financial institutions form a critical component of the economic infrastructure, providing the key links between Canadian savers and investors. Historically, four distinct types of financial institution have been the basis of our financial system: banks, trust companies, insurance companies and securities brokers. Each of these four could tap only some sources of savings and would make only certain types of investment. At present, this system is undergoing fundamental transformation. The four types of financial institutions are becoming less and less distinct as each takes on functions previously performed exclusively by one of the other types.

Rapid technological change, spurred by international competition, is one of the driving forces behind this transformation. These changes have made it possible for financial institutions to offer consumers "one-stop shopping" for financial services. Quebec is deregulating its financial institutions, and this action, in turn, has put pressure on other provincial governments to follow suit. Constitutionally, the federal government holds exclusive jurisdiction over the banks, while provincial governments regulate the securities markets and the brokers that operate within them. The constitutional regime governing the trust and insurance companies is more complex.

The current constitutional arrangements have proved adequate to the effective regulation of the four types of financial institution, but the convergence described above raises new constitutional issues. If the four types are disappearing, the distinct regulatory regimes organized around them automatically become obsolete. The Economic Council of Canada has argued that in their place, we should adopt a "functional" approach to regulation, applying uniform rules to the performance of specific financial services such as stock broking, regardless of the institution performing them.[7] For example, the federal Bank Act would regulate the "banking" functions of trust companies. In this respect, technological developments in the financial sector seem to require the same sort of regulatory change already mentioned above as relating to telephones and telecommunications. The issue, for our purposes here, is whether the existing division of powers can permit effective regulation based on function.[8]

This issue has several facets. Does development of an effective, functional system of regulation require federal leadership? If it does, has the federal government constitutional authority to provide such leadership? If it has, would exercise of such leadership provoke substantial provincial opposition? And, most significant, what are the most important directions to pursue?

These questions are much easier to ask than they are to answer. With respect to the first, the record is mixed. Despite the regulatory fragmentation, we have developed a highly efficient, nationally integrated financial system. For a very long period, the banks have served as nation-wide institutions.

Recent developments in other branches of the financial industry are also moving in the same direction. Indeed, it has been one of the historic regional grievances in Canada that the financial industry has been too concentrated and therefore insensitive to the financial needs and opportunities of specific areas.

Provincial regulation of the stock markets constitutes a particularly interesting example. In principle, there seems to be a strong argument for federal regulation. In practice, we have achieved much the same result with provincial jurisdiction because of the leading role that Ontario, the centre of the Canadian financial industry, has been able to play, often in partnership with Quebec. One research study prepared for this Commission[9] argues that there is no pressing reason to tamper with this arrangement: provincial regulation has satisfied national purposes. Other research[10] is less sanguine about the future. Technological change, the increasing international integration of capital markets, and the desire of provinces, especially Quebec, to regulate markets in pursuit of provincial development goals are all likely to place greater strains on the existing system in the near future.

In light of the importance of our financial institutions for effective economic development and adaptation to a more competitive world, it is essential that we find answers to these questions with all possible speed. The investigative committee which recently produced a report on the regulation of Canadian financial institutions,[11] a federal joint committee comprised of representatives of the federal government and the industry, investigated some of these problems. This process did not fully involve the provinces, which is unfortunate, given that much of the expertise in this area is provincial, and in view of the divided jurisdiction noted above. This is an area in which the Council of Ministers Responsible for Economic Development could monitor developments.

Adjustment and Social Policies

Within a framework of freer trade and effective policies of stabilization and infrastructural development, Canadian workers and employers must adapt creatively to changing economic circumstances, moving out of activities with declining prospects and seizing new opportunities. We shall review three groups of policies, all designed to facilitate this process. In all these areas, both federal and provincial governments play important roles.

Reducing Obstacles to Market Allocations

In Part III of this Report, Commissioners spelled out some major recommendations to reduce barriers to market allocation of resources. We emphasized the importance of restraining the natural political impulse to "bail out" specific industries. Obviously, this issue involves no question of the division of powers in the federal system: our call is simply for restraint. Yet Canadians should recognize that federalism probably increases the tendency to pursue "rescue" policies. Industries in trouble, whether large or small in economic terms, are important in the lives of individual provinces and communities.

Provincial governments may therefore have a comparatively large stake in those industries. Therefore, if the federal government resists the impulse to bail them out, there will be much greater pressures on the provincial governments to intervene, and for them to add their voices to increase the pressure on the federal government.

In one respect, a less-interventionist federal industrial policy will tend to mitigate intergovernmental and interregional conflict. One common source of regional grievance is the perception that political considerations motivate highly visible discretionary federal bail-outs which favour particular regions. A common reaction is, "Why did you not do the same for us?" In the long run, greater restraint by the federal government in taking such decisions should strengthen general perceptions of its fairness and even-handedness.

Competition policy and product standards are vital to effective market allocation. Effective competition policy is essential to developing the full benefits that can accrue from an economic union. Canada has not been very aggressive in encouraging competition, and one reason for this may be our constitutional situation. Canadian legislation relating to competition has found its constitutional justification almost exclusively in the federal power to make criminal law. This arrangement has resulted in limiting the policy tools and the range of remedies available, and in creating some ambiguity about the location, federal or provincial, of the power to launch prosecutions. It provides an excellent example of the tendency for the exigencies of federalism to constrain the tools and instruments through which policy is pursued.

The recent Canadian National Transportation case[12] decided by the Supreme Court cleared up some of these questions. In his concurring judgment, Mr. Justice Brian Dickson argued that the regulation of competition is one of those activities which provincial governments could not practically or constitutionally enact, for "If competition is to be regulated at all, it must be regulated federally." Mr. Justice Dickson raised the question of whether this situation implied that the federal government could justify legislation on competition under the general trade and commerce power set forth in section 91(2), rather than under the criminal law power. In Commissioners' view, it is essential to resolve this ambiguity. Clearly, regulating competition is an aspect of overall regulation of trade and commerce throughout Canada. We propose, accordingly, that section 91(2) be amended explicitly to include federal regulatory power over "competition".

Closely related to competition policy is the regulation of labelling and product standards. The recent cases involving Labatt's and Dominion Stores appear to have thrown the federal powers in this area into considerable confusion. These decisions invalidated important sections of the federal Food and Drug Act on the grounds that they purported to impose standards on products that were made and traded intra-provincially. In the Labatt's case,[13] however, the product in question was beer, a standardized product, advertised and sold across Canada by national companies, which simply happened to be made in breweries in each province. To see brewing and a host of analogous kinds of production as a local activity is, as one economist commented, "dangerously out of touch with the modern economy's seamless web of production, promotion and sale of consumer goods."[14] In the Dominion Stores

case,[15] the issue was federally defined grading standards for apples, where much the same analysis applies. Taken together, these decisions appear significantly to narrow the interpretation of the federal power under section 91(2) to regulate trade and commerce throughout the country. Widely varying standards and definitions in commonly used products can impose high costs on producers and consumers. Thus Commissioners recommend a further addition to the general trade and commerce power: the regulation of product standards.

Neither of these cases involves important regional issues. In both, effective remedies seem beyond reasonable provincial capacities. Few provinces have shown interest in legislating in these fields. Indeed, in earlier rounds of constitutional discussion, a majority of provinces signified their willingness to contemplate a constitutional amendment with respect to product standards.

A final element favouring elimination of obstacles to market allocation is a view that Canadian governments should move toward reducing, or at least rationalizing, the burdens of regulation in as many fields as possible. Again, this is a general recommendation that Commissioners urge on both orders of government. In a number of fields, such as environmental standards, consumer protection and occupational health and safety, economic actors find themselves subject to regulation from two or more sources, either in the form of ten different provincial regulatory regimes, or in the form of federal and provincial regimes. This plethora of systems can be costly. On the other hand, in the field of the environment, we recommend a strengthened regulatory framework. In many instances, these are relatively new areas of government activity into which both orders moved, and in which stable relations have yet to be worked out.

Commissioners wish to emphasize two points. First, where there are divergent provincial regulatory regimes, the most appropriate model is harmonization of provincial laws through interprovincial mechanisms. Secondly, where the problem arises out of a division of regulatory regimes between federal and provincial orders, we believe, as with telecommunications and finance, that the appropriate principle is functional regulation: the regulation of specific activities rather than of specific institutions.

Encouraging and Facilitating Adaptation

Throughout our Report, we Commissioners have emphasized the need to encourage mobility of workers from areas of low to high employment opportunity. We have recommended a Transitional Adjustment Assistance Program (TAAP) to increase incentives for relocation and training. We have urged removal of existing incentives, found especially in the Unemployment Insurance system, that support certain types of inefficient industries. We have also called for more effective collection and dissemination of information about job opportunities across the country. The federal government has authority to address all these issues. We do realize, however, that the emphasis on adjustment through mobility does seem to push against the emphasis on "place prosperity", that is, on sustaining existing communities, which often underlies federal regional policy and much provincial industrial

development policy. In our view, Canadians must continually balance place prosperity against national efficiency and individual mobility against the preservation of communities. Government action can certainly increase the prosperity of some places in some circumstances. Where this is not possible, TAAP offers an ideal form of adjustment assistance.

Training. Commissioners argued in Part V that the development of a skilled and adaptable Canadian work-force is essential for effective adaptation to new possibilities. We argued, too, for shifting the balance between institutional and on-the-job training in the direction of the former approach and claimed that the TAAP would help to achieve this end. Training activities are a field of long-standing and complex federal-provincial relationships. On the one hand, training is an essential element of national economic management, closely linked to many other federal programs, such as Unemployment Insurance, and to the successful meeting of the needs of a national labour market. On the other hand, training is part of the educational process, which is a matter of provincial jurisdiction.

Through shared-cost programs, the federal government has helped to develop vocational training schools and community colleges in the various provinces. Under the federal Adult Occupational Training Act, the emphasis shifted to the federal purchase of student places in training courses for individuals selected for training. Under the National Training Act of 1982, somewhat greater emphasis was placed on funding training through the private sector, a thrust with which Commissioners sympathize. There is much room here for experimentation and innovation. We do not believe, however, that it is necessary to shift powers or responsibilities. Since "training" is such a multi-faceted process which can extend through a whole lifetime, federal and provincial governments, and the public and private sectors, must all participate. The need here is for effective co-ordination. We believe that within a broad national framework, the government of Canada and of each province should work out a specific mix of programs for that province; the duty of the federal government should be to contribute its perspective of the needs of the national labour market, and that of the province to contribute the prespective of its market.

Education. Almost every one of our values, from national identity, to social and cultural values, to economic effectiveness, affects education. In Part V, Commissioners noted the special concern of many intervenors for the character and quality of Canadian education. We concluded that Canada's educational institutions, particularly those of the post-secondary sector, are not always fully ready to facilitate adaptation or to emphasize excellence. Significant changes must be made, and we argued that there is a strong case for reorientation of federal activity in this field to assist in making them.

The federal government already acts extensively in education, for the most part in post-secondary education and research. In 1983–84, the federal government spent more than $3 billion on education-related matters; more than half of this amount consisted of cash payments for post-secondary education under the Established Programs Financing (EPF) arrangements.

There are no conditions attached to the EPF transfers, and the amounts allocated no longer bear any direct relationship to actual spending in the field.

Commissioners make few recommendations with respect to primary and secondary education. There is little scope for federal activity here. The interprovincial Council of Ministers of Education (CMEC) has done extensive work co-ordinating curricula and facilitating exchanges and the like, and it could extend its work. We believe that more needs to be done to monitor quality and standards in primary and secondary education, and to conduct related research. Ideally, changes in these directions would be the result of a private-sector initiative, and the work done would influence both orders of government. Finally, we note that in the Constitution Act, 1982, Canadians did commit themselves to one crucial "national standard" in education: the right to education in the local minority official language in every province, subject only to the condition "where numbers warrant".

Commissioners believe that post-secondary education is so much part of a national and indeed even an international, system, and is so necessary to innovation, both because of its training of skilled personnel and because of research, that reorientation of the federal role is essential, even though we believe that the provinces can and must retain jurisdictional responsibility in this sector. In Part V, we developed two broad options. The first is to channel federal support for post-secondary education directly to students. A move in this direction would require careful consultation with provinces. Since, under present arrangements, the federal government's share of funding of post-secondary education varies considerably from province to province, it would be essential that the transition not introduce regional inequities.

Such a scheme of unconditional direct grants to students would, Commissioners believe, be a constitutional exercise of the spending power. However, if the federal government were to use the grants as a more active instrument of federal intervention – for example, by using them to determine admission standards to universities, or by providing differential grants scaled to particular fields and disciplines – the situation would become more complex. Such use might be challenged successfully as federal legislation in an area of provincial jurisdiction and therefore an invalid use of the spending power. On a more practical basis, it could produce havoc in the system if provinces and universities were continually scrambling to adapt to changing federal definitions of needs. Such a situation could arise if the provinces exercised little influence over these definitions, and if the federal government had no responsibility for the financial or administrative difficulties that their decisions produced. For these reasons, we do not believe that student grants or loans should be used differentially in this way.

If Ottawa and the provinces decide that the federal government should concern itself more with the content of educational policy, a second option would be to restore some conditionality to federal transfers in support of post-secondary education. The federal government would relate the transfers to actual spending and tie them to some clear national objectives. If we were to move in this direction, it would be essential, first, to spell out such objectives precisely.

More generally, Commissioners believe that considerable federal-provincial consultation is essential to determine realistically and productively overall levels of funding and of national educational goals in the post-secondary field. We note with sadness that concern with fiscal arrangements, rather than with the aims and purposes of post-secondary education, has dominated federal-provincial relations in this field.

Sharing the Benefits and Burdens of Adjustment

In Part V of this Report, Commissioners argued that an essential element of adjustment is shielding or protecting those who find themselves harmed by the process. Effective social policy – a well-designed social safety net – is a prerequisite for successful adjustment. Failure to manage fairly the disruptive effects of change will accentuate political resistance to such changes. This is true for individuals, communities, provinces and regions.

Adjustment policy and social policy are thus inextricably linked. As in adjustment policy, so in social policy, shared jurisdiction is central. The growth of the welfare state accounted for much of the post-Second World War change in the federal system and became a central aspect of co-operative federalism. The Constitution Act, 1867 assigned to the provinces responsibility for most aspects of social welfare. By the 1930s, economic, demographic and social change, combined with changing conceptions of social justice, had demonstrated that the provinces alone could not construct a modern "social service" state. Some shared-cost programs in pensions, health and other fields were undertaken as early as the 1920s; during the Great Depression in the 1930s, the federal government assumed more responsibility for assisting provinces to provide welfare and relief to their residents. During and after the Second World War, federal jurisdictional authority in the social policy field expanded as constitutional amendments gave the federal government authority over unemployment insurance and pensions. Through use of its spending power, that government introduced the Family Allowance program. The spending power also made possible the development of shared-cost programs in health, post-secondary education, and welfare, programs which incorporated innovations originally undertaken by provinces.

Today, with the sole exception of social assistance, the federal government is responsible for operating all the major income-security programs in the country, and is the source of most of the funds involved. It is also a central participant in hospital and medical care, and in funding social services, as well as social assistance, through the shared-cost Canada Assistance Plan (CAP). The provinces are responsible for the organization and delivery of social welfare, social services such as family counselling, and health care.

There is considerable flexibility in social policy. Provinces vary in their administration and funding of health care, though the Canada Health Act has narrowed provincial differences. Provinces retain considerable discretion in setting rates for welfare payments and in the organization and delivery of services. Through tax credits and direct payments, provinces supplement federal Old Age Security. The federal Family Allowance program permits

provinces to vary payment methods in accordance with their own social priorities.

The social policy system has also been able to accommodate Quebec's distinctiveness. In 1964, new federal-provincial arrangements permitted Quebec (and any other province) to opt out of a large number of programs, and to receive the equivalent federal funds in the form of increased tax shares. Quebec was able to enact its own contributory pension plan, the Quebec Pension Plan, which remains closely co-ordinated with the Canada Pension Plan, which operates for the rest of the country.

The centre-piece for Commissioners' proposals in this area is establishment of a Universal Income Security Program (UISP), which would entail a universally available income supplement, subject to reduction at a relatively low "tax-back" rate. Such a scheme, delivered either through the federal tax system or by means of direct transfers, appears to fall within federal jurisdiction. The present federal responsibility for Family Allowances, Unemployment Insurance and Old Age Security clearly establishes a broad federal mandate for income security, of which the UISP is a logical development. Moreover, we believe that individual provinces acting alone would not be capable of bringing such a program into operation.

To create the UISP, however, would involve a major change in federal-provincial relations, a change which Commissioners think would be healthy for the federal system. The 50/50 sharing of responsibility for welfare payments under CAP would end, and the provinces would become solely responsible for the provision of any supplement above the established guaranteed income level. Changes in the tax system would help to finance the UISP. Under one recommended approach, provinces would cede some tax room back to the federal government, which would then deliver the entire program. Under a less desirable arrangement, provincial governments would superimpose a provincial layer of payments on the federal transfer. Particularly under the first option, the UISP proposal would involve a major disentanglement of federal and provincial responsibilities: the federal government would have authority over basic income support, which would be set at a national minimum; the provinces would be free to increase the level of these benefits by supplementing the federal payments. Our proposal would therefore increase federal and provincial flexibility, and significantly improve accountability at both levels.

Provincial opposition to the UISP is likely, however, if the effect of this proposed program were to increase provincial responsibilities while diminishing the funds available to the provinces. The federal government should develop the program in close consultation with provincial governments. The disentanglement that the UISP calls for would not eliminate federal-provincial interdependence because any future changes in the program's levels would have immediate consequences for provincial burdens.

If it is not possible to proceed immediately with the UISP proposal, Commissioners advocate a number of smaller interim changes in social policy. First, family benefits should be rationalized by replacing current programs with a single demogrant or tax credit, to be progressively "taxed back" for

families with incomes of over $26 000 a year. This change would not raise major federal-provincial issues. A second immediate reform, which we advocated in Part V, is the revision of the Canada Assistance Plan to reduce the features that lead to a "poverty trap", creating disincentives for recipients to re-enter the work-force. This step would require considerable federal-provincial co-operation and co-ordination. The appropriate vehicle for achieving this is the Council of Ministers Responsible for Social Policy which we shall shortly propose.

Commissioners have also proposed making a number of changes in the Unemployment Insurance (UI) system. We have suggested making it more of a risk-related insurance scheme, extending the qualifying period for UI benefits, and removing regionally related subsidies built into the program. These changes will have important regional and federal-provincial ramifications. Regionally related Unemployment Insurance benefits, combined with a short qualifying period, have become a major part of the social fabric of many communities in the Atlantic provinces. Moreover, unilateral federal changes in Unemployment Insurance inevitably have major repercussions for provincial welfare costs.

The changes Commissioners have proposed would have the greatest effect on the poorer provinces with high rates of unemployment. Under current arrangements, provincial governments receive some protection from federal reductions in the level of UI transfers: under CAP, the federal government picks up half of any additional welfare costs. If CAP disappears, however, this mechanism will not be available, and the more expensive UISP will replace it. The effect of these UI changes on provincial budgetary requirements must therefore be weighed carefully, and the government must ensure that compensation is available for provinces especially hard hit by them. The main purpose of this change, after all, would be to increase the incentives for individual mobility, and not to shift burdens onto the provinces.

Single-industry resource-based towns raise a special adjustment problem. A mine closure or some similar event can devastate such communities almost overnight. The costs of such events extend far beyond the workers actually employed in the particular resource sector affected: to ease the burden of such economic shocks will require co-ordination of the activities of all three orders of government. Commissioners therefore propose a mechanism analogous to that used in other kinds of emergencies: an *ad hoc* federal-provincial-municipal task force that would include representatives of the community to co-ordinate these efforts. In Part V, Commissioners suggested that the TAAP, which would be funded by the savings accruing from the Unemployment Insurance reforms noted above, should compensate for losses of assets, such as the value of housing, caused by the sudden undermining of the community's economic base.

Conclusions

Federalism is inevitably a complex system of government, and one that provides little comfort to those with tidy minds. Nonetheless, we Canadians have adapted it successfully to the requirements of our post-Second World

War Canadian society, and it remains a means of permitting policy that is sensitive to the wide diversity of needs and interests across the country. Canadian federalism has also been a source of dynamism.

This Commission has now canvassed goals and objectives, asking whether their attainment will require major changes in the structure and operation of the federal system. Some readers will infer that our answer is yes. We have, after all, made a number of suggestions for significant change: for strengthening the federal power over trade and commerce by adding competition and product standards, for redefining federal responsibilities in post-secondary education, to mention two. Yet as we have examined each area, Commissioners have found a great deal of potential for flexibility. Our vision is not of a central government hamstrung by federalism in the face of oncoming challenges; rather, we have seen the wide scope for action within federal jurisdiction. Moreover, we have directed a number of our recommendations to the provinces, rather than the federal government, and we have concluded in most instances that the provinces have the ability to respond. Finally, we have recognized that in many policy fields, shared jurisdiction is not a constitutional accident, but a faithful reflection of the co-existence of legitimate provincial and national concerns. To call for complete centralization of powers, or for extensive decentralization, in such areas would almost certainly lead policy makers to neglect important dimensions and to be less sensitive to vital interests. Thus we think that shared jurisdiction in a field such as training is both necessary and desirable. Moreover, we believe that it is possible to design effective mechanisms through which to achieve the required co-ordination.

In addition, Commissioners believe that federal jurisdiction over trade and commerce and over "Peace, Order, and good Government" can evolve in the light of emerging economic needs. The courts have constrained the trade and commerce power, and the federal government has used "Peace, Order, and good Government" largely as an emergency power; but both powers have sustained legislation of inherent national importance. We expect that this will happen again. The need, as before, will be to balance the vitality of federalism against national needs. Any legislative extension of these two forms of federal power should clearly address a widely experienced need which existing legislation, whether federal or provincial, cannot deal with adequately, and which, to be effective, must apply uniformly across the country. Furthermore, such legislation, to be acceptable, would have to respect existing provincial economic patterns; these patterns could not be set aside without a compelling, demonstrated, national need, and even then, only to the extent necessary to meet the defined national purposes. Thus, we believe it essential to protect valid provincial objectives against open-ended federal intervention in the pursuit of national goals; but there might well be cases in which judges might incrementally adapt the general federal trade powers, applying a concept of "compelling national interest" that is broader than an "emergency power", but narrower than a simple undefined national interest. We hope for further judicial creativity in developing such constitutional mediating principles.

The virtues of federalism remain important from the perspective of democracy and effective policy making. Not only does the existence of

provinces with wide powers accord with the political sense that we Canadians have of ourselves but, in addition, the provinces offer other channels of access, forums for accommodation of conflicting interests, and arenas for adaptation, experimentation and gathering of information. The very complexity of federalism provides a resilience and capacity to absorb shocks not always found in highly centralized systems.

Nevertheless, with both orders of government deploying so many instruments in the pursuit of economic growth in a competitive international environment, Commissioners recognize the need for a high degree of co-ordination. There has been much searching for the "right" mechanism to achieve this co-ordination, along with virtually continuous change in the political structures through which the federal government integrates national and regional perspectives in its own policy-making process. Commissioners believe that the recently developed mechanism of the Economic and Regional Development Agreement (ERDA) provides a promising model. ERDAs provide for bilateral co-ordination on basic goals, together with a division of labour based on agreement as to which government will take responsibility for which areas. They become the umbrellas under which the governments work out more detailed agreements between particular departments. Within this framework, we think it desirable, on grounds of accountability, that each government seek to take responsibility for final design and implementation of the relevant components of the larger agreement. In discussions, the federal government should emphasize the perspective of the whole national economy and of the integration of each region within it, and maximize linkages between regions. In accordance with our consistent emphasis on adjustment, we also believe that federal efforts should assist Canada's provinces and citizens to adjust to the new competitive environment.

The constraints that federalism imposes on economic management are not primarily constitutional. Rather, they arise out of the regional structure of our country. It is not lack of authority, for example, that will limit federal efforts to place less emphasis on place prosperity and more on individual mobility. It is political opposition – and the need to balance conflicting signals from different parts of the country – that will prove the real difficulty. For this reason we must rely on political institutions, both at the national and the intergovernmental level. To reorient the focus of Canadian economic policy will not be easy, because it will require construction of new consensus on our strategy of instruments of development and distribution. To form this strategy is a task for democratic political leadership, guided by much talk among citizens in a multitude of forums.

Notes

1. Canada, Department of Reconstruction and Supply, *Employment and Income* (Ottawa: King's Printer, 1945).
2. John D. Whyte, "Constitutional Aspects of Economic Development Policy", in *Division of Powers and Public Policy*, vol. 61, prepared for the Royal Commission on the Economic Union and Development Prospects for Canada (Toronto: University of Toronto Press, 1985).

3. Samuel H. Beer "Federalism: Lessons of the Past; Choices for the Future", in Center for National Policy, *Federalism: Making the System Work* (Washington, D.C.: The Center, 1982), p. 20.
4. This study has been summarized in Roger F. Swanson, *International Perspectives on the Canada-U.S. Relationship* (New York: New York University Press, 1978), pp. 221–65.
5. See P.R. Johannson, "British Columbia's Relation with the United States", *Canadian Public Administration* 21 (Summer 1978): 212–33.
6. See Richard Schultz and Alan Alexandroff, *Economic Regulation and the Federal System*, vol. 42 (Toronto: University of Toronto Press, 1985).
7. See Economic Council of Canada, *Efficiency and Population: A Study of Deposit Institutions* (Ottawa: Minister of Supply and Services Canada, 1976).
8. Nicolas Roy, *Mobility of Capital in the Canadian Economic Union*, vol. 66, prepared for the Royal Commission on the Economic Union and Development Prospects for Canada (Toronto: University of Toronto Press, 1985).
9. See Thomas J. Courchene, *Economic Management and the Division of Powers*, vol. 67 (Toronto: University of Toronto Press, 1985).
10. Schultz and Alexandroff, *Economic Regulation and the Federal System.*
11. Canada, Finance Canada, *The Regulation of Financial Institutions* (Ottawa: The Department, 1985).
12. *Attorney General of Canada* v. *Canadian National Transportation Ltd.* (1983), 3 D.L.R. (4th) 16 (S.C.C.)
13. *Labatt Breweries of Canada Ltd.* v. *Attorney General of Canada* (1979) 110 D.L.R. (3d) 594.
14. David McQueen, "Commentary on James C. MacPherson, 'Economic Regulation and the British North America Act' ", *Canadian Business Law Journal* 5 (1980–81), pp. 225 and 227.
15. *Dominion Stores Ltd.* v. *The Queen* (1979), 106 D.L.R. (3d) 581.

Sharing the Benefits of the Economic Union

Canadian politics, it often seems, is the politics of regional interests and of regional grievance. Subjects which other countries more often discuss in terms of relations between capital and labour, Canadians discuss primarily in terms of regions and provinces. The question "Who gets what?" is expressed in terms of territory and geography. This is a constant of Canadian history, one grounded both in our varied social and economic structure, and in our political institutions as well. Canadians have recently emerged from a period in which this regional perception of advantage and disadvantage has been particularly evident. Throughout the 1970s, the issues which most divided Canadians seem to have pitted region against region. These perceptions frequently emerged in this Commission's hearings.

Across the country, we found a considerable sense of grievance: a sense that decisions made by the federal government do not reflect the needs of the regions affected by them, and less frequently, but still not insignificantly, that decisions are made which discriminate against certain regions. Survey results indicate that Canadians were divided in their responses to the question of whether their province had been treated fairly by the federal government. In a 1977 survey of five provinces, a slight overall majority believed that their province was treated fairly all of the time or most of the time. Only Ontario residents, however, were strongly positive in this view, while majorities in P.E.I., Quebec, Saskatchewan and B.C. considered that their province was treated fairly only some of the time, or, an infrequent response, none of the time. In a 1979 survey, more Canadians (31.5%) responded that their region paid more than its fair share of the costs of governing Canada than replied (5.4%) that their province paid less than its fair share. The most frequent response, however, (63.2%), with majorities in every province except Alberta (50.0%) believed that their region paid its fair share.[1] The picture, therefore, is mixed. The fact remains, however, that many Canadians sense that the "Confederation bargain" has somehow not worked out fairly, and that the federal government has at times been less the "national government" than the instrument of the most populous parts of the country.

Such beliefs stem from many sources. In part, they are the result of a sense of provincial identity in which the economic health of a particular province remains a vital reference point. The actions of provincial governments often reinforce these perceptions. They are, to some extent, a political, rather than an economic, phenomenon: a sense of exclusion from power in the national capital can powerfully reinforce regional grievances.

Regional grievance is not a new element in Canadian politics. Indeed, it has been a constant theme since the first days of Confederation. Regional protests have fuelled a succession of movements of political protest in the West: the Progressives, the United Farmers, Social Credit, the Co-operative Commonwealth Federation. Regional issues have also been a significant element of successive expressions of Quebec nationalism. While regional parties have been less successful in Atlantic Canada, groups such as the Maritime Rights movement of the 1920s have often expressed regional grievances in frequent calls for "better terms". Throughout Canada's history, regional grievances

have been expressed both as demands for more provincial autonomy that would allow provinces to shape their own future, and as demands for federal policies that would be more responsive to regional interests. Regional protests are simultaneously requests for a greater influence in national decision making, and insistence on the assertion of greater autonomy and freedom to make one's own decisions.

The sense of unfairness that has sometimes surfaced in Canadian experience has had different sources at different times and in different places. In the West, grievances were originally rooted in the perception that the National Policy treated the region as an economic hinterland to central Canada, as a source of raw materials and export earnings, and as a protected market for central Canadian manufacturing, transportation and financial interests. Historic conflict thus centred on issues such as the tariff and, to a lesser extent, on transportation policy. In the 1970s, it hinged on the provinces' sense that they were being denied the full benefits of the rising value of their natural resources, which they regarded as the means by which they could diversify their economies and shift economic and political power away from central Canada.

In the Maritimes, grievances were fuelled by the long decline of the Maritime economy in the nineteenth century, by the declining importance of the region to the country as a whole, and by the persistence of regional disparities. In the 1970s, resentment increased about continued dependence on transfer payments, at the same time that Nova Scotia and Newfoundland, in particular, realized the possibility of transforming their economies by developing off-shore resources. In Quebec, grievances stemmed from the perception that national policy favoured Ontario's economic development, and that the constraints of federalism limited Quebec's ability to take charge of its own economic development. Ontario also tended to react to the events of the 1970s in a "regional" fashion as it became aware that its dominant position in the Canadian economy was being threatened both by the increase in resource revenues in the West and by the assertions of nationalism in Quebec.

Provincial governments tended to express these regional grievances through complaints about the role and actions of the central government; they took the view that the pattern of economic development in Canada was not the product of natural economic forces, but rather of the exercise of political power by major interests acting through the central government. They also called on the federal government to redress the forces of the market by using its authority to compensate those regions which the market tended to leave behind.

Thus growing expectations of the role of government reinforced Canadians' tendency to see politics in regional terms. Moreover, the increasing importance of international forces on domestic life further supported a regionalist view. The diversity of provincial economic bases meant that international forces were likely to have different domestic effects. Consequently, regional strains of the 1970s pitted resource producers against resource consumers and manufacturers, or set areas with an interest in higher

resource prices against those with an interest in lower ones; they, however, were not primarily the product of domestically generated pressures, but rather of international forces which dramatically altered the terms of trade among Canada's regions.

All of these perspectives were reflected in the "battle of the balance sheets" that occurred in the late 1970s. This controversy involved elaborate and often polemical efforts to assess which parts of the country were or were not "losers", and to identify the regional distribution of the costs and benefits of federal government activities. There were few, if any, conclusive answers. It was easy enough to identify the sources of federal tax revenues, or show where Old Age Security, Family Allowances or regional development grants went; but it was much more difficult to assess the regional effect of broad structural policies. And indeed, to many Canadians, the entire attempt to identify regional winners and losers was misguided: was it not, after all, the national economy and the welfare of individuals which were important? These questions highlight the disjunction between our tendency to view Canada as a collection of regional economies with historic grievances, and our sense of Canada as a national economy in which each of the parts contributes distinctively to the well-being of the whole.

This approach also missed many of the more subtle dimensions of our sense of fairness with respect to the distribution of costs and benefits. Virtually all policies and programs distribute their benefits and costs differentially, and we assess such distributions in terms of many categories, including income classes, age and sex. Differences in regional benefits may be explicit and intentional, or they may be the result of redistributive policies defined in terms of other categories. For example, policies to assist the elderly will confer greater benefits in those provinces where the highest proportions of elderly Canadians reside. Moreover, where policies do deliberately discriminate, we tend to view them in different ways: discrimination in favour of the disadvantaged or the poor provokes different reactions from that in favour of the rich and powerful. Finally, we judge fairness not in terms of a single policy or program, but in terms of the cumulative effects of many policies; it is a systematic, repeated lack of response, or discrimination, which leads to alienation.

We Commissioners do not attempt to present our own balance sheet of Confederation. Rather, we focus on two specific policies: equalization and regional development. Both of these are aimed at alleviating the persistent regional disparities in the Canadian economy. Equalization and regional development are complementary policies. Equalization is intended to reduce the fiscal consequences of relative underdevelopment. Regional economic policy is intended to reverse underlying economic disadvantages. The more successful the latter, the less need there is for equalization.

Commissioners believe that the question of real and perceived fairness is very much a political issue. To the extent that Canadians focus their allegations on the "unfairness" and unresponsiveness of the central government and its agencies, reform must focus there. Fairness also has a federal dimension. It implies that provinces have a legitimate concern with the economic development of their own regions. It also suggests that provinces

must feel reasonably secure in the exercise of their constitutional powers and in the ownership of the resources within their borders. These last are essential to the exercise of an effective provincial role in economic development.

Equalization

Of all the issues discussed during successive rounds of constitutional debate, there was almost unanimous agreement to entrench in section 36 of the Constitution the commitment to equalization. In so doing, Canadians gave formal recognition to an essential component of the Confederation bargain: the idea that all citizens have a right to "reasonably comparable levels of public services" from their provincial governments at "reasonably comparable levels of taxation". Variations in policy to reflect local preferences were desirable; variation in the nature and quality of services because of inequalities in the ability to provide them was not.

The equalization program represents the most long-standing and explicit commitment to interregional sharing in Canada. It consists of unconditional payments from the federal government to the less well-off provinces. In 1985–86, these payments are estimated at $5 billion, payable to all provinces except British Columbia, Ontario, Alberta and Saskatchewan.

The apparent provincial-federal harmony suggested by agreement to entrench section 36 exists in spite of widespread misunderstanding about the actual nature of Canada's equalization arrangements. Equalization is often confused with regional development programs or income-maintenance and security measures for individuals. In the acrimony that followed the adoption of the National Energy Policy, Western separatist leaders sometimes portrayed equalization as a device for making direct transfers from energy-rich western provinces to energy-poor eastern ones. Various quarters have criticized equalization as too generous or as not generous enough; as necessary to an efficient allocation of capital and labour, or as a prime cause of distortions in these patterns; as too mechanical and routine, or as too *ad hoc*.

In Commissioners' view, equalization is a vital feature of the Canadian federation. While there are many reasons to be proud of what Canadians have achieved in this area, there is room for improvement. In view of the confusion surrounding the topic, Commissioners wish first to review the bases of our equalization arrangements.

Principles of Equalization

Equalization schemes would be unnecessary in a unitary state, where all taxes are paid to one government, and all public sector benefits flow from it. The government need not, and almost certainly would not, treat all individuals identically: higher-income groups would pay a larger portion of their income as tax; large families would receive more substantial basic deductions from gross income than would small families; those without earnings would receive more in the way of transfers than they would pay as tax. Such imbalances in

the tax-expenditure system would be deliberate; they would reflect, however imperfectly, a judgement about the fair distribution of benefits and burdens.

In a federal state, however, citizens are faced by two tax systems, and two sources of public goods and services. Their treatment by provincial governments would almost certainly vary. Some provinces would decide to provide relatively more goods and services through the public sector and to finance them through higher taxation. Others opt for more or less redistribution among income classes. Indeed, if there were not these differences among provinces, reflecting different local values or preferences, one of the main reasons for federalism would disappear.

Such provincial variations are not, in themselves, a problem. If governments faithfully implement the wishes of the local majority, the system is working as it should. Canadian diversity is reflected in variations in policy at the provincial level. With free interprovincial migration, the arrangement is even more likely to conform to citizens' preferences. In theory, by voting with their feet, citizens "sort" themselves into relatively homogeneous subgroups: those who prefer an active public sector go to provinces offering this feature, while others move to areas where the provincial government takes a different approach.

There is, however, another, less acceptable, reason for variation among provinces. Not all provinces were "created equal" in an economic sense. Per capita incomes vary owing to such factors as resource endowments, occupational and industrial mixes, degrees of urbanization, or ease of access to major markets. A lower average income, which reflects lower wages, smaller returns to investments, and less remunerative land and resource rents, means a lower fiscal capacity for the government of the region; that government will raise less revenue from a given taxation effort than will a wealthier neighbour. Consequently, a poorer province will either have to provide a lower level of government goods and services at tax rates comparable to those of other provinces, or it will have to impose higher tax rates to finance a comparable level of services, or it will "package" some combination of higher taxes and lower services. Whatever situation prevails, citizens in a poorer region will be treated differently by government from their counterparts in other provinces. This follows inevitably from the fact of unequal regional economic endowments.

Some might argue that such differences are simply the price of a federal system: provinces can only be truly free to design their own taxation and expenditure policies if they have full fiscal authority. If the result is a variation in interprovincial fiscal capacities, such variation is inherent in federalism. Federal income-maintenance and security programs will apply to those individual Canadians in genuine need of support.

Commissioners reject this argument for two reasons. First, and most important, this reasoning compromises our understanding of what it means to be Canadian. An essential element of citizenship in this country must be relatively equal access to basic government services, irrespective of place of residence. While Commissioners are content to see the provision of these services decentralized, we are loath to accept too much variation in individual

access to them across jurisdictions. This commitment to regional equality arises from the same foundations as our commitment to social welfare policies.

Equalization reflects Canadians' sense of a common obligation, of our interconnection and of well-being and satisfaction with the national community. These last convictions depend on our assurance that all of us are fairly sharing the benefits, and bearing the burdens, of maintaining our society. Equalization adds an important regional dimension to this sense of shared belonging: it implies that a strong Canadian community encompasses the existence of strong, healthy provincial communities. Individual equity alone does not capture our commitment as Canadians to these provincial communities. It is ultimately because of shared membership in the whole Canadian community that we understand the necessity for ensuring the vitality of each of its constituent parts.

If the first justification for equalization is one of equity and social justice, a second is efficiency. Recent research has shown that variations in the fiscal capacities of provincial governments can themselves constitute distortions which reduce aggregate national output. This result can be corrected by a properly designed equalization scheme. Since the efficiency argument is a recent one, and since it underlies so much of recent debate, as well as this Commission's recommendations, it is worth sketching briefly.[2]

National output is maximized when capital and labour are allocated across regions so that the contributions to gross national product (GNP) of the last unit of capital employed and the last unit of labour employed are identical. Under normal circumstances, free internal migration of capital and labour will automatically produce this optimal allocation of capital and labour. As long as productivity differences are reflected in wages or rates of return, and as long as at least a fraction of the labour force or of investors is sensitive to the earnings possibilities associated with such differences, migration will flow from low- to high-productivity regions.

But what if significant differences exist in the fiscal capacities of provinces? An employee who is contemplating migration is likely to compare not just private earnings across regions, but also the treatment to be expected from the public sector. If one jurisdiction promises greater government services relative to taxes than does another, and if expected earnings are similar, the migrant has an incentive to choose the location offering more generous treatment. The result could be an influx to this province, driving down wages and salaries to the point where the expected tax-expenditure benefits just offset the lower private earnings. The opposite is true of the fiscally poor region; private earnings must be higher to offset the relative paucity of tax-financed goods and services. This "fiscally induced migration" responds to policy signals rather than to market signals based on the most productive allocation. The result may be lower output, since there will be too many workers in fiscally generous regions and too few in the others.

Equalization payments provide a means of responding to both equity and efficiency problems in a federation. Provincial governments that have a fiscal capacity below an acceptable standard receive unconditional revenue

transfers, reducing the fiscal discrepancy among provinces. The transfers compensate, in effect, for the province's lack of a natural tax base. When fiscal differences are narrowed or removed, Canadians, wherever resident, achieve a more similar status in their overall relations to government, and the incentive for socially inefficient migration is reduced.

The transfers are intended only to make it possible for any province to provide basic public services at a prescribed standard without imposing undue taxation. Whether a province actually chooses to provide particular services, or how it allocates the funds, is entirely its own responsibility. As the Royal Commission on Dominion-Provincial Relations (the Rowell-Sirois Commission) stated, when discussing its National Adjustment Grants (the forerunner of equalization):

> *If a province chooses to provide inferior services and impose lower taxation it is free to do so, or it may provide better services than the national average if its people are willing to be taxed accordingly, or it may, for example, starve its roads and improve its education, or starve its education and improve its roads . . .*[3]

Thus, equalization payments are a means to ensure that all governments can adequately carry out whatever responsibilities they were assigned. Equalization involves no diminution of provincial freedom or authority, and no federal control over provinces. Indeed, to make equalization payments conditional in any way would obviate the very essence of federalism.

Equalization is an essential feature of Canadian federalism. It effectively reconciles the principle of provincial autonomy with the principle of equal access of all Canadians to basic government services. Without it, Canadians would require a more highly centralized federation or would need to be willing to tolerate greater differences in standards of living and less efficient migration of labour and capital. The Rowell-Sirois Commission was the first to make this point when explaining its proposal for National Adjustment Grants:

> *They are designed to make it possible for every province to provide for its people services of average Canadian standards and they will thus alleviate distress and shameful conditions which now weaken national unity and handicap many Canadians. They are the concrete expression of the Commission's conception of a federal system which will both preserve a healthy local autonomy and build a stronger and more united nation.*[4]

While circumstances have obviously changed from the post-Depression years of Rowell-Sirois, the sentiment is still valid.

To suggest that an equalization scheme is desirable raises two questions. First, should fiscal differences among provinces be fully, or only partially, equalized? There is a host of subsidiary technical issues associated with this question. Secondly, should the central government, the provinces, or the two orders of government combined operate and fund the program?

There is no right answer to the question, "How complete should equalization be?" The traditional response in Canada has been, in the words of the Rowell-Sirois Commission, that equalization is necessary to achieve "average

standards of services in every province." A former federal Finance Minister stated that the goal of equalization was to enable "each province to provide an adequate level of public services without having to resort to rates of taxation substantially higher than those of other provinces."[5] Significantly, nearly the same words appear in section 36 of the Constitution Act, 1982:

> *Parliament and the government of Canada are committed to the principle of making equalization payments to ensure that provincial governments have sufficient revenues to provide reasonably comparable levels of public services at reasonably comparable levels of taxation.*

Theoretically, it is relatively easy to design an equalization scheme that embodies the principle of reasonably comparable standards. In the approach that has evolved in Canada during four decades, the formula provides an equalization payment for any province in which average or representative provincial tax rates (not its own tax rate) would yield less revenue per capita than the yield in Canada generally. In the method used, an average or representative provincial tax base is first specified by listing all main revenue categories open to the provinces. Next, a representative provincial taxation effort is calculated. Here a taxation rate judged to be representative of the provinces overall is set for each of the revenue categories in the base. Applying those taxation rates to the base and standardizing for population, yields the revenue a province would collect if it had an average or representative fiscal capacity and levied average taxation rates. This figure represents the minimum amount of revenue that it is deemed a province of this size should be guaranteed.

The next step in the procedure is to calculate the actual tax base of each province. This calculation is done for each of the revenue categories contained in the representative base. Applying the representative or average provincial taxation effort (*not* the province's own tax rates) to this base produces the total revenue the province could raise if it taxed each of its revenue sources at national average or representative rates. If this figure exceeds the revenue floor as calculated above, it creates no problem.

Equalization entitlements are necessary, however, when a province's revenues from taxing its own base at representative or average rates fall short of the revenue floor. Since equalization is guaranteed to cover this shortfall, the province can duplicate the public sector performance of the representative or average Canadian province.

The important point to note is that the revenues which the province actually collects do not enter directly into the calculation. The comparison is not between what could be and what is; rather, it is between what could be if the province were the representative or average Canadian province, in terms of both tax base and taxation effort, with what could be if the province chose to tax its actual base at national average or representative rates. How the province actually taxes does not directly affect its equalization entitlements. If it taxes at greater than representative rates, its total revenue will be that much greater; equalization entitlements will not fall. Conversely, if it chooses to tax less, its equalization entitlement does not rise. This is the practical counterpart of the Rowell-Sirois principle of unconditionality.

To implement these general guidelines involves a large number of technical problems. What exactly would constitute a representative provincial tax base? Should all revenue categories potentially open to provinces be included, or only those they actually use? How should the situation be affected if not all provinces use all revenue sources open to them? Should it change if they do use all revenue sources available, but sometimes treat them quite differently? What is the proper basis for taxing each revenue category? Should the representative taxation level be hypothetical, or should it be linked to what Canadian provinces do in practice? Should profits of Crown corporations be considered government revenue? These are just a few of the possible questions to be considered in designing an equalization scheme. Sometimes, as we shall see below, the wrong design can create more general problems for equalization.

Canadian Experience

The first specific proposal for a formal equalization scheme was the National Adjustment Grants proposed by the Rowell-Sirois Commission. Previous attempts to even out discrepancies in provincial fiscal capacities were either implicit or *ad hoc*. The transfers to the provinces agreed to by the federal government in 1867 were, by their nature, equalizing in that they were per capita grants. There was no connection between the amount the federal government collected from residents of any province and the transfers made to that province. In addition, special payments were given to individual provinces or even to entire regions. New Brunswick received these special payments from the outset; Nova Scotia began to receive them a short time later. In 1926, the Royal Commission on Maritime Claims (Duncan Commission) investigated the financial claims of the Maritimes, and the Royal Commission on Banking and Currency in Canada (White Commission) did so, in 1933, for both the Maritimes and the Prairies. It took the depression of the 1930s and the imminent bankruptcy of several provinces to demonstrate that these *ad hoc* arrangements were not enough.

National Adjustment Grants, together with most of the Rowell-Sirois Commission's recommendations, were casualties of wartime emergency. The federal government assumed exclusive control of personal and corporate income tax and succession duties, paying "rents" to each province according to a predetermined formula which, like its forerunners, was implicitly equalizing. Equalization, as Canadians know it today, was formally implemented in 1957. The tax-sharing arrangement introduced in that year linked the amount that the federal government transferred directly to each province to the revenue collected from that province. Each province received 10 per cent of the personal income taxes collected in the province, 9 per cent of the corporate profits, and 50 per cent of federal succession duties. Clearly, 10 per cent of the personal income tax collected in a richer province represented more revenue per taxpayer than it did in a poorer one. To compensate for these differences, the federal government unconditionally transferred to each of the poorer provinces an amount that would bring its per

capita yield from these three standard taxes up to the average yield of the two wealthiest provinces (Ontario and British Columbia). By this calculation, every province but Ontario qualified for equalization transfers, and a total of $139.1 million was paid out to nine provinces in the 1957–58 fiscal year.

From the outset, the equalization system has become progressively more comprehensive. In 1962, provincial natural resource revenues were added to the tax-base calculation. The standard was also lowered to the national average yield of the taxes in the base. These two changes made Alberta and British Columbia ineligible for equalization payments. In 1967, 16 provincial revenue sources, including those not shared with the federal government, were added to the tax base. The number of taxes in the base was increased to 19 in 1972 and to 29 in 1977, thus bringing equalization more and more into line with real taxation practices.

During the 1970s, the equalization scheme was severely tested as a result of the dramatic increase in natural resource revenues concentrated in Alberta, British Columbia and Saskatchewan. Since the scheme involves federal payments, compensation was owed to all other jurisdictions, including populous Ontario and Quebec, for their lack of such revenues, even though the federal government, in a practical sense, did not have direct access to these revenues. Moreover, Ontario soon became a "have-not" province and would have qualified for payments. All of this was taking place in a period of rising concern about the size of the federal deficit in general. A series of *ad hoc* adjustments to the formula followed, mostly redefining the way energy revenues were treated. The rules were changed to exclude provinces with per capita incomes above the national average from eligibility for such compensation. Rising energy revenues required that the concept of "full equalization" be abandoned.

More than just technical or design issues were at stake during this period. The large energy revenues accruing to the Western provinces, Alberta in particular, raised anew the more basic question of determining appropriate equalization . Specifically, were other provinces entitled to larger equalization payments simply because Alberta's fiscal capacity was suddenly and dramatically increased? (In 1980, Alberta's "own-source" revenues had risen to 232 per cent of the national average.) Questions arose concerning, for instance, the way Alberta's windfall affected the demands a Nova Scotian placed on provincial public services. Past Canadian practice of reasonably comparable levels of services at reasonably comparable tax rates provided little guidance. Was the comparison to be made to the wealthiest provinces, as in the 1957 formula? If so, essentially full equalization of energy revenues was required. Or was it to be made only with national average tax yields, as in the system then in place, recognizing that this meant that slightly less than half of the energy revenues would be equalized? Were "adequate" standards more or less demanding than "comparable" ones? If so, this would imply the applicability of a relative rather than an absolute criterion. The federal government was finding even this more limited commitment increasingly difficult to finance. Without the energy-related changes to the formula, 1981–82 equalization payments would have been nearly $3 billion above the

level of the $4.61 billion otherwise estimated. Each additional dollar of resource revenue accruing to provinces would have required Ottawa to increase its outlay on equalization by 75 cents.[6]

Some analysts argued that there was no need to equalize any of this windfall gain. Because one province is suddenly wealthier, the ability of others to supply an acceptable level of public goods at an acceptable tax level has not been eroded. In other words, greater government revenues in one province do not create greater needs in another. Others argued for the alternative view that such dramatic differences as existed between the fiscal position of Alberta and the rest of the country were untenable. The fact that the largest province had experienced the greatest relative decline, and a smaller one had experienced the boom, gave political weight to this argument, since the residents of the more populous provinces could use their political influence on the national government to bring about greater sharing, either in the form of transfers or in lower prices.

For the first time, efficiency considerations also played a significant role in equalization debates. Some observers alleged that since Western energy revenues were only imperfectly equalized, an imbalance was created in the migration of capital and labour from one province to another. This imbalance, it was argued, was detrimental to Canada as a whole, since it was induced by government revenues rather than by enhanced economic opportunities. Research studies did indeed demonstrate some sensitivity of migration flows to net fiscal differences among provinces.[7] One contribution to the debate alleged that without a proper equalization scheme in place, the costs to Canada of moving to world energy prices would likely exceed those associated with keeping oil prices at an artificially low level.[8] The point was that efficiency dictated some equalization of resource revenues even if one were not convinced that it was required to achieve greater equality among Canadians.

The best-known exponent of this "new" view of equalization was the Economic Council of Canada (ECC) in its report *Financing Confederation: Today and Tomorrow*.[9] There, the concepts of provincial equity and economic efficiency were proposed as formal pillars of an equalization scheme, to replace the much less precise "comparable standards" criterion. This led the Council to propose full equalization of all provincial revenue sources, except those associated with resources. Only partial equalization of this last category was recommended. The Council argued that since resources are constitutionally the property of provincial residents, they should be treated as if they were private income and taxed at the prevailing personal or business-tax rate. Only the expected yield from applying this rate would count for equalization purposes. The ECC made a number of other proposals, most notably that the forgone revenue from low-priced hydro-electricity in Ontario and Quebec be counted as resource revenue.

The Council's views appeared too late to influence the negotiations leading to the current equalization measures. As part of the 1982 Fiscal Arrangements Act, these measures incorporated several changes from the previous formula. Equalization to the national average was replaced by equalization to a "five-province standard". Provinces were to be paid the difference between

their hypothetical revenue at national average tax rates and a representative level of funds obtained by applying national average tax rates to the weighted average per capita tax base of Ontario, Quebec, Manitoba, Saskatchewan, and British Columbia. Leaving Alberta out of the standard effectively did away with the energy-revenue problem; the formula simply ignores any revenue that province now receives. The exclusion of Alberta lowered entitlements stemming from resource revenues, but excluding the four Atlantic provinces raised entitlements based on most other revenue sources.

The 1982 Fiscal Arrangements Act also included other changes in equalization arrangements. Coverage was extended to include municipal revenues and 100 per cent of resource revenues; however, the exclusion of Alberta meant that the resource revenues included were a small fraction of those previously counted. A cap was placed on payments, limiting their growth to no more than the increase in the gross national product (GNP) since 1982. A minimum level of payment guarantee and transitional payments were included to offset the effect of particular changes in individual provinces. Quebec and Manitoba were the main losers from the changes; the position of the Atlantic provinces remained virtually unchanged. The effect of moving to the new system was to reduce equalization entitlements (including transitional payments) by 11 per cent or $560 million in 1982–83, although the payments were still some 13 per cent above those made the previous year under the formula then in effect.[10]

The Success of Equalization

Has equalization been effective in smoothing out differences in fiscal capacities across provinces? Have Canadians met the standards set by the Rowell-Sirois Commission 45 years ago? Since there is no precise measure of fiscal capacity, there are no definitive answers to these questions. Indirect measures, however, can be used to gain an idea of the influence of equalization.

The obvious first step in assessing relative fiscal capacities is to compare actual revenues per capita across provinces. These data are presented in Table 22-9. The first row indicates "own-source" revenue, that is, funds the provinces raised in 1981–82 by applying their own tax rates to their own taxation base. The variation among provinces is striking, ranging from per capita revenues of $1026 for Nova Scotia to $3900 for Alberta. The latter province, with its huge energy revenues, is admittedly an extreme example. By excluding Alberta and Saskatchewan, the range is considerably reduced: from $1026 to $1765. Nevertheless, there is a large disparity in the revenue available to the provinces; the four Atlantic provinces and Manitoba are the poorest, and Quebec, Ontario and British Columbia rank between them and Alberta and Saskatchewan.

The second row of Table 22-9 adds federal transfers other than equalization to own-source revenue. Since some transfers, are implicitly equalizing, the disparity among provinces is reduced to some degree, but it remains significant. Equalization transfers are added in the third row. This addition reduces significantly the disparity and the provinces' ranking changes.

TABLE 22-9 Equalization and Provincial Finances, 1980–81

Row	Nfld.	P.E.I.	N.S.	N.B.	Que.	Ont.	Man.	Sask.	Alta.	B.C.	Total
1. Own-source revenues ($ per capita)[a]	1 228	1 090	1 026	1 092	1 648	1 455	1 276	2 121	3 900	1 765	1 749
2. Own-source revenues plus federal transfers other than equalization ($ per capita)[b]	1 871	1 745	1 653	1 692	2 272	1 973	1 836	2 631	4 422	2 335	2 308
3. Gross provincial revenues (row 2 plus equalization) ($ per capita)	2 514	2 445	2 176	2 224	2 543	1 973	2 169	2 672	4 422	2 335	2 449
4. Equalization as a percentage of own-source revenues[c]	52.4	65.1	51.0	48.7	16.5	0.0	26.1	1.9	0.0	0.0	8.1

Source: Thomas J. Courchene, *Equalization Payments: Past, Present and Future* (Toronto: Ontario Economic Council, 1984), p. 153.

a. Population figures from Department of Finance (1982a, 15).
b. Same tables as in a above.
c. Equalization data adapted from MacEachen (1981, Table V-I). Own-source revenues calculated from Table II-4 of the same document.

Alberta is still the wealthiest province, but Ontario goes to the bottom of the list. Without resource revenues and decreed ineligible for equalization, Canada's most highly industrialized province apparently has the lowest fiscal capacity. The importance of equalization to some provinces is evident from the fourth row of Table 22-9. The payments amount to nearly two-thirds of the revenue Prince Edward Island is able to raise for itself and to about half the corresponding revenues for the other three Atlantic provinces.

The figures in Table 22-9, however, do not give an entirely accurate measure of relative fiscal capacities. They show the provinces' actual revenue, and therefore are a result both of revenue potential and of revenue-raising efforts. Since the purpose of equalization is to even out the ability of provinces to generate funds, a better test of the effects of the arrangement is to look at the results that would occur if each province were to apply the same rates.

Table 22-10 shows indices of tax base per capita for three periods since 1972. The first three rows demonstrate the considerable variation that exists for own-source revenue. While Alberta's own-source revenue is currently 217 per cent of the national average, Prince Edward Island's is only 55 per cent. The other Atlantic provinces do not fare much better. It is these figures, more than any others, which demonstrate the great need for equalization in the Canadian federation. Without compensation, the differences in the abilities of provinces to provide for their residents' welfare would be unacceptably high.

The variation among provinces has increased significantly since 1972, as a result of the sizeable Western energy revenues. The fourth to sixth rows of Table 22-10 demonstrate this point clearly. Note, however, that even without resource revenues, Alberta and Saskatchewan have still benefited the most from increased funds. This is because personal and business incomes are higher, retail sales are greater, and so on as a spin-off from energy activity. Finally Commissioners wish to point out the difference in Quebec's position in the two tables. Its relatively high figure in Table 22-9 compared to its relatively low position in Table 22-10 is a result of higher-than-average tax rates and demonstrates the importance of standardizing for actual taxation efforts when comparing relative fiscal capacities.

The seventh to ninth rows of Table 22-10 show the effect of equalization payments. These payments greatly reduce the variation among provinces. Prince Edward Island's revenues are now 83 per cent of a national average that is still highly inflated by Alberta's revenues. The position of the seven easternmost provinces varies only from 83 to 88 per cent of the national average. The addition of other federal transfers, as is shown in the final three rows of the table, reduces disparities further. The Atlantic provinces now have potential revenues of about 90 per cent of the national average. Ironically, Ontario now has the lowest potential revenues: 87 per cent of the national average. This is not because of low tax rates, as Ontario's tax effort is the average for the country; it does, however, explain why Ontario qualified for, but did not receive, equalization payments during the 1977–82 period. British Columbia and Saskatchewan stand fractionally above the national average; Alberta remains far out in front.

TABLE 22-10 Indices of Tax Base per Capita, Selected Fiscal Years

	(national average = 100)									
Measure of revenue base	**Nfld.**	**P.E.I.**	**N.S.**	**N.B.**	**Que.**	**Ont.**	**Man.**	**Sask.**	**Alta.**	**B.C.**
Own-source revenues[a]										
1972–73	62	59	72	71	85	110	90	85	134	120
1976–77	60	57	66	67	82	99	85	106	201	112
1981–82	59	55	66	66	78	94	79	112	217	111
Own-source revenues less natural resources										
1972–73	61	62	75	72	87	115	93	82	111	114
1976–77	62	62	72	73	89	108	92	101	128	112
1981–82	62	62	73	73	87	104	87	103	139	114
Own-source revenues plus equalization										
1972–73	85	84	87	87	90	104	93	94	125	113
1976–77	85	85	86	86	88	93	90	100	188	105
1981–82	83	83	84	84	86	88	88	105	203	104
Own-source revenues plus all transfer payments										
1972–73	95	102	91	92	95	101	95	93	121	106
1976–77	92	104	91	93	93	91	93	100	171	103
1981–82	90	96	89	92	90	87	90	106	186	102

Source: Thomas J. Courchene, *Equalization Payments: Past, Present and Future* (Toronto: Ontario Economic Council, 1984), p. 158.

a. Own-source revenues and equalization payments are determined on the basis of the *new* equalization formula as far as tax bases are concerned. What this means is that all renewable energy resource revenues and all property taxes enter the equalization formula. The equalization standard, however, is the national average level and not the five-province average that characterizes the present formula.

These figures demonstrate that equalization and other federal transfer payments are indeed producing an effect. They do a great deal to even out the access of provincial treasuries to public revenues. Commissioners would conclude that equalization has certainly contributed very significantly to reducing interprovincial differences in fiscal capacity.

The trend toward greater equalization appears to have stopped, however, and even perhaps to have been reversed, owing to the effect of energy revenues and, to a lesser extent, to that of the need for restraint: "Over time the level to which provincial revenues are equalized is falling relative to the national average level of fiscal capacity."[11] Thus, in 1972–73, after all transfers, no provincial government fell below 90 per cent of national average fiscal capacity. In 1981–82, however, two provinces did fall below this level. In 1972–73, the richest province had a capacity of 121 per cent of the national average; in 1981–82, it had 186 per cent of that average. More recent changes will also somewhat reduce the equalization commitment. It has been calculated[12] that for 1982–83, the new "five-province standard" reduces the total equalization payment by $732 million from what it would have been under the old formula, to $4.557 billion; but this reduction has been tempered by transitional payments to Quebec and Manitoba, the provinces hardest hit by the change. The capping of equalization payments by the rate of increase in GNP also signals that growth in equalization will not be open-ended.

Through equalization, Canada has dramatically reduced differences in the capacity of provinces to provide services for their citizens. Nevertheless, the disparities among provinces remain substantial, and the system has had great difficulty coping with the uneven effect produced by oil and gas revenues. Recent changes have reduced the overall level of equalization somewhat. We Commissioners also wish to emphasize our view that the concept of sharing, embodied in equalization, remains strongly supported by Canadians across the country. While specific aspects of the program are controversial, it is clear that the constitutional commitment of section 36 reflects national consensus.

Issues and Proposals

Canadians must first decide on the interpretation of the principle underlying equalization in Canada. Is a conservative interpretation of the words in section 36 of the Constitution Act, 1982, "reasonably comparable levels of public services at reasonably comparable levels of taxation", to prevail? Or is equalization to be a way for the less-prosperous jurisdictions in the country to share equally and automatically in the fortunes of their wealthier neighbours?

There is no correct answer to this query; the decision ultimately represents a judgement about the goals of Canada's federation. Commissioners are inclined to support a rather more generous interpretation of the nation's commitment to equalization than that inherent in the current equalization program. It is time, we believe, to go beyond a simple, minimum-standards criterion towards a fuller measure of revenue equalization. We base our recommendation for this move on one important reason: the provinces have clearly assumed a much greater role in the federation than they played in

1940, when Rowell-Sirois reported, or even in 1957, when the first equalization scheme was established. Individual Canadians are now much more dependent for a wide range of services on their provincial government. Given general acceptance that this is the direction which Canadians favour, the ability of provincial governments to provide these services becomes that much more important. Correspondingly, disparities among provinces become less tolerable.

The next question, to which, again, there is no correct answer, is: Who should operate the program? The answer depends on Canadians' view of the federation. Three models might be followed. First, equalization might remain the sole responsibility of the federal government. That government would almost certainly wish to consult with the provinces and with other interested groups, but it would not necessarily be bound by any representations. A variant of this model would give the provincial governments a somewhat more formal opportunity to contribute to program design, perhaps in exchange for granting the federal government access to tax sources such as resource revenues, which are now mainly a provincial responsibility.

The logic of the first model is that redistribution within the federation is, and should be, a responsibility of the national government. The problem is that the federal government's financial commitment is, in large part, a function of provincial taxation policies, yet Parliament is required to equalize revenue sources in which it does not share.

In recent years, a second, more confederal model, has attracted some attention. Some observers have suggested making equalization an interprovincial matter in which provinces would share among themselves. Each province's fiscal capacity would be calculated separately. Jurisdictions with a surplus would then contribute to a fund out of which payments would be made to financially disadvantaged regions. The calculations would include all revenue sources, even forgone revenue. The arrangement would be run exclusively by the provinces themselves; they would have to decide what percentage of fiscal surpluses would be taxed or what fiscal deficits compensated.

A third option is a "two-tier" scheme which would split equalization responsibilities between the two orders of government. While there are a number of proposals of this type, they all start by distinguishing resource revenues from all others, since resource revenues are fully within the provincial domain. The central government would continue to operate an equalization scheme similar to the pre-1982 arrangement, but without resource-revenue categories. Revenues to be paid out under this first tier would come from tax bases, many of which are shared with the provinces. Thus, if disbursements rose because of additional income-tax revenues in a rich province, the federal government would have access to the revenues, as well as responsibility for the payments.

Equalization of resource revenues would be the responsibility of the provinces as a group. Provincial governments would define the country's average resource-revenue capacity. As in the second model, provinces with revenues above this average would contribute some portion of their surplus to a fund from which payments would be made to provinces falling below the

average. Overall, the payments would balance exactly: total payments by resource-rich provinces would equal disbursements to the others.

Commissioners recommend that the federal government retain primary responsibility for operating the equalization program. The other two options are certainly attractive, but they suffer from two defects. There is no evidence, first of all, that the provinces would be willing to play the more prominent redistributive role required by the two other models. Trial proposals along these lines were met with great hostility a few years ago, and there is little reason to think they would fare any better today. Resource-rich provinces considered that such a scheme would deprive them of their rightful revenues; resource-poor provinces did not wish to be dependent on the good will of the more advantaged. More important, both schemes would deny the federal government some or all of its traditional redistributive role in the federation.

As we have seen, to translate the general principles of equalization into a workable scheme is an extremely complex task, especially in a volatile fiscal environment. With even minor alterations, an almost infinite number of possible "wrinkles" and statistical quirks can have important consequences for a particular province. Commissioners, therefore, can outline only some general recommendations which are consistent with our positions on sharing and with our view that the federal government is primarily responsible for equalization arrangements.

Canada should return to an equalization formula that includes all ten provinces in the base. The present system, which arbitrarily excludes five provinces from the calculation, allows too much room for distortion, strategy and unintended effects. For example, if a firm were to leave one of the excluded provinces, say Alberta, for one of the five included in the formula, say Ontario, then the equalization entitlements of recipient provinces would rise commensurate with the increase in the formula tax base. If the same firm were to move to Nova Scotia, the equalization scheme would be unaffected, since neither Alberta nor Nova Scotia is included in the five provinces used in the calculation. As one provincial finance minister stated (only half in jest), it may be to the advantage of the have-not provinces to push development expenditures Ontario's way. Equalization should be based on the broadest possible assessment of provincial fiscal capacities. To tinker with the number of provinces on which it is based in order to solve financial problems is undesirable and blurs the basic principles.

A portion of resource revenues – greater than zero but significantly less than 100 per cent – must be included in equalization. There is no magic figure, but the 20 to 30 per cent range seems an appropriate compromise between the extremes of theoretical purity and political reality. This sort of proposal has been endorsed by the Task Force on Fiscal Arrangements of 1981, the Saskatchewan government of the same year, and the Economic Council of Canada in its 1982 report.

The Task Force endorsed this proposal because, if natural resources were in private hands, 20 per cent of the sector's revenues could be expected to accrue to provincial budgets as taxes. This 20 per cent, therefore, should be the amount equalized. The Task Force also argued that only those resource

revenues used for budgetary purposes, and not those revenues being deposited in heritage funds, should enter equalization. In addition, resource revenues used to provide special or unusual benefits to citizens should be excluded. Commissioners believe that this is a reasonable approach to the thorny problem of which resource revenues to include. We also believe that the federal equalization payments arising from resource revenues should not exceed the revenues which the federal government can be said to obtain from taxation of resource activity.

The focus on rents from oil and gas resources ignores the implicit rents from other resource endowments. These, too, should be incorporated into sources of provincial revenue used in the equalization formula. Commissioners refer here mainly to the practice of underpricing electricity generated by provincial Crown corporations. The details of a proposal on this matter are included in the Economic Council's report.[13] We are content to endorse their view and to recommend that more work be done to make estimates of these forgone revenues more certain.

Finally, Commissioners believe that the idea of considering fiscal needs or the cost of providing services should receive careful consideration. The criterion of "reasonably comparable levels of public services" at comparable levels of taxation, set out in the Constitution, includes both sides of the equation. Most equalization schemes, however, focus only on the revenue side. They implicitly assume that the cost of providing services is the same across the country. This is obviously not so. Roads are more expensive to build in British Columbia than in Manitoba because of the terrain. A province such as Newfoundland, where services must be provided to a small, scattered, rural population, may incur greater costs than one where the population is more concentrated. Demographic profiles, which differ because of varying proportions of old people or of the unemployed, will lead to different levels of demand for services. "Reasonably comparable levels of public services" may therefore embody cost differentials, and there seems to be a strong case for building this component into the equalization system. The Australian equalization system, for instance, does so with considerable success.

There are, however, formidable obstacles to including expenditure needs in the equalization formula. To do so would require a "Representative Expenditure System"[14] to parallel the existing representative tax system. Canadians would have to agree on which provincial expenditures to include, and on how to assess differences in costs. Presumably, this assessment should reflect differences in per capita need (for example, the proportion of citizens of school age) and in unit costs (for instance, in building one kilometre of road). The formula would have to devise an "average" level of service, while leaving provinces free to make their own choices about whether to provide more or less of a given service. These are all formidable problems, both in concept and in the complexity of measurement and data collection that they entail. Their solution would require much more complete and standardized statistical bases. To delineate representative expenditures across the range of provincial services would entail more difficult political judgements than would agreement on representative taxes, and might also generate undesirable pressures for provincial uniformity. Nevertheless, over a long period,

Canadians have been successful in coping with the complexities inherent in an equity-based system of public finance. Commissioners believe that through the Council of Ministers of Finance, governments should begin to prepare the ground for an eventual incorporation of expenditure needs as a natural evolution of the equalization program.

Notes

1. R. Johnston, *Public Opinion and Public Policy in Canada*, vol. 35 (Toronto: University of Toronto Press, 1985).
2. See papers prepared for this Commission: Robin W. Boadway, "Federal-Provincial Transfers in Canada: A Critical Review of the Existing Arrangements", in *Fiscal Federalism*, vol. 65, and John Vanderkamp, "The Efficiency of the Interregional Adjustment Process", in *Disparities and Interregional Adjustment*, vol. 64 (Toronto: University of Toronto Press, 1985).
3. Royal Commission on Dominion-Provincial Relations, *Report*, Book II: *Recommendations* (Ottawa: King's Printer, 1939), p. 84.
4. *Ibid.*, p. 125.
5. "Statement by the Honorable Mitchell Sharp, Minister of Finance, to the Federal-Provincial Tax Structure Committee", in *Proceedings of the Federal-Provincial Conference, Ottawa, October 24–28, 1966* (Ottawa: Privy Council Office, 1966). Quoted in Thomas J. Courchene, *Equalization Payments: Past, Present and Future* (Toronto: Ontario Economic Council, 1984), p. 47.
6. Courchene, *Equalization Payments*, p. 190.
7. For a review of these studies, see Vanderkamp, "The Efficiency of the Interregional Adjustment Process".
8. Frank R. Flatters and Douglas D. Purvis, "Ontario: Between Alberta and the Deep Blue Sea?", Discussion Paper No. 402 (Kingston: Queen's University, Department of Economics, 1980).
9. Economic Council of Canada, *Financing Confederation: Today and Tomorrow* (Ottawa: Minister of Supply and Services Canada, 1982).
10. Courchene, *Equalization Payments*, pp. 350–55.
11. *Ibid.*, p. 161.
12. *Ibid.*, Chapter 12.
13. Economic Council, *Financing Confederation*, p. 122.
14. Douglas H. Clark, "Canadian experience with the representative tax system as a means of measuring the relative fiscal capacities of provincial and local governments"; Testimony before the United States Senate Committee on Government Affairs, Subcommittee on Intergovernmental Relations, April 6, 1983.

Regional Economic Development

For a number of reasons, few of the issues in this Commission's mandate have proved more perplexing than regional development. Our canvass of the research community revealed that relatively little is known about how and why regional economies grow. Many theories abound, but none has gained wide acceptance.

Canada's success in spurring economic growth and industrialization in poorer areas is difficult to evaluate. We have experimented with many types of programs, policies and strategies, but as Premier Hatfield of New Brunswick stated in a submission to this Commission:

> *...despite the claims that significant funds have been spent, nothing which has been started has made an appreciable difference in the disparity between New Brunswick and the rest of Canada, in so far as benefits from establishing a viable industrial base are concerned.*
>
> (Government of New Brunswick, Brief, December 31, 1984, p. 1.)

The best that can be said is that we may have prevented the less-developed regions from falling further behind.

Perhaps partly because of this limited success, regional policy has defied our best efforts to devise an appropriate management framework. There has been constant debate about the level of government that should design and implement programs, the criteria for judging need, and the appropriate link between regional policies and more general national economic initiatives, such as stabilization or transportation policy. We appear to have spent nearly as much time arguing about how to implement measures that were doomed to failure as we have in searching for new solutions.

In a federal system, regional economic disparity is an inherently contentious issue; Canada is no exception to this rule. Inequalities across regions are at least as unsettling as those among individuals within a community. Sometimes economic adjustment requires migration, which places an extra burden on the individual. In these respects, unitary states are no different from federal systems. In a federal system, however, migration can weaken the provincial communities which federalism is designed to protect. In these situations, community survival is at stake. When attachments to regional communities are as strong as they are in Canada, or when migration involves the loss of language and culture as it can for French-speaking Québécois, the costs of adjustment are that much higher. We must think of development, therefore, not only in terms of Canada as a whole, but also in terms of regional economies and the provincial communities associated with them.

This view does not stand without challenge. Criticism takes several forms. One view states that we should think about the economic development of individuals, not of regions, for individuals are the essential focus of policy initiatives. From this perspective, preservation or development of communities should not be an objective of public policy. Moreover, to focus on inequities among regions diverts needed attention from inequities that have nothing at all to do with regions or territory. So, too, the pursuit of economic efficiency may play down regional policies. To try to diversify provincial economies in

order to transform them into self-sufficient entities is to deny all Canadians the fundamental advantages of economic specialization and complementarity. Almost by definition, from this viewpoint, regional development policies divert resources from the places of their greatest productivity to places where they will produce less and thus reduce the output of the economy as a whole. There is, therefore, a direct trade-off between aggregate national wealth and the wealth of each region.

One reply to this criticism is that while there may be a short-term trade-off between regional development and national income, there need not be in the long run. To the extent that regions underemploy resources, those resources are not contributing their full potential to national output. The national economy will be stronger to the extent that each region develops its potential. The opponent of regional development policy would probably reply that granting the objective, regional policies have so far not transformed the economic bases of provinces to make them more productive. On this reading, we have been able to compensate for inequities through interpersonal and regional transfers, but we have done little to alter the conditions that hold back development.

This debate about regional policies is especially important today. Some participants have argued that in the present economic context and in the face of increasing international competition, regional development may be a luxury that we can no longer afford, at least at the levels and in the forms that we have known. The critics argue that we should submit to the discipline of the market and thus allocate resources to their most productive use, however well justified other goals might be in social or cultural terms. The argument is not that we should abandon regional policy, but that we should de-emphasize it, "tilting" policy more toward national efficiency and less toward regional development. Moreover, just as Commissioners have done in our earlier discussion of industrial and social policy, we should try to make clearer distinctions between "welfare-compensation" dimensions of policy and developmental dimensions.

If regional economic development were simply about national efficiency, Commissioners would tend to support the critics. However, as we have argued throughout this Report, well-being is a larger, more inclusive concept; and well-being in Canada has an essential regional component. Regional development policies remain vital, and they must include both the reduction of disparities inherent in the concept of interregional transfers and the development aspect inherent in the notion of making the best use of Canadian resources in all regions. Thus, while Commissioners are anxious to minimize distortions and to ensure that considerations of efficiency discipline the provision of regional development funds, we believe that regional development must remain an essential component of Canadian policy and, indeed, of the Confederation bargain.

Regional development can be as much a hornet's nest for a Royal Commission as for governments. The stakes are large, emotions are charged, Canadians have a history of handling the process badly, and they know little about how it actually works. Nevertheless, for the reasons we have given and

because of the constitutional commitment of the Government of Canada and of the provincial governments to "promoting equal opportunities for the well-being of Canadians" and to "furthering economic development to reduce disparity in opportunities",[1] regional policy cannot be ignored.

Economic Growth, Income Distribution, Adjustment and Federalism

To this point in our Report, we Commissioners have concentrated on three aspects of economic life: economic growth, income distribution, and adjustment. We have considered these aspects from the perspective of the national economy as a whole and in light of its effect on individuals. Our discussion has proceeded as if all economic activity took place at one geographic point. Economic growth referred to increases in real per capita gross national product. Research has classified income distribution according to age, sex, occupation, and language or ethnic group. Adjustment referred to the problems of reallocating capital and labour from sectors in relative decline to those in ascendancy.

The first step in making this analysis more realistic is to recognize that economic activity is spread across Canada and that workers and businesses have a geographic location as well as an industrial or occupational classification. We must now identify the factors that make particular regions grow, and determine how regional economies affect, and are affected by, national patterns. We must also compare incomes across regions. Do workers or investors in one part of the country earn the same rewards as their otherwise identical counterparts in another part? Even adjustment takes on added complexity, for migration now provides an alternative to a fall in an individual's real earnings.

Provinces have formal constitutional status and possess real economic and social powers which make them important centres of economic activity. They are also communities to which residents have political commitments and emotional ties. Thus it makes sense to consider them as economic regions and to talk about their welfare in the same way that we speak of Canadian interests and aspirations.

To add this federal dimension to our analysis makes that analysis more complex. The aggregate growth rate of a province is not merely a part of a broader economic process. We must consider the ability of a political unit to provide for the continuing economic future of its residents. The locations of jobs or investments are important. It therefore becomes important to ask whether individuals can secure their livelihood in the provincial communities to which they are attached. We must do more than simply compare incomes of otherwise identical individuals across Canada. We must compare the per capita real incomes of entire regions, taking into account the different mix of occupations, demographics and circumstances.

To add federalism to the analysis introduces a host of political and social concerns to the consideration of interregional adjustment. Out-migration, for example, is not simply another adjustment mechanism. If movement is large

enough, it threatens regional communities. Thus population movements that seem justified on grounds of economic efficiency may be unacceptable because of these broader political and social values. We judge policy makers not just by their ability to provide jobs for those seeking employment, but also in terms of the availability of employment opportunities in the parts of the country where the unemployed live.

We have moved out of the economic domain and into the political realm. In doing so, we must ask: How much weight should our nation put on the maintenance of regional communities? How much are Canadians willing to sacrifice, in terms of national efficiency, to guarantee this end? Should the level of resources we commit to regional development be related to the performance of the national economy, falling as national economic growth slows? Does a fair distribution of income imply that per capita incomes be equal across provinces? Has an individual a right to expect a job in his or her chosen region, with wages comparable to those obtainable for the same job in more prosperous regions? Before attempting to answer these questions, we must understand the pattern of regional disparities in Canada.

Regional Disparities

What do we know about regional economic disparities in Canada? For a start, per capita earned or market income (excluding transfer payments) varies significantly among provinces. In 1981, for example, as Table 22-11 shows, Newfoundland's per capita market income was only 53.8 per cent of the national average, while Alberta's was 114.1 per cent. In that year, only three provinces, Alberta, Ontario and British Columbia, were above the national average, although Saskatchewan was close, at 98.7 per cent. Manitoba and Quebec form the next group, at slightly over 90 per cent, followed by Nova Scotia at about 70 per cent, while the other three Atlantic provinces stood below two-thirds of the mean income. This general pattern has changed little over the 60 years for which data are available, although individual rankings of provinces have occasionally altered.[2]

Earned income is generally the initial measure of economic disparity, since it most accurately reflects the relative strength and productivity of the various economies. Other measures represent more fully the relative economic well-being of individuals. If we add transfers to individuals to their earned income, we can form a better picture of total personal income. By this standard, the poorest province is now at 65.1 per cent of the national average, and the richest is at 110 per cent; these figures still represent a difference of slightly more than three to two. If we add the effect of the progressive income tax by assessing after-tax income rather than gross income, discrepancies narrow further. Calculating income per household rather than per person has an additional dramatic effect. On these terms, Newfoundland's disposable income per household rises to 87.6 per cent of the national average, and Prince Edward Island and New Brunswick become the poorest provinces, with per capita incomes 79 per cent of the national average. The shortfalls in per capita income have now become less than half of what they were on the

TABLE 22-11 Alternative Measures of Regional Income Disparities, 1971 and 1981

Index	Year	(Canada = 100) Nfld.	P.E.I.	N.S.	N.B.	Que.	Ont.	Man.	Sask.	Alta.	B.C.	Vuw[a] (%)
Market income	1971	55.1	53.6	69.3	66.5	88.5	119.6	93.2	79.1	98.3	109.6	0.285
per capita[b]	1981	53.8	57.5	69.6	63.2	90.7	110.5	92.7	98.7	114.1	110.3	0.274
Personal income	1971	63.7	63.4	77.5	72.2	88.7	117.0	94.0	80.3	99.0	109.0	0.232
per capita[c]	1981	65.1	67.4	76.8	70.4	93.6	107.4	93.1	99.7	110.3	108.7	0.211
Personal disposable	1971	68.1	68.0	79.8	75.0	89.6	114.8	95.5	85.5	99.6	108.6	0.203
income per capita[d]	1981	67.3	71.6	78.7	72.3	90.8	108.3	97.9	104.4	109.0	109.4	0.195
Personal disposable	1971	90.1	76.2	84.9	84.4	94.1	111.1	91.6	82.8	97.6	99.4	0.136
income per household	1981	87.6	79.2	83.0	79.7	91.5	107.0	95.5	103.4	109.4	101.5	0.130
Real personal												
disposable income	1971	89.9	N.A.	82.7	89.3	96.2	106.3	96.4	88.3	97.2	89.8	0.102[f]
per household[e]	1981	81.5	N.A.	82.5	83.7	94.9	103.2	101.1	111.4	109.3	90.9	0.125[f]

Source: Based on data from Statistics Canada, *Cansim* (Matrices 555–562; 7002–7031) and *Census of Canada* (1971, 1981) as presented in Robert L. Mansell and Lawrence Copithorne, "Canadian Regional Economic Disparities: A Survey", in *Disparities and Interregional Adjustment*, vol. 64, prepared for the Royal Commission on the Economic Union and Development Prospects for Canada (Toronto: University of Toronto Press, 1985).

a. Unweighted Coefficient of Variation.

b. Defined as wages and supplementary income, net unincorporated business income, net farm incomes, and interest, dividend and miscellaneous investment income, all calculated on a per capita basis for the region as a percentage of that for Canada.

c. Personal income is market income plus transfers to individuals.

d. Personal disposable income is personal income less personal income taxes and contributions to social security.

e. Regional price indexes calculated from inter-city partial consumer price index (Winnipeg = 100, May 1971) and city consumer price indexes.

f. The values for this measure exclude P.E.I. and hence cannot be compared to those for the other income measures.

basis of earned per capita income. Adjusting for prices, in order to capture real purchasing power, produces another slight reduction in variations among provinces.

Why do earned incomes per person differ so markedly among regions? Two explanations tend to be offered, the first, perhaps, a little more frequently then the second: differentials in wage rates and differentials in employment rates. In other words, if Canadians actually employed in the poorer regions were to earn, on average, what their counterparts in wealthier areas earn, about one-half of the observed income disparity would disappear. The remainder would reflect the smaller proportion of people actually working. Thus the question becomes: Why do earnings and employment rates vary by region?

The most obvious answer to varying wages is that occupational and industrial structures vary. Fishermen do not make as much as corporate vice-presidents. If there are relatively more fishermen in Nova Scotia and relatively more executives in Ontario, earnings per capita will reflect the different occupational mix. Regional disparities in this circumstance, however, would reflect the usual spread of earnings across occupations or persons that characterizes all industrial societies.

Relatively little of the observed disparity appears to be grounded in occupational differences, however. Earnings for any given job, rather than differences in the types of job available, account for most of the income gap. The explanation for differential earnings lies in worker productivity. A number of factors might explain difference in output per employee. The "quality" and the amount of capital employed appear to account for some part of the gap: poorer regions have lower capital-to-labour ratios. Lower-income regions also have relatively fewer workers in the prime age groups and a work-force characterized by fewer years of education. Slower adoption of new technology, poorer management, fewer and smaller urban centres, and greater distance from important markets explain the remainder of the productivity gap.

To note these associations, however, is not to explain them. In fact, it is extremely difficult to sort out cause and effect. Education of the work-force appears to be lower in poorer regions because individuals with training are generally in a better position to migrate in search of better employment opportunities elsewhere. Lower capital expenditures per worker could simply reflect a poorer investment climate. The decision to adopt new technology as it becomes available depends primarily on the economic circumstances: the speed of adoption tends to reflect the buoyancy of the regional economy. Good managers tend to be promoted to head offices, irrespective of where they start out.

The other half of differentials in per capita earnings reflects lower employment rates in poorer regions. Typically, there are fewer people of working age in the poorer provinces; members of that age group, especially women, are less likely to seek work, and those in the labour force are more likely to experience unemployment. As with earnings, however, these patterns do not explain differences in employment rates. Lower participation reflects, but does not explain, a depressed economy.

On the basis of this analysis, three theoretical approaches to the problems of regional economic development may be distinguished. The first approach stresses interregional adjustment within the national economy. It focuses on the question: What adjustments must occur to equalize the rewards of similarly situated workers in different provinces, given the present underlying forces in the economy? The primary issue is removal of impediments to movement of labour and capital to the areas of their most productive use, that is, interregional adjustment. Theoretically, such adjustment would reward both labour and capital. It would not, however, equalize per capita incomes in each province. If skill levels, management quality, available technology and endowment of natural resources differ, then, even with perfect adjustment, average incomes will differ. Moreover, adjustment occurs largely through mobility of capital and labour: accordingly, this approach offers no guarantee of any particular level of economic activity in any province.

The second approach is compensatory. It emphasizes measures, not to facilitate adjustment, but rather to compensate individuals in a given region for the situation in which the market leaves them. Equalization transfers, considered above, are the Canadian archetype of this solution.

The third approach is developmental. Its policies are intended to stimulate economic development by addressing the underlying factors that cause relative underdevelopment. The market imperfections and the characteristics that each region brings to the national economy become the subject of government policy. Some of these characteristics—distance from markets or natural resources, for example—are relatively fixed, though transportation policies can alleviate the disadvantages of distance. Other aspects of economic structure, however, are more amenable, in principle, to policy efforts, and these are the object of regional development policy more strictly defined.

Canadians have experience with all three approaches: people have moved; incomes have declined; transfer payments have been made, and economic development programs established. In spite of all this, there has been remarkably little change in the level of measured disparities, although the differences do vary somewhat over economic cycles, widening in hard times, converging in good ones.

Interregional Market Adjustment

To ascertain how the pure theory of interregional market adjustment contributes to understanding regional disparities, we must address two questions. What pattern of income distribution should one expect to observe in a regionally diverse nation, such as Canada, in the ideal situation where all interregional trade and factor flows are complete? How does such an economy adjust to shocks to this equilibrium, and what are the implications of the adjustment for regional income distribution?

If there are no barriers to the interregional movement of goods and services, producers anywhere in the country can ship products wherever it is profitable for them to do so. If labour, capital and technology are also free to locate in any region, there is nothing to stop a construction worker in Ontario from taking a job in Quebec, or a dentist in Prince Edward Island from

setting up a practice in Alberta. How would these circumstances affect the distribution of income across provinces?

Under a number of highly restrictive assumptions, free trade in goods and services will equalize factor rewards across regions: wages, returns to capital, and product prices (excluding transportation costs) should be identical, regardless of province of residence. Factor mobility should operate in the same way. Thus, capital and labour will migrate in search of higher earnings to the extent that expected gains in real income to migrant or investor equal or exceed the costs of relocation. As individuals leave areas with lower wages, or capital moves from areas with lower rates of return, supply falls in relation to demand, pushing prices upward. The reverse happens in the region of destination, where prices decline as a result of greater supply.

If migration is responsive to expected differences in real income, theory is able to predict migration from high- to low-unemployment areas, taking into account wage differences. In fact, there are many kinds of labour in a complex modern economy; the variety reflects different types and levels of training, skill and experience, and hence different levels of wages and salaries. Migration can thus equalize earnings within skill groups, but not within the work-force as a whole. The same observation holds true for capital. In the short run, at least, firms typically commit plant and equipment to designated uses and cannot readily reassign them for other purposes. In addition, different investment prospects bear different risks to the investors and are thus likely to be undertaken only at appropriate rates of return. Capital mobility will equalize returns only within a given class of risk.

The theory of interregional market adjustment holds that migration will equalize wages (within skill groups) and "risk-adjusted" returns to capital, but not per capita incomes. This last equalization would occur only if each region had an identical endowment of resources, capital, technology and skilled labour. As long as economic bases differ, so will work-force characteristics and investment patterns. Land and resources are fixed elements in the economic base, and adjustment through trade and migration will not alter them. Regions with relatively large pools of skilled labour, or valuable resources, will have higher per capita incomes than regions with smaller pools of skilled labour or fewer resources. Adjustment, then, consists of the changes that occur within a given set of human and natural resources under internal free trade.

There are two important questions relating to market adjustment. How do trade and factor markets respond to those changes in relative prices and earnings potentials that result from economic shocks? How quickly does adjustment correct any disequilibrium? What happens, for example, when the value of one region's output falls over the long term perhaps as the result of a shift in the terms of trade against its exports, or the exhaustion of an important resource? Clearly, the region can no longer produce the same per capita income for the same number of residents as it did before. Two types of market response, or some combination of them, are logically possible. First, and most obviously, some residents could leave the region. As long as this population outflow is not destabilizing – that is, as long as it does not reduce the ability of the regional economy to produce goods and services

efficiently – fewer people will share a proportionately lower aggregate output, thereby restoring the previous level of per capita income. Alternatively, the region might support the same population, but at lower per capita incomes. Falling aggregate demand for the region's output will put downward pressure on output and factor prices. If these are flexible, full employment will result, but incomes will be lower. If prices are not sufficiently responsive, unemployment will result. It will also reduce aggregate income and restore equilibrium in the short run. Over time, the unemployed, if they are unassisted, will either have to migrate in search of employment, or will put downward pressure on local factor prices. Either way, the total income of the region will eventually adjust to the reduced value of its output that is the result of changed circumstances.

What does the same theory hold for the pattern of regional incomes and the efficiency of interregional adjustment? Differences in factor prices cannot exist for long if there is interregional mobility of products and factors, for market adjustments will eventually remove them. If markets are relatively efficient in recognizing and acting upon differences, factor prices will become similar across regions. If natural "frictions" or policy-induced distortions impede adjustment, however, the correspondence will not be as close. A number of public policies in Canada have been designed to facilitate this form of market adjustment.

Indeed, we Canadians have relied primarily on the individual decisions of private economic actors to facilitate adjustment through mobility of factors in response to changing economic incentives. Adjustment of this type has been quite effective in the past. For example, as the terms of trade shifted in favour of Western resource producers in the 1970s, not only labour but also capital and financial institutions responded. The subsequent shift away from resources has brought a corresponding flow of these factors to Ontario. The process of adjustment through the migration of labour and capital has been facilitated by a wide range of policies, including Employment Canada's efforts to match workers and opportunities, and grants or tax deductions against moving expenses to assist relocation. More generally, federal support for post-secondary education, health care and other public services help to overcome the barriers to mobility inherent in variations of provincial policy in these areas. Language policies also help to reduce some of the cultural barriers to personal mobility. We have already seen that equalization payments contribute to efficient reallocations of labour and capital.

Compensatory Policies

The second policy option is compensatory. Equalization payments provide the obvious example. Provinces qualify for these payments by virtue of an unacceptably low taxation base. Payments flow, by design, to some provinces and not to others. They are intended to offset natural economic disadvantages, not to change the underlying forces of the economy. Another example is the regional differentiation of Unemployment Insurance (UI) terms and benefits. The variability within the UI system acknowledges that unemployment is more likely to occur in some parts of Canada than in others and to

last longer when it does occur. More generous terms and benefits make up for these differences. It is, in general, these policies that produce the reduction of disparities in personal income treated earlier. The transfers applied can render market adjustments less necessary: they allow recipient regions to maintain consumption levels; they prevent real per capita incomes from falling; and they obviate the necessity for individuals to migrate who might otherwise have to do so. Hence the population base can remain intact, reducing downward pressure on wages. While these results may seem entirely positive in terms of individuals or families, from the market point of view, compensatory policies can hinder adjustment. Where there is a high level of transfers, wages and unemployment remain too high.

Developmental Policies

The third policy option, while still explicitly regional in focus, is developmental in intent. It has been defined as follows:

> *Economic development ... refers to the structural transformation of an economy such that, over time, it becomes increasingly capable of sustaining its capacity for further expansion out of its own, internal resources. Since the prerequisites for such sustained expansion include an increasingly differentiated and integrated economic structure, combined with incentives for its key actors to accumulate capital, to innovate, and to be efficient, the goal of development policy is to ensure that such prerequisites are created.*[3]

Developmental policies are not designed to adapt to, or to compensate for, economic circumstances; rather they address the means of changing those circumstances or of supporting specific regions in their attempts to alter their own capacities in order to overcome their disadvantages.

These developmental approaches often emphasize a broader range of historical, political and even cultural factors than do market-based theories. Some, in particular, see a pattern of cumulative forces, in which the dynamics of the market lead to even greater concentration of productive forces at the centre. Availability of large markets, of economies of scale, of sophisticated specialized services, of a highly skilled labour pool, and like circumstances all attract capital and labour from peripheral regions. Consequently, these regions lose many of their most dynamic citizens and are able to offer fewer advantages to new investors. Cumulative growth at the centre, in this view, can thus lead to cumulative decline elsewhere. Regional policies seek to counter these forces.

Canada has employed some form of regional development policy throughout its history. Much of development policy aimed at sectors has had a strong regional basis where sectors have been concentrated in one or a few regions. In the oil and gas, auto, fisheries and timber sectors, for examples, a substantial portion of activity has been concentrated in a few regions. At the turn of this century, the federal government imposed export duties on uprocessed logs to increase the extent of processing in central Canada and British Columbia. During the Great Depression, relief measures were targeted regionally; the Prairie Farm Rehabilitation Act is a well-known

example. Moreover, national development policies, such as those to enable or promote the movement of goods and services across the country have proved beneficial to the regions. The building and extending of our great national railways and highways fall in this category. Indeed, these implicitly regional policies have undoubtedly been more vital to regional development, broadly defined, than have the explicitly regional development programs of the Department of Regional Economic Expansion (DREE) and other comparable agencies.

Explicit regional efforts, however, had little part in federal economic policy immediately after the Second World War. Instead, emphasis was placed on promoting aggregate economic growth and stability, and on creating the outlines of the modern welfare state. The federal government expected that poorer regions, to the extent that they entered the calculations at all, would benefit from the general economic prosperity: "Regional development was seen as natural adjunct of national development."[4] By contrast, from the close of the Second World War, Britain used regional policy as a pillar of its post-war full-employment policy.

In Canada, the first explicit policies to be aimed at decreasing regional economic disparities were developed in the wake of the 1957 report of the Royal Commission on Canada's Economic Prospects (the Gordon Commission). Sustained national economic growth, the Commission and supporting research studies found, had not eliminated regional disparities. Political action soon followed in the form of Prime Minister Diefenbaker's announcement of the "Roads to Resources" program. In addition, the federal government introduced winter-works bonuses to support construction activity undertaken in times and areas of relatively high unemployment.

The Agricultural Rehabilitation and Development Act (ARDA) of 1961 introduced a long succession of boards, agencies, committees and departments. The target was rural poverty. The goal was to find ways to keep marginal farmers on the land through better techniques of land use. A more explicitly regional (as compared with sectoral) focus for development efforts came in 1962 with the creation of the Atlantic Development Board (ADB), although at the time, the new board was assigned only a research and advisory role.

Regional development took on added importance with the change in government that took place in 1963. In that year, the new government of Lester Pearson gave the ADB a program orientation and funds to disburse, most of which subsequently went toward social infrastructure projects. In 1964, ARDA became the Agricultural and Rural Development Act, and a new department, Forestry and Rural Development, assumed responsibility for its application. ARDA's focus changed from purely agricultural assistance to more general rural economic development. The new department designated Special Rural Development Areas for attention. The Fund for Rural Economic Development (FRED), established in 1966, had an even broader mandate: it was to implement comprehensive rural development strategies in locations judged to be "promising". Areas which did not meet the criteria were to receive adjustment aid; out-migration was deemed inevitable, and the only task was to make this process as painless as possible.

Not only rural areas received government attention. The federal government introduced the Area Development Agency (ADA) in 1963, to promote industrial development in poorer regions. Firms locating in designated areas could qualify for tax exemptions, for accelerated depreciation allowances and, with the introduction of the Area Development Incentives Act in 1965, for cash grants.

These early regional development efforts were scattered throughout the federal bureaucracy, each with different and sometimes tenuous links to the provincial governments concerned. In 1969, with the establishment of the Department of Regional Economic Expansion, consolidation of regional programs took place. Regional economic development was now to have a departmental focus; the new portfolio:

> *. . . was not to be just another line department but rather was to initiate and facilitate cooperative efforts between the line departments, when so authorized to coordinate the implementation of programs and, when necessary, to proceed on its own.*[5]

The appointment of a senior minister to the portfolio emphasized the importance to be attached to the task.

DREE continued to use many of the same policy instruments as its predecessors and also introduced new approaches partly because industrial assistance was added to its responsibilities. It designated certain urban centres in poorer provinces as "Special Areas", thereby making them eligible to receive funds that would support the provision of social infrastructure. These towns and cities were to be the "nodes" or "growth poles" around which economic development would centre and spin off throughout the region. Under the Regional Development Incentives Act (RDIA) the practice continued of designating certain areas as eligible to receive loan guarantees and subsidies for firms choosing to locate in them.

The initial enthusiasm that greeted DREE soon disappeared. Observers criticized the department on two grounds. First, its very policies became suspect. It soon gained the reputation of dispensing large sums of money with negligible results. The industrial incentives grants, in particular, attracted severe criticism. Some critics charged that these grants did not noticeably affect firms' locational decisions; that even when they did, such decisions involved only reallocation of economic activity from one underdeveloped region to another; and that the incentives DREE offered created significant and costly distortions. Even the infrastructure grants under the Special Areas program became targets, as "growth pole" theory fell into disfavour among planners.

The second major concern with DREE lay in its administrative approach. The department appeared to be too centralized and too inflexible, especially with respect to the economic development objectives of provincial governments. There was also considerable tension within the federal bureaucracy between DREE, with its explicit regional development mandate, and line departments, with their more sectoral approach. Often the latter – Transportation, Energy and Fisheries, for example – could affect a region's economy much more significantly than could any policy that DREE was able to mount with its limited funding.

As a result of these pressures, the federal government reorganized DREE in 1973, and instituted the system of General Development Agreements (GDAs). It negotiated with each province a separate agreement wherein the general developmental goals to be pursued were outlined. Committees of officials drawn from both orders of government devised specific projects that were to be run on a shared-cost basis by the province. DREE staff, including a senior Assistant Deputy Minister, were relocated to each of the regions, in order to provide more local expertise. In Newfoundland, the federal government paid for up to 90 per cent of project costs; it paid for 80 per cent of such costs in Nova Scotia and New Brunswick, 60 per cent in Quebec, Manitoba, and Saskatchewan, and 50 per cent in the three wealthiest provinces. Prince Edward Island continued to be covered by an existing federal-provincial development agreement. This DREE procedure was a radical departure from earlier forms of federal-provincial consultation on economic development.

The federal government's approach to regional economic development also changed. The emphasis on growth centres was abandoned. Projects were organized on a smaller scale, but were to encompass a wider range of sectors and to be distributed thoughout any given province. The province, more than a particular region, became the relevant planning unit, and "the focus on provinces meant that regional development policy was really provincial development policy".[6] It was during this period, too, that regionally differentiated investment- and employment-tax credits and Unemployment Insurance benefits were introduced.

Members of both the federal and the provincial governments soon began to criticize the GDA approach. Some provincial governments wanted even more control over program implementation, although most viewed the GDA period favourably, especially as compared to the arrangements that had preceded it and that were to follow. During the course of this Commission's hearings, we Commissioners heard a number of expressions of provincial support for the GDA approach. The real difficulties with GDAs were on the federal side. Ministers of line departments wanted more influence over DREE programs. They saw DREE as tied too closely to provincial priorities. As a result of these bureaucratic tensions, the intended provincial and federal co-ordination and integration of regionally sensitive policies encountered difficulties. Another ground for criticism was found: federal politicians considered that they were not receiving enough political credit for programs that were federally funded, sometimes to the level of 90 per cent. Provinces, however, were in a better position than the national government to represent themselves as the source of the largesse, and often took advantage of this opportunity.

A sometimes-bewildering succession of administrative reorganizations followed. In 1982, responsibility for regional economic development shifted from a particular department to economic ministries as a whole: "The regional perspective [was to] be brought to bear on the work of all economic development departments and in all economic decision making by the Cabinet."[7]

As part of the necessary reorganization, DREE's regional programs were combined with the industry and small-business interests of the Department of Industry, Trade and Commerce (ITC) to form a new Department of Regional

Industrial Expansion (DRIE). Both DREE and ITC were disbanded as separate departments. The Cabinet Committee on Economic Development became the Cabinet Committee on Economic and Regional Development, and the Ministry of State for Economic Development became the Ministry of State for Economic and Regional Development (MSERD). A number of other changes were made, including the appointment of senior Federal Economic Development Co-ordinators (FEDCs) for each province. The merging of regional development considerations with those of more general economic development policies was now complete, at least for administrative purposes. In the process, concern shifted from "regional development" in the sense, primarily, of development of slow growth areas, to "regional development" as the need to focus on economic development in each province.

The basic instrument of economic planning under this system was the Economic and Regional Development Agreement (ERDA), which the federal government was to sign with each province. As with the GDAs of an earlier period, these agreements were to be the overall planning documents within which specific policies and projects would be developed. Within this accepted framework, however, the emphasis would be focused on each government's direct delivery of its own programs, to allow the federal government its proper political due. Federal economic effort in a province and its links with provincial economic interests would be more fully co-ordinated through the FEDCs. Little in the ERDAs was original, and its projects turned out to be very similar to those of the GDAs.

Still further changes were in store. In June 1984, MSERD was disbanded. Responsibility for regional economic development was assigned to a single Minister of State for Regional Development operating under DRIE. In September 1985, even this position was abolished. Regional development policy is now the direct responsibility of the Minister of Regional Industrial Expansion.

Evaluation

How successful have been our regional development policies? To answer this question definitively would require an ability to compare the present state of economic development in those regions receiving assistance to its imagined state in the absence of such policies; unfortunately, such a task is impossible. Some research, however, has shed light on the effect of certain regional development policies.

Researchers have devoted most of their attention to RDIA grants, chiefly because they are the most visible and most contentious, even though industrial subsidies have represented only a small portion of total government spending on regional development. Initially, researchers tried to determine whether grants actually influenced the locational decisions of firms. A 1971 survey by the Atlantic Provinces Economic Council[8] (APEC) found that only 20 per cent of firms polled said that even without the grants, they would have located in the designated area. The other 80 per cent were presumably influenced by the grant to some degree, although the survey gives no indication as to whether the actual grants proved merely adequate or were

unnecessarily generous. A DREE study completed in 1973 produced results similar to the APEC's.

In 1977, the Economic Council of Canada published a comprehensive study of regional economic development in which it attempted to evaluate the effectiveness of DREE grants. It compared unemployment, income and migration rates in the recipient regions before and after the inception of the grant program. It concluded that "job opportunities in the Atlantic region have improved over the last few years, although nothing much seems to have changed elsewhere."[9] Nevertheless, it is impossible to establish that DREE policies necessarily had anything to do with this outcome.

To meet this uncertainty, the Economic Council undertook its own study of the success of grants in influencing firms' location in the Atlantic provinces. It found that 25 per cent of DREE-supported establishments were definitely influenced by the grant program, and that another 34 per cent were possibly so influenced. Little evidence was found that the subsidies "crowded out" other economic activity in the region, and so the net gain remained at 25 per cent to 59 per cent. As a final step, the Council compared the increment to national output from DREE-created jobs with the cost of providing those jobs. Even with conservative estimates of the grant's effectiveness in determining plant location, the program appeared to be successful. The additional contribution to national output from workers who would otherwise have been unemployed, more than covered the cost of the funds used.

The Economic Council's overall evaluation of the industrial subsidy program was cautiously optimistic:

> *Our own assessment of previous evidence, together with our analysis of data on the births and deaths of establishments in one region only (the Atlantic), has led us to the view that the subsidy program is far less successful than published estimates of job creation would imply. To that extent, the critics are right. But the subsidies, nevertheless, seem successful enough to be a paying proposition. The value of the jobs created appears to outweigh the inefficiency involved in locating production inappropriately.*[10]

The Council was unable to come to any definite conclusion on the other components of regional development policy, such as the infrastructure grants.

Other writers have been more critical of the DREE programs. One, for instance, concluded that:

> *In the current situation, the publicly-recognized RDIA goal is employment in certain depressed regions . . . DREE fails to achieve the greatest number of new jobs, and incurs a higher cost per new job created, by continuing with the subsidies which are inconsistent with their goals.*[11]

The specific complaint, based on rigorous statistical analyses of the program and its effects, was its bias towards capital-intensive production techniques. Another analyst was even more sweeping in the criticisms put foward:

> *In view of all the uncertainties inherent in the subsidization of firms – the absence of solid evidence that investment in the designated regions is really increased, the even greater doubt about employment, the effects on distribution*

of income among persons, the possibility of inequity in the government's dealings with firms, the probable reduction in national income in Canada as a whole, and the lack of any real assurance that modernization and progress are fostered in the designated regions – I wonder if it might not be best for the federal government to restrict its subsidy program to the support of poor people . . . and to such transfers to provinces as are agreed upon in federal-provincial negotiations, and to keep its distance from firms' decisions about the location of investment.[12]

A research paper prepared for this Commission, summarized the available evidence on regional development initiatives:

Despite widely varying policy thrusts and economic circumstances, there has been little improvement in the relative position of most of the poorer provinces as measured by income net of transfers . . . It seems reasonable to conclude that there has been no discernible progress with regard to regional development. This finding alone would appear to be a serious indictment of the many policy efforts, and very large public sector outlays that, it was argued, could achieve that goal.[13]

Nevertheless, as Commissioners have noted, it may be that the policies have prevented regional imbalances from getting worse. Nor has it been shown conclusively that if Canada had devoted greater resources to regional development, more progress would have been made.

Criticisms of regional development efforts have gone well beyond arguing that they are simply ineffective. A much discussed and controversial view partially attributes continuing regional economic disparities to the design of these transfers.[14] Economic circumstances create excess aggregate supply in a region. Wages and prices fail to adjust properly, with the result that unemployment triggers transfer payments of various kinds into the region, including individual compensation to the unemployed and additional equalization entitlements to the host provincial government. The receipt of these transfers blocks further adjustment in the form of out-migration or falling real wages. Without such adjustment the region is forever unable to regain its former economic standing, for its wage rates remain out of line relative to its labour productivity.

Transfers have been associated with some of the least suitable of the provincial economic policies.[15] The argument rests, essentially, on what is known as moral hazard. If provincial governments are not forced to bear the full costs of their actions, they will implement policies, highly attractive on some grounds, perhaps, which they would otherwise avoid. Unrealistic minimum-wage laws, language policies and restrictions on non-resident land ownership are three examples cited. These popular programs can be implemented because the distortions they cause are paid for, at least in part, by others. For example, Unemployment Insurance covers those persons who are displaced by minimum-wage legislation, while equalization payments offset some of the adverse economic consequences resulting from the other two examples cited.

This system results in a state that observers refer to as "transfer dependency". It creates a vicious circle in which economic misfortune begets

transfers which, in turn, father poor economic policies which beget further economic misfortune. All private, as well as government, economic agents in the recipient regions are acting rationally within the existing system of incentives, yet the outcome is continued economic stagnation. This situation causes increasing expense to the economic union as a whole.

Whatever the merits of this argument in principle, it is still subject to empirical assessment. Some evidence exists to support certain aspects of the thesis, but to date, no complete assessment has been made. Work on unemployment-insurance and labour-market adjustments[16] tends to support the notion that transfers do affect interprovincial migration. More than one analysis has concluded that the 1971 changes to the unemployment insurance scheme, which made it significantly more generous, acted to retard out-migration from the Atlantic provinces.[17] These studies suggested that this migration, given the relative income and unemployment levels of the source and probable destination areas, would be socially beneficial. Attention has also been drawn to research suggesting that:

> *The UI program reinforces the concentration of unstable and short term jobs in the regions with high unemployment and a high concentration of seasonal industries.*[18]

Commissioners note that such criticisms are directed at impediments to effective adjustment processes. They do not address the effectiveness of policies to improve the economic base of disadvantaged regions.

These debates centre on the uncertainties involved in developing regional development policies. The uncertainties operate at a number of levels. One policy choice must take into consideration aggregate national income growth and the growth of each particular province or region. The central concern here is whether measures to promote the latter reduce the former by diverting resources to areas of lower reward; or, conversely, whether in the long run, regional development programs contribute to the growth of the national economy. Commissioners' recommendations seek to minimize this dilemma by emphasizing that regional development policy should focus as much as possible on improving the productive capacity of poorer regions.

A choice must also be made between "compensatory" policies designed to minimize the gap between earned and total incomes, and those policies which are developmental, or which promote adjustment. "Compensation" is designed to soften the effect of market forces on individuals. In Part V of this Report, however, Commissioners have recommended redesigning Canada's social policies to enhance Canadians' concept of social justice while reducing the barriers to adjustment. These recommendations, if put into practice, will have important regional effects. We have shown, too in this chapter, that equalization, a compensation program, also has important positive implications for efficiency.

In addition, tension exists between interregional market-adjustment policies, which are aimed primarily at facilitating the mobility of labour and capital to areas of their greatest productivity, and developmental policies, which are aimed at improving the productive capacity of individual regions. We Canadians, Commissioners believe, have decided that policies must be

blended in order to make it possible for those who wish to move to do so; but the economic and social viability of all our regions must be promoted as well.

These policy decisions have been reflected in administrative tensions. As our analysis suggests, Canadians have never settled on a stable blending of policies in this area. We have moved from a sectoral orientation, under ARDA, to a more generally directed economic development approach, including adjustment out of the region, FRED, to a strategy of creating growth poles, under ADA and DREE. Specific policies have ranged from adjustment assistance to infrastructure grants, to tax breaks, to direct subsidies, to regionally differentiated investment and employment credits.

Nor have we Canadians settled on the proper relation between federal and provincial responsibilities for encouraging and supporting regional economic development. Early federal efforts were highly centralized and tended to ignore provincial wishes. During the GDA period, however, the reverse was true: the federal government financially supported province building. The pendulum then swung briefly in the opposite direction.

The federal government has been unable to form a satisfactory link between its regional development responsibilities and its broader role in managing our national economy. The most obvious manifestation of this failure is apparent in the constant rearrangment of the federal bureaucracy, first, to bring regional interests into a separate department, then to encourage all departments to consider regional implications, and finally, to drift back to the single-ministry concept. We are thus faced with three questions: What is the appropriate division of labour between the federal and provincial governments? How should the Government of Canada balance its regional economic with its national responsibilities? What policies and programs should be pursued?

Conclusions

We Commissioners would not go so far as to label Canada's continuing regional economic disparity a crisis. We do, however, view it as a serious problem. The nature of individual Canadians' future economic prospects should not depend so significantly on their province or place of birth. Regional development must therefore remain one of Canada's primary policy goals. Commissioners are equally convinced, however, of Canadians' need to reconsider our view of regional economic disparity, our notions of what we should do to overcome it, and our ideas about the institutional mechanisms we should bring to the task. Some of the propositions Commissioners advance are principles we are urging Canadians to accept, some are statements of economic constraints that Canadians have no choice but to accept, and some are conclusions drawn from our research and hearings. Together they form a package that we hope will serve to guide regional policy formation in the years to come. The proposals are designed to be consistent with this Report's broad themes concerning principles both of economic adjustment and of federalism.

Our first proposal concerns the concept of regional disparity. In our opinion it is time to stop viewing inequalities simply in terms of per capita income

differences. Transfers, both to individuals and governments, have rendered this focus unnecessary. Individual Canadians now have a variety of support mechanisms to fall back on in the event of personal hardship, and our proposals in Part V, especially those concerning the new Universal Income Support Program (UISP) and the Transitional Adjustment Assistance Program (TAAP), if adopted, will further improve this situation. Our equalization scheme, imperfect as it is in some respects, would allow each provincial government the means to provide its residents with a comparable level of public goods and services, without imposing the burden of unduly high taxation rates. There is, in fact, less variation in per capita incomes across regions now than there is among individuals within provinces. To the extent that Canadians are truly concerned with income inequality, our first priority should be the vertical dimension of the problem, that is, its application to individuals.

The core factors of regional inequality are wage differences for given types of employment, and variations in employment rates. A job is important, first and most obviously, because it provides a source of income. But it offers more than that. In a society such as ours, a steady job also provides a sense of self-worth and dignity that the most generous transfer scheme could never duplicate. In a federal state, there is even more at stake. The availability of jobs in a region also provides the population base necessary for the survival of that community.

Commissioners conclude that Canada's past policies have compensated quite adequately for regional economic disparities, but that they have been markedly unsuccessful in promoting self-sustaining economic development. The complex mix of transfer programs has substantially evened out per capita incomes across regions, but it has not provided the foundation for robust future economic development.

Commissioners also find some merit in the thesis that Canadians' difficulty in establishing acceptable employment rates in some parts of the country lies partly in the distortions created by a variety of well-intentioned, but misguided, economic policies. Canadians' concern with compensating regions for their economic shortcomings has been partially responsible for those regions' maintaining this status. We have neglected to structure policies and programs to provide the proper incentives to firms, workers and governments. A cycle of transfer dependency has been created whereby economic disparity begets compensation which, in turn, induces behaviour that sustains economic disparity. To make this point perfectly clear, Commissioners are not suggesting that transfer dependency explains all regional economic disparity. There were, after all, significant disparities of this sort in the decades before the 1950s, when few such transfer programs existed. We are simply suggesting that inappropriate incentives are part of the explanation of some of the present problems in this field.

Commissioners believe that regional economic well-being is the responsibility of all levels of government, including municipal government. The role of provinces and municipalities is clear. The justification for including the federal government lies in Canadians' concept of what it means to be a citizen

of this country and the practical need to integrate regional development with national development.

We come now to an important economic constraint which relates directly to the institutional design issue. There is typically, but not always, a fundamental conflict between the goals of regional economic development and those of national efficiency. The location of economic activity is normally not neutral. For a variety of complex reasons, some regions of Canada are simply better situated than others to support internationally competitive enterprises. Furthermore, as this analysis of our economic union has shown, the fewer the barriers to interprovincial trade flows, the more efficient is our national economy and the greater the ease with which capital and labour can be reallocated interregionally. Yet distortions in these markets are often the product of otherwise defensible efforts by both federal and provincial governments to encourage economic development in Canada's poorer regions.

A political constraint accompanies this economic one. The clashing of goals often means that regional economic development produces political tension which operates at two separate levels. The federal public service itself is torn between departments with a national and a sectoral focus, and those with a more explicit regional mandate. Added to this tension is the unavoidable federal-provincial conflict. Whenever the national government undertakes economic policies that are designed for a specific place, as regional development measures are by definition, it impinges on provincial government plans.

In the recommendations set forth in this Report, Commissioners focus both on the federal government's regional development policy, and on that government's implementation of its policy. As we noted above, the federal government has a legitimate role to play in regional development, but its involvement in this policy sphere has typically conflicted with its overall national responsibilities. Thus a further requirement emerges: whatever the federal government does in this field should not be inconsistent with provincial plans. This position is consistent with the basic principles of federalism, but it does not imply that the federal government must blindly support whatever development strategies the provinces put forward.

Does this complex of constraints leave any scope for federal initiative? We Commissioners believe that it does. We return to the two areas of disparity that we find important, wages and employment rates to define the proper federal role. Wage gaps are created because labour productivity for given types of employment is not equal across regions. If output per worker in poorer regions could be brought up to the level that exists in wealthier ones, one important source of regional differences would be removed. The same statement holds true for employment-rate differences: if any Canadian, irrespective of region, had an equal chance of obtaining permanent employment, the other main source of regional disparity would disappear.

The form that the Government of Canada's involvement in regional economic development should take follows logically from these observations. Our national government's responsibility should be to work to remove differences in labour productivity across regions and any factors that impair

the efficient operation of regional labour markets. If poorer regions adopt technology more slowly, the federal government might help to accelerate this process. If labour skills are deficient, it could help to provide retraining. If there are structural problems in matching labour skills with employment demands, it could establish information centres.

This proposal is an extension of the argument advanced in Part III of this Report. There the object in seeking government action was to correct for market failures of whatever origin. Intervention was seen as economically efficient or socially beneficial if Canadian firms were experiencing problems in adopting the latest technology or in reallocating capital and labour from "sunset" to "sunrise" industries or in improving the competitive position of groups in the labour force that historically have been unable to compete on equal terms. The private market-place fails in these instances when it does not generate the socially most desirable outcome.

Commissioners have simply added to this analysis another dimension that is inherent in regional disparities. Specifically, we would assert that the market has failed if it has not provided comparable firms in all regions of the country with equal access to capital, technology, and labour and management skills. In Part III, we asked whether private actors would bring the latest technology to Canadian industry at rates that would allow Canada to compete in the international market-place. If the answer was no, then an industrial strategy of some sort seemed justified. Here we ask whether these same agents will also diffuse this same technology adequately to all regions of the country. If not, then regional policies seem warranted.

These policies would not attempt to bring the same industrial or occupational structure to each regional economy. The object would simply be to ensure that industries that do locate naturally in poorer regions can produce as efficiently as their counterparts elsewhere. A brewery or government office in Atlantic Canada, for example, should be no less productive than its counterpart in Ontario. Almost certainly, however, there would continue to be a greater concentration of high-technology industries in the latter province.

A similar analogy applies to employment differentials. Commissioners are concerned about unemployment at the national level and seek policies to reduce it because we do not believe that the labour market is sufficiently responsive to effect this on its own. In Canada, however, as we noted above, unemployment has a marked regional dimension as well. The national unemployment figure is an average of consistently higher jobless rates in some provinces and consistently lower rates in others. Moreover, these differences tend to widen as aggregate unemployment rises and to narrow as it falls.

The inference to be drawn from the first observation is that all regional labour markets are not equally efficient at matching jobs and workers to meet given levels of aggregate demand. That the gap widens as national economic activity slows is evidence that changes in aggregate demand do not spread evenly to all regions. In both instances, markets fail in the sense that they do not operate equally effectively across the country. As with differences in productivity, then, this failure establishes the rationale for the federal government's regional policy.

It is considerably easier to establish that something should be done about differences in employment rates than it is to recommend exactly what to do. In part, the differences will disappear naturally, with elimination of productivity gaps and equalization of wage levels for given types of employment. As long-term equilibrium is established, there will be less out-migration of younger and more highly educated workers. Participation rates will also rise as the economic outlook improves. These two effects together will raise to the national average, the ratio of those seeking work to total provincial population eliminating part of the difference in employment rates.

The difficulty for policy purposes is compounded by the third component of differences in employment rates: unemployment rates that are much higher in poorer regions. It is important to be realistic on this point. There is absolutely no guarantee that as productivity levels, and hence wage rates, rise toward the national level, there will be enough jobs generated in the poorer regions to employ fully the existing labour force. Let us examine what underlies these possibilities. Suppose that federal and provincial governments raise labour productivity in poorer regions. Their action will have two distinct effects. First, a region will need less labour to produce any given level of output. Secondly, costs may fall for those products that the region produces in competition with suppliers elsewhere, suggesting that total output could increase. The net effect is uncertain. If the labour-saving bias in productivity improvement is strong and the scope for capturing new markets weak, net job destruction will result. The converse will occur under reverse conditions. To date, there is simply no firm evidence about the balance of these alternative outcomes in the different regions of Canada.[19]

It is at this point that Commissioners introduce a sharp distinction between federal and provincial functions in regional economic development. The federal government, we wish to suggest, should not involve itself directly in regional job creation. Its responsibilities end with its commitment to overcome regional productivity gaps and labour-market imperfections. It has served regional equality if identical employments fetch roughly similar compensations, and if adjustment to change in labour markets proceeds equally efficiently in all regions. In addition, the federal government should bring to discussions of regional development a direct concern with building complementary and mutually beneficial links among provincial economies. In other words, it should set regional policy in a national framework.

Provincial governments and their electorates typically want more than this from economic policies. Specifically, they have absolute employment targets as well. They wish generally that all current and future residents will be able to find suitable employment locally. This emphasis on place prosperity is both understandable and defensible when it comes from a provincial government. It should not, however, unduly concern the federal government. Commissioners believe that community preservation, to the extent that people want it, is ultimately the responsibility of citizens and of their local and provincial governments. The federal government must not stand in the way of achieving that goal, in the sense that its economic and social policies must not consistently discriminate against particular groups, but neither need it devote resources directly to meet that goal. Provinces, however, must have access to

such funds and be free to use them in this manner if they so desire. The following conclusions form the basis of our recommendations:

- In the interests of the efficiency of the national economy and of promoting interregional adjustment, the federal government should modify certain regionally distorting programs, in directions consistent with the analysis presented in Part III of this Report.
- The federal government should direct regional development programs toward improving regional productivity and the efficiency of the labour market.
- Provinces should take full responsibility for place-specific employment measures as part of their own regional development policies. In order to increase their capacity to address local needs, provinces receiving equalization payments should also receive Regional Economic Development Grants from the federal government.
- Co-ordination of these federal and provincial activities should take place through continuation of the mechanism of Economic and Regional Development Agreements.
- A sustained federal commitment to regional development requires that a single central agency be responsible for injecting regional concerns into the programs of individual federal departments and for co-ordinating federal efforts.
- Commissioners believe that the total federal financial commitment to regional development, which would combine the Regional Economic Development Grants with funds spent through ERDAs, should increase significantly over the next few years.

Notes

1. Constitution Act, 1982, s. 36.
2. This review is based on a research study for the Commission: Robert L. Mansell and Lawrence Copithorne, "Canadian Regional Economic Disparities: A Survey", in *Disparities and Interregional Adjustment*, vol. 64, prepared for the Royal Commission on the Economic Union and Development Prospects for Canada (Toronto: University of Toronto Press, 1985).
3. N. Harvey Lithwick, "Federal Government Regional Economic Development Policies: An Evaluative Survey", in *Disparities and Interregional Adjustment*, vol. 64, prepared for the Royal Commission on the Economic Union and Development Prospects for Canada (Toronto: University of Toronto Press, 1985).
4. *Ibid.*
5. Peter Aucoin and Herman Bakvis, "Regional Responsiveness and Government Organization: The Case of Regional Economic Development Policy in Canada", in *Regional Responsiveness and the National Administrative State*, vol. 37, prepared for the Royal Commission on the Economic Union and Development Prospects for Canada (Toronto: University of Toronto Press, 1985).
6. Lithwick, "Federal Government Regional Economic Development Policies".
7. Office of the Prime Minister, Press Release, January 12, 1982.
8. Atlantic Provinces Economic Council, *The Atlantic Economy: Fifth Annual Review* (Halifax: The Council, 1971).

9. Economic Council of Canada, *Living Together: A Study of Regional Disparities* (Ottawa: Minister of Supply and Services Canada, 1977), p. 158.
10. *Ibid.*, p. 125.
11. Robert S. Woodward, "The Effectiveness of DREE's New Location Subsidies", *Canadian Public Policy* (Spring 1975), pp. 228–29.
12. Dan Usher, "Some Questions about the Regional Development Incentives Act", *Canadian Public Policy* (Autumn 1975), p. 575.
13. Lithwick, "Federal Government Regional Economic Development Policies".
14. Thomas J. Courchene, "Avenues of Adjustment: The Transfer System and Regional Disparities", in *Canadian Confederation at the Crossroads: The Search for a Federal-Provincial Balance*, edited by Michael Walker (Vancouver: Fraser Institute, 1978).
15. *Ibid.*
16. Jean-Michel Cousineau, "Unemployment Insurance and Labour Market Adjustments", in *Income Distribution and Economic Security in Canada*, vol. 1, prepared for the Royal Commission on the Economic Union and Development Prospects for Canada (Toronto: University of Toronto Press, 1985).
17. Jean-Michel Cousineau, "La mobilité interprovinciale au Canada: le cas de l'Ontario, du Nouveau-Brunswick et de la Nouvelle-Écosse", *L'Actualité Économique* 55 (1979): 501–15; and Stanley L. Winer and Denis Gauthier, *Internal Migration and Fiscal Structure* (Ottawa: Economic Council of Canada, 1982).
18. Cousineau, "Unemployment Insurance and Labour Market Adjustments".
19. See the Economic Council of Canada's Newfoundland reference for an extensive discussion of these effects: *Newfoundland: From Dependency to Self-Reliance* (Ottawa: Economic Council of Canada, 1980).

Federal-Provincial Fiscal Arrangements

Fiscal arrangements are at least as important an institution of the federation as the machinery of intergovernmental relations. Like other countries with federal systems of government, Canada has departed a long way from the fiscal equivalent of watertight compartments, where each government carries out its taxing and spending decisions independently. In Canada, both orders of government exploit the major sources of taxation; tax changes by one order will therefore have immediate consequences for the other. Moreover, revenues flow between governments in massive amounts; attempts by the federal government to constrain expenditures are difficult when a quarter of its spending is in the form of transfers to the provinces; the same is true of provinces with respect to municipalities.

Taxation has a long and complex history in Canada, and fiscal arrangements have been a constant preoccupation of federal-provincial relations since 1867. The British North America Act gave the federal government unlimited taxing authority, while it restricted the provinces to direct levies. Since this meant that the lucrative customs duties and excise taxes of the day were removed from the provinces, the federal government agreed to make specified annual payments in "full and final settlement" of all claims on it. Under these arrangements, the provinces collected only 27 per cent of their total revenues in the first years of Confederation. Their taxation effort, including initial forays into direct taxation of income, increased gradually in the late nineteenth century and again after the First World War as their expenditure responsibilities grew. The federal government also began to levy income taxes during the First World War. Nevertheless, by the time of the onset of the Great Depression, provincial and local authorities were collecting over 70 per cent of Canadian public revenues.

The scramble for revenues in the 1930s led to a "tax jungle" of double-taxation and conflicting regulations. The overall structure of federal-provincial finance was extensively examined in the historic work of the Royal Commission on Dominion-Provincial Relations, the Rowell-Sirois Commission. The Commission recommended that the federal government collect all personal and corporate income tax and death duties, and remit funds to the provinces, but this recommendation met stiff resistance from the provinces. However, the Second World War brought about what a Royal Commission's recommendations could not. The federal government took over these tax sources for the duration of the war and, in exchange, made specified grants to the provinces under the Tax Rental Agreements. By most accounts, this was the high point of centralization in the Canadian tax system, just as the half decade leading up to the Depression had been the high point of decentralization.

The Tax Rental Agreements continued after the war, although with significant modifications in scope and structure, including the withdrawal of Quebec and the partial withdrawal of Ontario in 1947. Renewed in 1952, the first major change in the agreements came in 1957, when provinces were given a choice: they could continue to "rent out" the direct taxation field to the federal government; or they could levy their own income taxes and

succession duties, and have the government in Ottawa provide an offsetting "abatement" of federal tax payable. At the same time, fiscal equalization payments were explicitly introduced for provinces where income tax and succession duties yielded less than an Ontario-B.C. average. In a subsequent series of federal-provincial negotiations, the abatement of federal taxes was steadily increased to provide more "tax room" to the provinces. The federal personal income-tax abatement, originally set at 10 per cent of the federal tax payable, rose to 28 per cent by 1967. In 1962, in a further legal change, provinces were required to impose their own corporate and personal income taxes. However, the federal government would continue to collect provincial taxes free of charge as long as they conformed with federal rules under provisions of tax collection agreements. Otherwise, the provinces were free to establish and administer their own systems, which Quebec did for both corporate and personal income taxes, and which Ontario did for corporate income taxes.

Through these successive arrangements, wartime fiscal centralization was dramatically changed. If we look only at revenues raised by each level of government from its sources, the federal share declined from 73.9 per cent of the total in 1945, to 67.1 per cent in 1955, and to 43.3 per cent by 1983. The provincial and local share rose in the same years from 26.1 per cent to 32.9 per cent, to 56.7 per cent. At the same time, intergovernmental grants increased, making the shift even more dramatic. After transfers are accounted for, federal revenues dropped from 69.2 per cent of the total in 1945, to 32.6 per cent in 1983, and the provincial and local share rose from 30.8 per cent to 67.4 per cent.[1] The broader historical pattern, expressed in terms of gross national product (GNP), is shown in Table 22-12.

There are other indicators of relative decentralization and increasing flexibility. From the inception of the Tax Collection Agreements, provinces were free to fix their tax rates above or below the amount of the federal abatements. Their flexibility was enhanced later, when abatements ceased for personal income taxes. The provinces were to introduce various tax credits against provincial tax payable, thus increasing their autonomy and flexibility. These changes also led, especially in the 1970s, to increased diversification in provincial tax rates. In 1985, provincial personal income-tax rates as a percentage of the federal tax ranged from a high of 60 per cent in Newfoundland to a low of 43.3 per cent in Alberta and 43 per cent in the Northwest Territories. Provinces also gained more flexibility with respect to the grants they received from the federal government. A larger proportion of federal grants took the form of either unconditional payments (equalization) or block grants with few and broad conditions.

Intergovernmental transfers also increased: as a proportion of federal expenditure, they rose between 1945 and 1983 from less than 4 per cent to more than 18 per cent. Each government levies its own taxes, but only the federal government raises its entire revenue, excluding borrowing, of course, through taxation. The others – provinces, local authorities, and hospital boards – rely, to varying degrees, on transfers from other governments. In 1983, for example, the federal government received slightly more than $70 billion in revenue and transferred nearly $17.5 billion. In other words, for

TABLE 22-12 Total Government Revenue Expressed as a Percentage of Gross National Product, Before and After Exclusion of Intergovernmental Grants from Revenue of Recipient Government, Selected Calendar Years, 1926–1982

Year	Federal	Provincial[a]		Local		Total,[b] Excluding Grants
		Including Grants	Excluding Grants	Including Grants	Excluding Grants	
1926	7.6	3.4	3.0	6.7	6.3	16.8
1939	8.6	7.1	5.5	7.2	6.6	20.7
1946	22.1	6.1	4.6	4.4	3.7	30.4
1955	17.6	6.5	4.8	4.9	3.8	26.1
1965	16.4	11.4	8.9	7.5	4.8	30.3
1975	19.2	18.0	13.5	8.5	4.4	38.9
1982	18.4	20.8	16.5	8.8	4.7	42.0

Source: Canadian Tax Foundation, *The National Finances 1983–84* (Toronto: The Foundation, 1984), Table 3.7.

Note: Since figures are rounded, there may be some disparity in the totals.

a. Includes Newfoundland for years subsequent to 1947.
b. These totals also include revenues of hospitals and of the Canada and Quebec Pension Plans.

every three dollars the federal government collected in taxes for its own use that year, it collected an additional one for the sole purpose of turning it over to another political authority, most of these funds went to provincial treasurers.[2]

By far the largest category of transfers are federal contributions to health, education and welfare programs. In 1983–84, over $11 billion, or just over 60 per cent of the cash transfers, are accounted for in this manner: $7.6 billion under Established Programs Financing, $3.1 billion for the federal share of Canada Assistance Plan payments, $70 million for other health and welfare, and $182 million for bilingualism in education. The other large category is general purpose transfers of unconditional – principally equalization – entitlements, which total nearly $5.5 billion or about one-third of the total cash transfers. Miscellaneous transfers such as payments to municipalities and territories account for the remainder.[3] These payments are summarized in Table 22-13. Table 22-14 summarizes payments for previous years.

The more than $17 billion the provinces received as cash transfers in 1983 represented a fifth of the total funds at their disposal that year, a drop from just over a quarter in 1975.[4] The provinces, in turn, remitted one-third of their total revenue – $27.8 billion – to local governments and school and hospital boards. On a net basis, the provinces paid out over $10 billion more than they received. In effect, they financed their entire expenditure on goods and services from their own revenues or, in some instances, by borrowing. Local governments, by contrast, raised only about half of their total revenues

TABLE 22-13 Estimated Federal Transfers to the Provinces, Territories, and Municipalities, Fiscal Year 1983–84

	Nfld.	P.E.I.	N.S.	N.B.	Que.	Ont.	Man.	Sask.	Alta.	B.C.	Territories	Total
						($ millions)						
Statutory subsidies[a]	9.7	0.7	2.3	1.8	4.7	6.0	2.2	2.2	3.6	2.5	—	35.7
Equalization												
Current year	536.0	114.8	536.0	488.5	2 475.5	—	290.5	—	—	—	—	4 440.6
Transitional payments	—	10.5	66.6	28.4	473.5	—	177.3	—	—	—	—	756.4
Prior years	−14.3	2.1	0.2	0.6	142.0	—	12.5	−22.9	—	—	—	120.1
Reciprocal taxation	10.5	4.1	23.9	12.5	47.0	64.5	na	—	—	na	—	210.5
Public utilities income tax transfer[a]	15.7	1.0	—	—	1.7	−9.7	0.3	—	116.6	3.3	−0.4	128.5
Youth allowance recovery	—	—	—	—	−252.8	—	—	—	—	—	—	−252.8
Total general purpose transfers	557.0	133.2	629.0	531.8	2 891.6	60.8	482.8	−20.7	120.2	5.8	−0.4	5 439.8
Established Programs Financing												
Cash payment												
Hospital insurance	92.5	19.9	137.8	113.1	751.8	1 307.9	159.5	172.0	254.7	421.7	8.9	3 439.9
Medicare	31.9	6.8	47.4	38.9	258.9	450.3	54.9	59.2	87.7	145.2	3.1	1 184.3
Post-secondary education	56.1	12.1	83.6	68.6	447.3	790.2	95.7	104.1	150.9	254.8	5.5	2 068.8
Extended health care	21.8	4.7	32.4	26.6	246.5	333.3	38.7	37.4	88.7	106.8	2.7	939.5
Total cash	202.3	43.5	301.3	247.2	1 704.5	2 881.7	348.8	372.6	582.0	928.5	20.1	7 632.5
Canada Assistance Plan[a]	71.4	19.7	93.2	119.2	909.4	848.1	99.3	125.5	343.6	496.8	14.0	3 140.2
Other health and welfare[a]	1.0	0.2	3.0	3.1	—	37.4	4.5	3.4	9.3	6.8	1.4	70.1
Bilingualism in education[a]	2.0	1.1	3.4	18.8	92.6	44.6	5.2	2.4	5.5	6.3	0.3	182.2
Group insurance	—	1.2	0.2	0.5	5.8	22.3	14.2	59.3	38.8	2.7	—	145.0
Territorial financial arrangements[a]	—	—	—	—	—	—	—	—	—	—	445.6	445.6
Municipal grants[a]	1.9	0.7	12.2	10.4	51.3	102.1	11.6	5.5	13.2	19.6	2.5	231.0
Other[b]												364.0

TABLE 22-13 (cont'd.)

	Nfld.	P.E.I.	N.S.	N.B.	Que.	Ont.	Man.	Sask.	Alta.	B.C.	Territories	Total
	($ millions)											
Subtotal	76.3	22.9	112.0	152.0	1 059.1	1 054.5	134.8	196.1	410.4	532.2	463.8	4 578.1
Total cash transfers	835.6	199.6	1 042.3	931.0	5 655.2	3 997.0	966.4	548.0	1 112.6	1 466.5	483.5	17 650.4
EPF tax transfer												
13.5 personal income tax points	63.2	13.3	120.2	89.0	1 095.4	1 922.8	173.0	181.8	624.0	654.8	16.9	4 954.5
1.0 corporate income tax points	2.3	0.6	4.2	3.0	46.9	96.1	7.6	9.9	79.6	24.8	0.8	275.8
Contracting-out tax transfer												
16.5 personal income tax points to Quebec	—	—	—	—	1 338.9	—	—	—	—	—	—	1 338.9
Total tax transfers	65.5	13.9	124.4	92.0	2 481.2	2 018.9	180.6	191.6	703.6	679.6	17.7	6 569.2

Sources: Canada, Treasury Board of Canada, Press Release, 83/10, February 22, 1983; Finance Canada, mimeographed data; Canadian Tax Foundation, *The National Finances 1983–84* (Toronto: The Foundation, 1984).

a. As from Treasury Board of Canada, Press Release, 83/10, February 22, 1983.

b. Includes adjustment for Manitoba, British Columbia, and prior years not allocated by province.

TABLE 22-14 Summary of Federal Contributions to the Provinces, Municipalities, and Territories, Fiscal Years Ending March 31, 1974 and 1981

	1974[a]	1981[a]
	($ millions)	
Payments to provinces		
General purpose transfers		
Equalization	1 517.0	3 590.4
Share of federal estate tax	0.1	—
Adjustments for prior years	—	—
Share of income tax on certain public utilities	25.9	134.8
Grants in lieu of provincial property tax	2.8	6.5
Income tax guarantee	42.6	—
Share of tax on undist. income	—	45.6
Reciprocal taxation	—	145.3
Statutory subsidies	33.8	34.1
Sales-tax/reduction program	—	—
Recovery of youth allowances	−53.1	−163.4
Other	0.2	—
Total general purpose transfers	1 569.3	3 793.2
Specific purpose transfers		
Hospital insurance	1 073.2	2 474.3
Medicare	676.2	857.1
Other health services	39.1	641.8
Social services	721.3	2 052.3
Education		
Post-secondary	485.1	1 600.3
Other	99.0	178.9
Transportation and communications	47.1	71.4
Other	248.4	642.8
Total specific purpose transfers	3 389.1	8 518.9
Total payments to provinces	4 958.4	12 312.2
Payments to local governments		
General purpose transfers	64.0	157.7
Specific purpose transfers	101.0	151.9
Total payments to local governments	164.9	309.5
Payments to territories		
General purpose transfers	85.3	273.0
Specific purpose transfers	10.8	48.7
Total payments to territories	96.1	321.7
Total federal payments	5 219.4	12 943.4

Source: Canadian Tax Foundation, *The National Finances 1983–84* (Toronto: The Foundation, 1984).

a. As from Statistics Canada, Federal Government Finance, Catalogue No. 68-211, various years.

themselves, and hospital boards only about 5 per cent. These latter jurisdictions are the main net recipients in the intergovernmental transfer system which is in place today.[5]

Table 22-15 shows the historical evolution of these intergovernmental transfers. The proportion of the federal budget committed to such transfers has generally increased, and provincial dependence on them has been fairly constant. There has been a decline in both of these dimensions, however, in the last few years.

As Table 22-16 illustrates, provinces vary greatly in their dependence on federal transfers. In 1980–81, all four Atlantic provinces met almost half their revenue needs from federal sources, though this proportion dropped somewhat by 1984–85. Similarly, Manitoba's proportion declined, from 38 to 30 per cent. Quebec received almost a quarter of its revenues from the Government of Canada. Ontario, Saskatchewan and British Columbia each received about 17 per cent from federal sources. Alberta, with its large resource revenues, was least dependent on federal sources.

The pattern, then, is one of extensive interdependence between the federal and provincial fiscal systems, marked by a relatively high degree of decentralization combined with an impressive degree of co-ordination. Why has it developed in this way?

At first glance, a tax system in which each level of government is fully responsible for raising and spending its own funds seems attractive. It is the arrangement most compatible with the tenets of classical federalism: in its designated sphere, each order of government is free to exercise its policy discretion. It is only logical that all levels be given the financial means to carry out their assigned responsibilities as they see fit.

Such a system encourages fiscal responsibility and thus accountability. Like individuals, governments are more careful about their actions if they

TABLE 22-15 Transfers as Proportion of Total Federal Expenditures and Total Provincial Revenues

	Federal Transfers to Other Government			Provincial Transfers From Other Governments		
Year	Total Transfers ('000 $)	Total Expenditures ('000 $)	Transfers as %	Total Transfers ('000 $)	Total Revenues ('000 $)	Transfers as %
1945	157	4 298	3.6	164	621	26.4
1955	450	4 806	9.4	465	1 842	25.2
1965	1 431	8 551	16.7	1 379	6 328	21.8
1975	7 670	35 508	21.6	7 577	29 830	25.4
1983	17 361	94 507	18.4	17 123	82 561	20.7

Source: Statistics Canada, *Historical Statistical Compendium*, prepared for the Royal Commission on the Economic Union and Development Prospects for Canada (Ottawa: Statistics Canada, 1985), Tables 5.4, 5.5.

TABLE 22-16 Total Federal Transfers as a Percentage of Gross General Provincial Revenues

	1980 – 81	1984 – 85
Newfoundland	47.7	47.2
Prince Edward Island	52.8	47.4
Nova Scotia	45.8	39.7
New Brunswick	43.9	42.4
Quebec	22.0	23.1
Ontario	17.3	16.1
Manitoba	37.6	30.3
Saskatchewan	16.9	14.9
Alberta	7.7	9.2
British Columbia	16.1	16.9
Canada	20.1	20.5[a]

Sources: Figures for 1980–81 are based on data from Canadian Tax Foundation, *Provincial and Municipal Finances 1981* (Toronto: The Foundation, 1981), p. 46. Figures for 1984–85 are based on data from Karin F. Treff, "Provincial Estimates fro 1984–85", *Canadian Tax Journal* 32 (September-October 1984): 1003–12.

a. Includes the Territories.

know that they will be held directly responsible for them. This truism implies that the governments that do the spending should raise the taxes. It is too easy for governments to cater to narrow special-interest groups when they do not need to tax their constituents to finance the implementation of their promises.

Why, then, would a federation opt for any other system? There are a number of reasons. First, the provinces have an uneven fiscal capacity. For a given "tax effort", governments in poorer regions will raise less revenue than those in wealthier regions and, hence, will provide inferior services. Alternatively, they will have to tax at a higher rate to provide a comparable level of public sector goods and services. This poses problems of both equity and efficiency, and it is the primary justification for equalization.

A second problem is that separate income-tax systems are more costly to operate and are inconvenient for taxpayers. Two or more of the 11 different tax-collecting bureaucracies that such an arrangement would require, might stipulate that companies and individuals fill out each year potentially quite different tax-return forms. At a minimum, Canadians would want tax-collection efforts to be co-ordinated and governments to collaborate in the enterprise.

A third problem is that of matching revenues to expenditure responsibilities. Left to themselves, some levels of government would be unable to raise

sufficient revenue to carry out their constitutionally assigned expenditure responsibilities, while others would have more than adequate access to funds. The case has traditionally been made that the federal government has taxation capacity beyond its spending responsibilities, while the provinces, and especially the municipalities, are in the opposite situation. This circumstance is a result of the rapidly increasing demands on regional and local governments, coupled with inelastic tax sources. Recently the reverse has been considered more accurate; the federal government now faces the structural deficit problem, while the provinces – at least the resource-rich ones – have the capacity to run persistent surpluses. Whichever way the imbalance may run at any particular time, the implication of this position is that intergovernmental transfers are a necessary part of our fiscal arrangements.

An imbalance between revenue capabilities and expenditure responsibilities might arise because one order of government is excluded constitutionally from one or more of the important taxation sources. Another factor might be that while formal access exists, economic and political circumstances prevent authorities from making full use of some tax sources. Competition among the provinces or municipalities for investment or for skilled labour might lead those authorities to bidding down income and business taxes to, or even below, the costs of services provided. The central government faces less constraint in this respect. Thus it may be more efficient for the central government to levy the "correct" taxes on all income and redistribute the proceeds.

In the fourth place, regional governments operating in a completely decentralized tax and expenditure system might vary their tax and expenditure practices according to any local needs and aspirations they perceived. Such action is perfectly consistent with federalist principles, but it can pose problems for the nation more generally in the form of "spill-overs" and lack of tax harmonization. Both problems stem from the fact that individual jurisdictions tend to ignore the effects of their actions on residents of other regions.

It is inevitable in an economy where products and factors of production are traded between regions that taxation and expenditure decisions in one region will affect output, investment and migration decisions in another. Local authorities will have no reason to worry about these spill-overs, since they are not responsible for them; on the other hand they are not in a position to appropriate any of the political benefit from those spill-overs which are beneficial. Thus some governments may undersupply some services, such as higher education, the benefits of which they cannot fully capture because graduates may migrate to another jurisdiction. Under these circumstances, some citizens will be directly affected by the taxation decisions of a government over which they have no political control, and which they can neither reward nor punish; others, inside or outside local boundaries, will suffer from the undersupply of some forms of public services. One solution is to shift the taxation function and some aspects of expenditure to a more broadly based political authority, one that is responsible to all citizens affected by the policy it exercises.

Another problem stemming from spill-overs is that individual decision makers will not always make the correct decisions if they are not formally responsible for the outcomes. For example, jurisdictions that are able to "export" their tax burden – that is, shift it onto others – will tend to use this revenue source excessively. If citizens of other jurisdictions bear part of the cost, governments will tend to supply more services than residents might otherwise rationally choose. Tax exporting can therefore lead to government that is "too big". Similarly, if a jurisdiction cannot shift its tax burden outside its borders but fears the "leakage" of some of the benefits it provides, it might supply fewer government services than residents might rationally choose, thus producing a government that is "too small". Since a central government is by definition responsible to a more broadly based set of individuals, the spill-over effects of its taxing efforts are less serious, and it may, through shared-cost programs, be able to instigate more appropriate levels of expenditure on service programs under provincial jurisdiction.

A fifth problem is that Canada could eventually find itself with a completely disharmonized tax system in which taxation rates and even definitions of taxable income vary greatly across provinces. This state is the "tax jungle" which so concerned Canadians in the 1930s. Similarly, the nation could produce a completely disharmonized service-delivery system which lacked any portability of benefits and which made widely different services available from one jurisdiction to the next. In either situation, the principle of horizontal equity as applied to federalism would be eroded: that is, individual Canadians who are identical in every respect except in their province of residence and who should be treated equally by the government sector, would, in fact, be treated quite differently.

The obvious rejoinder to this concern is that the desire to implement different social and redistributive policies was the reason for establishing a federation in the first place. One can ask the central government to treat similarly situated Canadians in the same way, wherever they live, but the horizontal equity principle stops there: one cannot always expect provinces to do the same.

Another concern about the potential lack of tax harmony or national standards in service-delivery programs relates to economic efficiency. If labour or capital is treated differently enough by the various provincial tax-expenditure systems, location decisions can be affected; for example, when deciding upon whether and where to migrate, workers will take into account both their expected earnings and the package of government services they receive for taxes they pay. If this – rather than economic productivity – is what shapes decisions to move or to stay, then overall efficiency is sacrificed. However, if taxation can be arranged to remove all fiscal influences from the location decisions of capital and labour, and if governments can provide uniform services across Canada, economic output will again be at a maximum. How better is this uniformity to be achieved than by turning responsibility over to a central government and having it return part of the revenue to the provinces according to a pre-arranged formula?

Provinces can compete only for labour and capital, which are relatively mobile factors of production; but their treatment of less mobile factors, such

as land or equipment which is already in place, can vary. This situation may lead provincial governments to turn increasingly to just such sources to finance general expenditures. They bid down, perhaps to zero, some taxes, such as inheritance or succession duties, while they expect others, such as those on property, to bear a greater share of the burden.

In addition, if the processes of federalism engender harmony among provinces, their competition in the matter of tax and expenditure decisions may frustrate the achievement of provincial redistributive or economic-development goals. Generous redistributive schemes may drive out wealthy taxpayers and attract poor ones from neighbouring jurisdictions, undercutting the effectiveness of the scheme. Other provinces will quickly copy tax inducements to investment and in the end will achieve nothing. It may be that only a national government, which is able to exploit some monopoly taxing advantage, can implement a truly redistributive scheme or an effective development program. Distinct regional ventures in these areas, however attractive they may be in principle, may simply be infeasible.

A sixth problem with a decentralized tax and expenditure system is that it may impair the country's capacity to carry out meaningful counter-cyclical fiscal policy. Stabilization policy is traditionally held to be a logical function for the central government. Small regional governments will see most of their efforts dissipated because of the very open nature of their economies. Tax breaks will encourage spending on another province's output as often as they will promote expenditure on local production. Stabilization policy will therefore be less effective. Since the national economy is larger and more self-contained than any provincial economy, this problem is less severe for the federal government. For the Government of Canada to be able to carry out this role effectively, however, it must control a significant part of the total tax and expenditure base. Otherwise, provinces and municipalities might simply offset any federal measures by altering their own taxing and spending decisions in such ways as to reinforce, rather than counteract, the business cycle.

There are three common counter-arguments to this position. First, some economists now deny that any government, federal or other, can actually implement effective counter-cyclical stabilization policies. Secondly, even assuming that there can be a role for the federal government, it is not clear how large a share of total tax sources that government needs to carry it out. The share certainly does not amount to 100 per cent, as is sometimes implied, but it is difficult to know what would be a critical minimum. Finally, it is not necessarily true that provincial governments will act inappropriately.

As Commissioners noted in Part III of this Report, we do not agree that effective stabilization policies are impossible to implement, although we do suggest that several caveats should be observed in applying them. We also believe that the tax and expenditure base for the federal government is sufficient to allow it to conduct effective stabilization policies. We are further convinced that the harmonization of tax systems and the achievement of some national standards of service-program delivery are an important part of our Canadian nationhood; and we have noted instances, such as that relating to

post-secondary education, where the absence of conditions attached to federal funding arrangements may have resulted in a serious undersupply of services.

For these reasons we are convinced that the current interlinking of federal and provincial tax and expenditure arrangements is generally appropriate. This arrangement forms a solid basis for development and for program and institutional reforms.

Commissioners next address the mechanisms through which tax and program harmonization occurs. In what follows, we have not attempted to recommend specific proportions of overall revenues and expenditures appropriate for each level of government. In any event, these decisions might vary slightly from year to year, but more important, they can only be made pursuant to broader considerations of tax reform: before we can divide the pie, we must know its size, shape and flavour. That seems to us to require another investigation with a narrower mandate focused on the types of tax-reform issues raised earlier and the division of the resulting revenues.

Tax-Collection Agreements

The federal government presently administers and collects personal income taxes for all the provinces except Quebec. It defines what constitutes income, and what deductions are allowed the taxpayer, and it determines the amount of taxable income against which the provincial tax rate is levied. The provinces then apply a single percentage to the resulting "Basic Federal Tax", to calculate provincial tax payable before credits. At this point provinces are entitled to specify any tax credits of their own, such as those for property-tax allowances or political contributions. The federal government will administer these individual programs for a sliding-scale fee, provided that they meet certain criteria of simplicity and are not construed as altering the essential harmony of the overall tax system. This system is commonly referred to as "tax on tax". A taxpayer is taxed by the particular province in which he is resident on the last day of the calendar year.

The corporate income-tax arrangements are quite similar. The federal government defines the structure of the tax, and the participating provinces (all but Ontario, Quebec and Alberta) set their own rates against it. The provinces levy their rates, however, against corporate taxable income as defined for federal purposes, and not against federal tax payable. This means that the provinces are free to establish their own rate of tax or to vary rates, according to size of enterprise, for example. All provinces, even non-signatories, abide by a common formula for allocating the taxable income of corporations or businesses operating in more than one jurisdiction across provinces, a matter of great dispute in some other federal countries.

These principles suggest two questions concerning the current Tax Collection Agreements. First, do they provide an economical and convenient way of collecting tax revenues? That is to ask, do they minimize cost of administration and of taxpayer compliance? Secondly, do they provide the best possible trade-off between the wish to accommodate governmental autonomy and the need for fiscal harmonization?

There is little evidence to indicate how efficient the current Canadian arrangements are compared with those of a less centralized system. The Ontario Economic Council, however, attempted to estimate the costs to that province of establishing a separate personal income tax. It concluded that they would be "sizeable".[6] This suggests that co-ordinated administration and collection are valuable, and that a loss generated by the establishment of nine more agencies would be unfortunate.

The desirability of harmonization is a more powerful motive for tax collection agreements. The ideal federal tax system has been described as one in which:

> *One obtains the benefits of centralization in the form of tax harmonization and low collection costs while at the same time accommodating the desires of the provinces to pursue their own tax policies and structures in accordance with the desires of their limited constituencies in a manner which does not unduly fragment the economic union.*[7]

How well do the Tax Collection Agreements fare by this criterion?

The arrangements have served us well up to now. Canada has one of the most harmonized tax systems of any federation, notwithstanding its apparently decentralized features. Even non-signatories, for example, abide by the allocation formula for corporate tax. Yet the system still allows considerable regional diversity and offers much flexibility for provinces to decide how to raise their revenues.

The problem, however, is that this high degree of harmony and co-ordination shows signs of breaking down. Alberta has recently withdrawn from the corporate income tax agreements and established its own system. British Columbia has threatened to follow suit. Two provinces, Ontario and Alberta, have recently considered publicly withdrawing from the personal income-tax arrangements unless certain changes are introduced. In 1979, Quebec initiated a Stock Savings Plan which allowed a resident of that province to deduct up to $15 000 from provincial taxable income corresponding to purchases of new shares of Quebec companies. British Columbia recently introduced a Housing and Employment Bond Tax Credit which Ottawa has agreed to administer, and which will "erect barriers to interprovincial flows of enterprises and capital".[8]

A process which once was flexible enough to balance the need to accommodate regional diversity with the economic benefits of a nationally consistent tax environment has recently fallen somewhat short of meeting the challenge. In part, this is because the demands on it have increased significantly. Provinces now pursue a broader range of objectives in their economic and social policies, and are therefore much more insistent on indicating what tax policies they need.

When provincial and federal income-tax systems interlock, to change the federal revenue system can raise serious problems, for changes which increase or decrease taxable income necessarily affect the level of provincial revenues. For this reason, provinces have called for full consultation before such changes are made and have frequently criticized perceived federal failures to act on their request. Well-known examples of unilateral federal moves are the

introduction of indexing of personal income tax in 1974 and the significant structural changes of the federal budget of November 1981. (It was the latter move which prompted Ontario to consider the feasibility of withdrawing from the Tax Collection Agreements.) The tradition and practice of budget secrecy exacerbates the difficulty, since it effectively precludes advance consultations with, or advice to, provincial governments. The same is true with respect to federal understanding of proposed provincial budget initiatives.

There are two views about what should be done in the matter of the Tax Collection Agreements. One view holds that these arrangements should not be changed. Provinces have remained party to the Agreements to this point because they derive considerable benefit from them; a mass defection would be highly unlikely. Even if the process of fragmentation were to continue, however, it might not pose a serious problem. Canada's tax system is highly co-ordinated now, not because of the good will of politicians and public servants, but because the provinces, as small open economies, have little freedom to deviate from the practices of others without suffering economically. As locally sovereign jurisdictions, they are entitled to choose to do so anyway: poor decisions will be reflected in the results of the next election; good ones will be picked up and implemented by other provinces and eventually accepted by the federal government.

The alternative view does not deny the rationality of economic and political actors, but recognizes that some situations can lead them to behave in mutually destructive ways. Indeed, chains of action and reaction can leave everyone worse off than before. Rules which are commonly agreed to and clearly stated at the outset can do much, however, to prevent this type of mutually destructive behaviour.

Commissioners base a number of conclusions and recommendations on this analysis. The Tax Collection Agreements have served Canada well. They provide a considerable convenience to both citizens and governments. As a powerful inducement to maintain tax harmonization, they also strengthen the economic union. Therefore, they should be retained.

Nevertheless, the agreements are presently under considerable strain. The prominent role of provincial taxes in Canada's public finances, the often acrimonious nature of federal-provincial fiscal negotiations, and the tendency of provincial tax structures to diverge are all points that raise important issues. Canadians wish to maintain the agreements, but without diminishing either the accountability of legislatures or the flexibility of the system.

Provinces have two important concerns with the existing arrangements. First, the federal government is not required to notify provinces in advance of federal changes in the tax base or rate structure, although such changes will inevitably affect provincial revenues. However, the agreements provide a one-year revenue guarantee: where a federal change reduces provincial receipts by more than 1 per cent, provinces are compensated for the loss for one tax year, to give them time to adjust their rates in light of the change.

Unilateral federal changes are a greater problem for the personal income tax than for the corporate income tax, because of differences in the way the agreements are implemented. In the corporate case, provincial tax rates are applied to the federal tax base; this means that federal rate changes do not

affect provincial revenues; only changes in the base do so. In the matter of the personal income tax, provincial rates are applied after the federal rate has been set. This Commission recommends that the agreements be amended to place the personal income tax on the same footing as the corporate tax: that is, to apply the provincial rates to the common, federally-determined base. This measure would both reduce provincial vulnerability to federal tax changes and increase provincial autonomy, since provinces would be freer to make their own decisions about how progressive their tax structures should be. Earlier tax-collection agreements ensured uniformly progressive tax structures across the country; however, the permission given to provinces to include various tax-credit and -exemption programs in their tax administration has already modified this uniformity.

A second potential irritant is that while provinces and the federal government share the revenue base and have equal constitutional authority for taxation, it is the federal government which determines the tax base for provinces within the agreements. Some analysts argue that the tax bases should be determined jointly through negotiations among the participating governments and altered only by common consent.

This Commission does not recommend such a course. To require intergovernmental agreement on all changes to the tax base would unduly hamper flexibility and would reduce the federal government's accountability to Parliament for its financial activities. Under the present system, a province can opt out of the Tax Collection Agreements if it finds federal actions intolerable; the threat that it might do so is a reasonable guarantee of federal sensitivity to provincial interests. Moreover, under the agreements, provinces are permitted to request a variety of tax credits and exemptions which allow them considerable flexibility. The federal government will agree to administer such provincial programs if they meet three conditions: they must be administratively feasible; they must apply to income actually earned in the province involved; and they must not interfere, or have the potential to interfere, with the economic union. The great majority of provincial requests have been accepted, though some, such as British Columbia's proposals for a dividend tax credit for firms in the province, have been refused. Again, the incentives seem roughly right in this case: a province committed to a program can opt out of the agreements to implement it; the federal desire to avoid that occurrence should make it sympathetic to provincial proposals.

Although there is no need for fundamental change, two additional proposals would help to improve co-ordination of tax systems. First, as part of our larger concern to reduce the comprehensive budget secrecy Canadians have experienced and to ensure wide discussion of budget proposals in Parliament and provincial legislatures, Commissioners recommend that in developing any tax change which would significantly affect the federal-provincial relationship, the federal government consult with provinces in advance. Secondly, while we endorse the quinquennial review of federal-provincial fiscal arrangements, we suggest that the Council of Ministers of Finance should extend this consultation process to include a regular and broad review of current practices. To assist the Council, we recommend that a federal-provincial Tax Structure Committee of officials be formed to assess

definitions of taxable income, basic exemptions, marginal tax rates and related issues, and to monitor the division of tax room between the two orders of government in light of anticipated revenue and expenditure needs.

Commissioners emphasize that these proposals are meant to "fine-tune" a process which already works reasonably well. Co-ordination of fiscal arrangements and harmonization of the tax-collection system represent two of the achievements of our federal system.

Intergovernmental Transfers

As governments have extended their activities in the post-Second World War period, all federal systems have made increasing use of intergovernmental transfer arrangements. These arrangements permit one order of government to share in the funding of programs of another order by transferring funds or tax-collection authority. In Canada, the federal government transfers money and tax "room" to the provinces, and provincial governments transfer cash to municipal authorities and hospital boards.

In Canada, these transfers are massive. In 1983–84, the federal government transferred a total of $17.6 billion in cash payments to the provinces. Of this amount, about $5.5 billion took the form of "general purpose" or "unconditional" grants, mainly equalization payments. The remainder took the form of payments linked to specific programs. A total of $7.6 billion formed the cash portion of transfers under the Established Programs Financing arrangements, covering federal aid to health care and post-secondary education. Another $4.6 billion related to other shared programs. By far the most important of these is the Canada Assistance Plan, which received $3.1 billion. In addition, the Established Programs Financing arrangement, originally enacted in 1977, has divided the federal contribution to these programs into a cash portion and a transfer of equalized tax points. In 1983–84, the latter had the value of another $6.6 billion. The dollar value of all these transfers tripled between 1974 and 1984.[9]

The size of these figures suggests that management of intergovernmental transfers is a major issue for the federal system. Two sets of questions have loomed large in recent years and promise to pose difficulties for the future. The first set relates to whether there should be limits on the power of the federal government to spend funds in areas under provincial jurisdiction: To what extent should the federal government be able to use its spending power to project the national interest into areas not under direct federal authority?

The second set of questions arises from the serious strains created as governments struggle to restrain expenditure growth in order to reduce the size of public sector deficits: How will efforts to restrain spending at one level spill over to affect the programs of the other? Will cut-backs effected by one order of government increase the demand for services at the other? Alternatively, will they reduce the financial capacity of the other to pay for them? More specifically, should federal transfers to the provinces be protected or privileged in any way, given the high degree of provincial dependence on them?

While such concerns are never far from the surface in any federal country, both became particularly prominent in Canada after 1980. They were reflected, first, in the debates on federal-provincial fiscal arrangements and Established Programs Financing in 1982–83; later, they surfaced in the debate about health-care policy surrounding passage of the Canada Health Act in 1983.

Background

Intergovernmental transfers have been a key instrument in allowing the Canadian federal system to adapt to the new roles of government. While many of the new responsibilities of government clearly lay within areas of provincial jurisdiction, they were often beyond the financial means of provincial governments. Publicly financed health-insurance or greatly expanded post-secondary education systems, for example, were simply too costly for most provincial governments to support on their own. Moreover, in post-secondary education, where the mobility of graduates meant that spending by one province would spill over to benefit others, individual provincial governments, acting quite properly in their own interests, would provide a less extensive service than would be desirable from a national perspective. Federal assistance was required, therefore, to meet total national needs. Given the obstacles and objections to the constitutional transfer of all these responsibilities to the federal government and the broader desire to retain the advantages of federalism, a solution was found in the shared-cost program under which that government would pay part of the costs of meeting new needs. This program became the hallmark of post-war co-operative federalism, not only in social policy, but also in a wide range of economic development programs, such as construction of the Trans-Canada Highway. Today there are shared cost agreements, large and small, bilateral and multilateral, in almost every program category, and in virtually all government departments.

A wide variety of particular arrangements is possible under the shared-cost program. In general, these may be divided into two broad types: cost-matching arrangements and block-funding arrangements. In cost-matching arrangements, the federal government agrees to reimburse provincial treasuries for some fixed proportion (usually one-half) of provincial expenditures on programs covered by the agreements. The clearest current example is the Canada Assistance Plan, through which the federal government reimburses provincial governments 50 per cent of the costs of social assistance and social service programs, provided that the support goes to people "in need or likely to become in need". The post-secondary-education/financing arrangements in force from 1967 to 1977 comprised a slight variant under which the federal government transferred 50 per cent of institutional operating costs.

In block-funding arrangements, the federal transfer is less directly related to specific program costs and, instead, takes the form of an equal dollar-per capita transfer multiplied by the provincial population. The pre-1977

Medicare grant, for example, was based on the national average per capita costs of medical insurance programs in each year.

The major current block-funding arrangement is Established Programs Financing (EPF). Under that arrangement, transfers from the federal government to provinces are calculated in the following way. First, the per capita operating costs of health insurance and post-secondary education are established for 1975–76, the base year. Then one-half of this amount is compounded each year by an amount equal to the three-year moving average of nominal gross national product (GNP) increases. Finally, the result of these calculations is multiplied by the provincial population in the year for which payment is to be made. The subsequent transfer is made in the forms of cash and tax room. It is apparent, then, that block-funding transfers are not totally unrelated to program expenditures. EPF funding is related to 1975–76 program costs. However, the relationship deteriorates over time. There are also mixed transfer mechanisms: for example, the Hospital Insurance and Diagnostic Services transfers of 1957 to 1977 were based on 25 per cent of actual provincial expenditures and 25 per cent of national average per capita costs.

Cost-sharing arrangements may be more or less strongly conditional. In highly conditional programs, the federal government defines quite specifically the terms and conditions which provincial governments must meet in delivering programs if they are to qualify for the federal grant. Under less conditional arrangements, the provincial government receives funds almost regardless of the nature of its programs. The current funding arrangements for post-secondary education are highly unconditional: provinces receive transfers regardless of the support which they, in turn, provide for post-secondary education. By contrast, the current funding arrangements for health insurance under EPF and the Canada Health Act are highly conditional: provinces must deliver health-insurance programs which meet clearly defined criteria, and they are subject to clearly identified financial sanctions if they fail to do so.

Finally, as we have already mentioned, transfer arrangements may provide for the transfer to be in the form of either cash or tax-collection "room" which the federal government vacates in favour of provincial treasuries. The EPF arrangement, for example, provided for the federal government to withdraw from 13.5 percentage points of personal income tax and from 1.0 percentage point of corporate income tax, and allowed provinces to "occupy" that tax room and collect the revenues; this vacated tax room was intended to make up one-half of the total federal EPF transfer. Where funding is provided through tax transfers, federal control of provincial programs declines: tax points, unlike cash, cannot be cut or withdrawn; and provinces see tax points not as labelled for, or targeted to, specific programs, but rather as part of their general revenues. Responding to federal concerns that cash and tax transfers for post-secondary education were being diverted to other uses, provincial treasurers tended to reply that under EPF, there was no longer a direct link between the transfer and specific purposes; in their view, the transfer could be spent for any provincial purpose. While the federal

government considered the transfers to be "incentive grants", designed to influence provincial priorities, provinces tended to treat them as unconditional.

Taken together, all these elements of intergovernmental transfer arrangements make for a bewildering picture. However, the complexity provides at least one great service to Canadian governments: it makes the arrangements potentially very flexible. For example, if we Canadians wish to decentralize our fiscal system further and to provide more power and authority to provinces, we shall tend to choose arrangements which are block-funded, and which have few conditions and a significant tax-point transfer. On the other hand, clearly defined conditions can be imposed, among other purposes, to create a somewhat higher degree of centralization and national standards.

The federal and provincial governments have debated the character of transfer arrangements with the introduction of each major shared-cost program. In the 1950s and early 1960s, with the important exception of Quebec, there seemed to be broad consensus that these programs were an appropriate means to achieve desirable national standards, and to ensure that the full range of modern government services was available to all Canadians. Provinces themselves often called for greater federal financial involvement in the rapidly growing areas which were under provincial jurisdiction.

By the 1960s, consensus began to erode. Quebec governments had rejected shared programs even before the 1960s, on the grounds that they represented an unconstitutional use of federal spending power to invade provincial jurisdiction and to impose "national" values on a distinct Quebec society. This essentially negative reaction to federal programs was reinforced after 1960 as successive Quebec governments embraced the Quebec state and sought to use it to expand their own programs and to develop that province's society. The call, therefore, was not simply for federal restraint, but for increased provincial fiscal ability to pursue provincial priorities. One result was the Established Programs (Interim Arrangements) Act of 1964, which allowed any province to "opt out" of a large number of shared programs and to receive, through a combination of tax points and "topping-up" payments, funds equivalent to the funds that the federal government would have spent on the program if the province had chosen to participate.

Only Quebec took advantage of the arrangements to opt out, but as the welfare state matured, other provinces, growing more confident in their ability to manage their own affairs, increasingly resisted new federal initiatives. They also became more critical of federal "intrusions", arguing that they skewed provincial priorities, subjected provincial fiscal planning to the vagaries of federal decisions, and reduced provincial government flexibility, leading their legislatures to favour program areas where federal funding existed and to neglect those areas where it did not.

Further strains had developed by the 1970s. First, the federal government was concerned that Quebec's opting out and acceptance of tax points conferred a *de facto* special status; it therefore sought ways to restore the balance among provinces. Secondly, the federal government became more concerned about its ability to control its own expenditures; federal commit-

ment to supporting 50 per cent of program costs implied that the provinces' decisions determined a large part of federal spending. Moreover, the federal government worried that shared-cost programs generated few incentives to restrain spending: the arrangements implied that provinces could count on "fifty-cent dollars" for new expenditures; by the same token, if they did restrain spending, provincial treasuries retained only half of any savings.

All these forces pushed the federal government towards less centralized fiscal arrangements and underlay passage of the Established Programs Financing Act in 1977. The details of the arrangements were complex, but the principles were reasonably clear. Decentralization would be achieved by block-funding, by tax-point transfers and, for post-secondary education, by elimination of any direct link between either program expenditures or the terms and conditions under which programs were delivered. Overall costs would also be reduced by severing the links between payments and actual program costs; henceforth payments would be tied to increases in GNP, which, at the time, was rising more slowly than program expenditures. Federal contributions would be controlled and provincial incentives to restrain expenditure growth increased. Moreover, since the payments would be recast into a combination of cash and a transfer of tax points, all provinces would be brought more closely into line with Quebec.

The arrangements represented a major step towards greater provincial autonomy, towards "disentanglement" of federal and provincial responsibilities, and towards restraint. Once again, the flexibility of intergovernmental transfer arrangements had been demonstrated. However, the arrangements did not go the whole way to decentralization: the conditions attached to hospital insurance and Medicare remained unchanged; and provinces agreed to consult the federal government with respect to spending on post-secondary education.

By 1982, the situation had changed. First, rapid inflation in nominal GNP caused federal transfers to increase even faster than they would have done if they had remained tied to actual spending. Then, because of a guarantee built into the EPF formula (that the value of the tax points transferred to the provinces would always at least equal the value of the cash portion of the grant), as the recession hit, and as the yield of the transferred tax points declined, the proportion of federal transfers in the form of cash payments increased. Moreover, since transfers were no longer tied to program spending, the federal government believed that it had lost what little control it had once exercised over program content and standards. In a sense, the provinces had done with a vengeance just what EPF had invited them to do: they had restrained their expenditures in both health care and post-secondary education. In the health field, many provinces were experimenting with "user fees" and "extra billing" to limit the costs of health programs to provincial treasuries and thus reduce provincial, but not federal, spending. This led to federal concern that provinces were diverting funds to other purposes, with the result that, in post-secondary education especially, the federal share of total costs was rapidly increasing. Moreover, public opposition to perceived cut-backs and, particularly, to extra billing and user fees in health services translated into calls for federal action. Finally, in the wake of the Quebec

referendum and the constitutional debate, the federal government had become increasingly concerned about fiscal decentralization and the erosion of federal power. It believed that it had made too many concessions to the provinces, reducing its ability to affect vitally important programs, to account to Parliament for its expenditures, and to maintain direct links with citizens.

The federal government considered that the time had come to redress the balance; in 1982, it sought to regain some control over total expenditures and to restore a degree of influence for its programs. It capped, or established an upper limit on, transfers for post-secondary education and announced its intention to seek negotiations aimed at developing national standards and a defined federal role in that field. It also proceeded to develop the Canada Health Act. Its aim was to define clearly the original program conditions: universality, portability, accessibility, comprehensive coverage and public administration. In addition, it undertook to eliminate extra billing and user fees by applying dollar-for-dollar reductions in the federal transfers to provinces which used these devices. No federal-provincial agreement was reached on any of these issues, but since these were federal spending programs, the federal government was able to proceed on its own.

The intergovernmental debate focused on the complicated details of alternative formulae for transfer arrangements. The debate raised a larger question, however, about which alternative, in 1982, Canada should pursue. On the one hand, we could move farther along the path indicated by the EPF in 1977, and continue to decentralize transfer arrangements by making the transfers totally in terms of equalized tax points, by extending them to the Canada Assistance Plan, and by eliminating the conditions in the original Medicare and hospital-insurance programs. On the other hand, we could move back from the 1977 arrangements and return to more conditional funding arrangements by requiring provinces to be more accountable to the federal government for their use of federal transfers, and by developing a more direct policy-design role for the federal government. EPF might well have responded to the political requirements of the time, but it falls squarely between these two alternatives. And this, argues one observer, accounts for the instability of the arrangements. His conclusion with respect to post-secondary education applies to other areas as well:

> *The Government of Canada must decide whether it means the PSE [post-secondary education] fiscal transfers to be program-related or not. If it believes they* should *be, then the scale, and/or the rate of growth, of the federal payments (transfers) must be related to some measure of the scale, or [to] the rate of growth, of expenditures in the provinces on or for PSE . . . If, on the other hand, the Government of Canada means simply to make an unconditional per capita grant to the provinces . . . then all reference to post-secondary education should be removed from the Act. It is as simple as that.*[10]

The issues raised by EPF and by the Canada Health Act extend to larger questions about the federal spending power and its place in Canadian public policy.

The Federal Spending Power

Most shared-cost programs, as well as many programs (such as family allowances) which make payments to individuals, represent exercise of the federal spending power. The spending power is usually regarded as one of a number of general discretionary federal powers. Unlike the declaratory and disallowance powers, however, the federal spending power is nowhere explicitly defined. Rather, it is held to derive from more general principles. In part, it derives from the power of Crown prerogative, for all public revenues belong to the Crown, which is "a person capable of making gifts or contracts like any other person, to anyone it chooses to benefit." The Constitution requires that the Crown have the approval of Parliament or legislature; when this approval is obtained, the government may distribute revenues as it sees fit. This view implies that the donor of public revenues has the power to attach conditions to the grant, and the recipient has the power to refuse it.

The spending power has also been justified in the Constitution Act, 1867, under section 91(1A), "The Public Debt and Property", and under section 102, which authorizes a Consolidated Revenue Fund. Together these sections are said to confer on the federal government the right to spend for any purpose "provided the legislation does not amount to a regulatory scheme falling within provincial powers."[11]

Remarkably little constitutional assessment of the spending power has been attempted in the courts. Federal-provincial/shared-cost agreements have not been the subject of extensive legal challenges, and it does not appear that there are constitutional restrictions on the federal power to offer conditional grants to the provinces. The provinces are ultimately protected by their power to refuse to participate in these agreements; in political terms, however, this power may be more theoretical than real. The remaining constitutional uncertainty lies in grants awarded by the federal government to individuals and institutions, especially when such grants might be interpreted to constitute regulation within an area of provincial jurisdiction. Again, in this instance, the limited jurisprudence provides little guidance.

The question of limiting the federal spending power lies primarily in the political realm. This Commission believes there are a number of considerations which must be brought to bear. First, the federal government, in the name of national citizenship and the national political community, has the right and responsibility to respond to emergent needs and to changing conceptions of the national interest. The record of the past emphasizes the fact that the national interest is not static: rather it changes in response to changing international circumstances, changing issues, changing conceptions of citizenship, and changing aspirations. Matters once considered of purely local interest can, and do, become defined as national questions which demand national responses. There will often be emerging issues where provincial activity, even within provincial jurisdictions, is not a matter of indifference to the federal government. Where the federal government does not possess the constitutional authority, and where provinces are unable or unwilling to respond effectively to new needs, there is in the future, as there was in the past, a case to be made for wide federal freedom to put forward proposals for shared-cost programs.

The values of federalism, however, suggest that this ability should not be entirely unconstrained. The spending power introduces a necessary degree of flexibility into the federal system, but taken to its extreme, it can undermine the system by eroding the distinctions between federal and provincial responsibilities. On a more practical plane, federally imposed conditions in shared-cost programs – especially those which change frequently and without consultation with provincial governments – can hinder provincial attempts to plan and rationalize their activities and can admit possibly arbitrary and disruptive federal interventions into provincial administrative systems. To assess the federal spending power, we must therefore balance, on the one hand, the national interest and the associated concept of changing national objectives or values and, on the other hand, the preservation of the diversity of federalism and the administrative integrity of provincial systems.

Three other criteria must also be considered. Accountability must be a central aspect of our institutional reforms. One view of accountability argues strongly against the use of the spending power to promote shared-cost programs, for such programs can undermine the accountability of both orders of government. Provinces spend money which they are not responsible for having raised. The federal government transfers money to the provinces, but has little control over the manner of its spending. Citizens cannot hold the federal government accountable because they receive the services through the provincial government rather than directly. And Parliament cannot hold the federal government responsible because the federal government cannot specify precisely how the funds have been used. Under the Established Programs Financing arrangements, the severance of transfers from program costs and the lack of either effective program standards or enforcement mechanisms has accentuated this problem.

The principles of accountability push in the direction of disengagement. In principle, disengagement could be achieved either by transferring full responsibility for programs to the federal government or by transferring the full revenues required to the provinces. For health and education programs, the former strategy is not a real possibility in the Canadian federal system, although it might work for other, less contentious programs. The latter strategy would severely constrain the capacity of the federal government to act in the national interest on behalf of all Canadians. The development of clear conditions both for program delivery and for accounting provides an alternative approach to the accountability problem: with an appropriate legislative base, Parliament could hold the federal Cabinet responsible for its spending if the Cabinet, in turn, were able to hold the provinces accountable for their expenditure of the federal funds transferred to them.

Flexibility is another criterion which cuts two ways. In a larger historical sense, the spending power and shared-cost programs have made an essential element of flexibility available to the federal system. In a narrower sense, however, federally imposed conditions can reduce the flexibility of provinces in the operation of the programs. A classic example is the hospital-insurance program, where the focus on acute-care facilities inhibits experimentation with preventive medicine and chronic-care and after-care facilities. Some observers vigorously argue that the recent Canada Health Act, with its more

stringent federal sanctions against user fees and extra billing, its restatement and redefinition of the original program conditions, and its "suggestion" of how provinces might negotiate with physicians over fee schedules, has significantly reduced the capacity of provinces to experiment with more efficient delivery systems.

A final criterion is the desire to minimize administrative and decision-making costs. This consideration, too, argues for disentanglement. The more detailed the conditions of shared-cost programs, the more extensive are the bureaucratic resources that must be devoted to negotiation, monitoring and reporting, and the more room there is for bureaucratic wrangling. These considerations led the Royal Commission on Dominion-Provincial Relations (the Rowell-Sirois Commission) to warn against the "difficulties of divided jurisdiction" and to advocate retention, as far as possible, of the principle of "watertight" jurisdictional compartments. Hence it recommended that where federal initiative was essential, there should be a transfer of jurisdiction: shared-cost programs should be a last resort.

How can we balance these criteria and come to some conclusions about the appropriate uses of the federal spending power? Over the past two decades, advocates of change have made many proposals to clarify that power. There has been widespread agreement, even by federal governments, that the spending power should be subject to some constraints or limitations. Several possibilities have been examined.

One possibility is to abolish the spending power in areas of provincial jurisdiction. This proposal has received little support, for in the name of federalist purity, it would impose far too much rigidity. Indeed, since one impetus for many of the shared-cost programs was the desire of provinces for financial help in rapidly growing areas, it would likely be as unacceptable to many provincial governments as to the federal government. Commissioners therefore reject this option out of hand.

A second option would be to subject the federal spending power in areas of provincial jurisdiction to some form of consent mechanism. This is perhaps the most widely-canvassed approach: various mechanisms have been proposed by provincial governments, by the Quebec Liberal Party, by authors of the Pépin-Robarts Report, and by the Canadian Bar Association, among others. These groups would have used the device of a reformed Senate, made up of direct provincial delegates, to reach provincial consensus. Consent could also be registered by a First Ministers' Conference, or, as in our constitutional amending formula, by the supporting votes of an appropriate number of provincial legislatures.

In 1969, the federal government proposed that the federal spending power be explicitly laid down in the Constitution, that its power to make unconditional grants be unrestricted, and that conditional grants in relation to federal-provincial programs which are acknowledged to be within provincial jurisdiction require "broad national consensus" before Parliament exercises its power. The consensus would be determined jointly by Parliament and the provincial legislatures.[12] In later constitutional discussions that took place between 1979 and 1981, the federal government also expressed its willingness to embrace a substantial provincial consent mechanism.

Such proposals provide a strong guarantee of the federal principle: they provide a very strong incentive for the federal government to look first to its own jurisdiction and to consult before proceeding, in order to maximize its chances of winning the requisite provincial support. They also ensure the fullest possible debate: the federal government would be required to mobilize public support for its proposals, and provinces would have to justify any opposition before their own legislatures and electorates. It is probable that most of the major programs now in existence would still have been developed under such a scheme; the greater bargaining power this method gives to provinces, however, suggests that their legislatures might have been able to use the need for consent to win more favourable terms from the federal government or to gain leverage in other policy domains. Commissioners are not inclined to favour consent mechanisms which are too rigid, or which unduly hinder the Parliament of Canada from exercising its legitimate rights and performing its responsibilities.

A third option is provincial opting-out, an approach with which we have had considerable experience in the past. The concept is incorporated in the new constitutional amending process. In a sense, the right to opt out of a shared-cost program has always existed; no province is constitutionally obliged to participate. Most opting-out proposals, moreover, significantly reduce the provincial costs entailed by including compensation, or "fiscal equivalence" payments, to the non-participating provinces. Thus, the Canadian Bar Association recommended that any province should be able to opt out of a program and receive compensation equivalent to the amount of money it would have received from the federal government, provided that the province agreed to provisions respecting interprovincial portability. The 1969 federal proposal also included fiscal compensation, but in the form of grants to citizens, rather than to provincial governments.

Serious objections have been raised against opting-out. There is the fear of a chequer-board Canada, for of what validity are "national standards" if they exist in some provinces but not in others? Would federal MPs be permitted to vote on programs which do not operate in their home provinces? Why should federal revenues be turned over to provincial governments that are unwilling to participate in national programs which have broad public support and are constitutional? In spite of all these contrary arguments, however, opting-out has been defended on the grounds that it introduces a high degree of flexibility into the federal system. In particular, it allows a response to the distinctiveness of Quebec, while avoiding a situation in which Quebec might be able to block a program which is considered highly desirable in other parts of the country.

The spending power has been a vital instrument of flexibility and of response to changing definitions of the national interest. Commissioners believe it should be retained, subject to a number of guidelines. First, while we believe that this power is and should be a broad one, we are also convinced that it is not unlimited. We consider the judicial distinction between the federal legislation which makes grants or gifts and that which involves direct regulation in the fields of provincial jurisdiction, though it is not fully developed, to be the appropriate one. We believe, for example, that federal

loans, tax credits or grants to post-secondary students would be constitutionally justified, but that if they were to be used to require universities to establish entrance conditions, they could be challenged as an invasion of provincial jurisdiction. We hold the opinion that it is appropriate for the Supreme Court to spell out the constitutional limits more fully as it considers future cases.

Secondly, following the Rowell-Sirois Report, we believe that in principle, the federal government should look to a shared-cost program as a last resort, rather than as a first resort. Indeed, in many cases, it will be desirable to seek to mesh federal and provincial activities under a shared-cost program. In general, however, the democratic objectives of accountability and clarity of roles are more effectively secured if a government pursues programs under its own jurisdiction.

Thirdly, use of the spending power in an area of provincial jurisdiction requires broad national consensus. A reformed Senate with stronger regional representation would provide one device to secure this end. However, since such a Senate would represent individuals, and not governments, and since it is governments which are involved in the development and administration of shared-cost programs, even a reformed Senate would not provide a sufficient solution. Provincial governments must be directly and fully consulted.

Federal-Provincial Ministerial Councils should provide an effective vehicle for consultation. Commissioners would go beyond this proposal, however, and require the Prime Minister to make every effort to obtain broad consensus of First Ministers in advance of federal legislative action. Under present arrangements, consultation almost always occurs over new programs, since it is essential to their success that provinces agree to participate. Consultation is even more necessary, however, when the federal government proposes either to alter the terms and conditions of a program or to terminate it; since provinces are already participating, it is difficult for them to respond to such changes by leaving the program. We therefore believe that there should be considerable advance notice and opportunity for debate before conditions are changed or programs are terminated. It could be standard practice, for example, to design shared-cost programs so that they operate for five-year periods, as has been done with fiscal arrangements. At the end of each five-year period, the program would be renegotiated, but neither order of government would be able to alter the conditions unilaterally within the period.

Finally, we believe that flexibility and opportunities to innovate will be enhanced to the extent that the conditions of shared-cost programs are stated in terms of goals or ends, and the federal government does not dictate specific administrative means, but leaves their determination to provincial experience and initiative.

Federalism and Fiscal Restraint

A potential source of significant tension in federal-provincial fiscal relations in the present context concerns the cutting and trimming of programs for financial reasons. Again, the problem flows from interdependence and from

the likelihood that in the foreseeable future, all governments will be anxious to restrain expenditure and to manage their finances. The efforts of one order of government to do so will inevitably affect the budgetary situations of the others.

This development can come about in several ways, even when there are no fiscal transfers involved, and when each level of government is operating in its own jurisdiction. For example, a federal tightening of unemployment-insurance provisions might generate increased demand for provincial welfare services. In turn, provinces might try to reduce their welfare burden by instituting short-term/work programs which would last just long enough for the participants to qualify for Unemployment Insurance. More generally, one government's reductions in almost any area would be likely to generate political pressures on another order to step in to fill the gap. Commissioners make no recommendations here; the problem simply calls for sensitivity.

Of more direct interest are intergovernmental transfers. As fiscal conditions have become more volatile in recent years, numerous government actions have been taken which affect the level of transfers: these include a rapid series of changes in equalization as the system tried to respond to escalating oil and gas revenues in the 1970s; the capping of the escalators for post-secondary education and health-insurance transfers in the mid-1970s; or the more recent capping of post-secondary education transfers under the "Six-and-Five" anti-inflation program.

The question which arises is whether such transfers should be in some way insulated or protected from these kinds of budgetary changes. One perspective suggests that indeed they should be. This argument is based on the need for fairness and certainty, as well as on recognition of the high degree of provincial dependence on intergovernmental grants. Provinces, it is claimed, have been induced to participate in these programs on the understanding that the federal government would continue their support. They cannot effectively plan their own budgets if the amount of transfers remains uncertain. A particularly strong argument is sometimes made that equalization payments should be shielded from federal measures to control deficits, especially in light of the constitutional commitment to sharing now found in section 36 of the Constitution Act, 1982.

Those who view the situation from the contrary perspective ask: Why should the programs which happen to be delivered through intergovernmental mechanisms be privileged in any way over other kinds of federal expenditure? True, we justify these programs by reference to national objectives and national standards, but programs fully in federal jurisdiction presumably have similar justifications. True, budgetary uncertainty makes planning difficult, but tax revenues are also inherently uncertain; indeed, coping with uncertainty is part of the problem of governing. While the federal government may have induced provincial governments to enter particular program areas by offering cost-sharing arrangements, provincial governments have often initiated the requests for federal sharing. Moreover, if intergovernmental programs are protected, then any federal restraint measures will have to be concentrated disproportionately on a limited range of unprotected programs. Thus, in 1984, with about one-fifth of federal spending taking the form of

intergovernmental transfers and another fifth covering interest on the national debt, federal restraint measures would have to be concentrated on relatively few areas of discretionary spending. If transfers to individuals are also to be considered protected, then almost 70 per cent of federal spending would be locked in, and federal flexibility would be greatly reduced.

An interesting sidelight on these intergovernmental transactions is that it has fallen to the federal government to assume responsibility for most of Canada's public sector deficit. Without the tranfers, the federal deficit would be much smaller and the provincial deficits much larger. Thus, in 1982, the federal deficit, excluding intergovernmental grants, stood at $4.7 billion, but after the grants were included, it rose to $20.5 billion. The same thing happened at the provincial-municipal level. Before transfers were counted, provinces had a surplus of $7.4 billion; after grants to local authorities and hospitals were included, the provinces were in deficit by $1.6 billion. Local governments and hospitals are the massive recipients of transfers: collectively, they were in deficit by $25 billion in 1982, based on their own revenues; after transfers from other governments, they were roughly in balance.

In light of these considerations, how might Canada retain a desirable degree of federal flexibility and accountability to Parliament, while assuring provinces of some stability for their planning, and while protecting them against rapid unexpected variations in federal spending? The simplest option would be to require the federal government to give the provinces advance warning of proposals to cut federal transfers. One year's notice before the implementation of cuts, for example, would give provinces some time to adjust their revenues and expenditures to planned changes. This scheme, however, would provide only limited protection for provinces.

A second possibility is to review federal-provincial/transfer arrangements every five years and to limit the changes that the federal government can make, between reviews, without provincial approval. Such an arrangement could, for example, allow the federal government to adjust payments in any given year by up to 5 per cent; any greater changes would require provincial consent. An appropriate formula would have to be worked out. Alternatively, the federal changes in intergovernmental transfer programs could be linked to the average level of reductions in non-transfer programs.

A number of other proposals governing the application of federal restraint have also been made. For example, social programs could be insulated from any reductions. However, since these programs represent well over 80 per cent of all intergovernmental transfers, to exempt them would severely constrain the federal government. Another possibility is to vary the amount of reductions to take account of differences in provincial levels of need; we Commissioners discuss the difficulties of such a procedure in our analysis of equalization. Finally, provinces with higher revenues could bear the brunt of reductions, and poorer provinces could be protected. We believe, however, that the equalization program, and not individual shared-cost programs, is the appropriate mechanism for dealing with revenue disparities.

Again, to achieve balance is fundamental: the federal government must have enough fiscal flexibility to control its own budget, but it should not be able to cut with impunity transfers for shared-cost programs. We believe that

to give one year's notice of changes in these programs provides inadequate protection for the provinces. Rather, we consider it best to specify in advance the limits on permissible reductions. Furthermore, apart from conditions spelled out in the enabling legislation, the federal government should leave the provinces full freedom to decide for themselves how best to adjust their own programs and administrative systems to any reductions.

Finally, Commissioners believe that the managing of restraint is likely to cause major strains in the federation in the coming years. The temptation for each order of government to pass off its fiscal problems to the other will be acute, and the political pressure on the federal government to react to provincial measures will grow. To deal with such inevitable tensions will require a high degree of common trust, open exchange of information, and resilient institutions.

Notes

1. Calculated from Statistics Canada; *Historical Statistical Compendium*, prepared for the Royal Commission on the Economic Union and Development Prospects for Canada (Ottawa: Statistics Canada, 1985), Tables 5.1, 5.2, 5.3, 5.4.
2. *Ibid.*, Tables 5.4, 5.5.
3. Canadian Tax Foundation, *The National Finances 1983–84* (Toronto: The Foundation, 1984), Table 16.2.
4. Canada, Finance Canada, *Economic Review, April 1984* (Ottawa: Minister of Supply and Services Canada, 1984), Table 54.
5. *Ibid.*, Tables 55 and 56; and Canadian Tax Foundation, *The National Finances 1983–84*, Table 3.6 for hospitals (1982 data).
6. Ontario Economic Council, *A Separate Personal Income Tax for Ontario: An Ontario Economic Council Position Paper* (Toronto: The Council, 1983), p. 130.
7. Robin W. Boadway, "Federal Provincial Transfers in Canada: A Critical Review of the Existing Arrangements", in *Fiscal Federalism*, vol. 65, prepared for the Royal Commission on the Economic Union and Development Prospects for Canada (Toronto: University of Toronto Press, 1985).
8. Thomas J. Courchene, *Economic Management and the Division of Powers*, vol. 67, prepared for the Royal Commission on the Economic Union and Development Prospects for Canada (Toronto: University of Toronto Press, 1985).
9. Canadian Tax Foundation, *The National Finances 1983–84*, Table 16.2.
10. A.W. Johnson, *Giving Greater Point and Purpose to the Federal Financing of Post-Secondary Education and Research in Canada*, a report prepared for the Secretary of State of Canada (Ottawa, 1985), p. 23.
11. Canada, Government of Canada, *Federal-Provincial Grants and the Spending Power of Parliament* (Ottawa, 1969), p. 12.
12. *Ibid.*, pp. 36–42.

Intergovernmental Relations and the Institutions of the Federation

Commissioners have already reviewed the strengths and weaknesses of Canada's national institutions. Here we discuss more comprehensively the institutions of Canadian federalism: the division of powers, the amending formula, and the machinery of intergovernmental relations. Given the difficult policy choices with which we Canadians are confronted, how can we reform these institutions so as to facilitate effective policy making? How can these institutions better reflect the democratic values of openness, accountability and responsiveness that underlie the optimum approach to institutional change? This Commission's terms of reference asked that we respect "the spirit of the Constitution" and "assume a continuing Canadian federal structure not significantly different from its present form." Here we provide some thoughts about that spirit and suggest refinements to that structure, in light of Canada's current needs and values.

One of the most insistent messages which we Commissioners received in our hearings was that relations among federal and provincial governments appeared to be in disarray. There was simply too much conflict, too much bitterness and mistrust. Federal-provincial relations gave the impression of steady confrontations, with reporters and camera crews standing ready to dramatize the conflicts. The capacity of the country to deal with the concrete and pressing issues put forward seemed vitiated in a struggle – of more interest to the governments involved than to the citizens they represented – for position, for status, for "turf". Such conflict troubles Canadians because it diverts attention from the substance of policy and threatens to undermine confidence in our political institutions, perhaps even in the legitimacy of the constitutional order itself.

Canadians were concerned, too, about the actual or potential threats our practice of federalism holds for democratic values. As governments have more and more shared responsibility, it has become harder and harder for Canadians – and indeed for governments themselves – to determine which authorities are responsible for what areas of administration. Intergovernmental relations, a product of shared or overlapping responsibility, disproportionately involved the executive and bureaucratic levels of government. Intergovernmental consultation and agreement have removed important areas of policy from parliamentary control. Preoccupied with the intergovernmental dimension of their responsibilities, policy makers may be less inclined or less able to respond to groups whose concerns are not territorially defined. The intergovernmental process is often secretive, and issues disappear into the intergovernmental maze. As vital issues have been caught up in this process, interest groups have realized that their concerns are at stake. For this reason, they have insisted on broader access to the process, as demonstrated in the constitutional discussions of 1980–82 and in the debates on the Canada Health Act in 1983 and 1984.

The record demands, however, that these criticisms be tempered, for even in the periods of most bitter conflict, effective policy co-ordination was maintained in many areas. Moreover, the personalities of the chief partici-

pants and the weaknesses of the institutions are not the sole sources of conflict. Some features of the relationship do spur conflict: the primary cause has been genuine differences in interests, both regional and intergovernmental, differences which are, in effect, a natural outcome of regional diversity in the federation. In the consequent struggles, governments represented not only their own political interests, but also important visions of Canada and the material interests of their residents. It is unrealistic – indeed undesirable – to expect our institutions and intergovernmental arrangements to eliminate conflict. Nevertheless, we must try to ensure that they will not generate and perpetuate unnecessary conflicts based primarily on concerns for status.

Competition among governments, overlapping of functions, and duplication of services are inherent in federalism; indeed, they are one of its chief advantages. Policy is likely to be more responsive when citizens can turn to another level of authority if they find that the first does not listen to their concerns, and when governments compete for voters' allegiance. When issues are debated in intergovernmental forums, as well as in the legislatures, the full range of policy concerns and options is more likely to be canvassed. Thus, while we Canadians must seek to establish mechanisms that avoid the intensive conflicts of recent years, we must also recognize that federalism, like other elements of Canada's institutional framework, encourages competition and adversarial relationships which are seen as essential methods for enhancing the well-being of Canadians.

Finally, the very concept of accountability becomes complex in the federal context. The basis of accountability must remain the political responsibility of each government to its own residents, in 11 systems of government, rather than one. For our federal system, however, the Constitution provides an additional standard of accountability. Thus each legislature's majority, however large, will be subject to some restraints. The Canadian Charter of Rights and Freedoms limits the autonomy of governments. To the extent that governments make formal agreements, as in shared-cost programs, for instance, they have commitments to one another on the basis of contractual federalism. We should also realize that the problems that federalism poses for responsible government are only part of the challenge that the growth of the state poses for democracy. Thus we Canadians must seek to establish balance in our federal institutions. We must try to find middle ground between unregulated competition and implausible harmony, and between accountability of governments to citizens and collaboration among governments. These considerations suggest that it is important to define more clearly the "spirit of the Constitution".

Federalism and Constitutionalism

Constitutionalism in our federal system derives from several sources. First, there is constitutional law as interpreted by the Supreme Court of Canada. Secondly, there is convention: long-standing evolving principles, such as that of responsible government, and unwritten practices which, by tradition, by repeated precedents, and by the fundamental commitments of leaders, have become an accepted part of our constitutional order. The remedy for

violations of convention lies chiefly in the political process, although the courts may, on occasion, intervene. In the recent Constitutional Reference case, for instance, the Supreme Court of Canada recognized and defined the convention of substantial provincial consent to constitutional amendments as an integral part of our Canadian constitutional order, though not a judicially enforceable requirement. Thirdly, there is the concept of prudence, or self-restraint, on the part of decision makers. This quality is more than the simple desire to avoid antagonizing voters: politicians ought to have in mind – and often do – the effect their actions will have on the wider social fabric; of the extent of conflict these actions are likely to engender; of the consequences for national unity; and of the co-operation required of other jurisdictions. The chief elements of the spirit of our Constitution derive from these varied sources. They help Canadians to reconcile majority rule and minority rights, the interests of Canadian society and of provincial societies, and uniformity and diversity.

The spirit of our Constitution applies to the federal government and Parliament and to the provinces. One example of its workings is the evidence of the self-restraint of majorities in the House of Commons. In a country as diverse as ours, with provinces differing widely in population and with two major linguistic communities, respect for minority interests is critical. In some circumstances, insistence on the rights of a simple majority in Parliament and in the country is a recipe for disunity. To bridge diverse interests requires leadership of an especially high order, genuine respect for minority interests, and the search for policies and goals that will unite, rather than divide, Canadians.

The Constitution has given our federal government certain broad powers to act within areas of provincial jurisdiction and even, it may be, to bring about *de facto* changes in the division of powers. The powers of reservation and disallowance, now by convention virtually "dead letters", were once actively employed. Commissioners recommend that these powers be finally interred through an appropriate constitutional amendment.

Through the declaratory power, the federal government may declare that certain works and undertakings within a province are for the general advantage of Canada or for the advantage of two or more provinces. Though it remains available, the declaratory power has not been used in recent years. Through what is known as the "spending power", the federal government can attach conditions to financial grants to governments, institutions and individuals or can assign the expenditure of large amounts of federal revenue to the provinces. The "Peace, Order, and good Government" clause (Constitution Act, 1867, s. 91) permits sweeping, if only temporary, federal involvement in areas that are otherwise subject to provincial jurisdiction. Each of these powers has been the subject of important controversies, and there have been proposals that they be either abolished or limited, perhaps by the courts, perhaps by some kind of mechanism for reaching provincial consent before they are used.

Commissioners believe that the declaratory power, the spending power, and the "Peace, Order, and good Government" clause are important and flexible devices for use in an uncertain world, and that the national government

should retain them. Nonetheless, although we do not recommend formal limitations on their use, we consider these powers to have such potentially sweeping consequences for federalism that they must be exercised with special restraint, generally only after extensive discussion, and only when other federal powers provide no effective means through which government can act.

The spirit of the Constitution imposes equally important constraints on our provincial governments. Just as the federal government must tread cautiously when its activities affect provincial jurisdiction, so provinces must restrain their broad powers to spend, to engage in public ownership, or to tax, all of which can impinge on federal powers and on the interests of other governments. The provinces, too, must respect minorities. They must be sure that as they stimulate economic development, they do not impose excessive costs on the citizens and governments of other jurisdictions. This Commission has proposed some means to help ensure that this principle will be practised. Provincial adherence to such norms is all the more important as their functions have grown, and as they have claimed a right to help shape national policies. They, too, must take some responsibility for the whole institutional system of which they are a part.

The Division of Powers and Constitutional Flexibility

Commissioners' assessment of the institutions of federalism begins with the division of powers. Some critics have argued for a thorough rewriting of the division of powers set forth in the Constitution. Judicial interpretation and evolving practice have so shaped sections 91 and 92 of the Constitution Act, 1867 that they no longer provide a coherent guide to citizens or governments about the allocation of responsibility. The categories set out in those sections largely reflect mid-nineteenth-century attitudes towards government; they bear little relation to the functions of the state today or to the concepts and terminology of policy discussion. The areas of *de facto* concurrent federal-provincial jurisdiction have multiplied far beyond the formally designated fields of immigration, agriculture and pensions. This evolution of the division of powers, some would argue, has contributed to a Constitution that acts as a very weak disciplinarian of governments; in fact, say such critics, our Constitution has become highly permissive, offering a large number of "pegs" on which governments can hang almost any action they wish to justify.

Why not, then, modernize the division of powers to reflect more accurately the ways Canadians think about government today? There are several reasons why Commissioners do not make such a proposal. First, the Constitution, along with subsequent judicial interpretations, should serve not only as a guide to future action, but also as a record of our national past. It should force Canadians to rethink the lessons of former years. An evolving constitution reflects the movement of a complex society through time. It is not a continuous process of writing on blank slates. To rewrite *de novo* would be to erase the record of our collective experience and the lessons it contains.

Secondly, we see as a virtue the permissiveness and uncertainty of our Constitution. Our "living Constitution" gives us a great deal of flexibility in

adapting to new concerns and needs. The importance of this freedom is obvious when one considers how difficult it is to modernize and clarify the division of powers. Just to codify past judicial decisions into a statement representing the current situation would be a massive—and controversial—task. Moreover, none of the broad distinctions that one might think of to guide a fundamental revision appears easily applicable in an age of interwoven policy areas. Distinctions between social and economic policy or between national and local considerations often seem arbitrary. In everyday experience, changes in technology and communications and new patterns of thinking influence us constantly. It is not easy to make precise distinctions in our complex age.

Another reason for hesitation about comprehensive constitutional revision is that any reallocation of the full range of constitutional powers to accord with current concepts of government would probably become obsolete almost the day it was put in writing. Rather than gaining certainty and clarity, we might, instead, experience a long period of even greater uncertainty while we worked out the full meaning of new concepts and phrases. Indeed, we are now witnessing a process of this nature with respect to Canada's Charter of Rights.

The obvious increase in the number of areas of shared jurisdiction has not so blurred the division of responsibilities between governments as to make meaningless sections 91 and 92 of the Constitution Act, 1982. While "grey" areas abound, the headings of the Act do set out the different functions of each order of government. A broad set of powers, together with access to the national rostrum that Parliament provides, enables our federal government to speak for all Canadians as citizens of a national community, to express our national will, and to concern itself with relations among citizens and regions.

Our federal government lacks unlimited power to act wherever it sees fit, since it is disciplined by the Constitution. Potentially sweeping federal powers, such as "Peace, Order, and good Government" and the "Trade and Commerce" power might have curtailed much provincial activity if they had been broadly defined, but the judiciary sharply constrained them. Certainly, a much broader trade and commerce power in the U.S. Constitution has led to greater centralization. Because of the discipline imposed by the Canadian Constitution, federal representatives, in pursuing national goals, often need the co-operation of provinces, which undertake direct action in many of these domains. The division of powers, though introducing an element of complication, illustrates that the federal government has a responsibility and an orientation to the national interest quite different from the responsibilities of individual provinces.

The provinces, too, have many economic, social and cultural powers that impinge on national policy. Section 92 of the Constitution Act, 1867 gives them wide authority to provide local services and to regulate relations among individuals and groups. Moreover, the provinces possess important land and property rights. Thus provincial actions can have major effects on national policy.

As we have seen, there have been challenges to the current allocation of powers. Throughout the 1970s, various provincial governments called for an

extension of their jurisdiction in many areas; for limitations on a variety of federal discretionary powers; and for direct provincial participation in a number of fields of national policy making, especially those with major regional implications. These initiatives reflected the desire of many provinces to exercise greater control over their own economic and social development. In addition, some asserted that the voting power of central Canada and unbalanced representation in federal cabinets and governing parties led to federal policies unfair or unresponsive to the interests of the smaller provinces. These provinces therefore sought to counteract policies harmful to their interests, and demanded a voice in preventing them. Commissioners do not believe that the call for general decentralization of, or strong limitations on, federal powers is warranted. The present division of powers does not unduly hamper provinces in meeting the needs of their populations. Nevertheless, to the extent that the federal government has wielded its powers in ways unresponsive to the interests of some regions, Canadians must reform the processes and structures of the national institutions and improve intergovernmental institutional arrangements.

Representatives of the alternative view argue that the present constitutional arrangement unduly hampers the federal government's ability to pursue the national interest, and that our national government might require still greater powers. Again, this Commission does not believe that such a view is warranted: in most respects, the constitutional authority of our federal government is adequate. Provincial powers do not hamstring Ottawa's ability to respond to problems. Thus we Commissioners do not find, on the basis of our examination of the economic union and of policy management in the federal system, any compelling case either for significantly increasing centralization or for promoting decentralization. We see no merit in efforts to restore the classic model of "watertight compartments". In any event, such an enterprise would be doomed to failure. Certainly, disentanglement in specific areas might reduce confusion and the costs of decision making; generally speaking, however, overlapping of authority and *de facto* concurrence are not only inevitable, but also desirable. Shared responsibility opens up the possibility that the federal and provincial governments might compete to respond to citizens' problems. In this competition, the need to win popular support can temper the self-interest of governments. This assessment, however, does not deny the need for change and clarification of responsibility. It might well be to the advantage of Canadians to find ways to shift governmental powers back and forth in a more flexible fashion between provincial and federal governments. We recommend two possible methods of doing so.

The first method would be to amend our Constitution to permit legislative, as well as administrative, delegation of powers from one order of government to the other. Delegation of legislative powers has both critics and defenders. Its major advantage is flexibility. Responsibility for a particular matter might be transferred from one level of government to another without constitutional amendment. For any given issue, it is not necessary, however, to transfer responsibility to or from *all* provinces. This leeway makes our constitutional system even more flexible. Legislative delegation also permits *de facto*

consolidation of responsibilities for certain matters or activities which might otherwise have to be regulated under several constitutional powers by both levels of government. In addition, it offers some greater measure of certainty to private actors who, in some circumstances, might come under conflicting regulatory requirements.

Critics argue that legislative delegation would undermine the constitutional distribution of powers and promote governmental uncertainty, confusion and diminished accountability. They argue that such delegation might threaten federalism by opening the possibility of massive centralization or, alternatively, of drift towards highly decentralized confederalism. It is argued that powers, once delegated, would be impossible to recover.

Commissioners are sensitive to the existence of risks and benefits, but on balance, we consider that in practical terms, the federation would benefit from the possibility of legislative delegation. We do not, however, envisage such active resort to this procedure that the constitutional balance would be eroded. Under the present Constitution, governments may delegate administrative responsibilities to administrative bodies established by other levels of government. Commissioners propose expansion of the power of intergovernmental delegation to allow one jurisdiction to delegate law making authority over a particular matter to another jurisdiction. The legislatures of the jurisdictions concerned should consent to such delegations in advance. These transfers of authority might be for defined periods or for periods of indefinite duration; they might take place between the federal government and one, all or a few provinces.

The second method for transfer of responsibilities is the intergovernmental accord. The concept of an accord as an agreement with special status has only recently been made part of our federal practice, and at present it has no clear legal or constitutional status. Intergovernmental agreements, contractual or informal, have a long history; such arrangements include the Tax Collection Agreements, shared-cost programs, the General Development Agreements, and the Economic and Regional Development Agreements. There have been numerous interprovincial agreements as well. They have been a useful means of combining flexibility and a greater measure of certainty about intergovernmental matters.

The term "accord" appears to go beyond such agreements. An accord and the language associated with it seem to have some of the characteristics of a treaty and to imply some form of special standing. An accord is not a constitutional amendment, but it is more than a simple administrative agreement which any government could change unilaterally because of the doctrine of parliamentary sovereignty which prohibits one administration from binding its successors. An accord is more than an agreement backed by legislation, which a legislature could repudiate. The 1985 Atlantic Accord drawn up between the federal government and Newfoundland to provide for joint management of offshore resources and the sharing of revenues argues for clarifying both law-making delegation and accords between governments. It involves a significant shift of power and responsibility to the province and to a joint board. However, the new decision-making body is to apply existing federal resource-management legislation to the extent compatible with the

Accord. Because there is no constitutional power to delegate legislative authority, both the province and the federal government must pass "mutual and parallel" legislation to implement the scheme, and thereafter each must pass any amending legislation in identical form. The Accord provides that neither government will amend the legislation or regulations implementing the Accord without the consent of the other. This restriction on parliamentary and legislative freedom is not constitutionally valid. For this reason, the parties have provided for the possibility of entrenching the Accord in the Constitution itself if the Government of Newfoundland should obtain the requisite support from other provinces.

Accords raise a number of questions for the future. Have we here a new status for certain agreements between governments that might prove more flexible than formal constitutional amendment? Could governments use such agreements to set up temporary arrangements and procedures not capable of unilateral repudiation? Could terms be specified in a more detailed manner than would be suitable in the Constitution, but with comparable stability? Would such agreements be more easily modified in light of experience, but in the meantime provide greater certainty for all concerned? And if the answer to these questions is yes, should we give accords clearer legal status and enforceability? We conclude that we should, and we recommend an amendment to the constitution to permit such agreements and to give them legal standing. Intergovernmental agreements made pursuant to the amendment could not be terminated by any government or its legislature alone. The consent of all parties to the agreement would be required. In effect, for the term of the agreement (if specified), Parliament and the legislatures involved would be constitutionally permitted to bind their successors.

Constitutional Amendment

In the long term, amendment of the Constitution will remain an important device for adaptation of the federal system to new requirements. At the time of Confederation, Canada's Constitution contained no general procedure for amendment. In 1949, the federal government received the power to amend the Constitution in some areas that lay within federal jurisdiction, exclusive of changes affecting the division of powers, the Senate and other critical provisions. This gap in Canada's constitutional machinery has been politically embarrassing and had unfortunate practical consequences. Despite numerous attempts, however, Canadians did not acquire a general amending formula until 1982. Before that date, proposals for constitutional change always involved endless disagreement about methods of achieving them.

Now the rules are clear, if complex. Our new amending formula contains "provincialist" elements which represent the compromise required to forge constitutional agreement in 1981: it treats all provinces equally, and it denies the two largest provinces the veto that many earlier formulae had incorporated. There is no explicitly regional requirement applicable to building the requisite degree of consent. Most substantive amendments require the assent of the House of Commons, the Senate and two-thirds (that is, seven) of our

provinces, representing at least 50 per cent of the Canadian people. A few critical institutional matters, including changes to the amending formula, require unanimity. Amendments affecting some, but not all, provinces require the agreement of those involved. The most important form of protection for individual provinces is the opting-out provision: any province may decline to be bound by an amendment derogating from its powers or privileges. If an amendment affects education or other cultural matters, a province that chooses to opt out has the right to reasonable compensation.

A number of the new formula's features appear to make constitutional amendment easier to achieve: proposed amendments can now be initiated in any of 11 legislatures; amendment need no longer involve the complex "package deals" characteristic of past attempts. No province has a veto, and the Senate has only a suspensive veto. Despite these significant elements of flexibility, Commissioners do not expect frequent amendments. It remains relatively easy to construct a coalition large enough to block proposals. There is no provision for popular ratification to override the positions of governments. Most important, while opting-out may facilitate amendment even if some provinces object, we think that it will limit the frequency of change. Even if only one or two of the larger provinces opted out of any proposed amendment, the action could destroy the effect of any suggested change. More important, if provinces were to use the opting-out provision, the prospect of a "chequer-board Canada", where the operative Constitution varied from province to province, would loom large. We would expect any federal government to regard such a prospect with considerable misgiving and probably, indeed, to withhold consent if a pattern of opting out developed.

In practice, the new amending procedure may differ little from a requirement for unanimity. Constitutional amendment will probably occur only in non-controversial areas where a high degree of consensus has developed. However, Commissioners expect considerable reliance on the rich variety of other institutional devices available to Canadians; in particular, our governments are likely to use formal and informal agreements and delegation. Indeed, it is, in part, because we foresee this growing resort to these other instruments that we are led to recommend constitutional amendments to permit legislative delegation and binding intergovernmental accords. Such devices fill common substantive needs and "lower the stakes" of intergovernmental bargaining by allowing for renegotiation in light of experience.

A central element in any federal constitution is a final court of appeal to act as umpire of the system. Constitutional conflicts arise constantly. They may enter the judicial process through litigation initiated by citizens or private interests, or as a result of government actions, such as the reference procedure. Until 1949, Canada's umpire was the Judicial Committee of the Privy Council (JCPC) of the United Kingdom. Its interpretation of the British North America Act made Canada's Constitution far less centralized than the words of the Act seemed to imply. In 1949, however, the Supreme Court of Canada became our final court of appeal in constitutional matters. Its record since then demonstrates continuing sensitivity to the principles of federalism in the context of a changing society. In case after case, the Court has ensured the maintenance of a balanced federalism.

During the 1970s, heightened intergovernmental conflict greatly increased the volume and sensitivity of constitutional cases before the Supreme Court. On contentious matters such as energy, the Court's role was critical. Now, with the advent of our Charter of Rights, it may become even more so. There will be challenges to the actions of both orders of government, not only as to whether they have acted *ultra vires*, but as to whether they have violated the Charter. These considerations have led observers to suggest that the Court should be accorded a more explicit constitutional status, and that the procedures for the appointment of judges should be re-assessed in light of the court's enhanced constitutional role. We shall address these issues later in this Report.

Although judicial decisions may clarify the limits of constitutional jurisdiction within our federation, and although delegation of powers, accords and other arrangements may help to define governmental responsibilities, nevertheless federal-provincial and interprovincial relations will remain central to adaptation of the federal system. Accordingly, Commissioners turn to the structures and processes of intergovernmental relations in Canada.

The Machinery of Intergovernmental Relations

The machinery of intergovernmental relations helps to manage the complex linkages among the governments of Canada as each level of government operates across many policy areas and deploys a wide range of governing instruments, including spending, taxing and regulating. Subject to the limits of the division of powers, and given always the potential of the Supreme Court to act as final arbiter, the activities of federal and provincial governments are interwoven in many policy fields. Constant interaction is required as leaders at each level respond to the changing demands of citizens in an evolving economic and social context. The challenge, then, is for Canadians to design intergovernmental machinery for managing this interdependence and to do so without sacrificing our other political values.

It should be clear from the previous pages that Commissioners do not intend to suggest that the ideal or the primary goal that Canadians should seek in a reformed set of intergovernmental processes is continuous harmony and the avoidance of all conflict and controversy. We should expect – and we shall continue to have – a great deal of competition within the consultative forums of the federal system. The federal government, concerned with the whole country and serving a nation-wide electorate, will differ in policy matters from provinces serving more limited constituencies. Inevitably, governments will compete to gain the credit for distributing the pleasant policies and try to pass on the blame for the painful ones. Inevitably, different provincial governments will reflect the different needs arising from their particular economic structure and the social make-up of their jurisdictions. The democratic process in the federation involves competition for public support as governments try to produce the policies their constituents demand. The challenge is to ensure that competition does not impose excessive and disproportionate costs on other jurisdictions, that it is carried out in such a way that the interests of citizens play the foremost part in shaping its

outcome, and that the credibility of the institutions of federalism is not undermined. Indeed, while co-ordination is the desired result, the process of achieving it is often competitive and adversarial.

Commissioners do not desire governments within the federation to act jointly in every undertaking, binding one another to the lowest common denominator. Such a policy would deprive federalism of one of its major virtues: the opportunity to use diversity to advantage and to reap the rewards of flexibility and experiment. Total unanimity would be a recipe for paralysis and immobility. It would also clash with the principle of Cabinet responsibility, which makes each government answerable, through its legislature, to its own electorate.

Intergovernmental relations in the federal system involve several levels of interaction. At one end of the continuum, policy making is completely independent: governments take action without consulting others or considering their interests. Under this arrangement, other jurisdictions must adjust independently. A significant portion of federal and provincial policy making takes this form. Governments are, and should be, free to act autonomously within their own jurisdiction. When their policies have a major effect on other governments, however, interdependence requires explicit attention to the interests of others.

The second level of interaction is characterized by consultation. On this level, each government recognizes the effect of its actions on other jurisdictions and the fact that all are acting in the same areas and/or in closely related areas. Here it is important to provide the means for governments to keep one another informed and to provide opportunities for persuasion, pressure and influence. In an interdependent federation, areas of common action represent a large and recently growing category. Accordingly, the institutions which this Commission proposes are designed to encourage close and continuous consultation across a wide range of policy areas. Commissioners believe that governments in a federal system must strive for "a mutual comity which never overlooks advance notice and consultation [and] always strives for accommodation. This is just a necessity for a genuine working federal system in a developed country in the late twentieth century."[1]

The third level of intergovernmental relations involves efforts to achieve co-ordination. Here, governments will try to develop commonly acceptable policies and objectives which they will then implement within their own jurisdiction. The co-ordination of activities can take place in several ways. These ways can range from the general search for a common economic policy framework at a First Ministers' Conference, to detailed agreements on how federal and provincial policies will mesh in a particular province, as in the Economic and Regional Development Agreements.

Finally, there is joint decision making, which requires that federal and provincial governments act together, committing themselves to particular courses of action and standards of conduct. Shared-cost arrangements take this form. It is in this context that fears arise that the accountability of responsible governments will be sacrificed to the need for intergovernmenal consensus. We Commissioners share these fears, and we have taken them into account in making our suggestions for reform of intergovernmental relations.

Each one of these kinds of governmental interaction is exemplified in the vast network of relationships which have developed since the end of the Second World War, especially in the 1960s and 1970s. The "set-piece" First Ministers' Conference (FMC) provides the most obvious example. There are also many ministerial-level meetings on a wide range of subjects and even larger numbers of joint committees of officials. In addition to meetings of all 11 governments, there are hundreds, if not thousands, of bilateral meetings, or meetings between the federal government and groups of provinces. Interprovincial conferences have come to be of significant use, both in co-ordinating provincial responses to federal initiatives and – with less success – in harmonizing provincial policies. In addition to all these formal meetings, myriad informal contacts are made.

There has been considerable variation in the relations between the federal government and individual provinces. Canada has created an intricate network of intergovernmental relationships through which to manage interdependence, though these arrangements are nowhere mentioned in the Constitution and have almost no legislative base. This intergovernmental "industry" has been criticized on many grounds. To some observers, it constitutes a "third order of government", threatening to undermine the principles of parliamentary accountability. Other observers believe that the intergovernmental process introduces important biases into the consideration of public policy in Canada. They consider that the process focuses undue attention on the "second-order" questions of political status or on competition between levels of government rather than between parties, to gain credit among voters and to avoid blame. It is sometimes argued that in emphasizing the role of provincial governments, the intergovernmental process reinforces a tendency to define the regional dimensions of issues in terms of provinces, conveying the impression of homogeneity within provinces when, in fact, there are often as many differences within provincial jurisdictions as there are among them. The process also diverts attention from other problems, such as those relating to socio-economic status or gender, and reduces the opportunity for groups who represent such non-regional interests to mobilize and to secure a hearing. There is doubtless some truth in this view: the focus in intergovernmental discussions of economic policy differs from that chosen in discussions between the public and private sectors. This is an inevitable consequence of a federal system, but the difficulties should not be exaggerated. Intergovernmental discussions do take into account concerns expressed in the wider environment. When the public agenda emphasizes issues in which regional differences are slight, as in the construction of the post-war welfare state, the debates among governments can reflect that wider concern. Finally, federal or provincial Ministers and officials negotiating on specific matters frequently represent the interests of their client groups.

Another set of criticisms relates to the intergovernmental process itself. While there is considerable communication among governments, it is often sporadic and *ad hoc*. Governments naturally tend to call for consultations when it is to their political advantage; they are equally likely to ignore inconvenient calls. There has thus been no assurance that ongoing common problems will receive continuous attention. Even the issue of calling meetings,

especially First Ministers' meetings, has tended to be a matter of political debate which diverts efforts from the actual search for solutions to common problems. The public meetings, especially at the level of First Ministers, seem to put a premium on the strongest possible statements of position, rather than on a search for understanding and compromise. The process exposes differences more effectively than it contributes to their reconciliation.

In recent years, the intergovernmental process has been further hampered by the divergent expectations of participants. Provinces have tended to regard First Ministers' Conferences as opportunities to discuss the full range of federal policies and to assert an influence in national decision making. This tendency has been fostered by three developments. Provincial governments' growing strength and effectiveness permit them a claim to affect national policy and give many of them levels of expertise and knowledge equal, in certain fields, to that of the federal government. In the recent past, the weak representation in certain regions of the party in power has lent credibility to the provincial claim to represent these areas, even in national policy. Changes in the federal government's approach to managing our economy, have increased federal involvement in areas previously considered primarily provincial. Federal-provincial conflict tends to be more intense when governments are searching for new policy options in previously uncharted areas.

The federal government, on the other hand, has viewed First Ministers' Conferences on the economy as a mechanism for consultation on a wide range of issues. There have been occasional attempts at co-ordination, but it is probably fair to say that the federal government has resisted provincial suggestions to formalize a decision-making process on the basis of "executive federalism" primarily on the grounds that this would not fit well with the role of parliament in our system of responsible government. While the federal government acknowledges the helpfulness of provincial government views on national economic policy making, provinces have rarely welcomed the federal government's views on provincial policy or programs. Furthermore provincial governments have been reluctant to put forward views on how they might alter provincial policies to contribute to the resolution of fundamental country-wide problems. This imbalance in obligations at the First Ministers' table has led some observers to question what co-operative federalism really means.

Government growth has caused structural changes which have seriously affected intergovernmental relations. The role of "central agencies" and institutions, such as premiers' offices and Treasury Boards, has expanded as governments have sought means to achieve greater consistency and co-ordination in their operations. More centralized direction and attempts to establish greater fiscal and policy control over line ministries have been part of governments' efforts to identify and pursue more "global" or integrated visions of the public good. To some extent, these efforts have weakened an earlier pattern in which intergovernmental relations were mainly conducted among ministers and officials in operating departments with a specific policy mandate. Federal and provincial officials within such departments often shared common policy and professional goals, and responded to the same

groups in the population. Their common interests and activities fostered mutual trust and a sense of common purpose. At the First Ministers' level and within central agencies, the goals of political status are likely to be more prominent, and governments are likely to be less constrained by group pressure. The goal of co-ordinating policy across all fields within a single government often conflicts with management of intergovernmental co-ordination within a policy area.[2]

In such recent issues as that relating to the Constitution, the status of governments has also caused intergovernmental tension. Constitutional reform dominated the intergovernmental process for much of the period from 1968 to 1983; it was fuelled both by Quebec's wish for an enhanced status and by the West's desire for a new deal. Debate on the Constitution called directly into question the status and powers of government. The questions it raised were powerful and symbolic, not easily subject to the kind of "splitting-the-difference" compromises characteristic of more concrete and less emotionally charged issues. Since the purpose of the participating officials was to defend their government's vision of Confederation, there were fewer ties of common interest. The general absence from the process of well-informed interest groups meant that no one held the participants accountable or encouraged resolution of differences. In short, debate on the Constitution brought out the worst features of the intergovernmental process. While more co-operative relationships existed in many areas, battles over constitutional and energy issues tended to poison the whole range of intergovernmental relationships, turning the process into one of "good guys" versus "bad guys".

The foregoing assessment might suggest that the machinery of intergovernmental relations is so cumbersome and ineffective that it is beyond effective reform. Commissioners disagree. We must provide intergovernmental institutions to meet the need for co-ordination in several major fields where federal and provincial government actions and responsibilities overlap. Therefore the institutional arrangements which we propose are intended to consolidate the existing intergovernmental structure. Our aim is not to multiply intergovernmental bodies, but to make effective the machinery Canada already has in place. We hope to ensure that actions which may seriously affect other levels of government will be assessed in advance and will increase the openness of intergovernmental relationships, rather than introduce new constraints and limits. We also believe that it is vital to ensure reform of the overall process to make it more consistent with basic norms of political accountability and to improve public access to, and understanding of, intergovernmental relations.

Commissioners wish to encourage institutions and processes that will facilitate common trust, for without some general understanding of shared purpose, the best-designed institutions will fail. But shared purposes alone are not enough to establish positive relationships: they need to be supported by effective consultation and debate if co-ordinated results are to emerge. The constructive elements will arise from co-operation and recognition of the legitimacy of differences.

Proposals

Commissioners therefore propose that the First Ministers' Conference (FMC) be entrenched in the Constitution. First Ministers should meet annually on a fixed date, and other sessions should be called as necessary. The First Ministers' Conference is the capstone of the intergovernmental structure.

Throughout the recent constitutional debates there was discussion concerning a regular First Ministers' Conference. The FMC has been a major goal of most provinces, and at times, the federal government endorsed their aim. At the First Ministers' Conference held at Regina in February 1985, Prime Minister Mulroney committed his government to annual meetings on the economy for the next five years. Some might object to institutionalization of this most contentious federal-provincial body, where political differences predominate. Commissioners believe, however, that official status for the FMC would acknowledge the need to arrange a satisfactory forum of interdependence, and for federal and provincial governments to co-ordinate policies and activities. To ensure openness and accountability, some FMC sessions should be held in public, though private discussions should take place as necessary. To make the meetings fixed and regular would remove one of the more contentious aspects of recent FMCs: the arguments about when and whether one should be called. To a great extent, regular Conferences will avoid the build-up of hostilities and the artificial inflation of governmental and public expectations that result from such jousting.

The central purpose of FMCs should be to provide a forum where federal and provincial leaders can discuss policy needs and explore possibilities for action of national importance in both levels of jurisdiction. The FMC would not be a legislative body, and its decisions would not be binding on governments. Rather than legislate, it would seek a common policy framework. Formal voting rules, as such, would not be necessary. Legislative follow-up to discussions in the FMC and in the other bodies Commissioners suggest would be the responsibility of governments.

Nevertheless, the FMC would need to organize its own affairs. Commissioners envisage creation of additional Ministerial Councils, a step which we propose below. The FMC could restructure the Councils as necessary, define their mandates, assign them tasks, and receive their reports. It might wish to establish a voting rule to cover decisions about the structure, composition and mandates of Ministerial Councils.

Critical to the success of any intergovernmental institution is adequate preparation. This includes extensive prior discussion of the agenda, sharing of information, and private exploration of possible areas for agreement or compromise. The FMC could create an independent secretariat to support preparatory work, perhaps by upgrading the Canadian Intergovernmental Conference Secretariat, which now provides administrative services. This move would introduce into the system a group of officials whose objective would be the success of the system itself. Conversely, it would create some difficulties. An autonomous intergovernmental bureaucracy similar to the Commission of the European Community, for example, would be counter to

Canadian norms of responsible government. Commissioners therefore recommend the use of a better-established Canadian institution: a permanent committee of senior officials like the Continuing Committee of Officials on Economic Matters. Such a committee, with members designated by the First Ministers, should be appointed to support the FMC.

Although Commissioners have rejected the option of an independent secretariat to serve the FMC directly, third parties, not tied to the day-to-day interests of governments, can often help to facilitate agreements, by providing optional perspectives and new information, and by finding solutions that participants may be too involved to see. An Advisory Panel on Intergovernmental Relations might fulfil these functions and help the public to understand federal-provincial issues. We have looked at two models: the long-established Advisory Commission on Intergovernmental Relations (ACIR) in the United States, and Australia's Advisory Commission on Intergovernmental Relations. These commissions, established by legislation, consist of representatives of the federal and state governments (and, in the United States, of municipal governments), served by a small professional staff. In each country, the Commission studies various issues, conducts research and holds conferences. Their work has made notable contributions to good intergovernmental relations.

Members of such a commission or panel could act as informal mediators to help resolve conflict among governments. The techniques of mediation, developed in settings from labour/management relations to great-power negotiations, might help to resolve intergovernmental conflict in Canada. An advisory group could ease those relations behind the scenes, and provide information and analysis both to governments and to the public. First Ministers might eventually wish to consider the creation of such a body to assist in providing some or all of the possible contributions we have noted. Commissioners would suggest, however, that this additional element be considered only after some experience has been gained with the new structures and procedures we are recommending for the FMC and Councils.

Meetings at the ministerial level now cover many areas of government policy, but they, too, suffer to some degree from their sporadic nature. With some exceptions, notably the meetings of Finance Ministers, they do not provide continuous interaction and sharing of ideas and information. Commissioners recommend strengthening these relationships as part of our larger purpose of increasing the emphasis on concrete policy problems. This shift of focus is much more likely to occur in groups created to concentrate on specific problems. We therefore propose that the First Ministers' Conference appoint a number of Councils of Ministers to serve in major functional policy areas. Again, the meetings of Ministerial Councils should be held regularly, presumably more frequently than FMCs, to encourage development of common perspectives and exchange of information, and to establish trust among the participants. Like the FMC, Ministerial Councils would be served by continuing committees of officials. This Commission does not propose to list all the Councils that might be established or that already exist in some fashion. Our purpose is to suggest a core framework of federal-provincial mechanisms that would, in a more streamlined way, support First Ministers

in their collective and individual responsibilities. Commissioners propose that three central Ministerial Councils be established in the fields of Finance, Economic Development and Social Policy, areas related to major themes developed earlier in this Report.

The Council of Ministers of Finance

The Council of Ministers of Finance (or the Conference of Finance Ministers) stands as Commissioners' prototype for the other councils. Finance Ministers and Treasurers have met regularly for many years to monitor and negotiate fiscal arrangements, to discuss economic projections, to compare notes before budgets are prepared, and to discuss macro-economic policy. Our proposal simply formalizes the existence of the ministerial Council on Finance and requires, again, that it meet more frequently. Furthermore, its importance would be enhanced by our proposals for greater federal-provincial co-ordination in the budgetary process. This Council, as we discuss in the section on fiscal arrangements, would be supported by a new federal-provincial body of tax experts, the Tax Structure Committee, to conduct research and monitor developments in taxation.

The Council of Ministers Responsible for Economic Development

As Commissioners mentioned earlier, protection of the Canadian economic union is not simply a matter of preventing the erection of barriers or of finding the right enforcement officer. Rather, successful operation of the economic union requires that Canadian governments build a common set of purposes that will lead to co-ordinated effort in all the economic development activities in which governments engage. A Ministerial Council for Economic Development would provide the principal focus for discussion of such purposes and means to achieve them.

The successful operation of Canada's economic union also requires exchange of information among governments in order to prevent, especially at an early stage, the escalation of policies that are harmful to other jurisdictions. The Council of Ministers responsible for Economic Development would therefore monitor and assess the state of our Canadian economic union. Through the Council, governments might develop "a Code of Economic Conduct", as described above. The Council would seek agreement on common objectives in economic and trade policies and would encourage mutually beneficial linkages among regions.

A vital adjunct to the Council would be a Federal-Provincial Commission on the Economic Union whose members would be named by the Council. The Commission would monitor the state of the Canadian economic union, conduct research to identify barriers and possible areas for greater harmonization, and report publicly to the Ministerial Council on these matters. It would also provide for official hearings of individuals and groups who believe that existing barriers significantly frustrate their own activities. It would investigate their complaints, weigh them against other considerations,

and report both to the public and to the Council, offering recommendations for action.

Such a body would ensure public involvement in discussions of our economic union. It would also provide an independent source of advice aimed at strengthening the economic union. Moreover, by requiring governments to justify their actions publicly, it would increase their accountability. Commissioners anticipate that it would discover many areas in which differences in licensing standards and safety regulations neither serve distinct provincial or federal public purposes nor protect the public. Many, indeed, are simply the product of tradition, inertia and lack of awareness.

The Council of Ministers on Social Policy

The importance of social policy to many facets of Canadian life and the high degree of shared responsibility in the field of social policy strongly suggest the need for a Council of Ministers on Social Policy. Such a body could consider all facets of social policy, especially in the shared fields covered by the Established Programs Financing (EPF) and the Canada Assistance Plan (CAP). The recommendations on social policy set out earlier in this Report suggest a large number of reforms which will require intergovernmental consultation. Consultation with practising professionals and interested groups and individuals is particularly important in this area. Commissioners would encourage Parliamentary Committees to take a more active part in forming social policy, conducting research on the issues involved, and holding public hearings.

The FMC could establish other ministerial councils as necessary. It might, for example, appoint councils in such areas as employment training and the administration of justice. These structures would provide a framework for greater coherence in the federal-provincial system. Less structured forms of interaction would also occur automatically, in bilateral and interprovincial discussions of specific issues. Indeed, as we have noted, many such relationships already exist, and we see no reason why this process should not continue to evolve.

Throughout this Report, Commissioners have stressed the need to make governments more accountable to legislatures and voters. We have noted that the intergovernmental processes of executive federalism can sometimes undermine clear lines of accountability. We need continuous effort to minimize this tendency. Moreover, the intergovernmental process must be kept open to public view. Some of the proposals made above will assist this process. For example, the Federal-Provincial Commission on the Economic Union, in assessing complaints, will provide a public window. The proposals that the First Ministers' Conference be open, at least in part, will facilitate the same objective: governments will be accountable for their performance. If more functional and substantive discussion takes place between governments, participants should become more aware of the interests of affected groups.

This Commission, however, believes that even more could be done. Governments must be held accountable for their conduct of intergovernmental affairs. The best way to hold them accountable is through a parliamentary

or legislative committee. In recent years, the Task Force on Federal-Provincial Fiscal Arrangements (the Breau Task Force), parliamentary committees on the Constitution, and similar provincial bodies have demonstrated the value of parliamentary scrutiny of intergovernmental matters. All tempered the tendency of intergovernmental forums to focus on "who does what" with a healthy emphasis on what is to be done. Standing committees at both levels would be able to monitor these relationships more consistently. Commissioners therefore propose that Parliament and the legislatures establish permanent standing committees responsible for intergovernmental relations.

Interprovincial Harmonization

So far, Commissioners have concentrated on the federal-provincial dimension of intergovernmental relations. There are many interprovincial relationships and some important interprovincial institutions. Since the early 1960s, leaders of Canada's provincial governments have met annually in the Premiers' Conference. These meetings at first concentrated primarily on co-ordinating approaches to issues of provincial concern. More recently their aim has been to unite provinces in their response to federal initiatives, especially in relation to fiscal and constitutional matters. On a few occasions, provinces have forged compromises among themselves in order to take up a common position. The office of Conference chairperson rotates among the premiers; the incumbent often speaks for the provinces in dealings with the federal government. Provincial agreements are likely to affect federal-provincial relations, particularly on issues where provinces share common policy interests, mainly those, like the Constitution, that relate to their status as governments. On other economic and social questions, different regional needs and interests will often divide provinces as much as they do federal and provincial governments. Provinces will often wish to deal individually with the federal government, rather than as part of a group.

Within an economic union, harmonization of policies across jurisdictions is vital.[3] As we have seen, differences in product standards, licensing rules for occupations, and codes of commercial law can inhibit mobility and trade among member jurisdictions. It is necessary to seek a balance between the autonomy of member-states to enact policies to suit their own conditions and the uniformity that facilitates transactions among them.

In a federal system like Canada's, the federal government properly plays a central role in harmonization. This is why constitutional authority over interprovincial trade and commerce is federal, and why Commissioners believe that fields like competition, telecommunications and product standards should be primarily federal matters. The proposed Code of Economic Conduct is also a step toward harmonization. It is aimed at ensuring that federal and provincial economic-development activities do not erect barriers to the Canadian economic union.

There remains, however, a large domain of provincial regulatory activities derived mainly from provincial authority over property and civil rights. These activities can lead to variations in practice among provinces that inconven-

ience economic actors wishing to operate on a national plane. Where varying provincial laws create difficulties, transfer of responsibility to the centre is not the only possible response. An alternative device encourages provinces to harmonize their laws as much as possible, where this is necessary for the effective integration of the Canadian market. Much harmonization, of course, occurs spontaneously: all provinces are under similar pressures from constituents, and their policies are unlikely to vary much. As a government prepares to act in a field, it is natural for it to look first at the ways others have drafted their legislation. Innovations begun in one province can thus spread to others.

Canadians should also ask what mechanisms exist to promote more complete harmonization. The oldest such mechanism is the Uniform Law Conference of Canada, formerly the Conference of Commissioners on Uniform Law, founded in 1915. Its membership, which meets annually, includes representatives from the federal government, all the provinces and the territories. It has published more than sixty uniform acts in many fields. Twenty-four have been accepted in six or more jurisdictions, but only one has ever been adopted in all jurisdictions. There are many explanations for the modesty of this record. The Conference has a small secretariat and few research resources. Its members are all full-time officials employed elsewhere. The focus on drafting uniform laws has diverted attention from concentration on broad principles. The draft laws, developed in the common-law tradition, have met with little response in Quebec, with its Civil Code tradition. The Conference has done little to enlist outside groups in its work or to lobby for the adoption of its proposals.

A different mechanism for fostering harmonization is the formation of ministerial or official working groups. One such institution in Canada is the Council of Ministers of Education, which is intended to promote better exchange of information and development of common curricula. More narrowly focused committees have also had success. These include, for example, a federal-provincial group working on a central registry for security interests in aircraft, which was established in 1983.

Efforts at harmonization require strong pressure from outside, as when groups inconvenienced by provincial variations mobilize to promote unity. Federal and provincial law-reform commissions could exert such pressure. It would be relatively simple to extend their mandates to include responsibility for examining possibilities for interprovincial harmonization, although so far there has been little movement in this direction. Another important vehicle is professional groups with a nation-wide mandate, such as the Canadian Bar Association or the Canadian Institute of Chartered Accountants. In 1963, the Commercial Law Section of the Canadian Bar Association created a committee of experts to prepare a model Uniform Personal Property Security Act. The Committee has been influential in modernizing and harmonizing law in this area which is vital for interprovincial business transactions. At least seven provinces have passed, or are likely to pass, legislation embodying most of the features of the model law.

What are the lessons of this record of interprovincial harmonization? The evident lack of drive behind these efforts could have several meanings.

Perhaps there is already a significant degree of harmonization; perhaps existing gaps in harmonization pose relatively few costs; perhaps there is a great unfulfilled need for new institutions. Commissioners incline to the first two explanations. Overall, however, we believe that greater harmonization would maximize the advantages of the economic union. We do not recommend creation of additional institutional structures: the institutions we have described already should prove ample. Thus, the Council of Ministers for Economic Development will undoubtedly address interprovincial harmonization, as will the Federal-Provincial Commission on the Economic Union. The latter provides an opportunity for private actors to press for improved harmonization in particular areas. Similarly, the other ministerial councils can commission working groups to examine harmonization. The Premiers' Conference could look at the issue, delegating specific tasks to ministers or officials. Thus, mechanisms exist to respond to needs as they develop.

Conclusions

Commissioners have designed these proposals to rationalize the structure of intergovernmental relations. We wish to facilitate management of interdependence in the federal system, for Canadians cannot recreate the classic watertight compartments of federalism. We have made a number of suggestions for disentangling federal and provincial activities, such as a clearer division of labour in regional development policy and replacement of the Canada Assistance Plan by a federally operated income-supplementation scheme to which provinces would add their own programs. We believe that as the Councils of Ministers look at other programs, they can accomplish much more in terms of understanding and clarifying which government should implement which programs.

Commissioners have recommended some constitutional changes and have emphasized the need for more flexible procedures to promote delegation and intergovernmental agreements. There will remain many intergovernmental relationships arising from shared responsibilities and the need to adjust policy to changing needs. We Canadians can gain much by rationalizing the structure that already exists and by providing more effective forums for consultation and co-ordination. Commissioners' proposals should provide for more consultation and for mechanisms to ensure that this consultation is open to public scrutiny.

We Commissioners urge Canadians to consider our proposals for reform of intergovernmental arrangements in relation to our other recommendations for institutional change, especially those pertaining to the reform of national institutions. The federal government, in the conduct of its responsibilities, must possess the capacity to represent and accommodate the interests of all regions: intergovernmental relations are not a substitute for full regional representation at the centre. Similarly, enhanced regional representation in national institutions is not a substitute for intergovernmental relations. The existence of a formal division of powers and of two strong orders of government means that co-ordination is essential, no matter how regional representation in national institutions is achieved. Thus we see reform of the

centre and reform of the institutions of the federation not as alternatives, but as complementary: Canada needs not merely one or the other, but both, for different purposes.

Reform of national institutions along the lines Commissioners have proposed should change the character and dynamics of federal-provincial relations. Stronger representation from all provinces in national institutions will ensure that regional concerns will be represented in caucus and Cabinet. Moreover, through its Members of Parliament, a more regionally representative government should be able to communicate effectively with citizens in each province, in developing support for programs and initiatives and in responding to local needs. Such a government will be able to provide more effective leadership and to counter the claim that the provincial governments are Canadians' only legitimate representatives of local interests. One consequence of the present regionally imbalanced structure of representation in national institutions has been the almost impossible burden it placed on the intergovernmental process. A lesson of the recent past is that political integration comprises too large a task to be discharged by a single set of institutions. A healthy federal system is one in which there are multiple links binding together federal and provincial levels. These links exist, not just between governments, but in political parties, in bureaucracies, in the media, in associations of all kinds and, ultimately, in the minds of citizens.

Commissioners do not wish to conclude this discussion of intergovernmental relations without noting the profound importance of personal associations in social, commercial and family life that link Canadians in different parts of the country. In a federal society, the informal ties of citizens to one another, as well as to the state, are important means of moderating or restraining excesses. Communication across regions moderates tendencies to excessive differentiation; it also serves as the foundation for the tolerance of diversity which, in its turn, provides a healthy check on the unifying authority of the national government. Ultimately it is citizens who must discipline the conflicts among their governments.

Notes

1. J.A. Corry, "The Uses of a Constitution", in Law Society of Upper Canada, *Special Lectures 1978, The Constitution* (Toronto, 1978).
2. J. Stefan Dupré, "Reflections on the Workability of Executive Federalism", in *Intergovernmental Relations*, vol. 63, prepared for the Royal Commission on the Economic Union and Development Prospects for Canada (Toronto: University of Toronto Press, 1985).
3. Ronald C.C. Cuming, "Harmonization of Law in Canada: An Overview", in *Perspectives on the Harmonization of Law in Canada*, vol. 55, prepared for the Royal Commission on the Economic Union and Development Prospects for Canada (Toronto: University of Toronto Press, 1985).

CHAPTER 23

Citizens, Communities and the Federal State

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Introduction: The Charter and Living Constitutionalism

The Canadian Charter of Rights and Freedoms and other provisions of the Constitution Act, 1982 involve the citizens and communities of Canada more fully in the constitutional order than they have previously been involved. Provisions of the Charter and the manner in which they are applied and interpreted by courts, legislatures and Canadians themselves will, in the years ahead, significantly alter relationships between our citizens and their governments. Canadians will take some time to adjust to the Charter. Commissioners' purpose in examining the Charter, therefore, is to make more widely known some of its possible implications. We wish to promote greater understanding and consideration of the problems and opportunities that arise from the Charter and in so doing, perhaps to assist in the process of adjustment. In this section of our Report, therefore, we Commissioners examine some of the ways in which we believe the Charter will affect Canadian politics and society in the future.

The Constitution Act, 1982 was the culmination of two years of intense negotiation and public discussion involving federal and provincial governments and many interested groups and persons across Canada. It was adopted after four years of almost continuous discussion, six years of prolonged crisis of national unity, fourteen years of sustained efforts to entrench the fundamental rights of citizens in the Constitution, and more than fifty years of search for an all-Canadian formula for constitutional amendment. When it emerged, the Constitution Act, 1982 was the product of this process: a compromise document reflecting both principle and pragmatism. It also signalled the beginning of a new era of Canadian constitutional history.

All the key actors in the constitutional reform process had a hand in shaping the Constitution Act, 1982. The signatures on the final accord were

those of the First Ministers or their delegate. Parliament played a significant role in formulating the resolution discussed by the First Ministers. The people of Canada participated both through the public hearings of the Special Joint Committee of Parliament and through intense lobbying efforts at various stages of the Constitution Act's genesis. The Supreme Court of Canada's important constitutional decision of September 1981 rekindled discussions between the federal and provincial governments.

The Constitution Act, 1982, represents a constitutional reform package. It is impossible to understand or explain each provision without reference to the Act as a whole. A comprehensive procedure for amending the Constitution of Canada effectively crowns the achievement of Canadian sovereignty over our domestic Constitution. In addition, the Constitution Act, 1982 has added a Charter of Rights and Freedoms to the basic constitutional law of Canada.

New institutions may be created and constitutions written or amended in relatively short periods of time. Once in place however, the institutional and constitutional framework profoundly affects the manner in which future public issues emerge, as well as the way in which they are resolved. The words of every constitution betray the era in which they were written, and the Charter of Rights and Freedoms provides no exception. Our Charter was enacted in 1982. It therefore reflects many of the concerns of the social movements of the 1970s, as well as that decade's intense concern with national unity. In the matter of equality rights, for example, the Charter differs markedly from the Canadian Bill of Rights legislated 22 years earlier. Moreover, we cannot understand the Charter's provisions on language and personal mobility rights without reference to political events of the 1970s.

Just as the approach to human rights has changed significantly over the past few decades, it will undoubtedly change in the future. Shifts in the balance between individual rights and the interests of the community as a whole, new understandings of the causes of discrimination and the ways in which it operates, and new concerns about equality will come to our attention. As societies evolve, their composition, needs and aspirations change. As a society grows and changes, so too does its understanding of the need to protect human rights and of what these rights may entail. The Charter will help to shape this evolutionary process.

How does an entrenched charter or bill of rights interact with this process? An entrenched charter provides at least a minimum guarantee and secure base of citizens' rights, but it should also adapt to meet new social conditions and challenges. The balance is not unlike that required in any constitution that aspires to survive periods of tumultuous change. A number of provisions in the Canadian Charter of Rights and Freedoms point to the need to develop a Charter jurisprudence that is sensitive to such a balance. The first section of the Charter states clearly that the rights and freedoms it guarantees are subject "only to such reasonable limits prescribed by law as can be demonstrably justified in a free and democratic society." How the courts balance the rights guaranteed by the Charter with the needs of society will help to determine how the Charter contributes to the development of our "living" Constitution. The Constitution Act, 1982 itself contains certain principles that are fundamental to this process of development.

The Charter and Parliamentary Supremacy

The Constitution Act, 1982 declared for the first time that the Constitution "is the supreme law of Canada and any law that is inconsistent with the provisions of the Constitution is, to the extent of the inconsistency, of no force or effect."[1] As part of the Act, the Charter of Rights and Freedoms is the supreme law of the land. This guaranteed constitutional protection of rights and freedoms supports Commissioners' view that the Charter is a new pillar of the Canadian constitutional order. Its arrival has especially important implications for the tradition of parliamentary supremacy in Canada. Legislation of Parliament and of the provincial legislative assemblies must conform with the Constitution, including the Charter.

The new supremacy of constitutional law has implications for Canada's institutional framework, as it has the potential to affect historic relationships between legislatures and the judiciary, as well as between citizens and their governments. Examination of the Charter as a pillar of the constitutional order must take into account the powers and authority of the courts in protecting the rights and freedoms guaranteed in the Charter because the courts must determine inconsistencies between the Constitution of Canada and legislation. The Charter reinforces the courts' general responsibility for this judicial review by assuring court access to anyone whose rights or freedoms guaranteed by the Charter have been infringed or denied. The courts also assume a vital role in determining the forms of compensation or redress that any such person may receive: the Charter provides that courts may order "such remedy as [they consider] appropriate and just in the circumstances."[2]

Two other significant provisions provide further insight into the role that may be expected of courts under the Charter and illustrate the subtleties which pervade the new supremacy of constitutional law in Canada. Section 1, the "reasonable limitations" clause, and section 33, the "general override" provision, contain limitations on the rights and freedoms guaranteed by the Charter. These two provisions indicate the sensitive constitutional balance between courts and legislatures.

The general override provision enables Parliament or the legislature of a province to pass laws that are inconsistent with some, but not all, of the Charter's guarantees. It was included in the Charter at the insistence of provinces concerned about changes in the relative power of legislatures and courts. The major concern was that the entrenchment of rights would detract from the principle of legislative supremacy. The override provision retains some aspects of that supremacy.

Designated pieces of legislation may operate despite the existence of Charter protection for the fundamental freedoms, including freedom of conscience, of opinion and expression, of peaceful assembly and association (s. 2), legal rights (ss. 7–14), and equality rights (s. 15). However, to give effect to a legislative override of any of the Charter's guarantees, Parliament or the legislative assembly must expressly declare that an Act will operate notwithstanding a constitutional guarantee included in section 2 or sections 7 to 15. Such an express declaration will have effect for a period of up to five

years, at which time it may be extended by the legislative body. This ensures that at least once every five years the legislating body will reconsider the specific use of the override. In such cases, parliamentary debate will provide the primary forum for scrutinizing the use of the general override power and for ensuring that its use is consistent with appropriate standards of responsible administration.

Commissioners are anxious that the Charter's general override provision should contribute to public awareness of legislation limiting the constitutional rights of citizens in Canada. In our view, overriding legislation should include a declaration of intent to legislate, notwithstanding a provision of the Charter, and should include not only reference to the specific rights being overridden, but also an explicit indication of the purpose of such legislative action. Such a statement of purpose would help to establish the scope of limitations and could also be referred to in discussions on whether to extend an override after the five-year period.

Shortly after Queen Elizabeth II proclaimed the Constitution Act in April 1982, Quebec's National Assembly passed legislation exempting Quebec laws passed prior to the Charter from sections 2 and 7 to 15 of the Charter. Quebec legislation that post-dates the Charter includes an express declaration of the non-applicability of these sections of the Charter. Although the National Assembly took these actions to reinforce the Quebec government's general repudiation of the Constitution Act, a legal challenge arising from the Quebec measure presents the Supreme Court of Canada with an opportunity to establish important rules about the use of the general override provision and the obligation of governments to adopt a specified form and content for invoking this clause.

In addition to its basic significance for parliamentary supremacy, the general override clause will have important consequences for the interaction of guarantees of rights and Canadian federalism. Since the national and provincial governments are able to enact the general override power in certain circumstances, wide variations among provincial governments' policies respecting fundamental, legal, and egalitarian rights in Canada are permitted. Variations in citizens' rights across the country are a possible consequence. The degree of variation which emerges will depend, in part, on the characterization of the right in jurisdictional terms. For example, if the courts decide that many of the fundamental freedoms, such as freedom of expression or legal rights, belong within federal jurisdiction, extensive variation is unlikely. In such instances a provincial override would obviously not apply, and courts could rule invalid provincial laws violating these rights, on the basis that the provincial government acted beyond the scope of its legislative authority under the Constitution Act. In areas within provincial jurisdiction, however, variation may be quite profound.

The use of the override by the national government would not result in rights variations among Canadians, but would of course take precedence over the specific right or rights with which the legislation is in conflict.

In Commissioners' view, the existence of the general override clause enables the courts to enforce more strictly the Charter guarantees of fundamental freedoms (s. 2), legal rights (ss. 7–14), and equality rights

(s. 15). Knowing that governments have recourse to a legislative override power if they believe the judicial tests are particularly inappropriate, courts should be able to establish very stringent tests for otherwise limiting fundamental, legal and egalitarian rights through the reasonable limitations provision of section 1 of the Charter.

In addition, the inclusion of the general override clause suggests to Commissioners that the drafters intended to provide few other opportunities for limiting the Charter's guarantees. This conclusion is supported by an examination of section 1, the second general authority for limiting the Charter's guarantees. Section 1 of the Charter has been called the "restrictive" clause, the "general limitations" clause or the "reasonable limits" clause. It applies to all the rights and freedoms guaranteed in the Charter. This provision makes explicit what in many constitutions is merely implicit: that no right is absolute. Circumstances may arise when some rights have to be balanced with other rights; there must be a balance, for example, between freedom of speech and protection of the reputation or privacy of individuals, and between the rights of individuals and the interests of the community. Nonetheless, conditions under which limitations on the rights guaranteed in the Charter can be imposed are stringent.

The section 1 provision makes clear that the rights and freedoms set out in the Charter are "subject only to such reasonable limits, prescribed by law, as can be demonstrably justified in a free and democratic society." It is for the courts to determine whether these conditions have been met in any particular circumstance. Early court judgements indicate that the onus of proof for meeting these conditions will fall on those who seek to limit rights and freedoms, rather than on those who claim that their rights and freedoms have been infringed or denied. Already the courts have indicated that they will not be satisfied by legislatures simply declaring that they deem an action to be reasonable and justified.

Changes to the wording of section 1 throughout the constitutional drafting process had the effect of making it more difficult to justify limitations on Charter rights. Initial drafts had provided that the Charter's guarantees were "subject only to such reasonable limits as are generally accepted in a free and democratic society with a parliamentary system of government." The accepted stronger wording that subsequently became the basis of the Constitution Act, 1982 required that limits be "prescribed by law" and be "demonstrably justified in a free and democratic society." These more stringent terms suggest standards of justification that will not be met through simple parliamentary consensus or executive decision.

Section 1 has the potential to affect profoundly the judicial process in Canada. In effect, this clause requires courts to determine whether legislative actions are justified and reasonable in a free and democratic society. Given the nature of the judicial process, courts can make such assessments only on a case-by-case basis. As noted above, however, the courts have already begun to establish their general approach. They appear to have adopted tests to ensure not only that the objective of proposed limitations is justified, but that the means of achieving it are also acceptable. In Commissioners' view, section 1 is meant to ensure that limits imposed on the rights and freedoms guaranteed in

the Charter are not only reasonable, prescribed by law, and demonstrably justified, but also constrain rights as little as possible in order for them to achieve their objectives. These criteria restrict legislatures and emphasize once again that legislative enactments and government practices must be consistent with the guaranteed rights and freedoms set out in the Charter.

Commissioners believe that the Charter marks a significant change in Canadian constitutional law and entails major consequences for the tradition of parliamentary supremacy. The Charter has enshrined the fundamental rights and freedoms of citizens in their relations with governments. Henceforth, provisions of the Charter interpreted by the courts will constrain government activities. The extent to which the Charter will directly affect Canadian society will be determined by the scope of the Charter's applicability, an issue also addressed in the Constitution Act, 1982.

The "applications section" of the Charter indicates that it applies:

> *(a) to the Parliament and government of Canada in respect of all matters within the authority of Parliament including all matters relating to the Yukon Territory and Northwest Territories; and*
> *(b) to the legislature and government of each province in respect of all matters within the authority of the legislature of each province.*[3]

The meaning of "Parliament" is relatively straightforward. The term "government" is much less precise and could be interpreted in a number of different ways. For example, government could encompass only the legislation, regulations and administration of Parliament and the legislative assemblies; more likely, it could also extend to Crown corporations, regulatory agencies and the judiciary. It could also be interpreted to include agencies and organizations that receive their funds from governments. It could even incorporate the contractual relationships of governments. While it seems clear that the drafters did not intend the Charter to apply to all aspects of private activity, there is a sizeable "grey area" where it is difficult to determine whether particular actions are "governmental", especially today, when governments act through a wide range of instruments and mechanisms.

The existence of a range of other plausible possibilities reflects the complex and pervasive interdependence of state, society and the economy noted throughout this Report. To define the extent of the term "government" is likely to be one of the most complex exercises in Charter interpretation. There is probably no one "correct" interpretation, but already there is a sizable literature offering various definitions and approaches.

The Supreme Court of Canada has attempted to come to terms with the meaning and scope of "government" in a number of past decisions. These approaches may usefully inform its definition of the term in reference to the Charter. No one seriously questions that the activities of a delegate of Parliament or of a legislative assembly will be covered by the Charter. With respect to the Charter, lower courts have upheld the general rule governing delegated authority: subordinates cannot do what their principals cannot do.[4] Similarly, the Supreme Court of Canada recently held that the term "government" includes regulation-making activities of various boards and

agencies, where these regulations are made subject to the approval of government.[5]

Other court decisions have distinguished between the public and private nature of an activity to determine whether that activity is rightfully considered a part of government.[6] By adopting such an approach, the court was able to conclude that a Crown corporation may be public in some aspects of its activities and private in others. This approach seems to Commissioners a flexible means of ensuring that the Charter has effect in the grey areas where public authority is exercised, as well as in the more visible legislative forums.

Commissioners believe that courts should take a flexible approach in determining whether an activity is governmental in nature, focusing in each case on the purpose of the specific actions in question. There are no firm rules to determine when private action becomes public action or vice versa. A "government-function test" would undoubtedly include within "government" such legislating bodies as municipal governments and school boards and such regulatory bodies as the Canadian Transport Commission and the Canadian Radio-television and Telecommunications Commission. It would not automatically cover the corporate and commercial activities of Crown corporations.

To determine when an actor is performing a public function is only part of the difficulty of defining the scope of government. There remains the matter of determining the amount of government involvement permissible in an activity before that activity becomes governmental – and thus subject to the Charter – rather than private. For example, if an organization of private interests receives funding from the government, should it be subject to the provisions of the Charter? Similarly, if an organization has a government contract to perform certain services, is that organization bound by the Charter, at least to the extent of its performance responsibilities under contract?

In Commissioners' opinion, infringement of rights may occur at the periphery of government involvement as easily and as often as in the more visible legislative process. A broad application would be a recognition that indirect governmental action may be as restrictive of individual rights as direct governmental action.[7]

Regardless of how courts interpret "government" in the context of section 32 of the Charter, Parliament and the legislative assemblies can use their authority as granting bodies and contractors to ensure that private organizations receiving public monies comply with the spirit of the Charter. Such compliance can be a component or condition of the funding or contract agreement. Using the approach known as "contract compliance", for example, a government can insist that firms doing business with it comply with specified hiring and personnel practices that conform to the spirit of the Charter. In such an instance, the firm would be complying with government regulations or policy and not with the Charter *per se*, and the government would have to establish appropriate enforcement mechanisms. The use of such compliance regulations could extend the spirit of the Charter and its guarantees to a wide range of activities.

Notes

1. Constitution Act, 1982, s. 52(1).
2. *Ibid.*, s. 24(1).
3. *Ibid.*, s. 32(1).
4. *McCutcheon* v. *City of Toronto* (1983), 147 D.L.R. (3d) 193, at 203.
5. *A.-G. Quebec* v. *Blaikie* (1981), 123 D.L.R. (3d) 15.
6. *Berardinelli* v. *Ontario Housing Corporation* (1978), 8 C.P.C. 100.
7. For further discussion see Mary Eberts, "The Equality Provisions of the Canadian Charter of Rights and Freedoms and Government Institutions", in *The Courts and the Charter*, vol. 58, prepared for the Royal Commission on the Economic Union and Development Prospects for Canada (Toronto: University of Toronto Press, 1985).

The Charter and Civil Liberties

The Charter enshrines in the Canadian Constitution several categories of rights and freedoms which can be divided into two broad groups: the traditional civil liberties of democracies and the rights concerned with problems of cohesion in the Canadian political community.

The first group includes four classes of rights enunciated in the Charter:

- Fundamental freedoms (s. 2) of conscience, religion, thought, belief, opinion, expression, association, peaceable assembly and freedom of the press
- Democratic rights (ss. 3–5) to vote and run for office and the guarantee of regular elections
- Legal rights (ss. 7–14) including, among others, the right to life, liberty and security of the person; the right to be secure against unreasonable search and seizure; the right not to be arbitrarily detained or imprisoned; the rights to be told promptly of reasons for arrest, to retain counsel, and not to be denied reasonable bail without just cause; the right to trial by jury, except in specified instances; and protection from double jeopardy
- Equality rights (s. 15) prohibiting discrimination, including discrimination based on race, national or ethnic origin, colour, religion, sex, age, or mental or physical disability.

In the traditional view, this group of rights is sometimes referred to as "negative freedoms": they protect and secure the freedom of individual citizens by limiting the power of government. There is, however, a major departure from this approach. The affirmative action provision accompanying equality rights permits governments to pursue programs to ameliorate the conditions of disadvantaged individuals or groups, even if these programs may violate the equality rights of others. We shall return to affirmative action below.

The "negative freedoms" approach was the dominant philosophy in Canadian thought on human rights before the 1970s. It gained particular prominence in the post-Second World War period and shaped the 1960 Bill of Rights. It was the main theme in most general and theoretical discussions of civil liberties. Attention focused above all on protecting the rights of citizens by seeking limitations on the use of discretionary power by the ever-expanding administrative state.

Since the 1920s, pockets of support for more stringent controls on government powers have developed across Canada. For example, the 1933 Regina Manifesto of the newly created Co-operative Commonwealth Federation (CCF) made a strong call for human rights protections against what it considered excessive police powers in specific sections of the Criminal Code and unjust procedures under the Immigration Act. The CCF called, also, for anti-discrimination legislation and affirmation of a Canadian commitment to the fundamental freedoms of speech, of association and of the press. In 1945, a CCF Member of Parliament introduced in the House of Commons the first motion proposing a constitutional bill of rights. It was the beginning of a long campaign to have a bill of rights included in the Constitution, with

guarantees for minority rights, equality rights, civil and religious liberty, freedom of speech, and freedom of assembly. In 1947, the provincial CCF government in Saskatchewan introduced the first comprehensive human rights legislation in Canada.

Parallel to this activity, during the Depression and the period of the Second World War, various bar associations across Canada expressed concern about violations of basic civil liberties. They were concerned primarily with violations of the so-called "economic rights": the right to choose the place and type of one's employment; to buy and sell available goods in the open market; to fix, or bargain for, prices; to import and export; to enter into or expand business; to be free of price control; and to lease and to terminate leases.[1] In 1943, the Canadian Bar Association established a Civil Liberties Section which prepared annual reports on various problems relating to civil liberties during the 1940s and began to consider a proposal for a Bill of Rights as the decade closed.

Public concern over the abuse of citizens' rights by government broadened with two events in the 1940s: the wartime treatment of Japanese Canadians and the secret conduct of spy trials. Japanese Canadians and other Orientals had experienced discrimination in Canada before the war, but after hostilities erupted with Japan in 1941, the Government of Canada, using authority under the War Measures Act, obliged Japanese Canadians living along the Pacific coast to surrender their lands, homes and property, and forced them to move to internment camps away from the coastal area. Later the federal government relocated many to other parts of Canada. Relocation programs lagged, and in 1945 the federal government announced that those who did not want to relocate could be voluntarily "repatriated" to Japan once such action became possible. As it became apparent that the decision to repatriate was not always "voluntary", and that it would apply to naturalized and Canadian-born citizens of Japanese ancestry, public support for the Japanese Canadians and outrage over the repatriation scheme led the federal government to rescind the order in 1947. The wartime treatment of Japanese Canadians has become a deep scar on Canada's civil rights record.

Secret orders-in-council and spy trials associated with the Igor Gouzenko affair in 1945 and 1946 also contributed to popular concern for the better protection of civil liberties and legal rights and provoked sharp criticism of the government's conduct. Using powers granted under the National Emergency Transitional Powers Act, the Minister of Justice was empowered to detain "in such place and under such conditions as he may from time to time determine" anyone whom he suspected of being likely to communicate secret information to a foreign agent. A number of arrests were made. The government did not lay charges at the time of arrest, held many of those arrested incommunicado, and did not advise them of their legal rights. Subsequently, a Royal Commission investigation, conducted *in camera* by two justices of the Supreme Court of Canada, led to charges against many of those arrested. When the public learned of the extraordinary nature of the procedures followed, the government was severely criticized. The Civil Liberties Section of the Canadian Bar Association argued that if Canadians tolerated such violations of basic civil liberties in peacetime, then "we [were]

. . . in grave danger of having substituted for the rule of law . . . the alien principles of the Totalitarian State."[2]

These two events contributed to growing concern about the protection of civil liberties in Canada, which culminated in the 1960 Bill of Rights. Although the War Measures Act authorized both events, the 1960 Bill did not curb the powers available to the Attorney General under that Act, except by requiring that Parliament debate any proclamation of the Act. The Charter of Rights and Freedoms makes no mention of the War Measures Act, though the courts are able to determine whether or not, in curtailing a guaranteed right or freedom, a proclamation of the Act meets the reasonable limitation test set out in section 1.

Support for more protection against the abuse of governmental authority grew during the 1950s also, as a consequence of events in Quebec. The courts determined that various pieces of Quebec legislation, directed primarily against activities of the Jehovah's Witnesses and the Communist Party of Canada interfered with such basic freedoms as freedom of religion, of assembly, and of speech. Moreover, in the much publicized case of *Roncarelli* v. *Duplessis*,[3] the Supreme Court of Canada determined that Premier Maurice Duplessis, acting in his capacity as Attorney General, had exceeded the authority of his office in violation of the fundamental constitutional principle of the rule of law.

Increasing awareness of the need to protect fundamental human rights was not unique to Canada during the post-Second World War period. The United Nations, formed at the end of the war, took steps to outline a model of human rights guarantees in the 1948 Universal Declaration of Human Rights and in a number of later conventions. Some of the momentum for a Canadian bill of rights and some of the ideas about what it should contain, were the product of a post-1945, world-wide, human rights movement and of Canada's desire to be an international leader in this field, as in other areas of international affairs. In 1950, the Special Committee of the Senate on Human Rights and Fundamental Freedoms (the Roebuck Committee) recommended that Canada adopt a bill of rights modelled closely on the United Nations Declaration.

After the Second World War, Canadians were redefining the basic symbols of the Canadian state in light of our continuing evolution from colony to nation. During debate on the Citizenship Act in 1946, for example, one MP noted that even if a bill of rights did no more than make explicit the traditions of liberty in parliamentary systems, it would be a symbol for all Canadians, and especially for new Canadians, of the norms and values of our country. An increasingly heterogeneous and ethnically diverse population no longer appeared able to rely on unwritten protections of civil liberties: a written code was needed.

Thus, when Parliament agreed to the Bill of Rights in 1960, the legislation reflected an idea whose time, in Canada, had come. The "negative freedoms" approach to civil liberties shaped the Bill, which guaranteed to citizens freedom from various forms of state action. The first two sections of this bill contained most of the guarantees of rights.

The first section established the continuity of its content with the existing practices and traditions in Canada:

> *It is hereby recognized and declared that in Canada there have existed and shall continue to exist . . . the following human rights and fundamental freedoms.*[4]

This section included equality guarantees prohibiting discrimination based on race, national origin, colour, religion or sex. The guarantees, limited to "equality before the law and the protection of the law",[5] were entirely consistent with the "negative freedoms" approach of this Bill, but they would seem inadequate to a later generation concerned as much with substantive equality as with procedural guarantees. Nonetheless, the Bill reflected the major equality concerns of its own day.

The second section of the Bill outlined guarantees of legal rights. An express declaration of Parliament could override these rights, but in the absence of such express declarations, the rights and freedoms outlined in the section would prevail. The protection of civil liberties under the Bill of Rights disappointed civil libertarians. With the major exception of the Drybones decision[6] in 1970, the Supreme Court of Canada was unwilling to elevate the Bill of Rights to a special constitutional status. As Supreme Court Justice Bora Laskin said in 1972:

> *. . . compelling reasons ought to be advanced to justify the Court . . . [employing] a statutory (as contrasted with a constitutional) jurisdiction to deny operative effect to a substantive measure duly enacted by a Parliament constitutionally competent to do so, and exercising its powers in accordance with the tenets of responsible government, which underlie the discharge of legislative authority under the British North America Act, 1867.*[7]

Even as the 1960 bill was being legislated, critics noted a number of weaknesses. The bill would apply only to matters of federal jurisdiction; even in the federal sphere, it had the status only of simple legislation and was not in any sense an entrenched or an overriding document. It explicitly permitted Parliament to legislate, notwithstanding its provisions. Some observers also foresaw major developments in human rights that would render the Bill of Rights inadequate almost immediately. In particular, some Canadians had begun to think that negative freedoms insufficiently guaranteed the rights of citizens. To limit the abuse of state power was necessary and desirable in a Bill of Rights; but it was necessary, also, to provide for means by which government could actively intervene on behalf of the rights of citizens and secure conditions which would allow all individuals to enjoy their rights. These views became increasingly popular, especially among members and activists in the civil rights movements of the 1960s.

The American civil rights movements of those years focused first on the rights of American Blacks, but as the movement developed, its message of equality was adapted to the interests of many other groups including women, the handicapped, young and old people, homosexuals, lesbians and others. Supporters of most of these movements wanted more than negative rights and freedoms. They demanded that government actively intervene to dismantle the obstacles to equality.

The Charter of Rights and Freedoms has moved Canada in this activist direction. While it continues to stress the traditional negative freedoms, it encourages governments to pursue greater equality for Canadians. For example, the guarantees of equality rights in the Charter enable governments to combat the underlying causes of discrimination more directly. The drafters of the Charter recognized that social and economic conditions can prevent enjoyment of equality rights; they believed that the freedom and rights of citizens require positive interventions of government, as well as the traditional negative freedoms.

The equality rights in the Charter (s. 15) expand on earlier equality provisions in two obvious ways. The provisions reflect a broad concern with the social and economic origins of inequality. The bases of discrimination specifically prohibited in the Charter – race, national or ethnic origin, colour, religion, sex, age or mental or physical disability – are not exhaustive; there is also a general guarantee of individual equality. Moreover, the guarantees of the Charter add "equality under the law" and "equal benefit of the law" to the equality categories previously found in the Bill of Rights. The equality rights guarantees are perhaps the most dramatic example of changed thinking on fundamental human rights since 1960, but similar patterns of change are also found in the other civil liberties of the Charter. This is true, for example, of the legal rights provisions, contained in sections 7 to 14.

Section 7 of the Charter, which begins with a general statement of legal rights, and which acts as an umbrella provision for the detailed sections that follow it, states that:

> *Everyone has the right to life, liberty and security of the person and the right not to be deprived thereof except in accordance with the principles of fundamental justice.*

Like other provisions of the Charter, this section deals, in constitutional terms, with relations between citizen and state. By setting out broad rights to "life, liberty and security of the person", the Charter underlines a fundamental value of Canadian society. The addition of "the right not to be deprived thereof except in accordance with the principles of fundamental justice" addresses vital issues of particular significance to criminal procedure. The phrase "principles of fundamental justice", which appears both in section 2 (*e*) of the Canadian Bill of Rights, and in the Charter, is designed to safeguard the right to a fair hearing, to notice of proposed charges, to present one's case before an impartial tribunal, and to cross examination. The drafters believed that a free and open court system based on adversarial testing of propositions and evidence designed to arrive at the truth is central to a free and democratic society. Such a system is an attempt to restrict possibilities for arbitrary action by the state.

In Canada, criminal law is the legislative responsibility of the federal government; criminal law is largely found in the federally-enacted Criminal Code of Canada. The provinces are responsible generally for the administration of justice, including criminal justice, within their own borders. The courts supervise the criminal-justice system to ensure its proper functioning, and impose rules for this purpose. The best known of these, the Judges' Rules,

contain conditions laid down by the British judiciary for procedures to be followed by police forces when taking statements from suspects.

The Canadian Bill of Rights continued the process of codifying both judge-made or "common" law and the principles implicit in the Criminal Code. Because of federal responsibility in this area, the fact that the Bill of Rights did not extend to provincial jurisdictions was not as important as it was for other guarantees of rights and freedoms. Thus the Charter's provisions concerning legal rights come from a long history of judicial interpretation and legislative enactment. The complex judicial evolution of the legal rights provisions in the Bill of Rights suggested the need for detailed provisions in the Charter.

The specific provisions contained in sections 8 to 14 of the Charter are designed to parallel the operation of the criminal process. Section 8 ("search or seizure") and section 9 ("detention or imprisonment") apply to citizens under investigation; section 10 relates to "arrest or detention"; and section 11 covers those "charged with an offence". Section 12 is a sentencing provision. Finally, two provisions applicable to witnesses round out the legal rights: section 13 provides that a witness, in giving evidence, cannot be incriminated in a subsequent proceeding, and section 14 provides interpretation facilities where a party or witness does not understand the language of the proceeding.

While the bulk of the legal rights provisions apply to the criminal-justice system, they are also important in other areas where citizens are subject to official control or regulation. For instance, while the definition of crime is a federal responsibility, provinces and municipalities impose sanctions in fields from securities law, where a penalty provision may include imprisonment, to parking offenses, where the $3 penalty is not yet extinct. The Charter now subjects proceedings related to these offences to the same legal rights that the Bill of Rights previously guaranteed for offences under the Criminal Code. Similarly, protection from "cruel and unusual treatment or punishment" is extended to the actions of a wide number of provincial institutions. Thus, for example, provincial mental health legislation, hospital acts, or procedures established for patients confined against their will may also be scrutinized by the courts in light of the Charter.

These legal rights provisions are designed as much to influence the administration of justice as to strike down or limit legislative initiatives. The administration of justice is the responsibility of the provincial Crown prosecutors as well as of the federal prosecutors, but legislative responsibility in criminal matters resides squarely with the federal government. To the extent that provincial behaviour in administering the law is governed by federal legislation which the provinces cannot amend, a province cannot alter its behaviour without the legislative support of the federal government. Thus, although the Charter's general override clause applies to the legal rights provisions, opportunities for provincial variations in criminal procedures are limited.

In the area of police powers, good administration and law enforcement necessitated a statement of direction to the criminal-justice community. Section 24(2) states:

Where, in proceedings under subsection (1), a court concludes that evidence was obtained in a manner that infringed or denied any rights or freedoms guaranteed by this Charter, the evidence shall be excluded if it is established that, having regard to all the circumstances, the admission of it in the proceedings would bring the administration of justice into disrepute.

In the course of an investigation, the police or the Crown may use inappropriate techniques and thereby obtain evidence that would not otherwise have been obtained. In what circumstances should evidence so obtained be admissible against an accused person? What is the appropriate sanction for activity that the court finds to be inappropriate?

The American "forbidden fruit" doctrine ruled that such evidence and all that flows from it are inadmissible in the courts. Thus juries do not hear a statement or confession that would otherwise be admissible or see physical evidence collected as a result of the statement. Suppose the police in Canada use a wiretap without appropriate authorization under the Criminal Code. In the conversations they record, they hear about the movement of drugs and thus effect an arrest. They have both oral evidence of a conspiracy and physical evidence at the time of the arrest. Fundamental policy choices arise in this situation. Should this evidence be admissible? If it is not, the suspects would be released; if it is, the courts appear to condone unlawful activity by agents of the state. Should a suspected felon be freed to compensate for the errors or wrongdoing of police personnel? The Charter gives judges considerable scope to control unacceptable police behaviour.

Legal rights will evolve within the general framework of the Charter, and it will be recalled that section 1 provides that both laws and actions that are demonstrably justified in some circumstances can be found valid despite apparent inconsistency with the Charter. However, the legal rights provisions themselves contain qualifications similar to those found in section 1. Phrases such as "principles of fundamental justice", "unreasonable search or seizure", "arbitrarily detained or imprisoned" or even "informed promptly" give the courts the responsibility to flesh out the evolving meaning of these standards.

The evidence rule outlined in section 24(2) and the internal qualifications in the legal rights guarantees require courts to consider the actions of the prosecution to ensure that in specific circumstances, an appropriate balance has been reached. These qualifications do not relate only to unreasonable laws, but to unreasonable activity. That is their principal thrust.

Notes

1. See Walter S. Tarnopolsky, *The Canadian Bill of Rights*, 2d ed. (Toronto: McClelland and Stewart, 1975), p. 5.
2. Canadian Bar Association, *1946 Proceedings* (Toronto, 1946), p. 144.
3. *Roncarelli* v. *Duplessis* [1959] S.C.R. 121.
4. Canada, Parliament, *Canadian Bill of Rights: An Act for the Recognition and Protection of Human Rights and Fundamental Freedoms* (Ottawa, 1960).
5. *Ibid.*
6. *R.* v. *Drybones* [1970] S.C.R. 282.
7. *Curr* v. *The Queen* [1972] S.C.R. 889, at 899.

The Charter, National Cohesion and the Canadian Community

The Charter contains some guarantees of rights best understood as efforts to promote social cohesion and national unity. The provisions in this group of rights are closely associated with the social role of the modern state as Commissioners have previously described it: that is, the task of representing and reconciling cultural, linguistic, territorial and other facets of our diversity. This broad group of rights in the Charter includes language rights, minority-language/education rights, mobility rights and the guarantee that the Charter is to be interpreted in a manner consistent with the preservation and enhancement of our multicultural heritage. These guarantees do not focus exclusively on individual rights. Though this remains a primary concern, these rights have profound implications for Canadian federalism and for relations between the national and provincial communities. This is particularly true of the minority-language/education and mobility rights.

Discussions during 1980–82 on these "national community" guarantees often seemed more a political tug-of-war between two levels of government than a discussion of the rights of citizens. The debate reflected that governments were quite naturally concerned with the consequences of the Charter's provisions for their jurisdictional authority, that the Charter was the centre-piece of the federal government's promise to the people of Quebec of "renewed federalism", following the Quebec referendum, and that inclusion of mobility rights was central to federal proposals for securing the economic union.

In the process of negotiation, the proposals were significantly altered. The provisions in the Charter reflect compromises and concessions. Federal-provincial relations and the issues of unity in the federation preoccupied Canadian politicians in the early 1980s and affected the Charter. Provisions of the Charter that relate to communities and national cohesion will illustrate the point. Commissioners will consider first the provisions respecting official languages and cultural groups and then turn to mobility rights.

Official Languages and Minority-Language Education

The Charter's guarantees for language rights and minority-language education are found in sections 16 to 23. In effect, sections 16 to 21 give constitutional status to parts of Canada's official languages legislation and to that of New Brunswick. Residents of Canada have the right to communicate in English or French with the federal government, to receive services in either official language where there is significant demand, or where it is reasonable for such services to be provided, and to use English or French in Parliament and in all courts of law under federal jurisdiction. Governments may expand, but not diminish, the rights guaranteed in the Charter.

Section 22 affirms that the language guarantees in the Charter do not abrogate or derogate "from any legal or customary right or privilege acquired or enjoyed before or after the coming into force of the Charter with respect to any language that is not English or French." However, the most significant

new language right created by the Charter appears in section 23. The Ontario Court of Appeal has suggested in a recent judgement that section 23 "creates a code which establishes minority language education rights for the nation."[1] Section 23 confers two rights:

- Parents who qualify under section 23 have the right to have their children receive publicly funded primary- and secondary-school instruction in the minority language of English or French wherever the number of children of such citizens warrants.
- Parents who qualify under section 23 have the right to have their children receive that instruction in English or French minority-language educational facilities provided out of public funds, again, where the numbers of children warrant.

Court judgements to date suggest that the number of parents required to make these provisions operational will vary from area to area within Canada.

There are three main criteria by which citizens can qualify for minority-language/education rights. Under section 23 (1)(*b*) the so-called "Canada clause", the children of Canadian parents whose primary-school instruction in Canada was in English or French have the right to receive their primary and secondary school instruction in the corresponding language if they live in a province where speakers of English or French form the linguistic minority. The brothers and sisters of children educated in English or French in Canada also have the right to primary and secondary instruction in the corresponding language. Canadian citizens also qualify for these rights for their children if their own mother tongue, the first language learned and still understood, is English or French. This last provision will not take effect in Quebec, however, until the National Assembly or the Government of Quebec authorizes it. This special provision for Quebec was part of an effort to accommodate the concerns of the provincial government on the future of French in Quebec, in return for the province's support for the package of reforms as a whole.

The rights expressed in section 23 pertain to individual citizens who live in a community with a significant number of others who have as their mother tongue the same minority official language. The courts must establish criteria for determining "where numbers warrant". Thus the continuing availability of this right will probably depend on the existence of appropriate concentrations of those speaking a minority official language. The number of children in any particular area may, in the future, fall below that needed to meet the "numbers" requirement. Courts may then conclude that public authorities in such areas no longer need to provide minority-language education and people who have become accustomed to these facilities may find them no longer available.

The section on minority-language education in the Charter confers positive rights. It requires governments to provide publicly funded facilities and/or instruction, where circumstances warrant, rather than merely permitting them to take action. Significant efforts to give expression to these rights in the federal arena date from the publication in 1967 of Book I of the Report of the Royal Commission on Bilingualism and Biculturalism. The Commission

recommended a number of steps, constitutional, legislative and policy-related, to enable the English- and French-language communities to co-exist and flourish in Canada.

Federal Official Language Legislation and Policies

Almost immediately after the tabling of the Report of the Royal Commission on Bilingualism and Biculturalism, the federal government adopted many of its recommendations. In 1969, Parliament passed the Official Languages Act, the first of a recent series of federal laws and programs to foster better relations between Canada's two major linguistic groups and promote linguistic equality in Canada. The Act improved on the British North America Act of 1867 by declaring English and French "offical languages", and by extending language rights to the activities of the Government of Canada generally and not just to those of Parliament. Henceforth the public had a right to communicate with, and to receive services from, federal departments, agencies, courts and Crown corporations in either official language.

To oversee implementation of the Official Languages Act, the government, in 1970, established the office of the Commissioner of Official Languages. The office has construed federal language policies broadly:

> *The whole purpose of the federal language effort is to resist the blandishments of a Canada split along language lines. The fundamental objective is to construct a society in which the minorities can expect to live much of their lives in their own language.*[2]

The federal government directs its language policies both at the federal public service and at Canadian society as a whole. In the federal public service, it has sought equitable participation of the two major linguistic groups, availability of government services in the two official languages, and establishment of both French and English as languages of work in the federal public service.

The proportion of francophones in the federal public service increased from 13 per cent in 1974 to 27.5 per cent in 1983, a figure roughly equivalent to the percentage of francophones in Canadian society. Areas of the country with a small francophone population, however, have very few bilingual public servants. In the four Western provinces, there were 50 000 federal public servants in 1983. Fewer than 800 of these were qualified bilinguals in designated bilingual positions serving approximately 185 000 francophones in the region.[3] The provision of federal services in French in those provinces suffers. Francophones are also underrepresented at different ranks and in different kinds of activities in the public service.

Failure to achieve an appropriate nation-wide distribution of bilingual public servants means that Canada remains a country divided along linguistic lines. Research suggests that the federal public service reflects a country divided into three groups: a Quebec group primarily French, but offering bilingual services; a narrow "bilingual belt" where services are provided in both official languages from Moncton, New Brunswick, to Sault Ste Marie,

Ontario, and anglophone Canada, where services are largely available in English only. The figures parallel the distribution of francophones in Canada: 80 per cent live in Quebec, and most of the remainder live in the Moncton-Sault Ste Marie bilingual belt.

Federal policies on language of work aim to allow official-language minorities a more natural, less restricted choice of working language in the federal administration. In practice, the goal remains elusive. Outside Quebec and the National Capital Region, French is rarely a language of work on a day-to-day basis. Setting up an infrastructure of "bilingual documentation" and "bilingual occupants of bilingual positions" has not made people feel free to work in whichever language comes most naturally. Data for 1981 released by the Treasury Board show that in internal communications in bilingual regions, anglophones use French 18 per cent of the time, while francophones use English 47 per cent of the time. In spite of the relatively low use of French by francophones, Treasury Board data show that francophones are relatively more satisfied than anglophones (72 per cent as compared to 49 per cent) with existing proportions of language use among public servants in bilingual positions. These data prompted the Commissioner of Official Languages to wonder whether "the question might reasonably arise whether we should leave well enough alone. In other words, is it not paternalistic to suggest that Francophones should want to use more French, despite apparent affirmations to the contrary?"[4]

The bilingualism program in the public service has had considerable success. In 15 years the participation rate of francophones has risen compared to their proportion of Canada's population, the number of bilingual anglophones has increased dramatically, and availability of bilingual public services has increased in some areas of our country. It is equally clear, however, that our bilingual goals for the federal public service remain elusive outside the limited bilingual-belt area; the language-of-work policy has had even more limited success.

The federal government also directs its language policies at the broader Canadian community. The objectives of these programs are to promote bilingualism among Canadians, to enhance and preserve minority official languages, and to foster an appreciation among all Canadians of the equal status of our two official languages. It is not Commissioners' purpose here to review these programs, but a brief comment on the program that the former Commissioner of Official Languages has called "a Canadian success story of the first order"[5] illustrates the rapid progress of bilingualism among anglophones.

According to one American authority on language acquisition:

> *Canadian immersion is not simply another successful language teaching programme – it may be the most successful programme ever recorded in the professional language-teaching literature.*[6]

Realization by anglophone Canadians of the economic and other benefits of bilingualism and widespread availability of the programs account for the popularity of French-immersion education in our country. Registration in these programs has grown phenomenally, and the number of schools offering

French immersion has increased by leaps and bounds. From 1977–78 to 1984–85, the number of schools offering French immersion programs increased by over 300 percent from 237 to 988. Total enrolment for 1984–85 is approaching 150 000.[7] Enrolment is still concentrated in the early grades, though there is a recent trend toward high-school immersion. Each year the size of the entering group grows.

Over the past decade, the federal government has encouraged several provinces to become officially bilingual. It expressed the hope that other provinces, particularly Ontario, would follow the example of New Brunswick, which declared a provincial Official Languages Act in 1969. Despite provincial support for immersion programs and minority-language education, as well as initiatives by provinces such as Ontario to increase bilingualism in the provision of public services and enhance French in other aspects of daily life, no province other than New Brunswick has so far passed, on its own initiative, legislation making French and English the official languages of the province.

While official bilingualism requires a supporting legal framework, bilingualism is not a matter simply of language laws. Recent public opposition to bilingualism in Manitoba and New Brunswick is a reminder that bilingualism policy in Canada can be set back by negative public reactions. It is therefore encouraging to note the public pressures for, and the positive responses of parents and children to, government-provided immersion facilities that will help to overcome language barriers. Yet much remains to be done. There must be further sustained effort to secure Canada's two official languages throughout the public service. Commissioners believe that it is important to consolidate the progress of the past and to continue to build on existing foundations. Our history, as well as more recent events, indicates that continued government leadership is essential.

Legislative and policy initiatives tell only part of the story of attempts to promote bilingualism and official language policy across Canada. The new constitutional rights to minority-language education and constitutional recognition of the two official languages, are central components of federal efforts to preserve and enhance official languages across our country.

Federal Constitutional Initiatives respecting Language since 1968

Since the Royal Commission on Bilingualism and Biculturalism recommended changes to the British North America Act, the federal government has advocated constitutional recognition of official languages and minority-language/education rights. That Commission recommended that section 93 of the British North America Act be amended to provide that:

> *Every province shall establish and maintain elementary and secondary schools in which English is the sole or main language of instruction, and elementary and secondary schools in which French is the sole or main language of instruction, in bilingual districts and other appropriate areas under conditions to be determined by provincial law; but nothing in this section shall be deemed to*

prohibit schools in which English and French have equal importance as languages of instruction, or schools in which instruction may be given in some other language.[8]

Elsewhere in its Report, the Commission argued that parents should be free to choose the official language in which their children would be educated, and that this instruction be publicly funded where numbers warrant.

In a 1968 white paper, *A Canadian Charter of Human Rights*,[9] Justice Minister Pierre Trudeau proposed that the recommendations of the Commission be entrenched in a constitutional bill. A year later, as Prime Minister, he elaborated. Language rights, he said, were individual rights that should be guaranteed to all citizens no matter where they live in Canada. Language rights, like other human rights, were essential protections for individual citizens, both in their relations with governments and in their relations with one another.[10] Following publication of the Report of the Royal Commission on Bilingualism and Biculturalism, the Government of Canada proposed to entrench language rights and minority-language/education rights. Its position remained essentially unaltered throughout the 1970s.

There was a gradual movement away from the philosophy of universal free parental choice, caused by events in Quebec in the 1970s and the efforts of successive governments in that province to stem the declining use and status of French among Québécois. Acting on the recommendations of the provincial Commission of Inquiry on the Position of the French Language and on Language Rights in Quebec (Gendron Commission, 1972), in 1974 the provincial government of Robert Bourassa declared French the sole official language of the province. This declaration was not welcomed by the federal government, which was encouraging the provinces to move toward bilingualism. Moreover, in an attempt to steer immigrant children into French schools, the Quebec legislation restricted access to English-language education to those with demonstrated fluency in English.

With the election of the Parti québécois and the introduction of the French Language Charter (Bill 101) in 1977, Quebec's policy diverged even more decidedly from that of the federal government. In addition to declaring French the sole official language, the Quebec Charter declared that French would be the only language of official record in the National Assembly, that judgements rendered by Quebec courts would be in French, and that the French text of legislation would be the sole authentic version. Other parts of Quebec's French Language Charter dealt with matters affecting the use of French at work and in daily life.

Quebec's French Language Charter also stipulated that with certain limited and temporary exceptions, only children with at least one parent educated in English in Quebec would be admitted to English-language public schools, unless a reciprocal agreement was established with other provinces to guarantee access to French schools for students whose mother-tongue was French. In 1979, in St. Andrews, Nova Scotia, Canadian provincial premiers, at their annual meeting, agreed among themselves to establish such a reciprocity (the St. Andrews Accord). However, the "Canada clause" provision in the Charter of Rights superseded this Accord, establishing access

to minority-language instruction for the children of citizens qualifying under section 23 of the Canadian Charter.

These developments in Quebec during the 1970s, from the Gendron Commission Report to the Parti québécois's language legislation, had inescapable consequences for the federal government's language policy. Quebec's language legislation reinforced the federal government's resolve to protect French-language communities outside Quebec. The demands of Quebec's anglophone minority for the protection and security of its language demonstrated that English- as well as French-language minorities in Canada were seeking guarantees. It was clear, however, that the Quebec government would not accept universal free parental choice, which it believed, worked disproportionate hardships on the future of the French language in that province.

The provisions for minority-language/education rights in the 1982 Charter represented a compromise for the Government of Canada. That government had moved away from universal free parental choice, which was replaced by the "Canada clause"; in addition, the clause affecting new Canadians was not to be enforced in Quebec without that province's consent. Quebec's government would not accept the proposal: it was convinced that education, including language issues, remained, and should remain, under provincial jurisdiction and not be subject to external criteria. It has still not assented to the Constitution Act, 1982. Nonetheless, these provisions of the Canadian Charter are now the basic law of the land, and have as much effect in Quebec as elsewhere in Canada. Recent court proceedings have found parts of Quebec's French Language Charter inconsistent with the Charter of Rights and have ruled that in cases of conflict the Charter of Rights will prevail.[11]

Multiculturalism

Section 27 of the Charter states that the entire document is to be "interpreted in a manner consistent with the preservation and enhancement of the multicultural heritage of Canadians." This section will probably moderate and control laws that are offensive to the principles of a multi-ethnic society and cultural tolerance. By specifying multiculturalism as a distinctive aspect of the heritage of Canadians, the Charter recognizes the contribution and needs of the many cultural communities of Canada.

As a policy objective, multiculturalism is a new goal in Canada. The settling of the Prairies by European immigrants in the early twentieth century, the use of Chinese labourers before that to build the Canadian Pacific Railroad, and the even earlier migration of American Blacks to Nova Scotia are all part of the popular mythology of Canada as a culturally diverse "mosaic". Yet, at the end of the Second World War, Canadian national institutions only weakly reflected Canadian dualism, and there was little recognition of ethnic diversity. In the post-war period, the climate of opinion encouraged changes in our collective self-definition as a national community. Extensive immigration after the Second World War may have made the transformation inevitable. Changes within Canadian society have brought

with them pressures to change the symbols of government and society to reflect the multi-ethnic composition of our national community.

The Royal Commission on Bilingualism and Biculturalism inspired contemporary federal policies of multiculturalism, just as it did the current approach to language policies. That Commission had not intended to devote much attention to the "other ethnic" aspects of its mandate, but after receiving strong representations from a number of ethnic groups, it devoted an entire book of its six-volume report to a review of the "third force" in Canada.

The federal government's concern with bilingualism helps to explain the timing of the policy of multiculturalism. Indeed, multiculturalism, introduced on the heels of the 1969 Official Languages Act, was the federal government's attempt to defuse some of Western Canada's criticism of the bilingualism policies. Nevertheless, to interpret multiculturalism only as a means to secure broader support for bilingualism, as some Canadians have done, is to miss other important matters. In fact, the policy of multiculturalism corresponded to several interrelated developments. The changing character of Canadian society after the Second World War brought a partial informal redefinition of the nature of the Canadian community. Within that community, a reallocation of status among linguistic and ethno-cultural groups was under way.

The federal government intended its multiculturalism policy to form another element in that reshaping of society:

> *A policy of multiculturalism within a bilingual framework commends itself to the government as the most suitable means of assuring the cultural freedom of Canadians. Such a policy should help to break down discriminatory attitudes and cultural jealousies. National unity if it is to mean anything in the deeply personal sense, must be founded on confidence in one's own individual identity; out of this can grow respect for that of others and a willingness to share ideas, attitudes and assumptions. A vigorous policy of multiculturalism will help create this initial confidence. It can form the base of a society which is based on fair play for all.*[12]

The Royal Commission on Bilingualism and Biculturalism expressed the premise of the federal policy: "Man is a thinking and sensitive being; severing him from his roots could destroy an aspect of his personality and deprive society of some of the values he can bring to it."[13]

Within a few years of introduction of the new policy, however, it became clear that a gap had developed between stated objectives and results. Some critics saw public support to third-force cultural groups as no more than assistance to ethnic folklore, and they called multiculturalism a "song and dance" routine.[14]

To other critics, the policy appears to maintain cultural distinctiveness among Canadians who are, in fact, living together in one national community. Many members of ethnic groups in Canada fear being "locked in" by ethnic boundaries. As one multicultural group told this Commission, "Ethnic Canadians . . . came here to be Canadians." (Council of National Ethnocul-

tural Organizations of Canada, Brief, October 31, 1983, p. 3.) Another group, however, told us:

> *As long as we have a society where the most appreciated values are those of the dominant group, whether it is the Anglo-Saxon group or the Anglo-Celtic group, to the detriment of values and traditions that other groups can offer, then these minority groups will always suffer discrimination even though it may not be legislated discrimination or overt discrimination.*
>
> (Thunder Bay Multicultural Association, Transcript, Thunder Bay, October 17, 1983 [vol. 26], p. 5191.)

Commissioners believe that multicultural policy should preserve ethnic diversity without isolating the very groups this policy seeks to assist. It should permit all Canadians to preserve and enhance the culture and traditions of their heritage, but it should also be consistent with Canadian aspirations for greater individual equality.

To adjust to a multicultural society requires more than mere recognition and accommodation of diversity at the symbolic level. When multiculturalism involves racial diversity – as has been increasingly true of Canada – a pressing need can exist to confront and combat racism. For visible minorities, racism can be a source of day-to-day anguish. Canadians do not think of themselves as racist, yet considerable evidence suggests that ethnic minorities, and particularly some "visible" minorities, are victims of systemic discrimination in Canada. A number of recent studies show that some visible minorities experience severely limited economic and social opportunities, and that the underlying cause is lingering racism.[15]

It is unlikely that transformation of the symbolic order, affirmative action programs, and even the Charter's prohibition of racial discrimination will root out systemic discrimination. *Equality Now*, the report of the Special Committee on Visible Minorities in Canadian Society, contains 80 recommendations to combat racial discrimination. These include proposals to improve language training for immigrants, introduce voluntary affirmative action in hiring and promotion policies, amend Criminal Code provisions respecting hate propaganda, extend support for multicultural arts, and promote respect for the observance of various national days and holy days of different cultures. We Commissioners have not, in our research, addressed the issue of racial discrimination in the same depth as has the Special Committee. We can observe, nonetheless, that racial discrimination in Canada results in an unjustified and indefensible denial of the rights of some individual Canadians and a tragic waste of human resources. Efforts must continue to increase individual equality throughout the Canadian community.

Mobility Rights

Commissioners wish also to consider mobility rights as they relate to Charter provisions concerning national cohesion. The Charter contains the first constitutional expression of mobility rights for Canadians.

Section 6 of the Charter guarantees the right to every citizen of Canada to enter, remain in and leave Canada. This right is in accordance with the

provisions of the United Nations International Covenant on Civil and Political Rights, ratified by Canada in 1976. The section guarantees, also, the right of citizens and permanent residents of Canada to live and seek employment anywhere in the country. The rationale for mobility rights within Canada is based on two assumptions: that barriers to personal mobility inhibit operation of the Canadian economic union, and that common citizenship implies freedom of movement within the country, unrestricted by provincially or federally created barriers.

Subsection 3 of section 6 restricts mobility rights in two ways. It permits limitations imposed by laws or practices of general application in a province (such as ordinary rules of employment concerning health, qualifications and union membership), where such laws or practices do not discriminate primarily on the basis of past or present province of residence. In addition, it permits provinces to impose reasonable residency requirements as a condition of eligibility for publicly provided social services. Subsection 4 enables provinces to pursue programs intended to ameliorate the conditions of socially and economically disadvantaged individuals when the provincial employment rate is below the national rate.

Quite apart from its potential to limit the mobility rights of Canadians, subsection 4 employs the terminology of "rate of employment", for which data are unavailable. The "rate of employment" is not the converse of the unemployment rate with which Canadians are familiar, the statistics of which are published monthly by Statistics Canada. One cannot infer that the rate of employment in a province is 90 per cent on the basis of knowledge that the provincial unemployment rate is 10 per cent.

Statistics Canada does publish statistics on the employment/population ratio which represents the number of persons employed, expressed as percentage of the population 15 years of age and over. However, officials of Statistics Canada and of several provincial Departments of Labour are not confident that these statistics would be accepted by the courts, for constitutional purposes, as appropriate indicators of the "rate of employment". So far the courts have not had occasion to pronounce on the issue. Thus, three years after the Charter came into affect, Canadians lack common understanding of the data base required to provide operational meaning to a key clause in the Charter which affects citizens' rights.

It is possible that when the "rate of employment" is defined by the courts, particular provinces with above-average rates of unemployment which represent the politically visible figure that evokes public reaction, may also have above average rates of employment and thus will be precluded from using subsection 4. It is also plausible that when a case finally reaches the Supreme Court, different governments will prefer different definitions and will employ competing statistical analyses to support their positions. The general assumption that all legislation is an experiment with the future applies with particular cogency to subsection 6(4) of the Charter.

This subsection, when judically interpreted, could affect the mobility of significant numbers of Canadians. The actual number of provinces entitled to implement measures intended to ameliorate the conditions of socially or

economically disadvantaged individuals in the province will depend on the distribution among the larger and smaller provinces of rates of employment.

In the light of this potential problem, it is well to remember that the provinces supported the right of personal mobility in the constitutional negotiations that preceded the adoption of the Charter. They sought amendments to the federal government's proposal on mobility rights, not in order to undermine the general purpose of the clause, but rather to ensure that provincial governments did not lose the authority to manage their societies effectively. As Allan Blakeney, then Premier of Saskatchewan, explained:

> *While remaining committed to the maintenance and improvement of the Canadian Economic Union, provincial governments must also accept their responsibility for providing economic opportunity to Canadians residing within their province.*[16]

A number of conditions limit the ability of provincial governments to override the mobility clause. Section 1 of the Charter, the "reasonable limitations" clause applies to provincial schemes for preferential employment. It stipulates that all restrictions on the rights and freedoms guaranteed by the Charter must be reasonable and demonstrably justified in a free and democratic society. Provincial laws, programs or activities must be directed at those who are "socially or economicaly disadvantaged." In provinces with below-average employment rates, programs may give certain preferences to residents meeting specific qualifications, but they must not impose blanket prohibitions of mobility. Perhaps most significant, from the perspective of the Canadian economic union, the provisions on mobility rights are likely to be most effective in the provinces where they are most needed: those where there is a greater chance of obtaining employment.

Commissioners believe that the courts will probably assume an important role in administering the mobility-rights guarantees. In so doing, they will become deeply involved in the task of reconciling national and provincial interests and citizens' rights. One observer has suggested that in determining the reasonableness of provincial actions limiting personal mobility, the courts will be obliged to balance the interests of the national community against the more particular interests of the local community:

> *There may then be no alternative to a balancing approach under which barriers to mobility will be unconstitutional unless the benefits created by their promotion of local interests demonstrably outweigh the burdens they impose on interprovincial mobility.*[17]

Commissioners also wish to note that even in circumstances where a province invokes its powers to limit the availability of mobility-rights guarantees, the federal government may still have considerable influence over the provision of mobility opportunities within that province. For example, the federal government might decide to prohibit mobility discrimination as a condition of provincial participation in programs that are jointly funded, or to attach comparable conditions to monies transferred to the provinces. However, the fact that limitations on mobility rights now have a constitutional status they

lacked before may make it politically more difficult for the federal government to secure contractual agreements overriding them. With respect to its own employees and employment practices, the federal government may, of course, establish its own practices, and possibly attach similar conditions to companies which work on federal contracts.

Notes

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16. Powers over the Economy, Opening Statements, Saskatchewan position presented at the First Ministers' Conference, Ottawa, 1980, Doc. 800-14/025, p. 2.
17. John B. Laskin, "Mobility Rights under the Charter", *Supreme Court Law Review* 4 (1982), p. 104.

The Charter and the Politics of Rights

The Charter provides new opportunities for the involvement of Canadians in public decision making. Based on its provisions, members of the public can question the actions of governments as they affect fundamental rights and freedoms of citizens. This is a new feature in the Canadian political process. Formerly the main judicial protections against legislated interferences with civil liberties and human rights were found in the division of powers. This division between the spheres of federal and provincial constitutional authority was often invoked to prevent one level of government from acting, even if such actions would be permissible if undertaken by the other level of government. Limited resort to the Canadian Bill of Rights was also available to protect rights at the federal level, as were less reliable arguments about an "implied" bill of rights in our parliamentary tradition which was also relevant to matters in provincial jurisdiction. More often, questions of fundamental rights violations simply were not raised before the courts.

Citizens now have a wide range of grounds from which to argue the violation of basic rights and freedoms. While the Charter selectively recognizes the supremacy of Parliament or the legislatures, this supremacy must be explicitly invoked by the legislatures either under the general override clause or under provisions qualifying mobility rights or permitting affirmative action programs. Furthermore, a court must be satisfied that the legislated schemes are reasonable and demonstrably justified. Thus the Charter provides important new opportunities for determining the limits of legislative authority.

During the three years that the Charter has been in effect, most of the visible action in establishing these limits has occurred in the judicial arena. Nonetheless, governments are already guided by the Charter in their day-to-day deliberations about new legislation and amendments to existing statutes and regulations. While the Charter may not appear to be in the forefront of the legislative process, it can never be far from the minds of the lawmakers.

As lawyers and their clients seek new interpretations and applications of the Charter in the courts, Canada will undoubtedly become a more litigious society. The Charter will also contribute to a greater consciousness of fundamental rights in Canada, among citizens and governments alike. In addition, the Charter may contribute to improving the democratic parliamentary process by providing a new incentive to discuss legislation fully, in terms of its implications for the rights and freedoms of citizens.[1] Thus, Commissioners believe that the Charter will alter the conduct of politics, both directly by bringing to bear on political decision making the spectre of judicial constraint and less directly by furthering the development of a political culture predisposed to review government actions from the perspective of the rights of citizens.

The Charter offers incentives to Canadian interest groups possessing the resources and the will to sustain costly and lengthy court proceedings. In the past, these groups have not made extensive use of constitutional litigation as a tactic in seeking to bring about a policy change. While various interest groups have challenged government regulatory policies sporadically, on grounds of federalism, there has been no Canadian parallel to the American interest-

group practice of initiating "test cases" supported by "legal defense funds". This lack is no doubt explained by the previous absence of significant constitutional prohibitions other than the federal division of powers, and the Canadian legal community's widely-held perception that policy making was not the proper business of the courts.

Some groups, however, have already begun to organize for such litigation. The recently established Legal Education and Action Fund for women is a good example. Its supporters hope that this fund, inspired by the successful example of the American Legal Defense and Educational Fund, Inc. of the National Association for the Advancement of Colored People (NAACP) and other similar programs in the United States, will ensure that women derive maximum benefit from the equality rights set out in the new Charter. This hope is premised on the belief that collectively supported efforts on behalf of women will be more effective than the individual legal initiatives women have undertaken in the past.[2]

Some groups and individuals will use the Charter to introduce issues to the political agenda and to advance particular causes in public proceedings. Is there a possibility that claims for entitlements based on the Charter will be over-used? Some may consider that the broad and general language of the Charter's principles provides almost unlimited possibilities for constitutional arguments across virtually all of public policy. Judicial decisions will contribute to setting limits to these possibilities and procedures, and the courts' early judgements will be crucial. But what will the public's attitude be toward use of the Charter? Will the Charter's emphasis on rights-based citizenship become the foundation for rights-seeking political behaviour?

Commissioners believe that the Charter will affect the ways Canadians think about and discuss politics. Over the past few decades, a popular language of citizens' rights has begun to emerge in Canada, and it has already affected political behaviour across a wide range of issues. In what ways, then, will the Charter's guarantees of rights affect the day-to-day political behaviour of citizens? Some analysts have argued that a strong tradition of rights seeking can erode the moral basis of a community and undermine considerations of duty and obligation. They suggest that the language of rights can lessen the willingness of community members to view their own rights in a balanced relationship to the rights of others and to the consensus underlying the community as a whole. In the broader context of the so-called "inflation" of human rights, one political philosopher has recently argued that rights-seeking behaviour and the advancement of rights claims on the basis that human rights are justified by natural law can disrupt the normal process of political bargaining and discussion:

> *Those who advance political claims under the aegis of human rights, believing that their causes are sanctified by the most powerful of all moral considerations, are in no frame of mind to negotiate ... Confronted by such massively heavy artillery, opponents of causes whose advocates invoke human rights are virtually compelled to resort to unduly heavy weaponry themselves ... The human rights perspective tends to extend political controversies beyond their plausible limits and thereby inhibits reasonable political debate.*[3]

Such a perspective does not depend on the legal or constitutional recognition of such rights; rather it presents essentially political claims as human rights. However, Constitutional recognition of a wide range of citizens' rights, many expressed in very general terms, can provide extra ammunition for those advancing such claims.

A seasoned federal public servant recently speculated about the challenges, as he saw them, of governing in a rights-seeking society:

> *The exquisite refinement of the overall field of human rights into a multitude of rights-seekers and rights-protectors has been a major development over the past ten years, and as the principal growth industry in government, rights have become a major preoccupation of public administrators . . .*
>
> *Canada is in danger of becoming a rights-ridden country . . .*
>
> *There is very little that can be done to contain the growth of the rights movement, given the difficulty of justifying opposition to any kind of right.*[4]

Commissioners do not wish to overstate the consequences of these developments. The Charter also expresses traditions of community values, and its tests of reasonableness and demonstrable justification clearly indicate that rights will not be extended on an unlimited basis. In the last analysis, however, only the citizenry itself can restrain the potential excesses of rights-bearing citizenship. The success of any charter of rights in enhancing the quality of citizenship relies at least as much on the degree of sophistication and responsibility that citizens bring to their use of the document as on its interpretation and enforcement by the courts.

In educating the Canadian public concerning their rights and freedoms, the Charter emphasizes the need for constant balancing between the reasonable and justified needs of the community and respect for the rights of its individual members. However, the Charter has clearly and appropriately shifted the balance in favour of the constitutional protection of the rights of citizens in their relations with governments. Certainly the benefits of this shift derive from an alert, fair-minded, and responsible citizenry, acting both individually and collectively in its political and legal affairs. It is good to be aware of the consequences that can follow when that trust is violated. But Commissioners believe that such awareness will reinforce Canadians' commitment to ground our community's future in the protected rights of individual citizens, and that it will strengthen the community as a whole. Similarly, such awareness will strengthen Canadians' resolve to protect and respect the rights of others and the collective needs of the community as a whole. Commissioners wish to emphasize that the Charter has provided a new defence for the protection of rights in Canada. Although the federal-provincial division of powers will remain important in some alleged violations of rights and freedoms, it will no longer bear the same responsibility. The Charter has placed protection of citizens' rights on a more independent footing in the Constitution.

Notes

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Equality Rights and the Charter

One of the recurring themes put forward at this Commission's hearings and a central message from representatives of women's groups, aboriginals, visible minorities and the handicapped was that Canada must work harder to become a society marked by more equality. Many of these groups challenged traditional notions of equality and outlined an interventionist role for governments in creating circumstances that would help individuals and groups to share the opportunities, benefits and burdens of Canadian society more fairly.

We Commissioners discovered at our hearings what is confirmed in the massive literature on equality: the understanding of equality has changed substantially at the popular level over the past few decades. The guarantees of equality rights recently incorporated in the Canadian Charter of Rights and Freedoms reflect many of these changes. The Charter-making process itself benefited from some of the most sustained and highly focused debates on equality ever to occur in Canada during the public hearings before the Special Joint Committee of the Senate and of the House of Commons on the Constitution of Canada.

There has been a significant shift in emphasis from procedural equality, that is equality before the law, to more substantive notions of equality. Many advocates of procedural equality hoped that prohibition of overt discrimination would secure equal opportunity. However, more and more Canadians have come to adopt the view that while removing procedural barriers is a necessary step towards equality, it is not a sufficient one. Social, cultural and economic conditions are obstacles to equal opportunity. In fact, many groups and individuals argue that equality includes not merely equal opportunity, but equal enjoyment of the outcomes and benefits of those opportunities. Notions of substantive equality address these concerns. The increased efforts of governments to combat the causes and effects of discrimination, and to ensure a more nearly equal distribution of the opportunities and benefits of Canadian society relate directly to this new concern for substantive equality.

By challenging traditional notions of equality, recent debates have forced reconsideration of some long-standing justifications for setting limitations on equality. Canadians have had to examine more closely common assumptions about inequality. During our hearings, we Commissioners heard that widespread social values and attitudes are at the root of persistent inequality in Canadian society, and that changing these values and attitudes should be an integral part of efforts to promote equality.

Equality has always been a powerful idea in democratic societies. The basic nature of any political community is reflected in its treatment of the issues associated with rights to equality. We Canadians can learn a great deal about the nature of our community by examining closely the guarantees of equality found in section 15 of the Charter. As with other powerful social ideas, however, equality is controversial, and the Charter's guarantees of equality will continue to provoke political debate and legal and political activity.

Guarantees of equality are only one part of the Charter. Interpretations of other sections of that document will affect the interpretation and application

of the equality guarantees. Of particular importance are the "reasonable limitations clause" (s. 1) and the "general override provision" (s. 33) which allows federal and provincial governments to override guarantees of equality.

Although section 15 sets out the Charter's basic equality rights, other sections may be directly relevant to the interpretation of the equality guarantees. For example, the sexual-equality guarantee of section 28 provides that: "Notwithstanding anything in this Charter, the rights and freedoms referred to in it are guaranteed equally to male and female persons." Section 28 applies to all rights covered in the Charter. Section 27, reviewed above, refers to the preservation and enhancement of Canada's multicultural heritage, while section 25 states that the guarantees set out in the Charter do not abrogate or derogate from any treaty or aboriginal rights pertaining to Native peoples. Sections 16 to 23 provide for the use of official languages and for minority-language education—cornerstones of equality programs for official language groups—and protect certain rights respecting other languages in Canada. In the absence of judicial interpretations of the Charter's equality guarantees, Commissioners can only speculate on their ultimate effect. We believe, however, that all of these provisions contain some signposts of the Canadian commitment to equality.

Section 15: Equality Guarantees

The guarantees of equality contained in section 15 of the Canadian Charter of Rights and Freedoms came into effect on April 17, 1985. The section reads:

> ***Equality Rights***
>
> *15(1) Every individual is equal before and under the law and has the right to the equal protection and equal benefit of the law without discrimination and, in particular, without discrimination based on race, national or ethnic origin, colour, religion, sex, age or mental or physical disability.*
>
> *(2) Subsection (1) does not preclude any law, program or activity that has as its object the amelioration of conditions of disadvantaged individuals or groups including those that are disadvantaged because of race, national or ethnic origin, colour, religion, sex, age or mental or physical disability.*

In effect, four guarantees of equality are presented in section 15(1): equality before the law, equality under the law, equal protection of the law, and equal benefit of the law. These four guarantees and the relevant provisions previously mentioned indicate that the constitutional order now embodies a very broad definition and concept of equality.

The guarantee of equality before the law is similar to that set out in the Canadian Bill of Rights. Our courts have interpreted the Bill of Rights as requiring equality in enforcement and application of laws. This guarantee is fundamentally important to procedural equality, but critics view its restriction to matters of procedure as a basic weakness. By 1982, there was a strongly perceived need to supplement this guarantee of procedural equality with rights of a more substantive nature.

The guarantee of equality under the law as stated in the Charter made clear that the guarantees of equality applied to the substance of legislation. Earlier the courts had interpreted equality before the law to apply only to the administration of the law. They had concluded that inequality in legislation itself was beyond the reach of the Bill of Rights. That interpretation severely limited the effectiveness of earlier guarantees of equality: it permitted legislatures to make distinctions on the basis of sex or race, or on other grounds, as long as the law was administered equally.

The guarantee of equal benefit of the law in the Charter avoids situations in which individuals could be deprived of basic legislative benefits. The new guarantee is intended to overcome unfortunate precedents. The Bliss case concerned a woman who had worked enough weeks to qualify for regular Unemployment Insurance benefits, but not long enough to claim maternity benefits.[1] Because her inability to work was the result of pregnancy, she failed to qualify even for regular Unemployment Insurance benefits. The court held that there was no denial of sexual equality: the discrimination was not between women and men, but between pregnant women and everyone else, a form of discrimination that was not prohibited. The court said also that the case had to do with benefits and that, in its opinion, the Bill of Rights did not contain a guarantee of equal benefits. Women's groups and others rejected this interpretation and fought successfully for the stronger guarantee now explicitly found in the equal-benefits provision of the Charter.

The right to equal protection of the law again echoes the Bill of Rights, although the latter guaranteed only the right to "the protection of the law". There has been little jurisprudence on this provision. An aspect of discrimination that may be encompassed by the equal-protection clause, but that is not included under the other guarantees is discrimination resulting from laws that appear to be neutral, but that have discriminatory effects. We shall review shortly the systemic discrimination that can result from these seemingly neutral practices.

Section 15(1) further states that these equality guarantees apply without discrimination and, "in particular", without discrimination on the basis of race, national or ethnic origin, colour, religion, sex, age, or mental or physical disability. The enumeration of some specific characteristics raises several questions. Can individuals complain about a denial of equality based on other grounds? If so, will the test for the validity of the challenged actions differ from the one applied in cases where discrimination on one of the enumerated grounds is alleged? For example, will the courts act against discrimination on the basis of age, which is enumerated in section 15, more stringently than against discrimination on the basis of sexual preference, which is not specifically mentioned? If there is such a scale, what is the principle for ranking the grounds?

The use of the phrase "in particular" in section 15 suggests that the list of grounds on which discrimination is prohibited is open-ended: while section 15 lists specific grounds on which discrimination is prohibited, this list is not exhaustive. If the courts follow the jurisprudence under the Bill of Rights, they will probably give protection on enumerated grounds. Will they treat non-enumerated grounds differently?

An individual arguing denial of equality rights on some ground not specified in section 15 might have to show that the specific ground deserves constitutional protection; such a requirement places an additional burden on the individual. The courts may prove to require substantial evidence before finding that legislation discriminates on the basis of non-enumerated grounds.

The courts will obviously be the central actors in establishing the application of section 15(1) of the Charter. But governments themselves can bring their own laws into conformity with the spirit of the Charter's provisions, especially where they become aware of discriminatory practices. Attitudes to equality change: one generation's idea of equality may seem discriminatory to the next. Where attitudes and understanding change beyond the established requirements of the Charter, governments, perhaps better than courts, can ensure that laws conform to the broad spirit and objectives of the Charter's guarantees.

Like the other rights guaranteed by the Charter, equality rights are not absolute. Some limitations on equality have received general support in the past: limits on various age groups, for example, in matters such as the age of majority, voting age and mandatory retirement. The equality guarantees in the Charter are subject to the general override power of legislatures, which means that governments can legislate notwithstanding the general constitutional guarantee of equality. The active constraint on governments in such instances is public opinion; in fact, governments need defend their actions in this regard before no other court. Where governments have not explicitly overridden an equality guarantee, the judiciary may itself consider whether a limitation is demonstrably justified, given the norms and traditions of a free and democratic society.

Thus two processes will shape the evolving meaning and scope of the Charter's equality guarantees. First, public opinion expressed through the political process may support recognition of new groups in terms of the equality guarantees, and will also condition the authority of governments to place restrictions on established equality rights through use of the general override provision. Secondly, judicial interpretation of the equality guarantees and of the justified limitations on equality in the context of a free and democratic society will have important effects.

The possibility of a scale of protected interests or grounds on which discrimination by governments is constitutionally prohibited will require further careful consideration. Some analysts have suggested that an approach developed in the United States may be useful. The equal-protection clause in the American Constitution does not enumerate specific grounds of prohibited discrimination. Thus, U.S. courts have had to determine, with reference to American history, which grounds are the most invidious and to devise standards to apply in scrutinizing offending legislation. Strict judicial scrutiny is usually applied to legislative distinctions based on race and nationality, for example. This means that the courts will strike down a law that discriminates on such grounds unless the government can demonstrate that it is pursuing a compelling end, and that the discriminatory classification is necessary to promote that interest. Where sexual discrimination is alleged, the courts have applied an intermediate test of scrutiny. Here, the discrimina-

tion imposed by a law must be substantially related to an important government interest, or else the courts will hold it to be an unconstitutional violation of the equality clause. The courts have devised a minimal-scrutiny test for legislation that discriminates on other grounds. Under minimal scrutiny, the American courts require simply that the classification rationally be thought to bear a relationship to a constitutionally permitted objective of government.

In Canada, the constitutional framework for the protection of equality differs from that of the United States. Our Charter explicitly provides that race, national or ethnic origin, colour, religion, sex, age, or mental or physical disability are worthy of constitutional protection. However, a legislative distinction based on age may not require the same degree of justification as one based on other enumerated grounds. For instance, there may be demonstrably justifiable government objectives related to distinctions based on age that would not be acceptable on the basis of racial classifications. The protection of children is a possible example. It appears to be possible within the framework of section 15 of the Charter and the general limitations clause contained in section 1 to recognize different degrees of justification.

Other sections of the Charter may affect the degree of constitutional protection accorded to members of a particular group. They may enhance or detract from protection relating to the classifications set out in section 15. The separate requirement that all the rights in the Charter apply equally to men and women (s. 28), for example, will probably strengthen the prohibition of discrimination on the basis of sex. Similarly, the guarantees of religious equality in section 15 may be strengthened by the general guarantee of freedom of religion as a "fundamental freedom" elsewhere in the Charter. Nevertheless, the constitutional protection given to denominational schools may restrict or qualify those rights. In addition, while section 15 guarantees equality without discrimination on the basis of age, the Constitution Act, 1867 places upper age limits on members of the Senate and members of the superior courts.

Thus we Canadians may not need to adopt the three levels of scrutiny developed in the United States, but our courts may require different degrees of justification for protecting various types of equality.

Equality and Ethnicity

As with the Bill of Rights which preceded it, the Charter prohibits discrimination on the basis of race and national or ethnic origin. Unlike the Bill of Rights, however, the Charter also outlines circumstances in which such distinctions become relevant for the rights of Canadians. It does so in the matter of language guarantees. While "national origin" and "mother tongue" are certainly not synonymous, the guarantees of minority-language education make distinctions among new Canadians largely, if indirectly, on the basis of their national origin, just as the guarantees also distinguish between Canadians who claim neither English nor French as their mother tongue and those who do.

The protection of aboriginal and treaty rights in the Charter may be a better example of the conflict that can arise between the equality rights of individuals and rights recognized on the basis of ethnicity. Sections 35 and 37 of the Constitution Act, 1982 and section 25 of the Charter recognize aboriginal and treaty rights. Some comments will illustrate the collective nature of these rights, and their potential conflict with the spirit of other sections of the Charter and with equality rights in particular. The Constitution Act, 1982 contains no directly comparable provisions for other groups.

In addition to recognizing and affirming aboriginal and treaty rights, section 35 of the Constitution Act, for the first time in Canadian history, recognizes Métis people, together with Indians and Inuit, as the aboriginal peoples of Canada. As amended following the Constitutional Conference of First Ministers in March 1984, section 35 guarantees all aboriginal and treaty rights referred to in this section equally to men and women. Through this amendment, section 35 now conforms with the Charter's provision of sexual equality. The innovative section 37 of the Constitution Act, 1982 provided for aboriginal participation in future discussion of constitutional matters that directly affect the aboriginal people of Canada. The consequent meetings were "a first" in Canadian history: in addition to the First Ministers, the leaders of major aboriginal groups attended.

Section 25 of the Charter provides that the Charter shall not be interpreted in a manner that abrogates or derogates from aboriginal rights. This section does not attempt to create new rights. As with certain other provisions in the Charter – those pertaining to language (s. 21) or to other rights not specified in the Charter (s. 26) – the function of section 25 is to ensure that the Charter does not diminish any rights and freedoms existing independently of it. As amended in 1984, section 25 provides that:

> *The guarantee in this Charter of certain rights and freedoms shall not be construed so as to abrogate or derogate from any aboriginal, treaty or other rights or freedoms that pertain to the aboriginal peoples of Canada . . .*

Several questions arise from the provisions on aboriginal rights in the Charter. Can section 25 be used to challenge existing laws that have limited or taken away treaty or land-claim rights? The courts will have to answer this question. More generally, how can, and how should, we balance the individual rights of all Canadians with the collective rights of some groups within the broader national community? Canadians as a whole will have to answer this type of question.

The dominant political culture in North America places great emphasis on the protection of individual rights and freedoms. In Canada, we can see that emphasis embodied in the 1960 Bill of Rights, in provincial and federal human rights legislation and, since April 1982, in our Charter. The aboriginal cultures, however, have a quite different emphasis. The 1981 Report of the Métis and Non-Status Indian Constitutional Review Commission, entitled *Native People and the Constitution of Canada*, states:

> *. . . the dominant socio-cultural system in Canada is liberalism which places emphasis on the individual, individual rights and private property. This is in*

contrast to the value system of Native peoples which places a far higher value on the collectivity or upon the community. It is ironic that non-Native Canadians, with all their liberal ideological baggage, cannot understand the significance to the Native peoples, or for that matter to any self-conscious minority group of being recognized as a collectivity. They do not realize that a cultural minority faces certain death by assimilation if the political system forces it to deal with the majority culture as individuals.[2]

It is from these different and, to a degree, conflicting cultural premises that problems arise in the protection of individual rights within the context of aboriginal communities.

When individual and collective rights conflict, which value system will prevail? Will it be the non-aboriginal Canadian society or the aboriginal community? What would happen if a member of a self-governing aboriginal community challenged that community's collective decision on the basis of his or her individual rights as enshrined in the Charter of Rights and Freedoms? Some analysts have argued that the purpose of section 25 is to ensure that aboriginal rights prevail over other provisions in the Charter.[3]

Aboriginal self-government, intended to provide protection for collective rights, introduces complexities for the protection of individual rights within the jurisdictional domain of aboriginal governments. Aboriginal organizations are particularly sensitive to this issue and recognize the need to balance individual and collective rights.

Some would argue that all individuals within aboriginal communities should be entitled to the full protection of the Charter and of the Canadian courts, that the Charter should apply within the jurisdiction of aboriginal governments as it applies within the jurisdiction of the federal and provincial governments, and that individuals should have access to independent appeal procedures. As Commissioners have argued in our section on aboriginal self-government, members of aboriginal communities should retain their rights as Canadian citizens. We view the Charter as contributing to a definition of Canadian citizenship. To exempt aboriginal communities from the individual-rights guarantees of the Charter would be to diminish fundamentally the citizenship of aboriginal Canadians.

The longstanding controversy over section 12.1.b of the Indian Act, which penalized Indian women who married non-Indian men by requiring them to forfeit their Indian status, demonstrated that these concerns about individual and collective interests are not simply abstract issues. They do arise in practice. Conflicts between collective rights, aboriginal rights and individual rights will arise; individuals living within aboriginal communities will appeal to external forms of protection. The manner in which such conflicts are resolved is integrally related to our sense of Canada.[4]

The multiple purposes of the Charter are the source of potential conflict between individual and group rights. The Charter not only encompasses the individual rights of Canadians, but it also addresses contemporary concerns about national cohesion. Earlier, Commissioners examined how the accommodation of provincial communities, both through the specific provisions respecting personal mobility rights and the general override

provision, may interfere with the mobility of individual Canadians and with other rights guarantees. We noted that over-use of these legislative powers could introduce so much variation across the country that the concept of individual rights in a national community could be undermined. We accepted that provisions for variation reflect the historic reality of the Canadian community and argued that recourse to these provisions will be moderated by the spirit of the Charter. The Charter recognizes certain fundamental rights and freedoms of Canadians in constitutional terms. This new status for citizens' rights requires that departures from stated constitutional norms be justified by those who have the authority to introduce such departures.

Commissioners believe that the provisions underlying the special status of various cultural groups in Canada can be understood on the same basis. The multicultural design of Canada, the official status of two languages, and the more recent official affirmation of aboriginal rights reflect deliberate choices worked out by the political process. Canadians value the cultural distinctiveness of our various ethnic communities, and we have self-consciously styled ourselves a country of immigrants; at critical points in our national history, we chose to develop as a bilingual nation, where mother tongue would carry certain special rights. Yet this celebration of group differences is at best only half of our personality. We are also a society of individuals, nurtured by the traditions of democratic liberalism. In such a society, one does not interfere lightly with the equality of citizens. Neither is the celebration of our group differences a justification for denying opportunities for individuals to develop their abilities to the full. Appropriately, section 15(1) of the Canadian Charter of Rights and Freedoms makes a broad and general guarantee of the equality of every individual and prohibits discrimination based on such grounds as race and national or ethnic origin. This is Canada's fundamental commitment to equality.

The Affirmative Action Clause

Section 15(2), a counterpart of section 15(1), protects governments from constitutional challenges in instances where they have taken positive action to rectify situations where groups are at a disadvantage because of past discrimination. Section 15(2) represents an exemption from subsection (1) where the object of a law, program, or activity is to ameliorate conditions of disadvantaged individuals or groups. This provision was included in the Charter to avoid problems which occurred in the United States when affirmative action programs were introduced. In a number of decisions, the U.S. Supreme Court ruled these programs unconstitutional. They were deemed to constitute a form of reverse discrimination contrary to the equal-protection guarantees. To avoid these problems, the framers of the Canadian Charter made it clear that any affirmative action program with the appropriate objective would be exempt from section 15(1).

Section 15(2) does not require that governments take affirmative action, although it is conceivable that the courts, through the remedies section of the Charter, could require that an affirmative action program be initiated in

order to remedy past discrimination. While the courts could do this, section 15(2) provides a valuable mechanism for governments to take initiatives toward the attainment of equality in Canada.

In an earlier chapter of this Report, Commissioners concluded that affirmative action is useful for achieving greater equality of opportunity and wage parity for men and women in the labour force. Affirmative action can also be used to combat discriminatory attitudes and to provide role models for disadvantaged groups. In recent years, it has become more popular as an instrument for combatting what is now commonly referred to as "systemic discrimination". The recent Royal Commission on Equality in Employment (the Abella Commission)[5] recommended mandatory affirmative action programs, both federal and provincial, for improving equality of opportunity for employment for women, the handicapped, visible minorities and Native peoples. Similarly, the recent Special Committee of the House of Commons on Visible Minorities[6] recommended the establishment of voluntary affirmative action programs to assist visible minorities to overcome systemic discrimination. In 1981, the Special Committee on the Disabled and the Handicapped[7] recommended that federal government departments, agencies, and Crown corporations expand or implement affirmative action employment programs for the disabled. In the past, this technique has also been used to promote the participation of francophones and Native peoples in the public service, as well as the participation of the disabled and of women.[8]

In this Commission's hearings, many groups and individuals spoke about various forms of systemic discrimination. This form of discrimination is invisible and often unconscious, having grown up over time and become embedded in our culture. It is different from overt discrimination, which manifests itself in clearly expressed prejudice. Overt discrimination occurs, for example, when a property owner says "I will not rent my apartment to a family on welfare," or an employer says "I will not hire a woman." This kind of discrimination is prohibited by law, and a victim of such prejudice can seek redress with Human Rights Commissions and through other legal protections. Systemic discrimination is of a different kind; it can operate unconsciously so that individuals may not be aware that their attitudes and behaviour systematically exclude or discriminate against some people. For example, seemingly neutral job requirements such as standards of height and weight may constitute a barrier to whole sections of society.

Systemic discrimination cannot be easily eliminated. To alter discriminatory attitudes and traditions involves changes in our public and economic institutions and practices, as well as in our personal lives. For instance, some participants in our hearings argued that to equalize employment opportunities for women requires that we, as a society, collectively change practices and attitudes toward family responsibilities, child care and the division of domestic work. It requires, as well, that we change early socialization and educational patterns by which we encourage one set of values for boys and another for girls. The Canadian Advisory Council on the Status of Women told us that the time has come for a re-examination of our societal attitudes and practices in these areas:

Education, adult training, community facilities, working hours, and support services for families with children must be re-examined to see how they are influenced by the stereotype of the traditional family, in which the woman devotes all her time to ensuring the well-being of the other members. These biases must be corrected, and we must change our social organization so that a mother can find the independence and financial security she needs in the labour market just as easily as a father can. The cooperation of all levels of government and the participation of all economic agents will be needed to bring about this transformation.

(Canadian Advisory Council on the Status of Women, Brief, November 30, 1983, p. 44.)

To be sure, there has been much progress on these matters in recent years, within families, in school counselling, in university-enrolment patterns and elsewhere. Public awareness of these matters is an important first step in the direction of greater equality. And in recent years, a growing number of community services and support networks have sprung up across the country to assist people who experience systemic discrimination. In our hearings, testimony abounded about the useful services these voluntary organizations provide. But these same intervenors were adamant that to rely on voluntary agencies and individual self-help is not enough. Active government involvement is required to eliminate systemic discrimination. There are several reasons for this.

First, the process would occur more quickly with effective government leadership. Without concerted government action, individuals continue to suffer the effects of discrimination for longer than is tolerable or necessary. In October 1984, the Report of the Royal Commission on Equality in Employment called for a "massive policy response to systemic discrimination".[9]

Secondly, as the Saskatchewan Action Committee on the Status of Women reminded Commissioners, the issue of equality is one which the whole of society must address:

The women's question . . . is one that needs to be addressed by all of us, not just women . . .

Women's issues, which basically are concerned with how we can operate on a basis of equality and independence in all aspects of society, have to be taken seriously, and it is our belief that this calls for nothing less than the restructuring of society, so that women, as society's largest minority, will have a chance to participate.

(Saskatchewan Action Committee on the Status of Women, Regina, Transcript, November 24, 1983 [vol. 5], pp. 10770–71.)

Failure to intervene can be regarded as tacit confirmation by government, and therefore by society as a whole, that we accept the existing patterns of discrimination. As the Abella Report argues:

If we do not act positively to remove barriers, we wait indefinitely for them to be removed. This would mean that we are prepared in the interim to tolerate prejudice and discrimination. By not acting, we unfairly ignore how inherently

invalid the exclusionary distinctions are, and we signal our acceptance as a society that stereotypical attributes assigned to these... groups are appropriate justifications for their disproportionate disadvantages.[10]

Finally, if groups or individuals have been disadvantaged in the past, it is not possible to make them equal simply by removing obstacles. For example, when the "separate but equal" doctrine relating to race and education facilities was declared an infringement of equal-protection guarantees in the United States, it did not immediately put Blacks on an equal footing. Years of discrimination, resulting in inferior education, meant that Blacks, on average, could not meet many job standards which were based on "white" educational norms.

The Canadian constitutional guarantee of equal protection of the law, combined with the affirmative action provision, allows governments to intervene against systemic discrimination. Section 15(2) of the Charter can serve as a mechanism by which governments can promote equality. In the first instance, such programs would have effect in the public service and throughout "government", as provided in the Charter's application section.

Although affirmative action is an appropriate means to combat many forms of systemic discrimination, we Commissioners do not wish to imply that it is a panacea for all disadvantaged persons. Affirmative action, as our review in the context of social security (Part V) indicated, is also not without costs to society.

It remains essential to retain and improve measures to equalize opportunities within, as well as among groups. For this reason, affirmative action proposals in labour markets are often accompanied by proposals to improve access to training and employment for the most disadvantaged members of a given sub-group.

A related policy difficulty is defining the disadvantaged group. Statistical categories can be very misleading. "Visible minority" may be one such category. Recent research indicates that on many scores – education, income, mobility, standards of living – there is a great variation among groups defined as "visible minorities". For example, male Filipinos (60 per cent) and Koreans (57 per cent) are much more likely to have attended college or university than Blacks (26 per cent) or Natives (17 per cent). Similarly, in 1980, the salary range of "visible minorities" varied widely: Canadian-born male university graduates of Japanese origin were likely to earn an average salary of $28 202 and their Chinese counterparts a comparable $24 370, in contrast to Canadian-born male university graduates of Indo-Pakistani origin whose average salary was $13 186. These data suggest that programs which do not distinguish among "visible minority" groups may not be directing benefits towards those who need them most.[11]

A further serious drawback to affirmative action – one that must continuously be weighed in the minds of legislators who introduce such programs – is that in favouring one group, they discriminate against another. The Charter permits this discrimination, and Commissioners believe that when a community decides to rectify the situation of its disadvantaged members, it is appropriate that such actions not be barred by the Constitu-

tion. Constitutional permission does not, however, resolve the difficult moral issue that must be faced: Does the desire for group-based equality of results justify the inevitable interference with individual equality of opportunity?

In some situations, systemic discrimination warrants the use of techniques such as affirmative action. Above all, however, Canada is a society committed to individual equality of opportunity. Short-term programs that interfere with this principle are acceptable only because Canadians believe that in the longer run, they contribute to genuine equality of opportunity for all citizens.

This Commission agrees that circumstances exist where inequalities are directly related to membership in some identifiable group within Canadian society. In such circumstances, steps can and should be taken to ameliorate the general conditions of inequality. We wish to emphasize, however, that equality ultimately applies to individual Canadians. The main redress for inequalities and the major emphasis on ensuring equality of opportunities for all Canadians should therefore be through government action in support of the individual as such, and not because he or she is a member of some particular group.

Notes

1. *Bliss* v. *Attorney General of Canada* [1979] 1 S.C.R. 183.
2. Métis and Non-Status Indians Constitutional Review Commission, *Native People and the Constitution of Canada* (Ottawa: Mutual Press, 1981), p. 2.
3. For example, Douglas Sanders, "The Rights of the Aboriginal Peoples of Canada", *Canadian Bar Review* 61 (March 1983), pp. 326–27.
4. For a more complete discussion, see Roger Gibbins and J. Rick Ponting, "An Assessment of the Probable Impact of Aboriginal Self-Government in Canada", in *The Politics of Gender, Ethnicity and Language in Canada*, vol. 34, prepared for the Royal Commission on the Economic Union and Development Prospects for Canada (Toronto: University of Toronto Press, 1985).
5. Canada, Royal Commission on Equality in Employment, *Report* (Ottawa: Minister of Supply and Services Canada, 1984).
6. Canada, House of Commons, Special Committee on Visible Minorities in Canadian Society, *Equality Now* (Ottawa: Queen's Printer, 1980).
7. Canada, House of Commons, Special Committee on the Disabled and the Handicapped, *Obstacles* (Ottawa: The Committee, 1981).
8. Canada, Public Service Commission, *A Report on Equal Opportunity Initiatives – PSC and Departments* (Ottawa, no date), Annex I.
9. Royal Commission on Equality in Employment, *Report*, p. 254.
10. *Ibid.*, p. 5.
11. For more discussion, see the argument of Conrad Winn, "Affirmative Action and Visible Minorities: Eight Premises in Quest of Evidence", forthcoming in *Canadian Public Policy*, from which the data on visible minorities are taken.

The Supreme Court of Canada and the Constitution: Institutional Implications

The Supreme Court of Canada faces demands on its decision-making capacity because of the federal character of our country, differing views on the limits of public action, the evolution of private law, and the introduction of the Canadian Charter of Rights and Freedoms.[1] A number of analysts believe that under the Charter, more policy decisions will be made by Canadian courts. Some, indeed, speak of the "politicization" of the judicial process, and suggest that we should anticipate its continuation. This process partly reflects the gradual "legalization" of society, for since the Second World War, more and more issues which have been drawn into the arena of public debate and conflict find their way to the courts for judicial resolution.

The demands made on the Supreme Court have implications for the structure and design of the judiciary. Commissioners do not believe that the institutional issues of the judiciary are a major national priority for reform. They are important, however, particularly as the role of the Court is seen to be expanding. In our brief review of the major issues, Commissioners wish to underline the need to be sensitive to the character of the judicial process and to the particular responsibilities of courts in our overall institutional framework.

Federalism, the Charter and the Composition of the Supreme Court

Conflicting views about the nature of Canadian society have often focused on the judicial process. Canadian federalism, involving two orders of responsible parliamentary government with overlapping jurisdictions, imposes on the Supreme Court of Canada obligations to decide constitutional matters. The abolition of civil appeals to the Judicial Committee of the Privy Council (JCPC), in 1949, meant the replacement of an external umpire by a Canadian tribunal appointed in accordance with a statute of the Parliament of Canada. At that point the Supreme Court assumed final responsibility for Canadian constitutional interpretation.

In the 1950s and 1960s, little constitutional conflict arose over the division of powers. In the 1970s, however, heightened intergovernmental conflict and increased reliance on regulatory powers greatly increased the volume of constitutional cases before the Court. Governments sought final resolutions or enhanced bargaining power, and private litigants tried to use the distribution of powers to constrain state intervention. On contentious matters, such as energy and constitutional reform, the Court's decisions have been of the highest importance. Inevitably, some observers have expressed concern about the legitimacy of the Court as a federal-provincial umpire. Could a court nominated by one order of government, they demanded, function as an impartial tribunal in division-of-power cases? Though studies of the Court's judgments since 1949 suggest that it has performed this difficult role in a balanced and sensitive manner, concerns of legitimacy continue to arise.

The Court's function in the federal system has given rise to various reform proposals, usually centred on the appointment process, and on the size and composition of the Court from the perspective of representation.

Regional representation was at the heart of most recent recommendations until the Charter of Rights brought new representational claims. At any given time since 1949, the Court has had no justices from five of the provinces and none from either territory. Since 1949, the Court has never included a judge from Newfoundland or Prince Edward Island, and for several decades did not include a judge from British Columbia.

Commentators have put forward claims for extended or more secure regional representation on the Supreme Court. If judges are selected from across Canada, the Court is more likely to be responsive to conditions and developments throughout the country. This argument supposes that a judge's connection with the law of a province or with regional conditions endues him or her with special knowledge of that region or province. This argument is an extension of concerns expressed by Canadians before 1949, when the JCPC in London served as the final court of appeal for Canadian law, including constitutional law. Such a regional pattern of judicial selection might better reflect the federal character of the Canadian Constitution and, it is argued, enhance the acceptability of decisions. Advocacy of this nature has been particularly extensive in recent years as a number of constitutional decisions of great significance to Canadian federalism have been placed in the hands of judges.

The suggestion that regional variations among the judges are important often meets with the reply that this regional quality is difficult to discern and even more difficult to bring to bear on the Court's decision making. Some observers have also criticized the suggestion because it takes no account of the differences within regions. British Columbians may wonder why, for Supreme Court purposes, they have been consigned to the same region as Alberta, Manitoba and Saskatchewan. Newfoundland does not have the same legislative, political, social or legal history as any of the Maritime provinces, yet most regionally oriented proposals would cluster all four provinces together for the purpose of selecting a judge. If geography and knowledge of local conditions actually are important factors in judicial decision making, then perhaps the appointments of justices from Quebec and Ontario should be geographically distributed throughout those two vast and internally diverse provinces. Perhaps members of the bench and bar from outside Toronto and Ottawa or Montreal and Quebec City, should be allocated seats on the Supreme Court bench.

Besides discounting intra-provincial differences, the regionalist approach to judicial appointments also tends to ignore judicial independence. The late Chief Justice Bora Laskin once remarked:

> *It saddened me that there was so little understanding manifested either about the nature of the Court's work or about the significance of the fidelity of its members to their oaths of office, so little appreciation of the importance of cohesion and collegiality in the dispatch of the Court's work. That work has no regional and, certainly, no political tie-in.*[2]

The Supreme Court deals "with national issues, with matters of general public importance that have no special regional connotation." The Court is a national institution, yet in a different sense from the Senate or the federal executive, upon whose actions it may sometimes be required to pass judgment. Furthermore, the argument in favour of emphasizing regional considerations in appointments may be weakened if the Court's role in deciding division-of-powers cases declines relative to its other responsibilities.

This Commission supports a view recently advanced by a leading student of the judicial process:

> *When we consider both the issues which the Supreme Court is called upon to decide as well as the nature of the adjudicative process, it is difficult to accept that the representation of regional interests either could be or should be prominent in the work of the Supreme Court. It seems very doubtful that there is a Western, or Atlantic or Ontario or Quebec position which must be articulated in the Court's deliberations if it is to make sound decisions on the subjects that are coming to dominate the Court's docket – namely, review of the federal administrative process, the interpretation of the Criminal Code and other federal statutes and disputes arising under the Constitution, including the Charter of Rights and the division of powers.*[3]

As the Canadian Bar Association Committee on the Constitution has pointed out, "A court is not a board of arbitration. It is a judicial body."[4] The members of the Supreme Court of Canada do not perform representative functions in the Canadian institutional and constitutional system. Judicial merit alone is the criterion by which the Court's membership and performance should be assessed. Accordingly, Commissioners reject arguments that the composition of the Supreme Court should be regionally representative. Existing provision in the Supreme Court Act for the appointment of Quebec members is based on the distinctive legal traditions of that province, and should be maintained.

Until recently, the Supreme Court's constitutional cases largely consisted of disputes or references about federal and provincial legislative jurisdiction. It was primarily in this context that relations between citizens and the state were adjudicated, although the Court did consider individual cases in relation to the Canadian Bill of Rights. The rise of Charter litigation will probably increase the number of cases involving citizen/state relations. In terms of successful motions for leave to appeal, Charter cases are already outnumbering other constitutional cases. This situation may give rise to new types of representational claims based on the social and economic characteristics of judges. Commissioners also reject these criteria for the selection of Supreme Court judges.

The Supreme Court Appointment Process

The process of appointment to the Supreme Court is frequently confused with the representation issue. That is, those who regard the Supreme Court as a representative body – a view Commissioners reject – also expect the appointment process to be representational. As new representational claims

are made, the appointment process is likely to emerge again as a subject of public concern. We attribute the current relative lack of interest in this issue, which was observable in our hearings, to the high quality of appointments that have been made under existing procedures. Whatever new process may be adopted – and we see no urgent need to replace the current arrangements – the judicial merit of appointees should remain the central criterion.

The chief issue in the appointments process is the perception that it does not adequately involve the constituencies of our political system. Although the existing informal procedures which the Prime Minister follows before he makes appointments to the Supreme Court do involve extensive discussions, some Canadians consider that they take too little account of concerned interests or advice. Numerous options have been put forward.

The *Report* of the Royal Commission on Constitutional Problems[5] (the Tremblay Commission), published in 1956, suggested that provinces should participate in the nomination of Supreme Court judges. The Victoria Charter proposals of 1971 contained a complex formula for securing the agreement of federal and provincial authorities concerning any appointment to the Court. It was recommended that the Attorney-General of Canada consult the Attorney-General of the province with which a potential appointee has the closest connection. If the two failed to agree on an appointee, the Minister of Justice would propose establishment of a nominating council; the choice among possible forms of this council would rest with the provincial Attorney-General. The body would consist primarily of the chief federal and provincial law officers or their nominees. The federal Minister of Justice would submit at least three names to the Council, from which it would make a recommendation. The Special Joint Committee on the Constitution in 1972 endorsed the consultative method set forth in the Victoria Charter, but questioned its failure to allow the provinces to nominate candidates.

Some of Canada's legal scholars favour a form of consultation or collaboration, such as a permanent nominating commission to be used, not just for the Supreme Court of Canada, but for all superior court appointments. The commission could consist of Members of Parliament and of provincial legislatures, representating all political parties, and including non-lawyers. It would maintain a list of suitable prospective appointees from which the appointing authority would choose appointees.

The Constitutional Amendment Bill, proposed in 1978, embodied the proposals of the Victoria Charter and took them one step further. It provided that after the Attorney-General of Canada and the provincial Attorney-General had agreed, or after the nominating council had broken the deadlock over an appointment, the nomination would then be submitted for ratification to a new "House of the Federation" which would replace the existing Senate and would be more representative of our federal diversities. The House would be required to affirm or reject the nomination within a limited time.

Ratification of Supreme Court appointments by a reconstituted upper house gained adherents during the constitutional debate of the 1970s. The Government of British Columbia favoured nomination by the federal government, after consultation with the provinces, and ratification by a reformed Senate. The Canadian Bar Association Committee on the

Constitution, the Pépin-Robarts Task Force on Canadian Unity,[6] and the Beige Paper of the Quebec Liberal Party[7] have made similar proposals.

An Alberta proposal specified that only the provincial governments would suggest appointees to the special constitutional panel it proposed. The Pépin-Robarts Report recommended that the federal Cabinet be required to consult with Quebec's Attorney-General before filling a civil-law vacancy. Where a common-law vacancy occurs, the Cabinet would consult all other nine provincial Attorney-Generals about possible appointees. The variety of suggested reforms is large, but all assume consultation or negotiation with a provincial Attorney-General or provincial representation in a reformed national upper house.

As Charter cases come forward in greater numbers, Commissioners would expect proposals for appointment procedures based on social and economic grounds, just as earlier proposals advocated intergovernmental arrangements. Because the Supreme Court adjudicates cultural, economic and social issues, new methods of selection might assess all "relevant" qualities of a potential appointee. In a research paper prepared for this Commission,[8] the authors discuss the possibility of an Appointing Council that would survey likely candidates and decide who should be named to the Court. Ideally, the Council's members would be diverse in vocational background, age, economic and social status, ideological orientation and racial, ethnic and regional origin. Instead of choosing judges according to region or other sociological criteria, the Appointing Council itself could reflect a cross-section of Canada. Partisan and regional considerations would arise at the time of selecting the members of the Appointing Council, rather than at the stage of judicial appointment. Commissioners are unconvinced, however, that such drastic reform is needed.

The appointment process is inherently political in the broad institutional sense. Measures to shift responsibility from the Prime Minister to some designated group or institution necessarily involve replacing one political process with another. Consistent with our view of the role of Parliament, Commissioners believe that if revised arrangements are to supplement the existing political process of consultation through the Prime Minister, the modified process should involve Parliament and should be equally broad. The elected Senate we have recommended would be an appropriate body to perform the ratification function in a rearranged appointment process. An elected Senate would be both broadly representative and regionally sensitive and thus would largely meet the traditional concerns of the provinces and the socio-economic concerns emerging from the Charter of Rights and Freedoms.

Constitutional Status

While the Supreme Court has some degree of constitutional recognition, as set out in sections 41 and 42 of the Constitution Act, 1982, and in section 101 of the Constitution Act, 1867, it is a matter of controversy whether it is entrenched to the degree that changes in its fundamental features require action by both orders of government. There are several arguments supporting

its more definite constitutional entrenchment. Some Canadians consider it inappropriate that the Court which adjudicates on the division of powers in the federal system is a statutory creation of the federal government. However impartial the Court's record, critics insist, its image of neutrality should be strengthened. Moreover, with the Charter only recently in place, we Canadians should ensure that nothing can block or obstruct judicial power to protect citizens' rights against unconstitutional government action. Constitutional status for the Court would confirm and safeguard its symbolic importance as defender of essential values in Canadian society.

Commissioners recommend explicit entrenchment in the Constitution of the status of the Supreme Court of Canada and, in particular, of its independence, although we believe it inappropriate to remove responsibility for the administration of the Court from the federal government.

Notes

1. See A. Wayne MacKay and Richard W. Bauman, "The Supreme Court of Canada: Reform Implications for an Emerging National Institution", in *The Courts and the Charter*, vol. 58, prepared for the Royal Commission on the Economic Union and Development Prospects for Canada (Toronto: University of Toronto Press, 1985).
2. B. Laskin, "What Everyone Should Know About the Supreme Court of Canada", address to the Empire Club, Toronto, March 12, 1981.
3. Peter H. Russell, "Constitutional Reform of the Judicial Branch: Symbolic vs Operational Considerations", *Canadian Journal of Political Science* 17 (June 1984), pp. 237–38.
4. Canadian Bar Association, Committee on the Constitution, *Towards a New Canada* (Montreal: Canadian Bar Foundation, 1978), p. 60.
5. Quebec, Royal Commission on Constitutional Problems, *Report* (Quebec: Éditeur officiel du Québec, 1956).
6. Canada, Task Force on Canadian Unity, *Report* (Ottawa: Minister of Supply and Services Canada, 1979).
7. The Constitution Committee of the Quebec Liberal Party, *A New Canadian Federation* (Quebec, 1980).
8. MacKay and Bauman, "The Supreme Court of Canada".