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ACTION FOR INDUSTRIAL GROWTH CONTINUING THE DIALOGUE

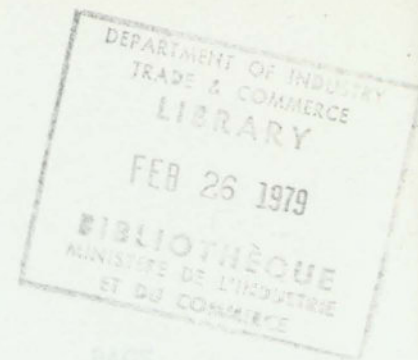


Government
of Canada

Gouvernement
du Canada

Board of Economic
Development
Ministers

Conseil des ministres
au Développement
économique



ACTION FOR INDUSTRIAL GROWTH:
CONTINUING THE DIALOGUE

The Federal Government's Response to the Recommendations of the Overview Committee Reviewing the Industry Sector Task Force Reports

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February, 1979

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PART I

ECONOMIC GROWTH AND COOPERATION

Introduction

The Overview Committee's report on measures to improve the competitiveness of Canadian industry is important to the federal government for three reasons in particular. First, the report and the process through which it was initiated is a significant and encouraging example of a new dimension in consultation and economic cooperation. Second, it highlights and re-emphasizes the importance of manufacturing industries in the Canadian economy. Third, it strongly reinforces the federal government's belief in the need to foster economic growth. The importance of the Overview Committee's report is a view also shared by the Provinces. At their conference in November 1978, First Ministers endorsed the consultative process and reaffirmed their commitment to the basic objective of sustained growth and to the fundamental role of the private sector in generating that growth.

The report was the culmination of the first phase of an important and unique consultative process. These consultations were begun in February, 1978 at the initiative of the Prime Minister and Premiers of Canada when twenty-three industry consultative task forces were created, each of which reviewed and made recommendations on selected sectors of industrial activity. The individual reports of these sector task forces stand on their own. The federal government is preparing separate responses to each of these twenty-three reports.*

The Overview Committee or "Second Tier Committee" as it became known, was created in July, 1978 with a mandate "to work directly from the task force reports and attachments to identify and make recommendations about factors and policies that cut-across sector lines, ... on broad economic policy and on issues important generally to manufacturing and tourism". The Committee was composed of five representatives from industry, five members of the Executive of the Canadian Labour Congress, an academic and a chairman from the private sector who had not been involved in the task force studies.

* The federal government released the first of the 23 responses February 1, 1979. The responses to the shipbuilding task force and the forest products task forces were released as part of a general announcement on the shipbuilding industry and the pulp and paper industry.

The purpose of this response document is to address the recommendations made by the Overview Committee in the context of its review of the reports of the twenty-three industry sector task forces. Part I of the response addresses certain of the general issues or expectations that have been raised by the consultative process to date and provides a brief summary of the government's response to the issues identified. Part II is the detailed response of the government. It addresses each of the Committee's recommendations. The response provides the following information: what action has been taken or is underway, an indication where specific positive action by government is difficult in the short term and finally, the factors that government took into consideration in preparing its response.

The Overview Committee's report was presented to provincial governments as well as the federal government. This document contains only the federal government's response. While the majority of recommendations made by the Committee are within the federal government's jurisdiction, it raises a number of major concerns which are the responsibility of provincial governments. The provinces, either together or individually, will need to appraise these. The federal government will endeavour to provide whatever assistance provincial governments request in helping prepare their responses.

The government views the publication of this response document as a continuation of the consultative process begun with the twenty-three industry sector task force studies. This response to the Overview Committee's report is therefore not final nor does it represent the end of business, labour and government consultations. Rather, business, labour and others as well are invited to react to the proposals which follow. Such a continuing dialogue is vital to ensuring that government support remains effective and focused.

The Process of Consultation

The Overview Committee report reviewing the work of the industry sector task forces is unique in the context of how public policy is made in Canada. While the federal government has always believed in an open and frank exchange of ideas and views, the process which culminated in the Committee's report has differed from past experiences in two ways. First, consultations have been more formalized and extensive than any previous similar consultations. Second, the initiative for assessing weaknesses and problems and for making recommendations was left to business and labour representatives. The Committee's report has, therefore, emerged from a consultative process which has been both extensive and intensive, involving almost 500 Canadians from just the private sector alone over a period of six or seven months. While the substance of what has emerged from the task force studies and Committee report is of considerable importance, the government views the process by which these recommendations have come forward as equally important.

The federal government also views the results of these consultations as central in evaluating existing policies and programs and for designing and implementing new ones. This reflects in part the government's realization that the problems and opportunities of industrial development must continually be reviewed and adjustments must be sought as conditions change. The challenge is to enable both industry and government to meet new opportunities from a stronger base and this must be underpinned by effective dialogue. The need for such consultation also reflects the public's awareness that the actions of the private and public sectors have become interdependent and that open discussions are required to ensure efficient and productive industrial activity.

In its report the Committee stated that:

both labour and business members of the Committee recognize the fundamental democratic responsibilities of elected governments to govern. The Committee, in putting forward recommendations for government action, does not seek to share this responsibility; governments must be responsible and must clearly be seen to be responsible for the decisions they take. The Committee does believe, however, that labour and business should be more actively involved in the process prior to decisions being made.

The federal government is committed to effective and open consultations with business and labour as outlined in this statement and will be seeking their views regarding how consultations might be continued.

Consultation while important is also difficult. Successful dialogue rests on identifying problems which are of equal concern to the participants involved and in defining challenges in such a manner that achievement and resolution are reasonably possible. In this context the Committee noted that:

when business and labour focus on specific problems or actions, wide areas of agreement can be found. In our view this provides a useful indication for any future activities of this kind; namely, that progress is more likely in cases where attempts are made to come to grips with industry sector-related problems rather than with those aimed only at establishing broad principles or goals.

The federal government believes this an important observation which should underline any future similar consultations.

Board of Economic Development Ministers

The federal government endorses the Overview Committee's view that:

central to improving the competitiveness and productivity of Canadian business is an economic policy that places a high priority on economic growth... This is the prior condition for improving the competitiveness and productivity of Canadian manufacturing industries.

Economic growth and economic development are closely related objectives, especially within Canada: they have acknowledged common ends. Both are aimed at creating new jobs, in enhancing prosperity for all citizens, private and corporate, and for maximizing the capacities and potentials of all the regions of Canada. To fulfill these goals requires a careful ordering of priorities, close business, labour and government cooperation and the successful support and encouragement of productive and internationally competitive industries.

The principal actors in such a process of economic development and growth must be the individual firm and its labour force. Accordingly, the thrust of government policy directed at growth must be to contribute to conditions that enable Canadian business and labour to excel in the provision of goods and services competitively to Canadians and to the markets of the world.

While this document contains a variety of detailed responses to help Canadian industry to meet this challenge successfully, the most important measure taken by the federal government is the creation of the Board of Economic Development Ministers. The Board has been made responsible for "coordinating the efforts of the Government to establish cooperative relationships with the provinces, business, labour and other public and private organizations for the industrial development of the economy. It is the intention of the Government that the Board will act as an authoritative instrument to ensure coordinated and timely federal governmental support to Canadian business and labour in the pursuit of economic development". The creation of the Board also gave further substance to the Prime Minister's statement of August, 1978, according unequivocal priority to economic growth.

It is the intention of the government through the Board of Economic Development Ministers, to add several new and practical dimensions to the priority it accords to development and growth, which are in line with the ideas and recommendations expressed by business and labour in the consultations.

First, the Board of Economic Development Ministers will, as the centrepiece of its responsibility, focus on ordering and setting priorities amongst the federal government's policies and programs in the field of economic development. An important part of this priority setting is the responsibility the Board has for allocating resources in support of these programs. This involves not only reviewing new proposals prepared by individual departments but of even greater importance, identifying areas where existing programs should be improved and more effectively coordinated. The Committee urged

governments to assign priorities to its recommendations consistent with lower inflation and real economic growth. The Committee also acknowledged that if all the tax recommendations in the task force reports were implemented at the same time, this would result in a massive and unacceptable reduction of government revenues. Determining priorities in such a way so as to avoid these problems and ensure real growth will be a major responsibility of the Board. It will seek through continuing consultation with provincial governments, business and labour, to assist the government to expedite the implementation of those of highest priority. This will be a major task of federal departments, singly and collectively as the case may be, and may require appropriate arrangements with provinces.

Second, the Board of Economic Development Ministers will concern itself with the effective and coordinated delivery of federal economic programs and services. The work of the industry task forces and the Overview Committee has shown Ministers that many of the government's programs and services are either not as well known and understood or not as well integrated with each other or not as responsive as they need to be. This is at present a major component of the Board's work program and two activities are underway. The first is to make information about the government's industry and economic support programs more easily available to businessmen. The second is the development of a compendium of economic development policies and programs of the Government of Canada. This compendium will enable the government to determine where overlaps or conflicts in programs exist, where further program development is required and eventually how federal and provincial programs might be better integrated.

Third, the Board of Economic Development Ministers has the responsibility for evaluating the effectiveness of various policies and programs and for ensuring that the right balance or combination of support programs exist. Such programs can range from direct expenditures which involve government alone in a specific activity to a variety of other support mechanisms which rely increasingly on the initiative of the private sector: that is, the government providing grants or loans, establishing regulations or simply providing the example and leadership. In this regard, the Board will endeavour to clarify what the major emerging economic development issues are and how they should be addressed.

Finally, in addressing questions of economic growth and economic development, the report of the Overview Committee does not specifically deal with the problems and opportunities confronting small business in Canada. This is a special concern of the government and specifically the Board of Economic Development Ministers. In some instances, these issues were also raised by particular industry sector task forces. The government has already undertaken to set many of these kinds of measures in place and to ensure that an adequate policy framework exists to support and encourage small businesses. The Board

will be considering additional measures. Some of the particular concerns in this regard will be the adequacy of existing debt and equity financing arrangements for small business, the bias of certain government policies such as procurement and competition policies and the nature of regulatory reform which may be required to encourage the growth and viability of small business.

Public and Private Sector Relations

As noted earlier, the federal government believes that the principal actors in the Canadian economy must be the individual firm and its labour force; that the route to economic prosperity is via the market system. In reaffirming this principle, there exist a number of views about the nature of government support, participation and intervention required. Governments in Canada have historically taken an active part in the process of industrialization. Such public participation reflected widely-held national or provincial perceptions that strong governmental involvement was needed to ensure the rapid development of a geographically extended infrastructure and to ensure the realization of major economic endeavours with adequate Canadian involvement and control. Much less consensus now exists on what kinds of direct governmental action are appropriate regarding future Canadian economic development.

The federal government considers that there is a continuing rationale for its participation in economic development in circumstances where project size, degree of risk or overriding national interest require a public presence. Its current role may be somewhat more diffuse, more incentive-oriented and less dominant, than it has been in the past, save perhaps in certain sectors. It can take the form of grants or loan guarantees (The Enterprise Development Program and the Regional Development Incentives Program) of limited equity participation (the Federal Business Development Bank), of joint public-private sector ventures (Syncrude) or of Crown Corporations (Petro-Canada, provincial electrical utilities, etc). The new Board of Economic Development Ministers has the responsibility for coordinating this effort and evaluating the effectiveness of the various policies and programs involved.

As the Overview Report notes, the question of government regulation was of common concern to all the industry sector task forces. At their Conference of February 1978, First Ministers requested the Economic Council of Canada to undertake a major review of this field. In light of this, the Committee did not make any specific recommendations on regulation.

The Council's recommendations will undoubtedly lead to the deregulation of certain activities. It will likely also point to the need to extend regulatory activity in certain areas. It will contribute as well to the efforts underway by governments to eliminate conflicting and overlapping regulatory activity within and between governments and provide a clearer focus on the costs and benefits inherent in new regulatory activity. The government views the Council's work in this area as critical for grappling with many of the

fundamental issues. The Board of Economic Development Ministers is providing the leading organizational focus for ensuring the government will be able to respond quickly and substantively when the Council makes its recommendations. A major concern will be to ensure that in changing existing regulations or making new ones, the individual's freedom of action is protected and is not unnecessarily circumscribed.

The federal government is conscious of the difficulties underlying labour's concern regarding the serious limitations in utilizing cost-benefit analysis in determining the adequacy of certain regulations. Significant difficulties do exist in assigning quantitative values that reflect a broad societal consensus. The government is committed therefore to making such studies publicly available prior to implementing regulatory change that might arise from them. This will give interested parties a chance to publicly question the values so assigned.

The Issues

The Overview Committee identified nine issues most commonly addressed by the twenty-three industry sector task forces. Part II provides a detailed response to the recommendations the Committee made on each of these issues. Very briefly, the effect of these responses will be the following.

a) Trade and Multilateral Trade Negotiations

The Committee's recommendations and the government's response support freer international trade based on an aggressive Canadian commercial policy. The government is committed to the concept of overall reciprocity as a fundamental aspect of the GATT multilateral trade negotiations. Such a policy would aim at maximizing Canadian trade opportunities in foreign markets while acting firmly to defend Canadian production and jobs threatened by the unfair trading practices of other countries.

b) Manpower and Labour Relations

The government's response in agreeing with the Committee's recommendations reinforces the important role the private sector has in manpower and labour relations activities. The measures outlined should enable business, labour and government to ensure that both present and future Canadian manpower needs are met. In particular, the new Employment and Immigration Advisory Council, an autonomous body whose membership is totally non-governmental, will investigate issues it chooses and make its recommendations public. The government agrees with the principles stated by the Committee that Canadian workers have the right to join unions and bargain collectively and is awaiting the completion of the work of the labour relations committee established by the Overview Committee.

c) Taxation

The essential issue raised by the Committee concerns the relative weight to be given to the various objectives a tax system can serve in addition to its primary purpose of raising revenues. In Business' view Canada's tax system should give clear preference to promoting the creation of wealth while labour's view is that it should be used as a major instrument for redistributing wealth. The response of the government is that neither view can be accepted exclusively. The specific responses to recommendations outline measures which attempt to ensure Canada has an equitable tax system along with adequate incentives for economic growth.

d) Research and Development

The Committee's major concerns with which the government agrees, were with the low level of national resources devoted to research and development, the need to aim for greater self-sufficiency in technology, and the provision of government support on a more flexible, longer-term basis. Increasing the levels of Research and Development in Canada is a shared private and public sector responsibility which the government will support by increasing the funds it makes available as well as by improving the quality and nature of its support.

e) Energy

The Committee and the government both agree that a carefully developed national energy policy will help to ensure that Canada maintains an efficient and competitive industrial structure. In addition to noting the government has published a national energy policy, the response proposes actions aimed at ensuring the optimal level of upgrading of energy resources and outlines a pricing mechanism which fully reflects pricing practices in the United States.

f) Transportation

A number of general concerns were expressed by the Committee regarding the trade-offs between equity and efficiency, the rate setting mechanism and the rate appeal process. Many of these concerns have been addressed in the context of the amendments to the National Transportation Act, the Department of Transport Act and the Railway Act. These amendments were given first reading on November 16, 1978 in the House of Commons.

g) Regional Development

The government's response, in agreeing with all the recommendations of the Committee, will ensure that federal government policies and programs will not create unnecessary industrial overcapacity or fragmentation. A central aim of the response is to provide a better and more public process of planning and industry consultation.

h) Government Purchasing Policies

The response of the federal government, which agrees with the recommendations of the Committee is aimed at greater standardization in design and specifications of products purchased by government, to extend such standardization to as many products as possible and to ensure a better coordination of standards amongst governments in Canada. The government agrees in principle that its purchasing policies should more directly promote Canadian industrial development. In particular, the government's purchasing policies are aimed at encouraging small business.

i) Rationalization

The Committee's recommendations and government's response both endorse the need for rationalization. While the initiative for rationalization must be left with the private sector, the government will support such initiatives by providing support facilities and, along with industry, help in easing hardships created by plant shutdowns occurring because of rationalization.

Conclusion

The Overview Committee made forty-six specific recommendations in its report. The government has responded to all of these recommendations. In the overwhelming majority of cases, forty-three of the recommendations, it was able to agree with the recommendation or with the underlying principles involved. In three instances the government was not able to support a recommendation made by the Committee. In those instances where the government agreed with recommendations, actions are outlined, many of which have been enacted since the report was made public in October 1978. Where further work is still required, which is only in a very few areas, this has been identified (see Annex I). An important responsibility of the Board of Economic Development Ministers is to ensure this work is undertaken and also to receive and channel any reactions or advice business, labour or provincial governments may offer.

The Overview Committee stated the following principles were basic to improving the competitiveness and productivity of Canadian industry:

- to stimulate economic growth and job creation as one of Canada's first priorities;
- to foster an environment of understanding in which more effective consultation can take place among labour, business and government;
- to recognize the vital importance that manufacturing industries have in enhancing the living standards of individual Canadians.

The federal government accepts and endorses these principles. The government believes that the measures outlined in this document can all be judged on these principles.

Finally, in concluding Part I of this document, the federal government wishes to reiterate the Overview Committee's statement that the recommendations of the Committee and the government's response to them do not provide an industrial strategy for Canada. Indeed, the many specific actions highlighted in this document only represent a part of the broad range of measures the federal government now uses or is presently developing to use in supporting the development of competitive Canadian industries.

PART II

THE FEDERAL GOVERNMENT'S RESPONSE BY ISSUE

The Overview Committee concentrated its efforts on the nine issues most commonly identified by all sector reports. The following section reproduces the Committee's recommendations on each of these issues and the response the federal government is prepared to make at this time to these recommendations.

TRADE AND THE MULTILATERAL TRADE NEGOTIATIONS

The thrust of the Overview Committee's assessment and recommendations generally supported "free-trade" but in a manner which actively took advantage of trade opportunities and which did not expose Canadian firms to unfair trading practices. The government agrees with this point of view. The concept of overall reciprocity is a fundamental principle underlying Canada's position in the GATT multilateral trade negotiations. In responding to the Committee's recommendations, a major undertaking of the government is to intensify its monitoring of other countries trade practices which attempt to circumvent agreements and threaten Canadian production and jobs.

Recommendation 1

That encouragement should be given to the formation of consortia to capitalize on export opportunities. This would be particularly advantageous in relation to design, supply and construction related to large-scale development projects. Particular support is required in removing legal impediments and developing instruments to cope with extraordinary risk factors in large foreign contracts. Such instruments should include competitive financing and insurance.

Response

Agreed

In reviewing measures intended to support the creation of consortia for trade purposes, the government did not find that any legal impediments existed which would present obstacles for business to capitalize on export opportunities. The government is therefore anxious to have business and labour identify any such impediments. To eliminate any other major obstacles to consortia formation, the government has established the "Ultimate Risk Insurance Program" whereby the government will provide excess loss reinsurance to support the operation of a program to provide insurance coverage against unknown and unanticipated risks for which insurance has previously not been available. The Minister of ITC announced October 13, 1978 the establishment of a \$100 million contingent liability authority to provide risk reinsurance. In addition, the Export Development Corporation has recently introduced a "Surety Program" which will provide cross-liability insurance within a consortium. In response to latter part of the recommendation of the Committee, the government is undertaking studies on the relative competitiveness of Canada's export financing instruments.

Recommendation 2

That Canada rely on the multilateral trade agreement route in its general trade policy; continental free trade should not be pursued as a general policy, but only as a selective sectoral strategy where appropriate.

Response

Agreed

The government is in agreement with the Committee's recommendation.

Recommendation 3

That, in the current round of Geneva trade negotiations, the Canadian negotiators should push for a phasing of the lowered trade barriers that allows the greatest ease of transition for affected industries. The Committee specifically recommends an 8 to 10 year phase-in period but with a provision for suspension of the implementation of trade barrier reductions for industries encountering particularly difficult problems of adjustment. Canada must not undertake on its own initiative - as was the case in the Kennedy Round - a rate of implementation faster than necessary under the Tokyo Round.

Response

Agreed in principle

There is a general consensus, which Canada supports, that the lowering of trade barriers resulting from the MTN should be phased in over an extended period, likely 8 years, - a period longer than was provided for under the Kennedy Round - to ease the process of adjustment. Consideration is also being given to the possibility of delayed implementation and/or a pause midway through the phase-in period which will allow account to be taken of concerns in particularly sensitive sectors.

Recommendation 4

There are certain manufacturing industries that are vital and where any degree of reduction in protection would be disastrous at this time. The Committee recommends that these industries be specifically exempted from the Tokyo Round. The key case in point is the clothing and textiles sector which employs close to 200,000 workers.

Response

Agreed in part

The Government recognizes that, in certain cases, difficulties may be encountered in adjusting to more liberal trading conditions. This has been carefully considered in developing the Canadian position for the negotiations. In the negotiations, use will be made of the limited scope for making total or partial exceptions

from the agreed formula for tariff reductions on industrial products. It should be recognized however, that while there may be industries "where any degree of reduction in protection would be disastrous at this time", the full impact of the MTN will not be felt until the late 1980's at the earliest in view of the extended phase-in period for tariff reductions. In this regard, demographic and labour force projections suggest that the employment environment will be much improved by that time over the present.

Recommendation 5

That the federal government develop a comprehensive adjustment assistance program that is based on an assessment of needs, industry by industry, in consultation with labour and business. It should be directed at industries that need assistance to capitalize on the opportunities provided by the GATT and at industries whose viability has been undermined in the trade negotiations.

Response

Agreed

The government recently announced a package of adjustment assistance measures intended to address the underlying concerns expressed by Canadian industry and labour in this recommendation. However, in light of the importance of these measures for industrial restructuring and future employment, the government agrees that further consultations with business and labour should be held and will make arrangements for these.

Recommendation 6

In the current set of trade negotiations, Canada should press for the maximum degree of multilateral reduction of non-trade barriers. However, to the extent that other countries subsequently circumvent any agreement along these lines, Canada must use non-tariff barriers on a competitive basis in order to protect Canadian production and jobs.

Response

Agreed

Reducing or eliminating non-tariff trade barriers is a major focus of the trade negotiations and an element to which Canada attaches considerable importance. Non-tariff measure codes are being finalized for certain key barriers and should go some distance towards reducing or eliminating the trade distorting effects of such measures. These codes and the surveillance and dispute settlement mechanisms associated with them should significantly benefit Canadian exporters by narrowing the scope for other countries to erode the negotiated terms of access to their markets.

Recommendation 7

That the federal government set up a formal procedure for monitoring unfair trade practices, including the creation of non-tariff barriers coming out of the Tokyo Round.

Response

Agreed in part

The government agrees that the monitoring of unfair trade practices is important. Such monitoring is carried out on a continuing basis by the government, in particular by the Department of Industry, Trade and Commerce. The specific purpose is to identify possible areas where access for Canadian exports might be impaired. As part of the Multilateral Trade Negotiations, the additional machinery in the various international codes being negotiated should provide an important supplement to present procedures. Because of the complexity of such monitoring, the government invites business and labour to bring any specific problems to its attention and for its review.

Recommendation 8

That appropriate mechanisms be found to simplify and reduce the cost of, and improve the speed and efficiency of, the safeguard processes which deal with trade-related matters such as injury determination, monitoring of non-tariff barriers and unfair trade practices, the determination of safeguard action, and tariff references.

Response

Agreed

The government agrees that adequate and speedy safeguard arrangements are vital to protect Canadian industry from unfair trading practices. In particular, the government recognizes labour's concern about the threat to Canadian jobs from imports that may have a price advantage in Canadian markets based on state-trading or labour-exploitative practices.

A code respecting safeguard procedures is close to being finalized in the Multilateral Trade Negotiations which will clarify the criteria and procedures for taking safeguard actions. The government will take whatever actions are necessary to ensure that Canadian industry has access to effective protection where warranted.

The GATT Anti-dumping Code is also being reviewed in the context of the Multilateral Trade Negotiations. Canada is participating fully in the review with a view to improving international protection against injurious dumping and, in due course, the government will consider how best to incorporate such improvements in Canadian procedures.

A variety of trade policy instruments do of course exist which can be employed, as in the case of footwear, clothing and textiles, in accordance with Canada's international rights and obligations, to facilitate adjustment to changes in competitive conditions or mitigate unfair competition. These include: emergency safeguard action such as surtaxes or import controls; anti-dumping and countervailing duties; and raising existing tariff levels.

The government reaffirms its commitment to streamline, wherever possible, the procedures associated with these instruments. For example, in March 1977, new procedures were announced to speed up the processing of complaints from Canadian manufacturers about the dumping of foreign goods. Ministers have also reassured industry that National Revenue will continue to treat "sales-below-cost" as dumping in cases where such sales are considered not to be in the ordinary course of trade in the country of export.

Finally, in recent years many governments have increasingly used subsidization as a means of promoting industrial development. Recognizing that subsidized imports can materially injure Canadian producers, the government announced in April, 1977, the promulgation of Countervailing Duty Regulations. The government now has the means whereby any domestic industry can seek legitimate protection from subsidized imports. A Subsidies/Countervail Code is being negotiated as part of the Multilateral Trade Negotiations. It is expected that this Code will clarify and strengthen the provisions of the GATT respecting subsidies affecting international trade.

MANPOWER AND LABOUR RELATIONS

a) Manpower

The recommendations of the Overview Committee underline the role the private sector can play in this area. The government supports this position. In its response the government seeks to reinforce the primary responsibilities labour and business have in the area of manpower planning and training activities. In the area of labour relations the government agrees with the basic statement of principles concerning labour rights in Canada. It is awaiting the completion of the report of the labour relation's committee created by the Overview Committee. Any measure of agreement which business and labour develop on the list of issues it outlines in its report will constitute a major step forward in labour relations in Canada.

In addition to a statement of principles regarding labour rights, the Committee noted that while there were "fundamental differences in approach" between its labour and management representatives on the unemployment insurance issue, both agreed that total unemployment insurance payments were too high and that more effective job creation was necessary. The Committee made no explicit recommendations regarding unemployment insurance, however.

The federal government shares the Committee's concern about the size of the Unemployment Insurance Program. Legislation passed by Parliament late in 1978 seeks to address this issue in a number of ways. The overall effect will be to reduce unemployment insurance by almost \$1 billion a year, while reducing the program's work disincentive effects. At the same time, the recently-announced 1979-80 Employment Strategy proposes increased support for measures in the private sector such as the Employment Tax Credit, Portable Wage Subsidies, and a Job Experience and Training Program financed extensively from Unemployment Insurance funds. These and other measures will produce an employment program in 1979-80 creating 113,000 person-years of employment for 368,000 participants at a total cost of \$710 million in direct expenditures, foregone net tax revenues, or developmental use of Unemployment Insurance funds.

Recommendation 1

In those industries where manpower resources, training and planning are inadequate, industry and labour should meet regularly to forecast needs and recommend training and education programs to governments, sector by sector. For an overall picture, an autonomous body, jointly supported by provincial and federal governments and by business and labour, should be created to integrate sector inventories of manpower availability and needs and to advise on manpower policy, training and educational requirements. This body would make reports assessing the medium and long-term manpower requirements.

Response

Agreed in part

The government strongly supports the recommendation that the private sector give higher priority to manpower planning and that it play a greater role in determining manpower policy and in advising on training and educational requirements.

The government endorses the recommendation for a multipartite body to advise on manpower and training policies, and believes that this need will be met by the new Employment & Immigration Advisory Council. The Council, which will be composed exclusively of non-governmental members, including representatives of both business and labour, will have the power to investigate issues it deems important and to make public its recommendations regarding employment and immigration policies. In addition, of course, the Employment and Immigration Commission itself is intended to provide for private sector input with one Commissioner representing business and another representing labour.

In the employment field, the government believes that the most effective approach to greater government/private sector cooperation will be to develop improved sectoral consultations and greater government/private sector cooperation at the provincial or

area levels. It is the federal government's intention to recommend strongly that business and labour have direct inputs into the federal-provincial manpower planning bodies in each province (called "Manpower Needs Committees" in most provinces).

Specific government/industry cooperative manpower planning and problem-solving projects are under way in certain sectors (eg. construction, machine tool manufacturing, shipbuilding and aerospace) and the government is prepared to enter into other such arrangements wherever feasible.

The Minister of Employment and Immigration will request the new Employment and Immigration Advisory Council to:

- a) review the 23 industry sector task force reports and assess the responses affecting employment and immigration policies and programs; and
- b) recommend ways of improving government/business/labour consultation and cooperation in the employment field.

Recommendation 2

Existing manpower funding should be significantly redirected to support job-oriented training. That is, much less emphasis should be placed on institutional training which involves little or no relationship to job opportunities. Such a shift in manpower programs would:

- result in a significant increase in "on-the-job" training and other programs related to identifiable jobs in the marketplace. Such training should take account of the need to adjust wages and training allowances in a manner that would encourage candidates to participate in such training. Firms also would be encouraged to participate more fully in such programs.
- be consistent with the recommendation of the Aerospace Task Force that a payroll levy be considered for those sectors that see a need for this approach and support its implementation. The purpose of this levy would be to spread the costs of this training among firms.

Response

Agreed in part

The federal government fully supports the recommendation that greater emphasis be placed on "on-the-job" training. Progress has already been made in this direction. The industrial training budget has increased substantially in recent years, doubling from \$42 million to \$84 million between 1973 and 1978 with a further increase to \$97 million proposed for 1979/80, while the institutional training

program budget has been stabilized and increasingly redirected towards apprenticeship and higher-level skill training. (Support for apprenticeship, for example, has increased from \$31 million to \$83 million between 1973 and 1978).

These developments have been reinforced by a federal government evaluation of the training program in 1977, together with subsequent renegotiation of federal-provincial training agreements which placed greater emphasis on training firmly linked to labour market needs and which focussed available additional training funds in employment growth areas.

In its 1979-80 Employment Strategy, the government has announced a new policy of direct support to critical trades skills training in "key" high-level trades. \$20 million is allotted for such training in 1979-80, with a proposed expansion to \$40 million per annum in the 1980's.

In expanding industrial training, however, the government wishes to ensure that public funds are not simply substituted for private ones and that a high quality of training be maintained. The committee's attention is also drawn to the fact that federal government's funding of institutional training includes the classroom portion of apprenticeship, which will amount to over \$100 million in the 1979-80 fiscal year. Continued government involvement in this aspect of institutional training clearly supports, rather than limits, industrial training.

The federal government is also taking steps to provide greater incentives to both firms and individuals to participate in industrial training. As part of its support for critical trade skills training, for example, the government is exploring means of increasing its overall support for such training and concentrating this support in the critical early years of training when firms' costs and trainee dropouts are highest. The government is also examining means of streamlining its delivery of industrial training, in the expectation that reduced administrative burden for participating firms will be a further training incentive for them. More generally, the government is also giving consideration to extending the duration of its financial support for industrial training past the present maximum of 52 weeks.

Regarding the Committee's specific mention of "the need to adjust wages and training allowances" to encourage individuals to take training, the government points out that the wages paid to industrial trainees are not directly established by the government but by the firm and the collective bargaining process. Government influence over trainee wages is, at the very best, indirect; federal financial support to training firms is based on the trainee wage (rather than vice versa) and is limited to no more than the maximum institutional training allowance. While an increase in this maximum allowance could induce some firms to increase their trainees' wages, the likely extent of this is not certain. In any case, the CEIC has already planned a general review of the training allowance structure which would include reference to particular issues such as this.

The government is prepared to explore with specific industry sectors the concept of "levy-grant" training financing on the understanding that such an approach would be voluntarily sought by the sector itself and not imposed by the government (as is the case in other countries).

Recommendation 3

While mobility programs are not alternatives to job creation in Canada, every effort should be made by governments to reduce impediments to individuals willing to move. For example, provincial actions or restrictions that reduce manpower mobility should be abolished. In addition:

- governments should establish or review mobility programs with the objective of ensuring that either through grants or tax concessions, unemployed individuals willing to move for full-time employment, but unable to do so because of the personal financial costs involved, will be subsidized to offset those costs.
- programs to assist individuals investigating job opportunities should include provision for spouses to accompany them.

Response

Agreed

The federal government strongly supports the committee's recommendation that "provincial actions or restrictions that reduce manpower mobility should be abolished". As evidence of this position, the government cites the federally-supported inter-provincial "Red Seal" program which is aimed at achieving interprovincial uniformity in the recognition of trades certifications.

Regarding the Committee's specific recommendations for government programs to encourage mobility, the recommended grants and tax concessions have in fact been in place for a number of years. Federal grants are currently available to cover both relocation costs and the costs of travel to seek work, while federal tax regulations allow relocation costs as a deduction from taxable income. Furthermore, the program of mobility grants (the Canada Manpower Mobility Program) is being reviewed with the aim of increasing its flexibility and adaptability to the expected needs of the 1980's.

The government is prepared to consider carefully the Committee's recommendation that job search grants include provision for workers' spouses to accompany them.

b) Labour Relations

The Overview Committee noted that on the whole the Canadian labour relations systems operated well and that the vast majority of labour contracts were settled without labour stopages. The Committee characterized the systems as having the following principles:

- a) the right of unions to exist in Canada,
- b) the freedom of association of workers as a basic democratic right, and
- c) the right to bargain collectively.

The government agrees with and accepts these principles.

The Committee has constituted a Labour Relations Committee to study labour relations in Canada and report to First Ministers. At the First Minister's Conference, the Prime Minister welcomed and endorsed this important initiative on the part of organized labour and the business community, and it received the general support of the Conference.

The agenda set by the Overview Committee for the Labour Relations Committee covers the issues currently in general contention between management and labour. Any measure of agreement the committee can develop on these will constitute a major step forward in labour relations in Canada. The federal Department of Labour is ready to extend to the Labour Relations Committee any assistance the committee may feel the Department can usefully provide.

TAXATION

The section of the Committee's report that deals with taxation reveals a divergence of views about the relative weight to be given to the various objectives a tax system can serve in addition to its primary purpose of raising revenues.

In an economic system where the principal economic actors are individuals and private firms, the Committee notes that policies, including tax policies, designed to maintain, or indeed increase, incentives are essential. The use of incentives in the tax system may also be necessary to allocate resources to areas where government perceives development to be required for national goals. The Committee recognizes that it would be unacceptable to so reduce government revenues by the provision of incentives that governments were unable to carry out functions which are essential to Canada's economic growth and social well-being.

A complementary but often competing role for the tax system is to effect a more equal distribution of income than the market may generate on its own. The ability of the tax system to contribute to social policy in such areas as the redistribution of income to lower-income groups may be weakened by the availability of extensive tax concessions.

Government tax policy thrusts over the recent past have occurred, and will continue to occur, in both areas. Tax incentives have been put in place to encourage private sector activity. Recent budgets have contained their share of such measures. In August the federal government moved to introduce a refundable child tax credit which, in conjunction with other changes in the child benefit system, ensures that these resources are better targeted to those to whom they mean the most.

There is also a divergence of views in the Committee report about the efficacy of tax incentives as a tool of economic policy. Business representatives felt that corporate tax reductions would encourage investment. Labour representatives felt that investment performance is constrained by low rates of capacity utilization, presumably related to insufficient levels of demand, and that corporate tax reductions would thus be ineffective.

The government cannot accept either view exclusively. It believes that there is a place for tax incentives to encourage particular sectors or activities as needed and to contribute to a longer term environment that is conducive to private sector expansion. It also believes that monetary and fiscal policies, including tax policies, must be set to maintain a growth in private sector demand consistent with adequate real growth and satisfactory price and cost performance.

The recent budget contains both types of measures. The federal sales tax was reduced with a view to stimulating aggregate demand while, at the same time, minimizing upward pressures on prices and costs and supporting Canadians' real incomes. This cut was in addition to the increase in disposable incomes brought about by tax indexing, the increased employment expense deduction and the reduction in the contribution rate for unemployment insurance. A number of budgetary measures directed at providing incentives to particular activities, were also proposed. Prominent among these was the enrichment of the investment tax credit and the R&D tax credit, their indefinite extension past June 1980 and the inclusion of transportation assets among those eligible for the credit. The government believes that such incentives will be a positive contribution to increased investment, to orderly planning of investment projects and to a more efficient transportation system.

Against this background the government's response to the Committee's specific recommendations in the tax area is as follows.

Recommendation 1

Changes in corporate taxation should be evaluated in the context of all the factors that determine international competitiveness. The differential treatment of corporations from country to country - whether in terms of the direct tax rate or in terms of tax concessions such as accelerated write-offs, tax credits, etc. - are as crucial as other cost items, including wages, transportation and tariffs, and should be considered in that light.

Response

Agreed

The Government of Canada recognizes fully that taxation of corporate income impacts significantly on the competitiveness of Canadian firms and their products in foreign markets. The maintainance of international competitiveness is an important determinant in the establishment of tax policy. When in the past other countries adopted new export-oriented policies, these were followed by significant changes in Canadian tax and expenditure policy to provide for industrial adjustment and maintain competitiveness. The Budget Paper, The Tax Systems of Canada and the United States, indicates that while tax revenue of all levels of government was some 1.8 percentage points of GDP higher in Canada than the U.S. in 1977, Canadians had the benefit of publicly provided health care services and transfer payments in the form of family allowances and old age security pensions. The dollar value of these three programs, which do not have any counterpart in the U.S., was about \$11.7 billion (measured in terms of government expenditures) in 1977-78 and far exceeded the difference in relative tax levels between the two countries.

In examining corporate taxation, it is found that the corporation income tax revenue in Canada, as a percentage of pre-tax corporate profits, have been consistently lower over the 1972-1977 period than is the case in the United States. In 1977 the difference was some six percentage points in Canada's favour. In manufacturing in 1973, the latest year for which data by sector are available, the advantage in Canada's favour was some 11.3 percentage points. These advantages result from more generous depreciation allowances and lower statutory tax rates in Canada. Notwithstanding this, the government has and will continue to enact changes in corporate taxation, in order to ensure that our tax system remains broadly competitive, and where such changes appear to be the best means to achieve particular economic ends.

The government shares the view that taxes cannot be judged totally in isolation from other factors affecting the private sector. However, while taxes paid are a cost of doing business, caution is advised in viewing taxation as an important means of offsetting other costs of business that may differ from those faced by firms in competing jurisdictions. A more satisfactory approach is to concentrate on improvements in efficiency and productivity which themselves will operate to lower directly these other costs. Concentrating on root causes may well require any one of a number of policies in the areas of industrial development, manpower, taxation and trade, to name a few. Such an approach is likely to provide more lasting benefits to Canada than is an approach that used tax changes to attack the symptoms of underlying difficulties in the Canadian economy. As has been noted, the government is committed to act on all of these fronts. Indeed, in some areas it has already acted.

Recommendation 2

A greater degree of coordination of fiscal policy should exist among levels of government to meet national goals. The need for more intensive consultation will become greater as provinces increasingly develop their own taxation systems (e.g., the personal tax rate structure as it now exists in Quebec).

Response

Agreed

While there almost always seems to be need for greater coordination of fiscal policy, it should be recognized that mechanisms to achieve this end have existed for some time and have been strengthened recently. Federal and Provincial Ministers of Finance have been meeting on a regular basis since the mid-1960's. The economic and fiscal outlook is discussed at these meetings and the discussions are supported by data prepared by federal and provincial officials.

More recently at the February, 1978 Conference of First Ministers, the need for increased coordination in setting economic objectives and developing policies to attain these objectives was recognized. This was reaffirmed at the November, 1978 Conference of First Ministers on the Economy. First Ministers agreed to convene their next meeting on the economy in late 1979 and have instructed appropriate ministers and officials to convene the necessary forums to address specific problems raised at the Conference.

With respect to tax systems there already exists a significant degree of harmonization of federal and provincial income taxes. Income tax collection agreements have been in effect between the federal and nine provincial governments since 1962. These enable federal and provincial governments to exercise their right to levy income taxes within a framework which simplifies the tax system and enables national goals to be met. The tax collection agreements provide for consistency in federal and provincial laws, a common formula to allocate income by province, and the completion of only one tax form covering both federal and provincial taxes. The arrangements have proven to be flexible to meet the evolving priorities of federal and provincial governments.

Recommendation 3

Some task forces observed that there are inconsistencies in the corporate tax rate and tax concessions from industry to industry (e.g., logging and forest products). Such inconsistencies should be reviewed and their continuation be dependent on a more clearly established rationale.

Response

Agreed in part

In the supplementary paper accompanying the Budget introduced in November 1978 the government expressed agreement with this recommendation. The paper stated, "Proliferation of a large number of tax incentives tailored to individual sectors or circumstances will in the end dilute the effectiveness of each incentive and risk serious harm to the efficiency of the Canadian economy while adding to the complexity of the tax system. In cases where special tax treatment now exists - for example, for small businesses, manufacturing, exploration, research and development - important national priorities have been identified. A corollary to assuring that incentives are introduced only where a major priority exists is that incentives should be frequently reviewed".

Recommendation 4

Some task forces recommended sales tax cuts or extension of current exemptions on products such as footwear and clothing. The committee recommends consideration of this approach both as a stimulus to demand for particular products and as relief to low-income groups for whom these items represent a particularly large proportion of expenditure.

The Committee is concerned, however, that in certain sectors a large part of the stimulative impact would be lost to imports. In such sectors, the committee recommends that other stimulative measures be considered.

Response

Agreed in part

The Budget of November 16, 1978 proposed a reduction in the general rate of manufacturers' sales tax from 12 percent to 9 percent. This measure was adopted for stimulative purposes and will have a beneficial effect on price and cost pressures. It will reduce taxes payable by \$280 million this fiscal year and by \$1 billion in 1979-80. Footwear and clothing are already exempted from the application of federal sales taxes and therefore other measures must be sought to provide stimulus for these industries. In fact, government has a range of trade measures in place for these products to permit an adequate share of the Canadian market to be available for domestic producers.

The government is generally not of the view that it should significantly expand exemptions from federal sales tax. To do so could effectively convert that tax into a set of special excise taxes applicable to only a very limited number of products.

Recommendation 5

The Committee concurs with the recommendations of several task forces that sales taxes on construction materials and equipment be removed.

Response

Disagreed

The government does not agree with this recommendation. The sales tax rate on building materials has been reduced from 12 to 5 per cent. The government has a wide range of measures that support housing. Further reductions in the sales tax on building materials would reduce the size of tax reductions that could be made available to the economy in general. The government does not believe that providing additional tax concessions to this sector, at the expense of other taxpayers, is appropriate at this time. It should be noted that the proposed enrichment and extension of the investment tax credit in the recent budget acts to lower the costs of investments in buildings and other structures, and thus acts to stimulate the construction sector, in much the same way as would a reduction in commodity taxes. The proposed changes to the investment tax credit have the desirable feature of also applying to investments in machinery and equipment.

Recommendation 6

A number of task forces made some specific recommendations on the problem of preferential treatment provided by the federal sales tax to imported products compared with domestically manufactured products. The Committee is aware that this issue is under intensive study and that there is still inadequate information on the impact of various potential solutions. Accordingly, the Committee is unable to categorically recommend appropriate modifications, but it urges that the current recognized discrimination against Canadian manufactured products be removed as soon as possible.

Response

Agreed in part

The Standing Committee of the House of Commons on Finance, Trade and Economic Affairs has already received a large number of submissions on the Report of the Commodity Tax Review Group. It is expected that the Committee, after it has finished its review, will make recommendations on the structure of Canada's commodity tax system. The Report recognizes that one of the major deficiencies of the current federal sales tax is the potential for differential tax treatment of competing domestic and imported products. This arises because part of the expenditure necessary to market imported goods in Canada may occur after the point of imposition of sales taxes (at the border on duty-paid value) while, for domestic manufacturers these costs may be included in the tax base. As well, the importer may enjoy a trade level advantage over his domestic competitors. This would occur, for example, if the importer was a wholesaler but where no representative wholesale situation exists for domestic goods. Domestic goods would then pay tax on essentially a value reflecting sale price to retailers.

The Report recognizes that "these two factors may place domestic producers at a serious disadvantage relative to importers of competitive goods". Furthermore, the Report notes the biases that may result due to the fact that the costs of transporting fully manufactured imports to Canada are not generally reflected in the value on which sales tax is levied. The Report examines alternative modifications to the structure of the tax and makes many specific recommendations which directly address the concerns raised. The government will decide on the appropriate course of action once it has heard the views of the Standing Committee.

Recommendation 7

The Committee notes that the deductibility of mortgage interest payments should be reviewed; such a review should give careful consideration to delivering the greatest benefits to the lowest income groups.

Response

Disagreed

The government has undertaken the review called for in this recommendation. The Minister of Finance provided a summary of its conclusions in the papers accompanying his budget of November 16, 1978, as follows:

The Second Tier Committee recommended a review of mortgage interest deductibility, particularly in the context of providing greatest benefits to lowest income groups. The government has presented its view of such a deduction. A consideration of proposals made to date for mortgage interest deductibility shows them to be generally regressive, discriminatory against tenants and to produce economically perverse effects on housing prices, capital markets and interest rates.

Recommendation 8

The Committee recommends that an in-depth study be made of the feasibility of implementing value-added based taxes in place of existing taxes.

Response

Disagreed

As noted in the 1975 federal Discussion Paper on Federal Sales and Excise Taxation, a value added tax (VAT) can be designed to be identical to any sales tax. The main advantage of a VAT, as a method of collection of sales taxes, is its effectiveness as a collection technique. The report concluded that there appeared to be little need for excessively onerous tax collection techniques given the tradition of voluntary taxpayer compliance in Canada.

Historically, a VAT has also been considered as a replacement for the corporate income tax, as some saw this as a means of promoting exports by exempting them from tax. Such a substitution would amount to a reform of the tax system. Significant considerations would arise, for example, in ensuring that such a structure was equitable in its treatment of corporate-source income as opposed to other income, of relatively capital and labour intensive firms, of operations with a different degree of vertical integration and in its acceptability to our trading partners. Such a structure could well preclude certain incentives that are rightly part of the current income tax system. Any partial substitution of a VAT for income taxes in only some sectors would pose further problems.

The last decade has seen dramatic changes in the tax system. At this time, stability in taxation and tax simplification is of paramount importance. It would not serve a useful purpose to embark on an extensive review of value added taxation at the present time.

Other Considerations

There are three other areas in the Committee report that are not recommendations but which deserve a response.

A large number of task forces recommended that the government adopt some form of inflation accounting in the measurement of business income for tax purposes.

The government does recognize the distortions that arise from use of historic cost accounting in an inflationary environment. It has come to be generally accepted that inflation not only leads to an overstatement of profit because of first-in first-out inventory and historic cost depreciation accounting, but also to an understatement of profit because accounting conventions overstate the real cost of corporation borrowing during an inflationary period.

When the implications of debt financing are recognized, along with the full implication of accelerated capital cost allowances, the investment tax credit and the 3 per cent inventory adjustment, the over-all level of Canadian corporation taxation does not differ greatly from what it would be under a comprehensive system of inflation accounting. Again, the need to maintain tax system stability indicates caution in any early movement to a comprehensive system of inflation accounting. There would also be many considerations in such a move related, for example, to the changes in tax burden on particular sectors in both directions that would result, tax complexity, the interaction between the corporate and personal tax, and the harmonization of Canada's tax system with that in other countries.

Labour representatives on the Committee asked that changes in the tax system be subjected to a review that assesses the impact the change has on the tax system as a whole and on the equity-efficiency balance in particular.

The equity and efficiency effects of tax changes are one of the basic considerations in labour's analysis. The comparison of taxes in Canada and the United States, published as part of the budget material provides a considerable amount of information on the equity and efficiency of Canada's system. First Ministers, at their conference on November 27, 1978 agreed to publish the federal-provincial review of mining taxation. From time to time it may well be appropriate to continue this trend. The government believes that intelligent policy choices and discussion require that such information be widely available. It is not of the view, however, that a full scale review of the tax system would be productive at this time.

The Committee disagrees over the taxation of capital gains. Business members felt that the tax should be liberalized or eliminated to increase investment incentives and because revenues were small in relation to administrative costs. Labour members felt that the tax should be expanded to tax all, rather than half of gains, on the basic philosophy that all income, however accumulated, should be taxed.

It must be recalled that the introduction of taxation of capital gains in 1972 included only one-half of gains in income for tax purposes and was accompanied by significant reductions in the marginal tax rates on higher incomes and by the elimination of federal estate and gift taxes. Removal or substantial reduction of tax on capital gains would undoubtedly give rise to significant pressure to reverse these other measures and would at least require their re-examination.

One-half of capital gains in income is subject to tax. The federal government has put in place other measures to ensure the burden of taxation from this source is equitable. Taxation of capital gains on family farms, whether incorporated or unincorporated is deferred as long as the farm property remains in the family. Similar treatment applies to gains on shares in a small business corporation. Capital gains are eligible for the \$1,000 investment income deduction. The 1977 budget doubled the amount of capital losses that may be deducted against other income from \$1,000 to \$2,000. Recent measures removed this limit in the case of losses on the sale of shares in a small business corporation. The enhanced dividend tax credit acts to reduce tax on those individuals who hold equity in Canadian corporations.

In relation to labour's point of view the government of course believes this taxation of capital gains is important. Indeed, there is not a country in the industrialized world that does not either tax capital gains or wealth on an annual basis, or estates and gifts. Many countries include more than one of these levies in their tax structure.

In this regard it should be noted that a relatively large share of capital gains accrues to a small number of upper-income taxpayers. Tax equity requires inclusion of capital gains in income subject to tax. The government is thus not prepared to eliminate the

tax on this income source. Substantial reductions in tax on capital gains would add greatly to the complexity of the tax system by re-opening a significant gap between the tax treatment of this income source and distributions from corporations in the form of dividends. This would necessitate re-introduction of rules to avoid tax abuse and thus act to negate the 1977 tax changes which simplified the corporate tax structure in the area of surplus stripping and corporate reorganizations.

The federal government has put in place more effective methods to encourage private investment that avoid the serious repercussions of removal of tax on capital gains.

RESEARCH AND DEVELOPMENT

The Committee's major concerns were with the low level of national resources devoted to research and development, the need to aim for self-sufficiency in technology, and the provision of government support on a more flexible, longer-term basis. In responding to the recommendations the government endorses the need for higher levels of R&D and outlines measures, many of which have been put in place within the last year, to improve the quality and nature of government support.

Recommendation 1

While the Committee does not want to set down a specific goal (e.g., a certain percentage of GNP), there should be a significant increase in the level and percentage of national resources devoted to R&D.

Response

Agreed

Science and technology have long played an essential part in Canada's development and are likely to influence our future in an even more dramatic way. The government recognizes this fact and is convinced that a vigorous and far-sighted Canadian research effort is vital. In light of this, the government has announced its intention to strive for a significant increase in the share of national resources devoted to R&D and has set a target for national expenditures on R&D of 1.5% of GNP to be reached by 1983. The government will be looking to the private sector to take every opportunity to increase its effort in this important area.

Recommendation 2

The increase in the share of national resources devoted to R&D will require more, not less, government support at all levels. The thrust of increased government support of R&D should, the Committee recommends, be in the direction of indirect activity (i.e., the provision of tax/grant support) rather than direct government R&D activity.

Response

Agreed

The federal government has recently announced new long-term policies and immediate measures aimed at increasing the level of R&D. The thrust of these measures has been to increase the level of R&D performance by the private sector, particularly by Canadian industry. The government's policies have further been aimed at encouraging Canadian industry to take advantage of the results of research conducted by university and government scientists. Its recent initiatives include:

A. Expansion of the Contracting Out Policy

Under this policy, departments are encouraged to look to the private sector for meeting their science and technology requirements rather than performing them in-house.

B. Tax Measures

Recent federal budgets have included important new tax incentives for industrial research and development. These measures are the following:

March 1977 Budget

Investment tax credit for current and capital R&D expenditures of 5 to 10% depending on the region.

April 1978 Budget

A special allowance of 50% on any increase in R&D spending over the previous 3-year average. This deduction is in addition to the basic immediate write-off that has been in place for some years. As a result, firms can write off up to 150% of eligible R&D expenditures.

November 1978 Budget

Indefinite extension of the investment tax credit as applied to R&D, and an enrichment of the credit to 10% or 20% depending on the region, and to 25% for all small Canadian controlled business.

C. Other Programs and Policies

On June 1st of this year, the Minister of State for Science and Technology announced, on behalf of the government, important new measures for stimulating research and development in Canada. These included:

- the commitment to use federal government procurement to stimulate industrial research and industrial development in Canada;

- new incentives to encourage job creation for scientists and technicians in industry;
- expansion of the National Research Council (NRC) Program of Industry-Laboratory Projects (PILP);
- creation of industrial innovation centres to aid industry;
- assistance in the development of regional centres of excellence; and
- increased funding for university research into areas of national concern.

In addition, the federal government has initiated federal-provincial discussions at the Ministerial level on research and development, as an indication of the strong priority given to this subject. The Minister of Industry, Trade and Commerce has also recently announced a generous enhancement to the innovation component of the Enterprise Development Program (EDP).

Recommendation 3

Direct government R&D activity should emphasize basic research. Developmental R&D done by government should be undertaken on the basis of consultation with the private sector and in view of specific market opportunities.

Response

Agreed

The present policy of the government is that the government's mission-oriented science and technology requirements are to be directed to the private sector for performance except in very limited circumstances where it is in the national interest to have this work carried out directly by the government. Thus, the government is endeavouring to progressively redirect its ongoing science and technology activities to the private sector. This has led to an increased participation by the private sector in meeting the government's science and technology requirements in areas such as national surveys and mapping, ocean hydrography, communications and transportation research, and food standards monitoring.

The government agrees that basic research should usually be done in universities and product and process development in industry. The government should provide the climate and assistance for this. This is the reason the government has put in place incentives, grants and a policy of contracting its science and technology needs where feasible. The government itself conducts research, of either a basic or developmental kind, when it is required by the national interest and is not being done by others.

Recommendation 4

Governmental assistance to R&D should be in the form of a package of available measures (i.e., tax measures in the form of write-offs and/or tax credits, or direct shared-cost grant programs) that can be applied flexibly depending on the characteristics of individual projects.

Response

Agreed

The nature and flexibility of use in the assistance available to industry is, the government agrees, an important factor promoting research and development activities. The federal government has endeavoured to provide its assistance through a wide range of instruments including tax measures (in the form of write-offs and tax credits), direct grant programs on a fully-funded or shared-cost basis, and through procurement measures. Although any single measure may not be available in all cases, in aggregate, the measures are intended to direct assistance to those cases where it is in the public interest to do so, and, in an appropriate form.

Recommendation 5

Since direct funding does reduce the risk shouldered by the entrepreneur, some "pay back" mechanism is appropriate in those instances where the research has led to a successfully commercialized and profitable venture.

Response

Agreed in part

The government agrees, in general, that a "pay-back" mechanism is useful in appropriate circumstances. However, in determining these circumstances, a variety of considerations need to be taken into account.

The government has tried to incorporate this approach into some of its programs. For example, the Defence Industry Productivity Program includes a section which provides contributions to defence or defence related R&D projects. These contributions are repayable out of the profits generated from the sale of the products. However, the administration of this pay-back provision poses major administrative problems and the process can be highly arbitrary due to allocations of overhead costs. The provision also involves substantial red tape and paper burden due to the need for audits and negotiations with the company. The large defence firms which use DIPP are currently required to pay-back the R&D contribution out of the profits generated.

Another example where the government has used a "pay-back" mechanism was in the original Program for the Advancement of Industrial Technology. It was found however to be contributing very little to the development of Canadian research and development activity. As a result, after several years, this mechanism was

modified to a shared cost approach, now used for the Enterprise Development Program. There are as well pay-back mechanism used in certain specific instances in the Enterprise Development Program, for example, under the Enterprise Development Program loan arrangements. A pay-back system is also used under certain government procurements where the Crown retains rights for patents developed under contract. More generally, the fruits of a successful undertaking will be shared with the public through increased tax revenues from the profits of a successful venture.

Recommendation 6

The Committee recommends that a special effort be made to assure a higher Canadian share of the R&D activity of foreign-based companies. Consideration should be given to the design of programs to achieve this end. R&D benefits to Canada should be given more emphasis as an explicit evaluation criterion used by the Foreign Investment Review Agency.

Response

Agreed in principle

The government substantially agrees with the Committee's recommendation that special efforts should be made to assure a higher Canadian share of the research and development activity of foreign-based companies. This is a matter to which the government is currently giving careful and increasing attention. During the past year, the Foreign Investment Review Agency has been giving increased emphasis to research and development benefits to be derived by Canada from foreign firms. This emphasis relates to the identifying of industry sectors where R&D is a key component of Canada's competitiveness, and to the securing of undertakings from foreign investors with respect to both the performance of R&D in Canada and the safeguarding of the Canadian firm's autonomy to exploit the research results to the maximum benefit to Canada.

In addition, the government is examining the ways in which its procurement practices could be changed to encourage its foreign-owned suppliers to conform to the government's principles of good corporate behaviour which are used by Industry, Trade and Commerce as a guide. (See Annex II, "New Principles of International Business Conduct"). The government has also recently established a task force on industrial benefits composed of representatives from the private sector. This task force will be looking at ways in which major projects in the private sector can be better used to obtain increased economic benefits to Canada.

Recommendation 7

The definition of "R&D" from program to program at one level of government, and from government level to government level, should be standardized. The Committee specifically recommends the definition used in the federal IRDIA program.

Response

Agreed in part

The government has been endeavouring to employ a standardized definition of research and development wherever possible. In fact, the definition used under the federal IRDIA Program follows this model, which is also the basis of the definition used in the Income Tax Act and by Statistics Canada. Where a different concept is used such as under the Enterprise Development Program, this is because it is specifically intended that the program apply to a broader area of expenditure, namely those expenditures associated with product innovation. Any change in the Enterprise Development Program criteria to agree with the IRDIA concept would involve a narrowing of government support to the innovation process.

Recommendation 8

Government assistance to R&D should be available over a sufficient period of time -- say 10 years -- in order to induce a long-run commitment to R&D activity on the part of the private sector.

Response

Agreed in principle

The government recognizes the importance of a long-term commitment to R&D. In fact, its assistance in this area is available under programs that are in place indefinitely or, as in the case of the special 50 per cent allowance, for increased R&D expenditures for a 10-year period.

Recommendation 9

Safeguards should prevent the transfer outside the country, without compensation, of R&D benefits financed at public expense.

Response

Agreed

The federal government shares the goal of increasing Canada's research and development effort with emphasis on development and use in Canada. The standard contracts signed under the innovation components of the Enterprise Development Program and the Defence Industry Productivity Program require that the results of development projects be exploited in Canada. Permission to exploit the results outside of Canada requires a Ministerial waiver.

ENERGY

The recommendations of the Committee calls for a more carefully developed national energy policy involving the federal and provincial governments in consultation with interested parties. The government's response notes that the federal government has a national

energy policy set out in "An Energy Strategy for Canada: Policies for Self-Reliance". This policy and related government measures cover concerns related to the up-grading of resources, financing and pricing.

Recommendation 1

A national energy policy should be developed by federal-provincial governments in consultation with interested parties. The objectives of such a policy should be:

- to ensure that Canada retains energy self-sufficiency in the long term;
- to develop energy exports in a manner which will positively ensure that Canada will not run out of appropriate energy sources in the future;
- to co-ordinate energy development plans and future use in Canada.

The Committee recognizes that such a policy effort might, in some instance, infringe on traditional rights enjoyed by the private sector prior to the energy crisis. The Committee recommends such intrusions be kept at a minimum consistent with the national interest and public good. This policy should take into account the welfare of the nation in the long term and should recognize that energy is one of the keys to Canada's survival as a trading nation, and its future self-sufficiency and is the basis for the future health and growth of its industries.

Response

Agreed

The federal government agrees that an energy policy responding to national requirements is of importance and fundamental to improving the competitiveness of Canadian industry. The government does have such a policy which was developed in response to the energy crisis and which incorporates the objectives stated by the Committee. This energy policy as set out in "An Energy Strategy for Canada: Policies for Self-Reliance" has nine policy elements including (i) appropriate energy pricing (ii) energy conservation (iii) increased exploration and development (iv) increased resource information (v) interfuel substitution (vi) new delivery systems (vii) emergency preparedness (viii) increased research and development and (ix) greater Canadian content and participation. Since the commitment to these policy elements was made, practical measures have been implemented with respect to all of them in order to meet certain specific energy-related targets which the federal government has set for itself.

More particularly, with regard to the objectives stated by the Committee, clarification is needed in the case of such terms as "self-sufficiency" and "self-reliance". The government, in pursuing a policy of "self-reliance", has the objective of ensuring that Canada's total energy needs balance-out with regard to imports and exports. In contrast a policy of "self-sufficiency" seems to have the objective of developing Canada's energy resources in such a manner and with such a distribution system as to make it unnecessary to import any energy requirements. In the event the Committee intended the government adopt such a policy, it should be aware that this might involve unacceptably high costs which would have to be borne by industry and consumers either directly or indirectly. With regard to the second and third objectives, these are provided for in the federal government's national energy policy. For instance, the legislation governing the National Energy Board's responsibilities and those of the Atomic Energy Control Board has provided for many years the type of export control called for in the recommendation.

The recommendation calling for a national energy policy to be developed by federal and provincial governments in consultation with interested parties, is a process which has proved exceedingly difficult in practice to pursue. The existence of very strong regional differences on energy policy matters for example, produce interests versus consumer interests which have to be dealt with by Energy Ministers and by First Ministers, makes such a consultative effort difficult at the best of times. Nevertheless, there has been and continues to be extensive consultation on all major issues in energy policy between the provinces and the federal government. The outcome of these consultations has been a great deal of cooperation on various energy matters within the context of the national energy policy as set forth in "An Energy Strategy for Canada: Policies for Self-Reliance."

Recommendation 2

A timetable should be established to bring these resources on stream in a way that would create an orderly flow of capital and extend the life of our non-renewable resources.

Response

Agreed in principle

The government agrees that the phasing of resource development is useful. The report "Financing Energy Self-Reliance" published in 1977 in part addressed this theme. The importance of such planning is that it enables government and the private sector to proceed on a number of fronts in the development of the country's energy resources. Such planning also assists in supporting projects that will be most economic. The effectiveness of such planning in the longer-term is limited however since rapidly changing domestic and international circumstances can affect decisions relative to any specific energy development project.

The report on "Financing Energy Self- Reliance" clearly established that there should be no major problems either with the macroeconomic adjustments or the financing associated with increased energy investment over the next 15 years. The Minister of Energy, Mines and Resources has tabled a list of potential future energy projects. The problem of providing for an orderly development of such projects, should they be economic, is of course facilitated through the exchange of information between business, government and over interested parties. In some instances, the federal government has become directly involved in the planning and financing of major energy development such as the tar sands developments (Syncrude) and the indirect involvement through Petro-Canada.

Recommendation 3

Pricing and taxation policies be so structured that adequate energy sources will be developed.

Response

Agreed

This is the objective of federal policy. The last two budgets have contained measures aimed specifically at increasing domestic supplies of energy. Examples include the frontier depletion allowance, which provides a portion of well costs above five million dollars, the special depletion for tertiary recovery projects, the policy of providing international prices to new non-conventional oil sources, and the sales tax exemptions for heat pumps, solar cells, solar furnaces, wind generators, etc. More generally, the federal policy has been to (i) impose appropriate income tax rates on energy production and development, (ii) provide extensive and generous reinvestment incentives to encourage new energy development, (iii) provide selected commodity tax exemptions for new energy industries where investment incentives are less appropriate.

Recommendation 4

The conservation of energy is an integral part of such policy and it is emphasized that there is potential for the more efficient use of waste products. For example, in the forest industry, current environmental constraints in this area should be re-examined. The program to establish energy conservation goals would also be enhanced by co-ordination between energy suppliers and users.

Response

Agreed

The conservation of energy as well as the more efficient use of waste products has been a continuing concern of the government. One of the specific measures intended to promote their objective has been the operation of industrial task forces in industry to examine ways and means of achieving greater efficiency in the use of energy.

The Department of Industry, Trade and Commerce operates an Industrial Energy Research and Development Program under which financial assistance is provided to industrial firms to undertake development of processes that reduce energy consumption. To supplement these efforts, the Minister of Energy, Mines and Resources established a program in mid-1978 amounting to \$380 million program over five years in promoting the use of solar energy and greater conservation in the forest industry.

Recommendation 5

Where possible energy should be developed and sold in the form that represents the optimum amount of upgrading.

Response

Agreed

While this has been a long-standing objective of the federal government in relation to all natural resources, the government has been particularly concerned that energy resources are being efficiently exploited. In addition to taking a general policy stance favouring such an objective the government has put in place or has redirected several programs to encourage upgrading of resources. These include incentive grants from DREE, research assistance grants from Industry, Trade and Commerce to aid in the development of new technologies, and other assistance programs. Resource upgrading has also been a principal criteria used by FIRA in its review of foreign investment applications, one which has achieved considerable success in new investments in upgrading. A fundamental objective of Canada's position in GATT negotiations has been to achieve access for processed Canadian resources, particularly to those markets which are currently the major recipients of unprocessed resources. The government has also introduced various legislative amendments such as the Imports and Exports Control Act (1974) aimed at encouraging upgrading. A recently introduced federal bill relating to uranium is partly aimed at controlling the development of uranium in Canada's interest. Specific tax incentives provide for lower tax rates for processing activity. (40 percent versus 46 percent.) These also include a two-year write-off for assets used in manufacturing and processing. These measures have helped to create an environment which encourages processing of resources, including energy resources.

Recommendation 6

The pricing policy for energy should ensure that Canadian secondary producers are not put at a cost disadvantage relative to their international competitors, particularly those in the United States. Therefore, serious consideration must be given to the appropriate U.S. pricing structure in establishing the pricing policy in Canada. At the same time, prices in Canada must change at a rate that does not exceed the capacity of the user industries to adjust.

It is also pointed out that without an appropriate link to U.S. prices, certain industries, such as the fertilizer industry, will have no incentive to expand.

Response

Agreed

The federal government's announced intention is to move energy prices toward world levels, bearing in mind the requirement that Canadian prices not exceed appropriate levels in the United States. The purpose of this policy is to assure the efficient allocation of resources without detrimentally affecting the comparative cost position of our industry relative to its main competitor.

TRANSPORTATION

Agreed in principle

A number of general concerns were expressed by the committee regarding the trade-offs between equity and efficiency, the rate setting mechanism and the rate appeal process. Bill C-20 (an Act to amend the National Transportation Act, the Department of Transport Act and the Railway Act) had first reading on November 16, 1978 in the House of Commons. This Bill lists a number of principles governing transportation policy which reaffirm the government's commitment to an effective and efficient transportation system. These principles will meet, to a significant degree, the general concerns of the committee and many of the specific concerns voiced by the sector task forces.

Some of the key principles are listed below:

- a) commercial viability will be an objective both in the operation of transportation services and in the provision of facilities and services;
- b) where government(s) decides that any such service and/or facility is required for the achievement of national or regional, social and economic development objectives, these objectives will take precedence over those of commercial viability whenever the two are in conflict;
- c) where a decision of government(s) requires that the achievement of these social and economic objectives takes precedence, the benefits and costs involved will be identified and any relevant additional costs assumed by the government(s) concerned;
- d) where effective competition exists, transportation rates and services will be established through the working of the market mechanism, but where no effective competition exists, transportation rates and services will be so regulated as to give transportation users the same protection as they would have if effective competition existed.

With regard to the rate appeal process, the law requires a prima facie case to be made to the Canadian Transport Commission (CTC) before the CTC will make an investigation. The CTC has been under no time limit to decide if a prima facie case has been established. An amendment proposed in Bill C-20 will expedite the process by judging a prima facie case to have been made if the CTC has not indicated otherwise within 90 days of an application for leave to appeal, and by providing for more informal appeal procedures. It might be noted that, in the past, the CTC has often acted informally (and successfully) as a catalyst in the resolution of carrier-user problems before they have become the subject of an official appeal.

Other amendments proposed in Bill C-20 concern the setting of freight rates under the Railway Act, and are designed to ensure that the freight rate structure remains flexible in the face of competitive situations, while protecting the user from anti-competitive behaviour on the part of the railways.

REGIONAL DEVELOPMENT

The principal focus of the Committee's recommendation was to ensure that regional development assistance was effective, created long term employment, did not result in unnecessary transportation or industrial over capacity and enabled the harmonizing of federal and provincial policies. The government agrees with this thrust. The response outlines measures already in place to promote these objectives by ensuring frequent business and government consultation, and providing flexibility with regard to the nature of assistance provided (tax incentives, grants or loans).

Recommendation 1

Provincial governments publish on a regular basis their priorities and compare their plans at federal-provincial meetings in an attempt to reach consensus and harmonization.

Response

Agreed in principle

While this recommendation falls largely within provincial jurisdiction, it is worth noting that a description of plans is provided to some extent in the federal-provincial General Development Agreements and Subsidiary Agreements which publicly spell out priorities for development and specific plans over a time horizon of several years.

Recommendation 2

To the extent possible, on proposed major government-assisted industrial projects, there be consultation with business and labour prior to grants being made with a view to minimizing national fragmentation or overcapacity in any industry.

Response

Agreed in part

The government is concerned with the issues of fragmentation and overcapacity. For this reason, among others, it is the policy of the Department of Regional Economic Expansion to discuss possible initiatives with affected parties except where such discussions are not considered feasible or would compromise confidential business information. Careful monitoring and continuous consultations with the Department of Industry, Trade and Commerce in the project evaluation process mean that the incidence of fragmentation or overcapacity due to the incentives policy is increasingly rare. Each project for which a grant is sought is examined to ensure that it responds to a growth opportunity and does not simply displace existing production. Fragmentation should not be confused with healthy competition that might result from increasing economic diversity in slower growth regions. For major government-assisted industrial projects, extensive consultations among departments and other groups take place before decisions are reached.

Recommendation 3

The primary reliance on the grant system as an incentive mechanism for industries to locate in the less-developed regions of the country be reconsidered and that loan or tax instruments be made available as appropriate. Where grants are made, they should be paid out over an appropriate period of time to encourage sustained operations.

Response

Agreed in part

The recent budget has enriched tax credits for investment (both general and for Research and Development) and employment and the regional tilt of these programs, following R.D.I.P. designation, makes decisions to locate and expand in slow growth areas more attractive. The question of favouring tax instruments over grants for regional grants for regional development assumes that tax incentives would be easier to administer. However, unless such assistance were to be provided on a completely unselective basis where many firms would acquire windfall receipts of public funds, some knowledge of the applicant's financial position is required. The tax status of an applicant is often even less predictable in advance than the profitability of the venture and detailed negotiations with each applicant would still be necessary if tax instruments were to be used selectively.

It should be recognized that, compared with the alternatives, grants have proven to be an effective instrument in Canada and many other countries. Among the advantages of grants are that they provide direct cash flow and that the cost to the taxpayer is visible and clearly understood.

Greater use of loan assistance is being considered be DREE but it must be recognized that care has to be taken to avoid unnecessary competition with existing public and private lending institutions and to avoid producing a situation where the taxpayer assumes all the bad risks.

Recommendation 4

The criteria for making incentives available to industry to locate regionally include:

- a) that they focus on import substitution as a means of developing a domestic market without damaging existing producers,
- b) the recognition that protecting existing jobs is as important as creating new jobs; therefore, modernization of a plant should be as eligible for assistance, and at the same level, as the building of a new plant,
- c) adoption of the approach that programs encourage industries that are "complementary to" rather than "in competition with" existing industry.

Response

Agreed in principle

The government agrees, in principle, with the list of recommended criteria but notes that a greater focus on the support of import substitution activities has to be consistent with GATT obligations. Both modernization and expansion of existing plants (which have among other effects the preservation of existing jobs) are already eligible for R.D.I.P. with a maximum grant of 20% of authorized capital cost. The government is currently giving consideration to raising the maximum limit that applies to modernization grants.

GOVERNMENT PURCHASING POLICIES

The principal concern of the Committee and the theme running through its recommendations was that the purchasing policies of the various levels of government in Canada were not being used in a manner supporting optimum industrial development. An additional concern was the industrial fragmentation caused by the locational requirements of some governments, the lack of coordinated standards between governments and an insufficient appreciation on the part of the governments in Canada concerning the extent to which foreign competitors derive advantage and strength from the purchasing policies of their home governments. The response of the federal government agrees in part with the concerns expressed and outlines measures

already in place or now under study, to coordinate standards more effectively, to support Canadian-based purchasing and to ensure foreign firms will not exploit the Canadian market in an unfair manner. The response also notes that to a fairly significant degree, the federal government's purchasing policies are aimed at encouraging small business.

Recommendation 1

Action be taken to standardize governments' design and specifications of as many products as possible. Such standardization should relate to the commercial market. The result will be economies of scale for Canadian industry such that unit costs are reduced, the public will benefit from the lower costs, and Canadian industries will be more competitive in the domestic and export markets. As sales increase there will be more investment and increased employment.

Response

Agreed

The need for a more standardized approach by governments regarding product design and specification requirements is a concern with which the federal government agrees and an area where it believes further action should be taken. In this regard, the government will endeavour to extend the process for purchases to additional products and to more public sector purchasers by encouraging provinces and municipalities to agree to use National Standards and Specifications.

The federal government is also taking a number of steps to achieve this. The Canadian Government Specifications Board is presently being restructured to include representatives of provinces, municipalities, industry and consumer associations. Within the federal government, the Treasury Board will direct that, where feasible, government departments and agencies standardize purchase requirements over time and aggregate them across departments so that maximum opportunities exist for scale economies and the development of Canadian sources of supply.

Additionally, the problem of standardizing design and specifications will be one of the topics to be explored by a joint federal/provincial working group that has been established by Ministers of Industry to examine areas of cooperation between governments in the use of procurement for industrial development.

Recommendation 2

The purchasing policies and practices of the various levels of governments should be more directly related to promoting industrial development in Canada, by taking into account:

- a) the tangible economic benefits to Canada of sourcing in Canada;

- b) the potential for offset arrangements where goods are sourced outside of Canada;
- c) the impact of their purchasing policies on rationalization and fragmentation of Canadian industries; and
- d) the extent to which their purchasing policies are consistent with the overall industrial development of Canada.

Response

Agreed

The federal government is establishing a mechanism to ensure that federal procurement is used effectively to promote industrial development as well as other socio-economic objectives, consistent with Canada's international obligations. Making better use of Canadian supply capabilities for public and private purchasing activity includes:

- a) development of a computerized Canadian source list for broad domestic distribution to trade posts and selected foreign purchasers;
- b) for large purchases, public and private, establishment of a government-industry review mechanism to maximize opportunities for Canadian-based suppliers to bid on domestic and foreign major projects.

With respect to the impact of governments' purchasing policies on rationalization, one of the options for consideration is a policy which would be aimed at supporting, on a selective basis, particular high-technology industries. Such a policy would result in procurement being directed to a limited number of firms in a product area so that quantities purchased would permit sufficient scale to enhance research and new product development and to develop a domestic competitive supply capability.

The joint federal/provincial working group on procurement referred to in the previous response will discuss this recommendation as a matter of priority and expects to put before Industry Ministers suggestions for coordinated purchasing arrangements which will be of assistance to all regions of Canada.

It should be noted that considerable work has been done by the federal government on the use of procurement to encourage the development of small businesses. As part of a package of initiatives aimed at small businesses the government announced last May that:

- a) the Department of Supply and Services will require that each major supplier appoint a coordinating officer for all subcontracts to small businesses in order to encourage more subcontracting to small firms by large companies receiving federal government contracts;

- b) companies bidding in government contracts will be requested to include in their tenders a plan to subcontract to small businesses; and
- c) the Comptroller General will examine methods to speed up payment on government contracts.

Recommendation 3

Governments recognize and take into consideration the realities of the trading practices of many foreign countries in the use of government purchasing power to enhance industrial development and should assure that purchasing practices in Canada are consistent with those of countries with which Canadians have to compete at home and abroad. This includes recognition of the impact on Canada of trading practices which are not legitimate under the GATT, including the dumping of foreign goods.

Appropriate purchasing policies by governments, including procedures, will reduce the incidence of dumping and that in turn will increase employment in Canada by potentially thousands of jobs.

Response

Agreed in principle

The federal government recognizes that foreign governments' purchasing practices can constitute a significant non-tariff barrier. Canada is participating in the negotiation of an agreement on government procurement in the MTN. This agreement is aimed at opening up a wide range of government procurement to international competition.

RATIONALIZATION

The Committee identified rationalization of Canadian industry as a process with considerable potential for improving productivity. The government agrees with this assessment. While the case is usually made for economies of scale in plant size and production, it is now thought that in many industries, operations necessary to capture these economies may not need to be as large as once presumed. This may be particularly so where numerically-controlled or computer-aided production is applied. Considerable economies, however, remain to be captured at the plant level and perhaps even more so at the firm level. For this reason, government fully supports the recommendations made by the committee in the area of rationalization. Specific undertakings are detailed below.

Recommendation 1

Domestic and international rationalization should be encouraged consistent with criteria such as job creation and skill development, industrial efficiency, increased domestic research and development, a more favourable balance of payments, and increased Canadian ownership.

Response

Agreed in principle

Measures to encourage domestic and international rationalization will be examined thoroughly by the government in consultation with industry and labour. These will include the possibility of policy discretion, mostly likely with respect to support programs, in favour of firms that demonstrate rationalization of Canadian facilities aimed at giving the Canadian operation a complete mandate for the development and marketing, both continental and international, of certain products. The "New Principles of International Business Conduct" (copy attached as Annex II) could be employed as a standard against which the performance of certain businesses would be measured.

In the consultative exercise, labour representatives urged that the Foreign Investment Review Agency screen foreign investments against the criterion of their contribution to the rationalization process. At this point FIRA uses this criterion when there is a clearly enunciated policy concerning rationalization in the industry sector in question. The use of rationalization as a criterion for foreign investment therefore depends on the development of a rationalization policy for appropriate sectors. This process has been significantly advanced through the sector task force consultations.

Recommendation 2

Federal and provincial governments should encourage setting up joint service facilities for operations that cannot justify such facilities on their own. Particular examples are joint private training programs and computer facilities.

Response

Agreed in principle

Governments recognize the importance of establishing joint service facilities for firms that cannot justify these on their own. At the federal level, productivity centres are being established to upgrade the technological capability of smaller firms. The Enterprise Development Program can make funding available to firms seeking to do feasibility studies into the establishment of joint design, marketing, transportation, warehousing and other facilities. Provincial research organizations provide services to improve management capabilities and industrial engineering. The federal government will conduct discussions with industry and provincial governments to identify the nature of additional support that may be justified to encourage further development of such joint facilities and to prevent program overlap among levels of government.

Recommendation 3

Competition legislation should be written in a way that encourages the rationalization process with provisions for appropriate checks and balances against the abuse of power contrary to the public interest.

Response

Agreed in part

Mergers of firms constitute one means by which scale economies and productivity performance can be enhanced. In the government's view, competition legislation cannot of itself actively encourage rationalization. This must be the task of other instruments. It should not, however, block mergers where economic advantages are demonstrable.

Under the Enterprise Development Program, special provisions are being made for 100% loan guarantees to sustain a failing firm where a viable merger is possible; to create risk reducing mechanisms to facilitate such mergers; and to fund feasibility studies into the merits of specific merger proposals. The footwear and tanning industries strategy recognized that fragmentation and scale problems must be overcome. As a result special provisions were instituted to provide financial assistance to firms to develop and implement rationalization plans, including mergers or acquisitions.

Recommendation 4

In the case of communities that would be adversely affected by plant shutdowns as a result of rationalization, there should be a community adjustment plan implemented which would include provisions for the application of existing programs (such as training and job-creation) as well as the bridging mechanisms that may not be part of existing ongoing programs (e.g., special pension provisions for those under the normal retirement age).

Response

Agreed

A variety of assistance programs are being developed or are currently operational each of which would have a role to play in assisting the community hard hit by plant shutdowns as a result of rationalization. The co-ordination of these programs and the identification of program gaps are issues which the government is prepared to consult on in detail with labour and industry. It should be noted, however, that the government also looks to the private sector to accept a greater responsibility (for example, in establishing special pension provisions for workers under normal retirement age) to ease special hardships created by plant shutdowns occurring as a result of rationalization initiatives.

Recommendation 5

The federal government should compile and publicize past rationalization cases in order to illustrate the potential benefits of rationalization.

Response

Agreed

The federal government will make available analysis it has done on the scope for enhanced productivity and market competitiveness through rationalization. It will, where the firms concerned agree, in addition, compile and publicize specific rationalization cases indicating where potential advantages and problems lie, and the assistance available to firms wishing to achieve rationalization of their facilities.

ANNEX I

FURTHER WORK REQUIRED

A number of tasks arise from the responses outlined in the previous text. Certain of these are actions to implement recommendations which the government has accepted. Others relate to further analysis that is underway to develop policy positions. They are summarized by issue below.

	<u>RECOMMENDATIONS</u>	<u>TIMING</u>
<u>TRADE AND THE MTN</u>		
1. Measures to improve the competitiveness of Canada's export credit facilities.	1	mid-year
2. Arrangements for further consultation with labour and industry on adjustment assistance.	5	mid-year
3. Improvement of safeguard procedures following outcome of the MTN.	8	year end
<u>MANPOWER</u>		
1. Implementation of recently-announced initiatives to encourage firms and individuals to participate in industrial training.	2	mid-year
2. Consideration of extending the duration of financial support for training past the 52 week maximum.	2	mid-year
3. Examination of management-labour proposals for levy-grant financing arrangements in sectors prepared to support them.	2	mid-yeer
4. Continuation of current review of mobility programs.	3	mid-year
5. Considerations of changes to mobility regulations to allow spouses to accompany recipients of job-search grants, instead of present arrangements whereby assistance is provided only <u>after</u> the initial job-search grant has resulted in a job offer.	3	mid-year

	<u>RECOMMENDATIONS</u>	<u>TIMING</u>
<u>TAXATION</u>		
1. Modifications in the structure of the commodity tax systems.	6	indefinite
2. Extension of the use of national standards and specifications by provinces and municipalities.	1	year-end
<u>GOVERNMENT PURCHASING POLICIES</u>		
1. Standardization by federal departments of purchase requirements over time and across departments.	1	mid-year
2. Establishment of federal mechanism for more effective use of procurement for industrial development.	2	mid-year
3. Establishment of a government-industry review mechanism to maximize opportunities for Canadian-based suppliers to bid on major projects.	2	year end
4. Federal-provincial working group to report to First Ministers on potential for cooperative use of procurement for industrial development.	2	year end
<u>RESEARCH AND DEVELOPMENT</u>		
1. Consideration of the use of pay-back mechanisms	5	mid-year
2. Examination of measures to ensure that foreign based companies do a larger share of their research and development in Canada.	6	year end
<u>REGIONAL DEVELOPMENT</u>		
1. Consideration of greater use of loan assistance in DREE programs.	3	year end
2. Consideration of increasing the limit on grants applicable for modernizing existing plant.	4	year end
<u>RATIONALIZATION</u>		
1. Examination of measures to promote rationalization including the use of policy discretion in favour of rationalized firms.	1	year end
2. Development of a rationalization policy for appropriate sectors.	1	year end

	<u>RECOMMENDATIONS</u>	<u>TIMING</u>
3. Identification of additional support required for joint service facilities.	2	mid-year
4. Consultation with labour and industry on the coordination of adjustment assistance programs for hard-hit communities and identification of program gaps.	4	mid-year
5. Publication of rationalization cases.	5	mid-year

ANNEX II

NEW PRINCIPLES OF INTERNATIONAL BUSINESS CONDUCT

These "new Principles of International Business Conduct" were announced by the government in 1975.

Foreign-controlled business in Canada are expected to operate in ways that will bring significant benefit to Canada. To this end they should pursue policies that will foster their independence in decision-making, their innovative and other entrepreneurial capabilities, their efficiency, and their identification with Canada and the aspirations of the Canadian people.

Within these general objectives, the following principles of good corporate behavior are recommended by the Canadian government. Foreign-controlled firms in Canada should:

1. Pursue a high degree of autonomy in the exercise of decision-making and risk-taking functions, including innovative activity and the marketing of any resulting new products.
2. Develop as an integral part of the Canadian operation an autonomous capability for technological innovation, including research, development, engineering, industrial design and preproduction activities; and for production, marketing, purchasing and accounting.
3. Retain in Canada a sufficient share of earnings to give strong financial support to the growth and entrepreneurial potential of the Canadian operation, having in mind a fair return to shareholders on capital invested.
4. Strive for a full international mandate for innovation and market development, when it will enable the Canadian company to improve its efficiency by specialization of productive operations.
5. Aggressively pursue and develop market opportunities throughout international markets as well as in Canada.
6. Extend the processing in Canada of natural resource products to the maximum extent feasible on an economic basis.
7. Search out and develop economic sources of supply in Canada for domestically produced goods and for professional and other services.
8. Foster a Canadian outlook within management, as well as enlarged career opportunities within Canada, by promoting Canadians to

senior and middle management positions, by assisting this process with an effective management training program, and by including a majority of Canadians on boards of directors of all Canadian companies, in accordance with the spirit of federal legislative initiatives.

9. Create a financial structure that provides opportunity for substantial equity participation in the Canadian enterprise by the Canadian public.
10. Pursue a pricing policy designed to assure a fair and reasonable return to the company and to Canada for all goods and services sold abroad, including sales to parent companies and other affiliates. In respect of purchases from parent companies and affiliates abroad, pursue a pricing policy designed to assure that the terms are at least as favourable as those offered by other suppliers.
11. Regularly publish information on the operations and financial position of the firm.
12. Give appropriate support to recognized national objectives and established government programs, while resisting any direct or indirect pressure from foreign governments or associated companies to act in a contrary manner.
13. Participate in Canadian social and cultural life and support those institutions that are concerned with the intellectual, social, and cultural advancement of the Canadian community.
14. Endeavour to ensure that access to foreign resources, including technology and know-how, is not associated with terms and conditions that restrain the firm from observing these principles.

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