



**Canada:
The State of the
Federation 1997**

**Non-
Constitutional
Renewal**

*Edited by
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FOREWORD

This year's edition of *Canada: The State of the Federation* represents a departure from past editions in that it was conceived with the idea of providing an integrated view on a selected theme. Hence, the longer-than-usual title to this the twelfth edition in this annual series.

This year's theme is non-constitutional renewal of the federation. From the time of the collapse of the Charlottetown Accord to the 1997 federal election there was a widespread conviction among political leaders at both the federal and provincial levels, and from both official language groups, that further efforts at constitutional reform would not be productive. This was reflected, for example, in the 1993 election platform of the federal Liberal Party and the 1995 platform of the Ontario Conservative Party. In both cases, the platforms were silent on the constitutional issue and the growing political gulf between a Quebec that had not yet signed on to the 1982 constitutional amendments and the remaining regions of the country.

This focus on non-constitutional strategy merits attention on two separate scores. First, it deserves attention in that it affects things that matter in the daily lives of Canadians, including policy goals and outcomes, democratic processes and the way our federalism functions. It is also important to know whether, and to what extent, it may have implications for a longer term political reconciliation between Quebec and the wider Canadian polity.

To shine light on these questions, two types of essays were commissioned. One was on policy issues that were selected as representative of the range of items that had been on the intergovernmental agenda over the last several years. Hence, the volume includes three chapters on social policy renewal, two on internal trade, one on the environment, and another on aboriginal affairs.

The second was on the intergovernmental strategies of individual governments. Alberta was selected because it has played a larger role in intergovernmental relations in Canada in recent years than its size alone would dictate. The election of the Conservative Party in Ontario has resulted in a radical reform agenda in that province with resulting consequences on intergovernmental relations. The change of premiership in Quebec also merits attention considering the state of political relations between Quebec and other parts of the country. An assessment of federal government strategy is also provided.

As is the tradition with this series, this volume also provides a chronology of major events in the federation from July 1996 to June 1997.

In keeping with the idea of this volume being more thematically organized, the work has already begun on the 1998 edition. The collection will serve as an examination of the changing political, social, economic, and cultural contexts in which Canadians find themselves at the end of the twentieth century. The redefinition of the state's role, changing conceptions of citizenship, the globalization of markets, new technologies, and the increased permeability of domestic cultures all combine to pose new challenges to the Canadian federation. These challenges have the potential to reorient the way in which Canadians articulate their more traditional political concerns such as language, federal-provincial relations, and social policy. The contributors to the 1998 volume will explore these challenges from a variety of perspectives and offer insight into how or if the federation will meet them.

As in previous years, this volume has been a product of team effort. I wish to thank the authors for their work and cooperation. Each chapter has been read by at least two independent readers and I would like to thank them also for their significant contribution. Thanks also to Mary Kennedy, Patti Candido and Tom McIntosh at the Institute, Marilyn Banting for copyediting, Valerie Jarus and Mark Howes of the Desktop Publishing Unit of the School of Policy Studies, as well as Michel Labbé and Chris Page for assistance with the translation.

Harvey Lazar
December 1997

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I

Overview

Non-Constitutional Renewal: Toward a New Equilibrium in the Federation

Harvey Lazar

Le rejet de l'accord de Charlottetown en 1992 et les élections du gouvernement Libéral fédéral en 1993, fut un point tournant dans la gestion de la fédération. Entre 1993 et 1997, les gouvernements fédéral et provinciaux ont placé les grandes réformes constitutionnelles de côté. Au lieu, souvent sans la participation du gouvernement du Québec, ils se sont concentrés sur des méthodes non-constitutionnelles pour tenter de renouveler la fédération. Ce chapitre donne une vue d'ensemble de ce qui a été accomplie par cette méthode non-constitutionnelle. Il explique pourquoi les gouvernements ont choisi cette stratégie et évalue son impact en relation avec quatre critères: l'efficacité des politiques et ses effets sur le fédéralisme, la démocratie et la réconciliation politique à l'intérieur du Canada. Il note que cette concentration sur les méthodes non-constitutionnelles a coïncidé avec la croissance de collaboration entre les gouvernements fédéral et provinciaux. Il suggère que cette croissance dans cette collaboration fédéraliste a du mérite. Il conclut qu'il a des influences qui travaillent pour et contre la continuation de cette approche collaborationniste, et que la façon dont ces forces se dérouleront auront des implications profondes pour le futur de la fédération.

INTRODUCTION

The failure of the Charlottetown Accord and the election of the federal Liberals in 1993 marked a turning point in intergovernmental relations in Canada. Whereas constitutional reform was the centrepiece of federal-provincial relations in the 1980s and early 1990s, the period since then has been overwhelmingly focused on the idea that the Canadian federation can continuously reinvent itself through non-constitutional means. The assumption has been that Canadian federalism has the capacity to adapt to changing needs and evolving circumstances regardless of the difficulty in implementing formal

constitutional amendments. The purpose of this volume is to take stock of what has been achieved through non-constitutional mechanisms during this period (1993-97) and to assess the nature and extent of federation reform and renewal that has occurred.

This first essay, which constitutes Part I, provides an overview of the effects of the non-constitutional approach. In so doing, of course, it draws heavily on the other authors. Accordingly, it is necessary to indicate briefly the scope and structure of the book.

Part II includes seven essays that concentrate on different aspects of the renewal process. Three of the chapters offer perspectives on social policy renewal, which has been at the heart of recent interprovincial and federal-provincial dialogue. Two chapters assess progress in implementing the Agreement on Internal Trade. The others deal with federal-provincial relations in environmental matters and federal-provincial-aboriginal relations. This selection of essays is not random. They were commissioned on the basis that they include some of the most difficult and current files in federation management and cover a large proportion of public expenditure and a wide range of intergovernmental practice.

Part III contains four essays. The first three examine the recent intergovernmental diplomacy of three provinces with a particular focus on the non-constitutional dimension of their policies. It concludes with a chapter on the non-constitutional approach of federal progress in implementing the Agreement on Internal Trade.

CHOOSING THE NON-CONSTITUTIONAL ROUTE: OTTAWA'S MOTIVES

The decision of the Canadian people to reject the Charlottetown Accord in 1992 put major constitutional reform into the political deep freeze. Leaders in the English-speaking regions of the country were of the view that further efforts to provide constitutional recognition of Quebec's distinctiveness would provoke an adverse political reaction that would further damage national unity. Within Quebec nationalist circles, both federalist and indépendantist, there was a belief that the rest of Canada had neither the interest nor the inclination to respond favourably to Quebec's constitutional aspirations. Constitutional fatigue was the order of the day.

Nowhere was the ennui more evident than in the federal Liberal Party's 1993 election platform — its famous *Red Book*. Reminiscent of the Sherlock Holmes' dog that did not bark, in over one hundred pages of carefully drafted analysis and undertakings, the *Red Book* chose to stay silent on the constitutional impasse and the seemingly widening political gulf between a Quebec government that had still not signed on to the 1982 *Constitution Act* and the

remainder of the country. The Liberals believed that their electoral prospects would be enhanced by being as different as possible from the Tories, and the Conservatives were identified with two failed efforts at megaconstitutional reform. Time and again, the Liberal leader, Jean Chrétien, expressed his disdain for the "C" word and argued instead that what Canadians wanted, more than anything else, was integrity in government and the dignity of work.

The electoral result seemed to justify this strategy. The Liberals swept to power with a substantial majority, winning 98 of 99 seats in Ontario and 30 of 31 in Atlantic Canada. In Manitoba they secured all seats but two. While the result was in many respects a handsome victory for Chrétien — the Liberals had won no less than four seats in each of the provinces — it was also noteworthy that the most politically disaffected regions had sent large majorities from regionally-based parties to represent them in Parliament. In Quebec the Bloc Québécois took 54 of 75 ridings while in the three western-most provinces the Reform Party was returned in 50 of 72 constituencies.

During the Liberals' first two years in office, the official antidote for Quebec's demands, and the alienation in western Canada, was "good government." The fiscal situation was tackled forcefully, especially through Paul Martin's 1995 budget and a comprehensive "program review." The latter put all departments through the financial wringer asking hard questions about whether it was necessary for government to be involved, whether the federal government was the appropriate order of government to be doing it and whether the job could be done more economically.

To be sure, the Liberals talked about the importance of job creation. In a speech in Quebec City on 18 September 1994, Prime Minister Chrétien remarked that it was unacceptable that unemployed Canadians who wished to work were unable to experience the dignity of putting bread and butter on the family table. There was the infrastructure program to at least give symbolic recognition to the weight that the prime minister attached to meeting his electoral commitments on job creation. But in Ottawa, restoring federal finances was seen to be inconsistent with the federal pump priming that might have otherwise helped to drive down the unemployment rate quickly. At the beginning of his term of office, the prime minister doubtless hoped that his government would identify the "silver bullet" that would enable both the deficit and unemployment to be reduced simultaneously. But gradually he and his government became reconciled to the idea that really substantial progress on the jobs front would require that the government first get its books in order; and by the time of the run-up to the Liberal's second budget, Paul Martin and the fiscal agenda ruled supreme in Ottawa.¹

As for constitutional reform, in an interview in December of 1993, the prime minister declared that his government would not hold constitutional talks with the Government of Quebec even if there were a majority vote in Quebec in favour of sovereignty. Five months later, during a visit through western Canada,

he repeated that he was elected to put people back to work, not to discuss a hypothetical separation. "If everyone were to shut up on that, I would be very happy," he was reported to have said. He continued: "The people of Canada, the people of Quebec included, are fed up with talking about the constitution."²

The election of the Parti Québécois (PQ) in September 1994 did little to change the position of the federal government on the merits of a new constitutional initiative. In the immediate aftermath of the election, Prime Minister Chrétien urged the PQ to hold its sovereignty referendum as soon as possible and reiterated that there would not be another round of constitutional talks. A month later he stated publicly that the federal government had no backup plan in the event of a "yes" in the coming referendum. In a speech in Montreal in February 1995 he dwelled on the achievements of the Team Canada trade missions overseas and the gains that this brought to Quebec, and all of Canada, noting at the same time Premier Parizeau's non-participation.

From time to time, the federal government criticized the ambiguities in the Parti Québécois' position regarding both the timing and wording of the promised referendum on separation. These occasional interventions suggested, however, that Ottawa was confident that the federalist side could handily win the referendum. This strategy was maintained up to the last few days of the Quebec referendum campaign when, in an apparently panicky effort to stem a tide in favour of those promoting Quebec secession, the federal government gave undertakings that it would, within the limits of its constitutional authority, recognize Quebec's distinctiveness and assure Quebec of a *de facto* veto over future constitutional amendments. In the event, the federalist side won the 30 October 1995 referendum by the slimmest of majorities.

The referendum results altered Ottawa's approach to national unity in some ways while leaving it unscathed in others. The consistency was reflected in the Liberal government's determination not to open the constitutional file.³ It remained closed during the last two years of Chrétien's first term of office, the Liberals being convinced that the consensus did not exist in the country for satisfactory constitutional resolution of various grievances, whether from Quebec, western Canada or Aboriginal Peoples. In this view, opening the file was bound to lead to failure and thus further damage national unity.

The prime minister acted swiftly to fulfill a number of commitments that he made to the people of Quebec toward the end of the referendum campaign. Thus, the House of Commons and Senate passed a motion recognizing Quebec as a distinct society within Canada in December 1995. Parliament also passed a bill in February 1996 guaranteeing that the Government of Canada would not make any constitutional changes affecting Quebec or any of the other major regions of the country without their consent (in effect lending the federal government's veto to the five regions). Although neither of these measures entailed constitutional change, they were an expression of the federal government's good faith to work toward an eventual constitutional amendment

in these two subject areas. For purposes of this volume, therefore, they are not treated as part of Ottawa's non-constitutional strategy.

Finally, the prime minister committed his government to renewal of the federation by specifying the roles and responsibilities of the two orders of government, by finding new models of federal-provincial cooperation in order to bring services and decisions closer to citizens, by making the federation more efficient, and by better reflecting the specific needs of the different regions of the country. It was this undertaking that was at the heart of Ottawa's non-constitutional approach.

In one sense, this latter commitment was simply an extension to the inter-governmental policies pursued in the first half of the mandate. The approach remained pragmatic and step-by-step, rather than a single large-scale package. But in another sense, there was a difference. The difference was in the breadth, intensity and determination with which the "renewal of the federation" through non-constitutional means was pursued. Increasingly, a litmus test for policy initiatives in Ottawa was whether they would help in the renewal of the federation.

"Renewal" had no precise meaning in the federal government's lexicon but it was clear that it did not include the transfer of authority to some provinces that would not be available to other provinces. Renewal accordingly excluded formal asymmetries. Moreover, while there was occasional talk that renewal could include moving powers to the federal government from the provinces in order to achieve economies of scale (an example often cited was securities regulation), this did little to obscure the fact that much of the debate was about which powers Ottawa was prepared to devolve to the provinces and under what terms and conditions.

A hypothesis of this essay is that the federal government's focus on non-constitutional renewal was motivated by a set of forces that may have made this approach the only politically viable option for managing the federation during the period under review here. One consideration was Ottawa's need to be able to show Quebecers that, contrary to the charges of the PQ and Bloc Québécois (BQ) and regardless of the difficulties in securing constitutional amendments, the country was not stuck with *status quo* federalism. Canada's system of governance was able to respond and adapt to changing needs and circumstances. In this perspective, agreements between Ottawa and one or more provinces that provided better policy, improved service delivery, reduced waste or clarified effective decisionmaking authority between orders of government understandably received increasing priority.

But improving federal-provincial relations for its demonstration effect was by no means the only influence on the federal government. As already noted, restoring the fiscal house was the overriding priority of the first Chrétien government; and since a substantial proportion of federal spending involved transfers to provinces, this led the federal government to open up its fiscal

arrangements with the provinces. Also, political leaders of virtually all party stripes and at both orders of government appeared to believe that extensive "overlap and duplication" between the provinces and Ottawa implied a large waste of taxpayer dollars and that a cleaner and clearer division of responsibility would accordingly save significant sums of money.⁴ This, too, pointed to a large change in the nuts and bolts of federal-provincial relations. But there was more. Voices from western Canada frequently carried a decentralizing tone or at least a demand for greater respect for the existing division of powers. New theories of public management were emphasizing a larger role for markets, for partnerships and for communities. At the same time, public opinion polls showed declining respect for government, including especially the federal government.⁵ In short, for Prime Minister Chrétien and his government, the need for a new set of relations with the provinces was driven by fiscal pressures and a government-reform agenda, neither of which required opening up the constitution, at least as much as it was by the Quebec factor.

Indeed, since a number of Quebec's traditional demands required constitutional amendment, the federal government's choice of a non-constitutional strategy was far from the ideal response to Quebec's aspirations. In some sense, it simply reflected Ottawa's judgement that other strategic options for responding to Quebec's disaffection were not practicable while, at the same time, some of the non-constitutional dossiers had to be dealt with for reasons largely unrelated to Quebec. In the circumstances, the best that could be done by Ottawa was to implement its non-constitutional approach with some sensitivity to Quebec's needs.

Alternative strategies were theoretically available and some were suggested. There were calls for radical decentralization, for example, from the Reform Party in western Canada and the Allaireists in the provincial Liberal Party in Quebec. But this was not in the cards for at least three reasons. The federal government perception was that Canada was already heavily decentralized in comparison to other federations.⁶ Second, the federal Liberals did not believe that the Canadian public wanted a radical decentralization.⁷ There may have also been a belief in Ottawa that such an approach would simply lead to a new and more radical set of demands.

A more centralized approach was if anything less viable. For one thing, it would have required dollops of federal money and Ottawa was in the process of withdrawing dollars from the system of intergovernmental transfers, not adding to them. Even with new money, several and perhaps most provinces would have been reluctant partners, having learned painfully over a period of years that Ottawa can be an unreliable funding partner. Moreover, several of the provinces were elected with mandates that indicated their strong commitment to the idea that the existing division of powers must be better respected (at a minimum). Such an approach would have also given excellent political ammunition to supporters of Quebec secession.

As for the constitutional approach, as already noted, opinion in Canada outside Quebec meant that a comprehensive constitutional strategy would be stillborn; and once the PQ was elected provincially there was even less reason to give attention to this option.

In short, the federal government believed that, at least for the period of its electoral mandate, it had little choice but to concentrate on the non-constitutional approach and to advance it in a way that best balanced the various factors noted above. Effectively, this meant dealing with issues, one at a time, employing legislative or administrative solutions, on the basis of the concrete circumstances of each file. In this sense, it was less an explicit strategy for winning the hearts and minds of the people of Quebec than an approach that presumed that good government and good policy would be as attractive to Quebecers as it would be to all other Canadians.

This strategy also fit well with the prime minister's preferred way of working. Jean Chrétien was more at home with an approach that promised concrete deliverables in bite-sized chunks than with more comprehensive schemes that required grand vision and that risked grand failure.

In this context, while the signals from the Prime Minister's Office in the aftermath of the Quebec referendum made it clear to federal ministers that new arrangements with the provinces were needed in order to demonstrate the "flexibility" of the federal system, the evidence does not suggest that any deal which could be sold to the provinces would necessarily win the personal support of the prime minister. The new arrangements had to provide better policy or better ways of implementing policies and therefore better government — not simply a federal-provincial deal for the sake of showing change.

A few examples, discussed more substantively later in this chapter or elsewhere in this volume, will illustrate the point that flexibility in federal-provincial relations was not given undue weight in the federal government's deliberations. Replacing the Established Programs Financing (the transfers for health care and postsecondary education) and the Canada Assistance Plan with the Canada Health and Social Transfer (CHST) was perhaps the most important decision taken by the federal government affecting relations with the provinces. With that decision, Ottawa eased up a little on the existing conditions that were attached to those transfers and committed itself not to establish any new conditions without the support of the provinces. But more significantly, the decision also enforced large reductions in planned transfers to the provinces reflecting the omnipresent federal fiscal agenda. These federal expenditure cuts were bound to play havoc with provincial finances and contribute to politically very difficult and sensitive reductions in provincial health, education, and social service budgets. For this reason, the federal government recognized that the CHST decision could not be helpful to its cause in the Quebec referendum. Yet, it announced the CHST decision before referendum.

In the case of labour market training, mainly due to political pressures from Quebec, the federal government agreed to transfer funds to the provinces. But it did not do so unconditionally. Rather, Ottawa insisted that the provinces recognize its role in the pan-Canadian dimensions of the labour market and it required provincial undertakings concerning language of service. A results-based accountability structure was also implemented for monies turned over to the provinces. Federal labour-market policy goals were therefore not abandoned although the way of reaching them led to a much larger provincial role.

The federal government refused to negotiate new fiscal arrangements with the Government of Ontario, notwithstanding strong and justified pressures from that province that Ottawa rectify past inequities. Here, too, the fiscal agenda won out, in this case over improved relations with Ontario. Also, the federal-provincial agreement to amend the Canada Pension Plan required large increases in contribution rates, indicating that Ottawa was not simply using intergovernmental agreements as a route to enhancing its popularity.

For Ottawa, therefore, federation renewal meant case-by-case management of individual files under which improved relations with provinces, including Quebec, were an important determinant of the federal approach but by no means the sole or even the overriding consideration. In that sense, the non-constitutional approach was less a strategy than an umbrella under which it was possible to group many federal initiatives and activities. What these measures all had in common was that they did not entail constitutional change, they generally involved less spending and they required new understandings between the two orders of government. This approach was characterized also by the idea that the kind of intergovernmental relationship that is appropriate will vary according to the functional realities and specific circumstances of each file.

The implications of this approach to public policy are mixed. On the favourable side, the flexibility that attaches to it allows for the specific facts of each case to be taken into account in improving policy outcomes. A diverse range of intergovernmental processes and institutional structures is at the disposal of governments to find the best possible solution and there is no dogmatism from the top that limits the scope for creativity. The result will frequently be "custom built," since the facts surrounding many files are unique.

There are also risks in this approach. Since the facts vary from file to file — and there will always be room for arguing about which facts are most relevant — it is difficult for provincial governments, and indeed the public, to understand Ottawa's overall sense of where the Canadian federation is or should be headed. No overarching view of federalism appears to underlie the government's approach. No deeply rooted set of principles is guiding its decision-making processes, through good times and bad. The result is that the federal government's behaviour is difficult to predict, making it an uncertain and at times unreliable partner for the provinces.

Of course, were there an intellectually rigorous philosophy from the federal government, and political discipline in adhering to it, the result would almost certainly be insufficient flexibility to accommodate adequately the diversity of provincial views and the differences across files. Therefore, this is not a plea for a single comprehensive theory of federalism as a basis for action by Ottawa. Rather, it is a caution that, in balancing the pressures that it has to deal with, there may be a need for a larger measure of coherence in the federal government's approach to the management of the federation. This is especially true to the extent that the government's strategy acknowledges the growing interdependence among orders of government and therefore requires an increased reliance on partnerships.

THE NON-CONSTITUTIONAL ROUTE AND THE PROVINCES

The federal government alone could not implement an effective non-constitutional strategy and the provinces and territories — with the frequent exception of Quebec after the election of the PQ — were at least as strongly committed to this strategy as was Ottawa. Accordingly, it is equally vital to understand what prompted the provinces to fasten onto this approach and to work with Ottawa on a wide range of issues.

The first point to note here is that provincial government leaders outside Quebec were reading the same polls as their counterparts in Ottawa. During the period under review here, they recognized that people in the English-speaking regions of the country were not prepared to support the kinds of constitutional amendments that might have been helpful to the federalist side in Quebec. For example, during the 1995 provincial election campaign in Ontario, the Conservative Party platform was as silent on issues of national unity as the federal Liberals had been in the federal campaign two years earlier. Second, like the federal government, the provinces were also faced with harsh fiscal circumstances and in some cases they were faster off the mark in making fiscal restraint a priority. The effect of this fiscal priority was to ensure their opposition to any possible enhancement of federal spending that might have privileged Quebec at the expense of other regions, reinforcing what Ottawa already knew about the non-viability of spending its way to national unity. At the same time, it helped to make them relatively understanding of the federal decision to cut back sharply on transfers to the provinces.⁸

Provincial leaders were motivated by other factors also. They wished to improve policy outcomes on some files (e.g., child poverty). They sought redress on others (e.g., Ontario's complaint about the unfairness of the way in which federal transfers to provinces are allocated). They apparently also believed that presumed economies could be achieved in still others (e.g., Alberta's and Quebec's claims for exclusive authority in labour market training).

They may have judged as well that a period of federal fiscal weakness was a good time to roll back perceived federal intrusions into their areas of jurisdiction (e.g., the concern of a number of provinces regarding the federal role in interpreting and enforcing the provisions of the *Canada Health Act*).

The extensive agenda and the scope of decisions flowing from the Annual Premiers' Conference in 1995 at St. John's and 1996 at Jasper are testimony to the provincial commitment to renewing the federation through non-constitutional means. The St. John's conference focused heavily on "social policy reform and renewal" and emphasized the "commitment to the objective of reducing and eliminating barriers to the free movement of persons, goods, services and investments among provinces and territories" under the framework of the Agreement on Internal Trade.

The communiqué from Jasper focused on jobs and growth and reaffirmed the importance to all governments of eliminating deficits and reducing debt. Premiers tackled the renewal agenda under a number of headings, including "rebalancing roles and responsibilities" and "social policy reform and renewal." The agreement among premiers on many issues excluded Premier Parizeau, emphasizing the gap between the Government of Quebec and other governments in Canada. The agenda and decisions of the 1997 Annual Premiers' Conference in New Brunswick indicated that there has been no change in approach since Jasper.

While provincial governments outside Quebec understood well the potential importance of federation renewal for national unity, and were sensitive to the need to act in a way that took account of Quebec politics, their change agenda was developed mainly on the basis of their own circumstances and needs.

ASSESSING THE NON-CONSTITUTIONAL STRATEGY

Nation-building, whether in the political or sociological sense, is never complete. Assessing progress normally entails a series of interim report cards rather than a "once and forever" measure of whether the nation has somehow "passed" or "failed" the test. What follows is, therefore, an interim evaluation of what was achieved during the life of the first Chrétien government (although the text occasionally reports on events prior to or after this period).

Four assessment criteria are used below. The non-constitutional strategy is considered initially in relation to the impact on three factors: policy effectiveness, the kind of federalism being practised in Canada, and democratic values. Finally, some preliminary consideration is given to the effects of the strategy for political reconciliation between Quebec and the wider Canadian polity.

POLICY EFFECTIVENESS

Given the weight attached to fiscal matters by federal and provincial governments, the analysis begins there and then deals separately with the four areas that are covered in the later chapters: social policy, internal trade, environmental policy, and aboriginal policy.

THE FISCAL AGENDA

The main policy priority during the review period was the need to improve public finances at both the federal and provincial levels. The record of success here, among both federal and provincial governments, was quite outstanding by virtually any standard. There is no extensive public record of the private discussions of the meetings of federal and provincial finance ministers. Nonetheless, it is evident from the annual budgets of each of the ministers that they were in broad agreement about the necessity of eliminating annual deficits and restoring the nation's finances. Progress was also discussed and reviewed periodically by federal and provincial leaders, as at the First Ministers' Meeting in 1995.

As for that part of the fiscal retrenchment that was imposed by the federal government through the cutbacks associated with the introduction of the CHST, this was implemented with rather less controversy in federal-provincial relations than might have been expected given the extent of the "hit" on the provinces. In some small measure, this may have been because the federal finance minister gave fair warning, almost 18 months, of what was coming. Partly it may have been due to the election of a number of provincial governments that made fiscal discipline a central feature of their policies. In his chapter, "Ontario and the Federation at the End of the Twentieth Century," for example, Sid Noel points to the fact that in its early months in office the Harris government was remarkably accepting of the CHST cuts. But it also had something to do with the fact that provincial governments recognized the inevitability of some large reductions (even if not as large as those that were imposed), that they lacked the power to prevent them and that somehow they would have to muster the political leadership to move beyond them. To be sure, some provincial leaders suggested that provinces were unfairly singled out in the federal cutbacks, leading to the usual exchange of numbers among the experts in fiscal federalism. Some premiers argued that if the federal government paid less for provincial programs, Ottawa should have less say about their content. But at least in the initial few years following the introduction of the CHST, these criticisms did not so dominate provincial reaction that it was impossible for the two orders of government to work together.⁹

The priority attached to improving public finances included wealthier and poorer provinces and governments that ranged from social democratic to radically conservative. After Premier Bouchard replaced Premier Parizeau, Quebec also committed to this goal. Overall, the extent of consensus and solidarity on the issue of public finances was quite remarkable.

Federal-provincial relations on taxation issues also received some attention during the review period. The Chrétien Liberals were elected in 1993 on a platform that included a promise to rescind the Goods and Services Tax. Not long after it was elected, the federal government began to interpret its electoral commitment as one that would be satisfied by a harmonizing of federal and provincial sales taxes. By the end of the federal mandate, however, harmonization agreements had been signed with three provinces only and to achieve these Ottawa had found it necessary to use costly fiscal incentives that had the effect of irritating non-signing provinces.

On a more positive note, the federal finance minister announced in late 1997 that Ottawa had agreed, after many years of federal-provincial discussion, to much enhanced flexibility for the provinces in the design of their income tax systems within the framework of the federal-provincial tax collection agreements. Whereas Ottawa's traditional position was that provinces would have to levy their taxes as a percentage of the federal tax payable, it appears that in the future provinces will be free to impose their tax directly on income and still use the federal government as tax collector.¹⁰

SOCIAL POLICY

The volume offers three chapters on social policy renewal — by Keith Banting, John Richards, and Harvey Lazar. While each author takes a somewhat different approach, all three touch in varying ways on the effects of the social policy renewal process on the first three of our assessment criteria, that is, policy effectiveness, federalism, and democracy. It is what they have to say about policy effectiveness that forms the basis for our remarks here.

Banting's focus is on the lessons learned from the post-World War II experience during which the modern welfare state was constructed.¹¹ The essence of his argument is that the combined federal and provincial postwar welfare state gave Canada, *de facto*, many of the elements of a social union; and that in relation to the equity and efficiency criteria that are usually associated with social policy, what was created merits high marks.

One of the few programs to receive enhanced funding during the first Chrétien administration was fiscal equalization. While Richards, "Reducing the Muddle in the Middle" is generally critical of intergovernmental transfers, he argues in favour of a strong equalization program. He also applauds the reduced conditionality associated with the CHST, although he would prefer that it eventually be phased out and replaced with an income tax point transfer

to the provinces. Richards similarly supports the direction of the most recent set of federal-provincial bilateral labour market agreements and is even firmer in his backing of the new National Child Benefit.

Lazar argues that federal-provincial relations became increasingly collaborative in the last two and a half years of the first Chrétien government following the enforcement of the CHST and that, in general, this has resulted in policy moving in desirable directions. In child benefits, the outcome should be some progress in reducing poverty among working families with young children while strengthening the efficiency of the labour market. The outcome of federal-provincial negotiations on the Canada Pension Plan was an enhanced level of funding for the CPP that should serve to improve its political sustainability. As for the new labour market agreements, which eight provinces signed with the federal government, they include an accountability structure that may serve as a prod on governments to improve results. Without wishing to be "Pollyannish," it is arguable that the public will, over time, be better served by the new arrangements in these three areas than those they have replaced.¹²

More generally, this was a period in which provincial and federal governments began to reconsider how to preserve the Canadian social union in the light of the damage done to the social safety net as a result of expenditure reductions. The provinces were initially (1994-95) skittish of venturing into this territory with the federal government, fearing that Ottawa would attempt to tarnish them with the political costs of the federal fiscal cutbacks that were then widely expected. But soon after Ottawa imposed the CHST, the provinces, except Quebec, took the initiative and have since been playing a major role in shaping the intergovernmental social policy agenda. As this volume was being finalized, at the urging of the provinces, debate was beginning about the possibility of a federal-provincial framework agreement on social policy. This has the potential to strengthen the social union and extend the social rights of citizenship.

Since the fiscal agenda trumped social policy over these years, there is no doubt that at the end of the review period, Canada had a weaker safety net at both federal and provincial levels than it did earlier in the decade. Within the new fiscal context, however, the intergovernmental process led to a number of measures that were, or had the potential to be, genuine improvements in policy, including in child benefits, CPP, equalization, and labour market training; and a federal-provincial dialogue had started for a framework agreement on social policy.

INTERNAL TRADE POLICY IMPLEMENTATION

The Agreement on Internal Trade (AIT) was signed in 1994 and it came into force a year later. There are widely divergent views as to whether the agreement

is a significant step forward in promoting a more perfect economic union and the economic rights of citizenship or simply a weak imitation of an international trade agreement. This dispute, for the most part, reflects differences of opinion about the provisions of the agreement as originally written, not observations about its practical effects on the behaviour of governments and other economic agents.¹³ This is a particularly relevant here for two reasons: the AIT contains numerous undertakings by governments to implement various commitments according to agreed timetables; and the way in which commitments are honoured also affects the ease with which its provisions can be used. Accordingly, the manner in which the AIT is being implemented is an appropriate test of policy effectiveness.

The heart of the AIT is the sector chapters that set out the various obligations to both reduce explicit barriers across borders and promote positive economic integration. One of the sectors most amenable to more integration is the government procurement market since it is directly within the control of the signatories to the agreement. Since the signing of the AIT, progress here has been significant. Non-discriminatory rules have been established and a common tendering system is expected to be operational within the next two years so that businesses anywhere in Canada will be able to access most public sector tenders on that single system. Schwanen, "Canadian Regardless of Origin," provides details regarding the implementation status of each of the commitments that governments have entered into noting which deadlines have been met and which ones have not. While Knox, "Economic Integration in Canada through the Agreement on Internal Trade," reports shortcomings with the bid-protest system, he concludes that "procurement at the federal and provincial level is more open and accessible across the country and, imperfect as it may be, Canada has an undertaking in place for a national public sector procurement market that was not there before."

In the case of labour mobility, the agreement requires that qualifications of certified workers from other jurisdictions be recognized and differences in occupational standards reconciled. At least 400 non-governmental occupational licensing bodies have been requested to participate and Schwanen reports that 300 have become engaged. Procedures are also now in force to remove barriers that individual Canadians face as they move from one region of the country to another. Knox cites several examples of individuals who were initially barred from practising their occupation in another province but who have used the consultation mechanisms of the AIT to resolve their disputes to their satisfaction. While it is too soon to know the extent of the actual progress that will be realized in this area, the early signs are promising.

The AIT facilitates economic integration by lowering the costs for firms doing business outside their home province. One example of progress is that the registration and reporting burdens have been eased for firms doing business

in more than one jurisdiction. A second relates to consumer protection where harmonization has been achieved in several areas (e.g., cost of credit). In several other sectors, the implementation process has been slower.

The report card on the AIT's dispute resolution provisions is mixed. The arrangements have proved effective in some cases. But the agreement and its provisions are poorly publicized. Solutions are too slow in coming and, if only for that reason, discourage those who have a need to resolve immediate problems.

The operating structures of the agreement are also weak. Knox observes that the Committee on Internal Trade (CIT) lacks authority relative to the numerous ministerial level intergovernmental committees that have grown up over the years in virtually all subject areas (sectors/chapters) of the agreement. This difficulty is compounded by the requirement that CIT decisions be made by consensus.

The agreement is a work in progress. Notwithstanding some achievement, the pace of implementation has been slower than originally planned. In part this may be because the attention of political leaders was diverted to more pressing matters, in particular, the fiscal agenda and the need for social policy renewal that came in its wake. Implementation also requires careful attention to thousands of small details, which is painstaking work that cannot realistically command the attention of first ministers.

This then suggests the need for stronger institutions at both the ministerial and secretariat levels to get the job done. The time has come for a set of decision rules that would enable the agenda to be advanced with something less than a unanimity rule. More transparency is also required if citizens, both individual and corporate, are to maximize their rights of citizenship under its provisions.

ENVIRONMENTAL POLICY

The record of policy achievement on the environmental front was disappointing. The Canadian Council of Ministers of the Environment (CCME) launched a major negotiating effort to better harmonize federal and provincial policy. The initial outcome was a comprehensive and complex Environmental Management Framework Agreement (EMFA) that would have devolved some authority from Ottawa, but the ministers ultimately decided not to proceed with this initiative. This was followed by a Canada-wide Accord on Environmental Harmonization under which subagreements were to be concluded on all areas of environmental management "that would benefit from Canada-wide coordinated action" and three such subagreements were developed on environmental assessment, standards, and inspection. While the Canada-wide accord was approved in principle in November 1996 by the CCME, the signing

date has been deferred twice since then and the House of Commons Standing Committee on Environment and Sustainable Development has recommended further delay (December 1997). Thus, at the end of the review period covered in this volume, it was not clear that this second arrangement would be ratified. In the meantime, events in the run-up to the 1997 Kyoto Conference suggested that both federal government and federal-provincial policymaking on major files like greenhouse emissions are inadequate.

Patrick Fafard, "Green Harmonization," documents a very extensive federal-provincial effort "marked by a considerable degree of cooperation" but with few tangible results. Since many groups with an interest in environmental matters are critical of the Canada-wide accord, as they were of the earlier EMFA, the delays are not necessarily a bad thing for environmental policy. But they also suggest a lack of accomplishment.¹⁴

POLICIES RELATED TO ON-RESERVE ABORIGINALS

Constitutional reform with respect to First Nations also remained on the back burner during this period and Ottawa instead chose to follow an incremental agenda of making agreements with aboriginal groups, and wherever possible, provincial governments. It refused to move away from this approach even after the report of the Royal Commission on Aboriginal Relations was released. Dealing with practical problems, one at a time, was as much the hallmark of the federal government approach to relations with First Nations as it was on the social, economic, and environmental agendas discussed above.

This strategy is documented by Audrey Doerr, "Federalism and Aboriginal Relations," whose method is to illustrate it by referring to agreements reached between Ottawa and various First Nations, often with the relevant province also involved. The focus is on three broad subject areas: land claims, education, and economic development.

On land claims in southern Canada, substantive progress has long been slow. There was, however, an increase in federal-provincial-aboriginal activity, especially in British Columbia — where with few exceptions land treaties were never signed with First Nations — and in Manitoba and Saskatchewan — where specific land claims required resolution. Accomplishments include the agreement-in-principle signed with the Nisga'a in British Columbia in 1996 and an agreement-in-principle among federal, Manitoba, and 19 First Nations in that province. Land claims settlements offer the potential of a stronger economic base for Aboriginal People and, for non-Aboriginal People, the prospect of greater certainty over the status of lands and in addressing third-party issues. While it may be many years before the outcome of this stepped-up activity bears fruit, these developments are encouraging. The recent Supreme Court ruling on the non-extinguishing of aboriginal title is a new development in

this process, however, and it remains to be seen how it will affect the settlement process.

In on-reserve education, the federal government legislates on schools and their operations and the provinces have effective responsibility for curriculum, standards, and teacher certification. Accordingly, to the extent that First Nations wish to assume jurisdiction and control over education, they need to deal with both the provinces and Ottawa. The potential benefit is that it simplifies the provision of educational services and places responsibility with the local community. Doerr provides recent examples of where this is occurring.

Economic development for on-reserve peoples remains a huge challenge for public policy. The rate of population growth is considerably faster than for the wider population and, on average, Aboriginal Peoples are much younger. Federal and federal-provincial policies, in conjunction with First Nations, emphasized institution-building in such diverse areas as aboriginal banking, oil and gas development, and property taxation as well as the more traditional federal-provincial-aboriginal joint development agreements.

Where policy is consciously developed in small chunks, it is difficult to generalize about effectiveness since the impact of those policies may be impossible to disentangle from the various other factors influencing outcomes for the target population. Moreover, where initiatives have a long time fuse, as is the case with land claims and education, there is yet a further barrier to commenting on policy effectiveness. Still, if the counterfactual to the kind of approaches described above is the traditional policymaking of Indian and Northern Affairs Canada, and the federal government's poor record in solving serious aboriginal social and economic problems, the direct participation of First Nations as equal partners in an intergovernmental process may be a genuine step forward.

SUMMARY ON POLICY EFFECTIVENESS

In summary, both orders of government agreed on the priority to be attached to restoring of public finances and made excellent progress on that goal. The finance ministers had less success in harmonizing sales taxes but, at the end of the review period, there were indications that long-standing federal-provincial differences regarding the amount of flexibility available to the provinces within the framework of federal-provincial income tax collection agreements might be resolved. There is a major work program under way to reconstruct the Canadian social union with provincial governments playing a leading role. Quebec has remained outside this initiative, illustrating the earlier argument that the non-constitutional strategy is not being motivated principally by concerns for political reconciliation with that province. Modest progress has been achieved in implementing the AIT. A variety of initiatives

are being developed and implemented in relation to aboriginal policy. While achievements are still small relative to what needs to be done, there were some steps forward in limited areas. The environmental area was the weakest area among those considered here. On that front, it was the failures that stood out.

THE EFFECTS OF NON-CONSTITUTIONAL RENEWAL ON CANADIAN FEDERALISM

The second criterion for assessing the effectiveness of the non-constitutional approach is its effect on the kind of federalism being practised in Canada. In this regard, it is important to recall that this recent focus has an honourable lineage. During the century following the Confederation of 1867, important adjustments were made in the way effective power was distributed between federal and provincial governments on a number of occasions in response to changing needs and circumstances; and these were generally implemented without constitutional amendment.¹⁵

In the decades prior to World War II, the two orders of government acted largely independently of one another in a relatively decentralized federation. The war years saw power centralized in Ottawa. In the immediate aftermath of the war, there was a short period of decentralization followed by a couple of decades of centralization in which the federal government used its spending power both to create federal-provincial shared-cost programs and to transfer money directly to individuals. These initiatives were often in areas of what would have otherwise been exclusive provincial jurisdiction. While both cooperation and conflict between Ottawa and the provinces marked this period, most provinces for most of the time were prepared to tolerate the larger federal role in return for the additional funding provided. The Government of Quebec did not share this view, however, consistently rejecting the political legitimacy of the federal spending power.

By the early 1970s, provincial governments were becoming increasingly concerned that shared-cost programs were distorting their priorities. As a result, block funding began to replace matching funds. This was also a period when areas of provincial jurisdiction became increasingly important public priorities (e.g., education, health care) and areas of federal jurisdiction less important (e.g., defence). Centralization peaked and there was once more a trend toward decentralization. But the size of the state remained far larger than was the case in the prewar years and so, despite the decentralization, the character of the federation was much different than the period of watertight compartments. The "mutual independence" of the prewar years was giving way to "mutual interdependence."

In short, prior to the period of intensive constitutional focus that began in the late 1960s and that came to dominate federal-provincial relations during the 1980s and the early 1990s, there were ebbs and flows in the effective distribution of power in the federation. It is also arguable that during these years, especially until the period of constitutional emphasis, Canada was one of the world's most successful federations. All of this suggests that the obsession with constitutional change that characterized the quarter century prior to the election of the Liberals in 1993 was in some sense a unique chapter in Canadian history. In this perspective, the recent focus on non-constitutional methods for dealing with pressures for change is a return to methods that have served Canadians well in the past.

How then do we characterize the federalism of the 1993-97 period under review? When examining the seven chapters in Part II as a whole, what emerges strongly is the *increase* in the extent of the *collaboration* between the two orders of government as well as the *diversity* in the methods of collaboration. This is not to suggest that these years were marked exclusively by such collaboration. To the contrary, the workings of the federal system remained an amalgam of arrangements that included a wide variety of federal-provincial, and in a few cases interprovincial, relationships. These included examples of classical federalism in which the two orders of government acted within their own jurisdiction largely independently of one another with no suggestion of hierarchy (e.g., both orders of government provided income support to unemployed people under certain conditions). They included as well cases of the federal government imposing conditions associated with shared-cost programs in areas of exclusive provincial jurisdiction (e.g., the federal requirement that provinces adhere to the conditions of the *Canada Health Act* to avoid financial penalty) and of non-hierarchical collaboration (e.g., the National Child Benefit).

But none of this was new. The architecture of the federation has long been based on a variety of different designs. What was new was the greater emphasis on collaboration by which I mean governments working together on a *non-hierarchical* basis in a way that reflects their *interdependence*. In this regard, the most effective work was found in the social area but only after a period of considerable tension when the provinces were suspicious that Ottawa would act unilaterally through its Social Security Review Process and indeed did act unilaterally through the CHST. After CHST, however, there was extensive federal-provincial collaboration on several social issues. There was, as well, the beginning of a debate regarding the possibility of national leadership in areas of exclusive provincial jurisdiction through interprovincial leadership.¹⁶ Collaboration did not always mean policy success. But even in the environmental area, the possibility of collaborative national decisionmaking through a formally integrated federal-provincial process was

explored via the EMFA. In the case of internal trade, there was much constructive work of a "nuts and bolts" nature going on but more might have been achieved with stronger institutions. As for the federal-provincial-First Nation relations, they were as diverse as the diversity that characterizes the circumstances from region to region.

The growth in collaborative federalism during this period may at first glance seem surprising. Much of the rhetoric from western Canada, as reflected in the federal Reform Party and the Klein government in Alberta, was suggestive of the disentanglement of classical federalism. The 1995 election of the Conservatives in Ontario resulted in another powerful voice apparently committed to such an agenda. In conjunction with a PQ government in Quebec and a large Bloc Québécois contingent in the House of Commons, it might have been thought that the political basis for enhanced collaboration would be lacking.

Yet underneath the rhetoric, the reality was sometimes different. In "Alberta's Intergovernmental Relations Experience," Gibbins notes that the Government of Alberta has had a long tradition of intergovernmentalism as a strategy for offsetting Alberta's weak representation in national institutions. In fact, Alberta was and remains a leader in the federal-provincial collaboration surrounding internal trade and it was the first of the provinces to enter into a bilateral labour market agreement with Ottawa in 1996. It also played a leadership role in the early work of the Provincial-Territorial Ministerial Council on Social Policy Reform and Renewal which, while calling for the end of federal unilateralism in social policy, at the same time acknowledged the federal government as a legitimate player in national social policy.

Spooked perhaps by the electoral price paid by the Peterson and Rae governments for their constitutional strategies, Premier Harris initially de-emphasized federal-provincial relations and focused his intergovernmental efforts on domestic policy (e.g., rationalizing roles with municipalities, school boards). But when his government did turn its attention to federal-provincial matters, it might have been expected to avoid the collaborative approach. Its rhetoric was small government and disentanglement whereas collaboration creates the image of complexity. The government also had a grievance against Ottawa because of its continued *de facto* financial discrimination against Ontario in a number of large programs. Further, with Ontario's economy continuing to integrate north-south, its self-interest in east-west collegiality might be declining.

Yet, Ontario recognized the pan-Canadian dimension in social policy and commissioned the Courchene report that in turn has helped to promote the idea of social union run collectively by the provinces. While relations with Ottawa were tense following a short honeymoon (e.g., Ontario Budget, 1997), Ontario nonetheless participated in collaborative efforts like the National Child

Benefit and current joint work on disability. The fact that collaborative federalism at the strategic policy level can lead to disentanglement at the program level may help to explain the interest of the Harris government.

As Réjean Pelletier shows in his chapter, Quebec has also been willing to participate in some collaborative activities especially under Premier Bouchard. This participation has stretched from Team Canada trade missions to a federal-provincial labour market agreement and included the internal trade and environmental files. At the same time, other provinces were strong supporters of collaboration. Both Saskatchewan and British Columbia, for example, played lead roles in creating the momentum to achieve the National Child Benefit.

When comparing the "collaborative" federalism of 1993-97 to the "cooperative federalism" of the 1960s, the fiscal context is an important distinction. Whereas the earlier period was one of rapidly rising public expenditure, and Ottawa was able to encourage provincial participation in national programs by undertaking to cover half the costs of the provincially delivered programs, the more recent period was within a framework of shrinking resources. Yet the intergovernmentalism that marked the years of the first Chrétien administration was if anything wider in scope than was the case two and three decades ago.

Two factors appear to be at play here. First, the incentive to collaborate does not disappear during tough fiscal times. It does, of course, decline in respect of shared-cost programs to the extent that Ottawa withdraws money from them. But shared-cost programs are not the only way in which the two orders of government impact one another and there are influences that work in the opposite direction. For example, fiscal tightness creates incentives for both orders of government to maximize the results from their expenditures and tax incentives but this may be difficult to achieve in areas where both orders of government are active unless they are cooperating with one another. In this regard, it is not uncommon for federal programs to operate through tax law or cash benefits and for provincial programs to operate through services, regulation or cash benefits in the same area. In these kinds of situations, either order of government may be able to thwart the effectiveness of the other unless they cooperate. The case of child benefits was an illustration prior to the recent creation of the National Child Benefit.

Fiscal tightness also increases incentives for downloading and uploading. But such gamesmanship also entails wasteful administrative costs that ultimately fall on the taxpayer unless governments work together to avoid such incremental costs. Even where there is no program overlap, the actions of one government can affect the other. Changes to the criminal code can influence provincial costs of administering the justice system and international trade or environmental commitments by Ottawa may force adjustments that affect provincial revenues or expenditures. While all of these examples also apply during periods of fiscal plenty, the incentive to do something about them is

stronger in tough times. All these factors have been at work in the period under review.

When comparing recent years to earlier periods of cooperation there is a second distinction worth noting. International borders matter less now in the economic, social, cultural, and environmental areas than they did three decades ago with consequences for internal borders as well. One result is a much bigger role for the provinces in areas that were once more or less exclusive federal domains. For example, globalization has led to international trade negotiations that involve items of provincial jurisdiction and therefore require provincial collaboration if international agreements signed by Ottawa are to be implemented. A second example is that growing numbers of Aboriginal People have left their reserves (crossed borders) and effectively become subject to provincial programming. These developments more than anything else reflect the increasing interconnectedness of what once were distinct activities and the consequential overlap of governmental roles with these changing circumstances.

While this interdependence has led to collaboration, it is different than the cooperative federalism of the Pearson era and the early Trudeau years. Existing shared-cost programs are much less conditional now than they were then. (The only large remaining shared-cost program with significant federally imposed conditions is, in effect, the health component of the CHST.) Also, Ottawa has undertaken to start no new shared-cost programs in areas of exclusive provincial responsibility without the agreement of most of the provinces and to compensate any provincial government that opts out of such agreements provided that province introduces a comparable program. This reduces significantly the amount of *hierarchy* between orders of government associated with shared-cost programs. Many of the other areas of recent collaboration, such as internal trade, CPP, and child benefits, involve partnership, not hierarchy.

The Canadian federalism of the interwar years was in significant measure characterized by *independence and non-hierarchy* between orders of government. The centralization of the war years entailed *independence and hierarchy*, with Ottawa in charge. The centralization of the 1950s and 1960s was something different because, by then, the role of the peacetime state was much larger than it had been in earlier decades and the relationship between orders of government had come to involve greater *interdependence* with significant elements of *hierarchy*. The non-constitutional focus of the years that coincided with the first Chrétien government, and especially the second half of that era, involved growing *interdependence* but with a greater respect for the idea that the two orders of government should relate to one another on a *non-hierarchical* basis.

THE EFFECT OF NON-CONSTITUTIONAL RENEWAL ON CANADIAN DEMOCRACY

With a substantial array of intergovernmental activity underway, and a case to be made that it should receive even more priority (see above comments on internal trade and the environment), a question that arises is whether so much intergovernmentalism is consistent with democratic processes and values. In his chapter, Banting suggests that concerns about "democratic deficits" in Canada have historically been linked mainly to big constitutional packages, not administrative arrangements. Indeed, there is no evidence that the public is about to reject politically the outcomes of recent federal-provincial agreements on child benefits, the Canada Pension Plan, or labour market training for such reasons. In these cases, however, governments have undertaken initiatives to reduce concerns about democratic deficits (e.g., through commitments to regular public reporting within a published accountability structure). In the case of environmental policy, Fafard reports that the failings were not attributable to a lack of openness in government. As for the implementation process around internal trade, these remain opaque, which has detracted from their effectiveness. Better and more regular information here would simultaneously serve policy goals and democratic values.

Overall, the more that governments use intergovernmentalism to solve problems, and the more these processes generate hard outcomes that matter to people, the more governments will need to give attention to democratic concerns. Among other things, this will require enhanced transparency on how intergovernmental decisions are made. Clearer lines of accountability regarding the responsibilities of the two orders of government (the more integrated the decisionmaking process of the two orders of government the more important to spell out what each has committed to do) will similarly be needed. And more attention will also have to be paid to more fully involving both legislatures and the wider public in the intergovernmental decisionmaking processes.

EFFECTS ON POLITICAL RECONCILIATION WITHIN CANADA

The effects of the non-constitutional strategy on the prospects for a political reconciliation between Quebec and the rest of Canada are difficult to assess. Accordingly, my remarks here will be both tentative and cautious.

The first observation is that the non-constitutional strategy has generally avoided the irritations that periodically serve to fuel support for the sovereignty side. This may be a "plus" for reconciliation. The strategy has also shown that serious policy challenges that involve both orders of government

can be managed well, as on the fiscal front and child benefits. To the extent that this illustrates a functional polity, this too may encourage a political environment that is conducive to reconciliation.

However, it is also worth noting that the areas of federal-provincial relations where Quebec was participating fully, including internal trade and environmental issues, have received relatively little high level attention from the federal government during the years under review. This lack of attention was understandable. From a national unity viewpoint, no special political sensitivity attached to these items because the Government of Quebec saw them as "business as usual." Moreover, there was arguably a more pressing set of issues that both orders of government had to tackle.

One of these pressing issues was social policy renewal. The Quebec government position on social policy is that it is an overwhelmingly provincial jurisdiction and that the federal role is based, for the most part, on what it considers to be an illegitimate use of the federal spending power (see the joint communiqué from the First Ministers' Meeting, 12 December 1997). To the extent that this view is widely shared by Quebecers, or that disputes about technical issues like the spending power are simply hard to understand, this social policy focus entails risk from the perspective of political reconciliation. This helps to explain why the federal government has pledged not to create new shared-cost programs in areas of exclusive provincial jurisdiction without broad provincial support and to provide financial compensation to those provinces that opt out if they create similar programs. It may also help to account for the interest of some provinces in promoting interprovincial, rather than federal-provincial, frameworks for national programs.

The spending power is not only used by the federal government, however, for shared-cost programs but also to effect cash transfers to individuals. Notwithstanding the Quebec government's view, Ottawa's constitutional authority to use this power appears strong, its political legitimacy generally accepted in much of Canada and it is an efficient way for the federal government to connect directly with citizens. It is not yet clear how far Ottawa intends to shift in this direction although the limitations the federal government has placed on itself with regard to shared-cost programs suggest the possibility of significant movement.¹⁷ Since the likely effects of such a movement on Quebec public opinion are uncertain, this issue is a "wild card" in relation to political reconciliation.

The discussion about social policy leads to a consideration of the effects of Ottawa and the provinces working together without Quebec at the table as a participating partner. In earlier periods, Ottawa and at least some of the provinces would have gone to great lengths to avoid "isolating Quebec." Today, governments appear to have reluctantly accepted that they must get on with business even if Quebec absents itself or assumes observer status only. The

issue here has less to do with the pros and cons of this practice on any single issue than its cumulative effects over time. While in no way intended as a training ground for operating a Canada without Quebec, other governments are learning how to do business with one another without Quebec's active participation much of the time.

The Quebec government may have its own reasons to find these developments attractive. They may help over time, for example, to support the nation-to-nation objectives of the Parti Québécois by effectively legitimizing the idea that the other provinces collectively, or some combination of the other provinces and Ottawa, are the embryo from which an "English Canada" might be born and with which Quebec may one day be able to negotiate the economic association or political partnership that Premier Bouchard has promised.

In brief, from a political reconciliation perspective, the recent heavy inter-governmental focus on social policy is high risk. At a minimum, therefore, relatively more high level attention than has been the case over the last four years should be devoted to items where there are convergent interests between Quebec and other parts of Canada. In "Searching for Plan A," Robert Howse states that this would nurture the "community of association" by thickening the economic and other ties across regions and language groups and without raising troublesome identity politics. With more progress on convergent interests, then areas of divergence might loom less significant.

It is also desirable to clarify what the roles and responsibilities of the provincial and federal governments will be in a new social union. The 1997 First Ministers' Meeting states that it will be developed in a way that respects the constitutional responsibilities of the different orders of government. Yet, it has been portrayed by the Quebec government as an assault on provincial powers. Since it is evident that larger provinces like Ontario and Alberta have no intention of agreeing to any such outcome, and a number of other provinces are also likely to be recalcitrant, the political risks of this initiative from a unity viewpoint seem larger than the substantive reality. This argues that, to the extent that social policy renewal remains high priority, there is urgency in defining with great clarity what is intended in this area so that individual Quebecers will be better able to appreciate what is being considered. For what it may be worth, one view of these discussions is that, contrary to what Quebec asserts, they do not indicate a new federal government unilateralism in which provinces would become more dependent on Ottawa. Rather, they reflect the idea that the Canadian federation cannot avoid the "mutual interdependence" of the modern world and that the "mutual independence" or watertight compartments of earlier periods in Canadian history are increasingly dysfunctional in a world of growing interconnectedness.

The non-constitutional approach of the 1993-97 period was never, of course, seen as a complete strategy for promoting political reconciliation within

Canada. It did not address either the symbolic or practical issues relating to the protection and promotion of the French language, for example. Nor did it address some of the symbolic and practical concerns of Canadians in the western-most provinces. But it has been about more than good government. It has also been about buying time while public finances were being restored, making progress on issues that required the attention of both orders of government, and allowing some of the emotions, on both sides of the language divide, to cool in the aftermath of the failures of both the Meech and Charlottetown Accords.

The fact that the pro-sovereignty side came so close to winning the 1995 Quebec referendum indicates that as a way of buying time it has been far from a complete success. Yet, the federalists did receive more than half the votes in the referendum; and it is possible, if less than certain, that there is greater openness in the other regions of Canada than there was two or three years ago to finding some basis for reconciliation. Since reconciliation depends as much on opinion in the provinces outside Quebec as it does on events within that province, this is noteworthy. The readiness of the nine premiers to re-open the constitutional file, as reflected in the Calgary Declaration, speaks directly to this point.

At this juncture, therefore, the mundane conclusion to be drawn about the effects of the non-constitutional approach is that it was a necessary step for healing the wounds of the country. It has helped to create the preconditions for another effort at reconciliation. But in and of itself, it is unlikely to be sufficient for that purpose.

An issue worth reflecting on in this context is the effect of Plan "B" on the non-constitutional approach. It was suggested above that the non-constitutional strategy has been developed in a generally non-provocative way. Recently, however, at least as seen through the media, it has received far less attention than the federal government's Supreme Court reference regarding the constitutionality of a unilateral declaration of independence by Quebec. Similarly, it has attracted less attention than Stéphane Dion's letters to Quebec government ministers about this same issue and the possibilities of Quebec being partitioned in the event of independence. In this sense, Plan "B" and the so-called "provocations" it creates may detract from the non-constitutional approach.

Yet, the interaction of the two strategies can be overstated. Even without a Plan "B" the non-constitutional files would not be headline material. They are too complex and technocratic. Also, in the delicate balancing act that Ottawa must attempt, Plan "B" has two distinct target audiences. In addition to persuading Quebecers that secession is an unnecessary, dangerous, and potentially very costly adventure, it is directed also at reassuring Canadians who live outside Quebec that their national government is not standing by idly in the

face of the threat of Quebec secession. To the extent that Plan "B" causes Canadians outside Quebec to believe that their interests are being protected, this may help to encourage them to be more open to some of Quebec's demands.

The non-constitutional strategy has not yet run its course from a reconciliation perspective. To the contrary, a strategy for reconciliation among Canadians that relies exclusively on constitutional reform smacks too much of recent failures. When the federal and provincial governments chose the non-constitutional approach, it was for all practical purposes all that was available. Such a declaration may be less true today. But an approach that demonstrates the ability of the federal system to adapt without constitutional amendment remains an essential ingredient to the process of renewing the federation. And the record of the last few years involves considerable achievement.

LOOKING AHEAD

Whether the collaborative federalism that has emerged in recent years should or will continue is an open question. The normative aspect of this issue is considered first.

There is much diversity in the functions of government. At the broadest level, governments set the public agenda by choosing priorities and creating general frameworks within which those priorities are pursued. Governments also do more pedestrian things like designing the details of programs and administering them. Given this diversity, it follows that collaborative federalism can operate at several levels that range all the way from strategic policy frameworks to program administration.

As society and economy become increasingly specialized and interdependent, it is difficult to imagine a world of watertight compartments at the strategic level. By strategic, in this context, we mean several things: the need for the two orders of government to exchange views regarding priorities; the need to identify the areas of overlap in their activities, and to understand the ways in which the behaviours of each may impact on the activities of the other; the need to exchange information regularly about their respective activities in the overlapping areas, and to seek agreement about relative roles and responsibilities in relation to the overlap. In some cases, even more will be needed including agreement about national objectives so that the discussion about roles and responsibilities is taken within the context of a specific public purpose.

The years under review suggest some movement toward this kind of collaboration, including agreement on national objectives. Federal and provincial governments made fiscal restraint a genuine priority during these years.

Through meetings of federal and provincial ministers of finance and their officials, a number of the activities noted in the paragraph immediately above were wholly or partly carried out. More to the point, had there been large differences between the two orders of government on the importance of the fiscal goal, it would have been close to impossible to achieve the success that was experienced in restoring public finances. Note that this conclusion did not require governments to agree on the specifics of how to achieve the desired results. The neighbouring provinces of Alberta and Saskatchewan used quite different methods, for instance, to reach their balanced budget goals.

A second example is in the fairly broad agreement among governments over the last couple of years about the priority attached to social policy renewal. Without such agreement, efforts at protecting and promoting the idea of the social union would have been dysfunctional, as was the case early in the life of the Chrétien government when it attempted to initiate a national social security review. Once again, the more recent agreement did not, and does not, presume collaboration on all aspects of government activity in pursuit of that priority. Moreover, the fact that Quebec remains outside the agreement may eventually limit what is achieved in this broad area.

The principal point here is that in the absence of some measure of cooperation in priority setting, and activities linked to the priorities, public policy risks gridlock. When the role of the state was tiny, as at the time of Confederation, this may not have been true. But the time is long passed when the world of watertight compartments was functional. The Rowell-Sirois report that was published more than a half-century ago chronicled the huge differences between the size of the state in the 1930s and what it had been in 1867. What they found then is, of course, far truer today.

The reality of a PQ government in Quebec City imposes a strain on priority setting nationally. Yet setting aside the PQ's sovereignty project, Quebec's priorities were not noticeably different from those of other Canadian governments. Notwithstanding its apparent disdain for fiscal priorities during the 1994 Quebec general election campaign, the PQ subsequently decided to make a balanced budget a priority. Under Premier Bouchard it has participated in Team Canada trade missions. The Quebec government even agreed with other governments regarding the priority of social policy, including the components of social policy identified by the Federal-Provincial-Territorial Ministerial Council on Social Policy Renewal. This was reflected in the news release from the December 1997 First Ministers' Meeting in which Quebec went on record as "sharing essentially the same concerns" about social policy (even though it did not agree that this priority should be part of the intergovernmental agenda). The fact that the PQ had similar broad priorities may help to explain why, despite some huge political differences with the rest of Canada, the practical "on the ground" policy impact was somehow manageable.

The view that collaboration is a corollary of modern governance in Canada is not intended to suggest that all issues, which in some way involve either directly or indirectly the two orders of government, are best handled through collaboration. There are and will remain areas where the classical model of federalism will continue to serve Canadians well.

Within Canada, however, at the strategic level, the number of areas where governments act completely independently of one another is more likely to decline rather than increase and for much the same reason that national governments find that they must increasingly deal with cross-border issues. The real world is becoming more and more interconnected across geographic regions and subject areas. Accordingly, the need for collaborative federalism can be expected to grow.

Collaboration can be managed well or badly and not all forms of collaboration are equal. Collaboration that requires the agreement of both orders of government on a regular basis, or that requires the agreement of all provincial governments, as well as Ottawa, risks inaction. For example, the decision rule for the AIT, which appears to require a consensus of all governments, is one reason that governments are not moving as swiftly as they had undertaken to meet the various milestones for AIT implementation. Second, collaborative arrangements frequently lack transparency and clear lines of public accountability and this raises questions of both democratic legitimacy and policy effectiveness. Third, intergovernmental arrangements that require all provincial governments to follow the same rules and the same approaches in areas of provincial jurisdiction, perhaps because of some federal government carrot or stick, risk losing the experimentation that federal systems can offer. Such an approach should be the rare exception. Indeed, involuntary collaboration that imposes this kind of commonality in provincial programming is based on the idea that Ottawa is the senior partner in the federation. As such, it offends the federalism principle that is a bedrock of the Canadian compact and is certain to weaken further the fragile political consensus on which the Canadian polity now depends. This list of dangers is not an argument against collaborative federalism so much as it is a set of cautions as governments navigate through its many shoals.

Finally, while collaboration at the strategic policy level may be increasingly necessary, this observation does not in any way presume the need for more collaboration in respect of program design or administration. At this level of governmental activity, we can reasonably expect to see a diversity of programmatic specifics that include both disentangled and collaborative approaches and, even occasionally, federal government unilateralism. Where there is also collaboration at the programmatic or administrative levels, however (for instance, where federal and provincial governments create a "single window" so that citizens can obtain both federal and provincial programs from

a common office), it is reasonable as well to expect a clear delineation of exactly which government is responsible for what. Where that occurs, collaboration and disentanglement may be as much complementary activities as they are ideas in conflict.

Leaving aside arguments about the merits and demerits of collaborative federalism, questions also arise about the likelihood that it will continue. It was noted above that Quebec remains a limited partner preferring a more disentangled approach to many issues. Some provinces, notably Ontario and Alberta, may also wish to continue testing the scope for collaboration at the interprovincial level where the issues involve exclusive provincial jurisdiction only.

The emerging position of Ontario merits particular consideration here, not only because it is the largest province but also because, among the provinces, its intergovernmental strategy is the one that is undergoing the largest transformation. Ontario's economy has become more dependent on trade with the United States. Its government was elected following a commitment to shrink and simplify government and cut taxes (in contrast to its predecessor). It also has large grievances against the federal government. Taken together, these factors point to a government with an incentive structure in transition. Where Ontario was once likely to equate its interests with the national interest, the new context suggests more weight on regional, particularly regional economic, interests.¹⁸

Three conclusions flow from these considerations. First, although Ontario has participated fully in collaborative intergovernmentalism, its enthusiasm for this approach will almost certainly be conditioned by the readiness of Ottawa to respect provincial jurisdiction and the degree to which the approach generates outcomes that address Ontario's priorities. Second, by virtue of its growing dependence on international trade, Ontario has less economic reason than it once did to tolerate the current federal-provincial fiscal arrangements and the amount of implicit equalization that now flows either directly (e.g., CHST, labour market training) or indirectly (e.g., unemployment compensation) from Ontario via Ottawa to the less prosperous regions of the country. It will therefore be a more demanding partner in future federal-provincial negotiations. Yet, and this is the third point, it is also in Ontario's interest to encourage the new collaboration. The more effective that collaboration is, and the better Canada functions, the less the risk that Ontario will have to deal with the disruptive economic and other effects of the secession of a large economic neighbour and partner.

Policy statements by the federal government in the 1997 Throne Speech and the second *Red Book* suggest that the second Chrétien administration may remain on the collaborative course. The circumstances that led the federal Liberals to pursue a collaborative approach in the first mandate, however, are not identical to those that prevail today, suggesting that a change of strategy

is within the realm of possibility. In particular, the federal fiscal situation has improved, thus opening the door to Ottawa using financial resources to exercise leadership, which in turn raises questions about the mechanisms it might use for this purpose. Given the federal commitment to not introduce new shared-cost programs in areas of exclusive provincial jurisdiction without a wide measure of provincial support, this suggests direct transfers to individuals or creative use of the income tax system. To the extent that such direct federal initiatives are possible without thwarting or complicating provincial programs in overlapping areas, there can be little objection to them.

But the areas that Ottawa targeted in the 1997 Throne Speech — children, youth employment, health care, and innovation — all involve matters where there is extensive provincial programming. Unilateral federal initiatives in these fields run the risk of generating policy outcomes that are at cross purposes with provincial measures; and in that event, there is an even larger risk of reducing the fragile trust between most of the provinces and the federal government. New unilateral spending initiatives by the federal government in the education or health areas are likely to be particularly unhelpful, in this regard. It is the provincial governments that are now paying the political price for higher postsecondary tuition fees and reduced levels of health-care services which flowed in significant measure from the federal reductions in transfer payments to provinces just a couple of years ago.

These items were discussed at the First Ministers' Meeting in December 1997 suggesting that the federal government has not fixed on a unilateral course. There are different explanations, however, about what is motivating the federal government. It may have avoided new spending initiatives in the above-noted areas mainly because there is still considerable fiscal caution in Ottawa. In this sceptic's view of federal government motives, further spending initiatives are simply being deferred until the second half of that government's electoral mandate when Ottawa's fiscal position is likely to be stronger and the temptation to spend or to reduce taxes for partisan purposes even greater.

The alternative view is that Ottawa, while still less than fully coherent in its federalism strategy, is nonetheless groping toward a more collaborative vision of the federation. *Accordingly, on matters where the federal government has an interest, but there is also undeniable provincial jurisdiction, it will stay on the table with the provinces until there is agreement among governments.*

Collaboration requires provincial support and at times their leadership. The provincial initiative in social policy suggests that most provinces are open to this strategy for managing the federation. If this is so, this leaves much of the onus on the way Ottawa responds.

Collaboration requires hard work and patience, without any certainty of agreement on the issue under discussion. For the federal government, therefore, there is always the risk of gridlock and missing out on short-term political

gains. Where there appears to be a public appetite for action, and Ottawa has the tools to act alone, the temptation to act unilaterally will be great.

The dilemma for the federal government is that the short-term gain on any single file may be at the price of long-term pain in terms of federation management. For without increasing collaboration in the areas of overlap, there is the virtual certainty of deteriorating relations between the federal government and the larger English-speaking provinces, as a minimum. If this occurs, then the impact on future efforts at political reconciliation within Canada can only be damaged.

The challenge for the federal and provincial governments is to find a new equilibrium point in federation management. Growing interdependence is a reality of modern society. Managing that interdependence with sensitivity to the federal structure of the polity is crucial to what lies ahead.

NOTES

1. See Edward Greenspon and Anthony Wilson-Smith, *Double Vision: The Inside Story of the Liberals in Power* (Toronto: Doubleday Canada, 1996).
2. The references to statements by the prime minister, on this page and the next, are drawn from Anne Poels, "Chronology of Events 1993-94," in *Canada: The State of the Federation 1994*, ed. Douglas M. Brown and Janet Hiebert (Kingston: Institute of Intergovernmental Relations, Queen's University, 1994); Andrew C. Tzembelicos, "Chronology of Events 1994-95," in *Canada: The State of the Federation 1995*, ed. Douglas M. Brown and Jonathan W. Rose (Kingston: Institute of Intergovernmental Relations, Queen's University, 1995).
3. I am referring here to large-scale constitutional reform.
4. I am aware of no objective evidence to support this claim by political leaders.
5. Ekos Research Associates Inc., *Rethinking Government*, 95-1 (Toronto: Ekos Research Associates, 1995), p. iv.
6. Ronald Watts, *Comparing Federal Systems in the 1990s* (Kingston: Institute of Intergovernmental Relations, Queen's University, 1997), pp. 69-73.
7. Ekos Research Associates Inc., *Rethinking Government 1995, Final Report* (Toronto: Ekos Research Associates, 1996), pp. xx-xxi.
8. I am not arguing here that the provinces accepted easily the cutbacks imposed by the federal government, as will be evident later in this essay. Rather, the point being made is that, given the magnitude of the federal cutbacks, the provincial reaction was remarkably tepid.
9. In the discussions of federal and provincial finance ministers in December 1997, the distribution of the anticipated federal "fiscal dividend" was a significant controversy. Provincial ministers told the media that Ottawa should give higher priority to restoring transfers for existing provincial programs rather than starting new programs that would deliver benefits directly to individuals in areas that

the provinces argue to be in their jurisdiction. See *The Globe and Mail* 10 December 1997, pp. A1 and A10.

10. The statements were reported widely in the media during the meeting of federal and provincial finance ministers in December 1997.
11. Banting's contribution was designed to create the historical context for the other two social policy chapters (and for that reason it concentrates on a time period that is outside the years mainly under review here).
12. Collaborative work is also under way to improve programs to bring persons with disabilities further into the mainstream and to extend the children's agenda beyond the National Child Benefit. In areas of health policy as well, there is a substantial intergovernmental agenda. In these latter three cases, it is too soon to know what the policy results will be, but it is noteworthy that the intergovernmental collaboration appears to be systematic.
13. Michael J. Trebilcock and Daniel Schwanen, *Getting There: An Assessment of the Internal Trade Agreements* (Toronto: C.D. Howe Institute, 1995).
14. A harmonization agreement was signed in early 1998 between the federal government and nine provinces. Quebec did not sign.
15. Richard Simeon and Ian Robinson, *State, Society, and the Development of Canadian Federalism* (Toronto: University of Toronto Press, 1990).
16. Provincial-Territorial Council on Social Policy Renewal, "Progress Report to Premiers No. 2," (mimeo), 1997. Institute of Intergovernmental Relations, *Assessing ACCESS: Towards a New Social Union* (Kingston: Institute of Intergovernmental Relations, Queen's University, 1997).
17. This issue was a significant point of controversy in the public communications of Premier Bouchard at the time of the December 1997 First Ministers' Conference.
18. Thomas J. Courchene with Colin R. Telmer, *From Heartland to North American Region State* (Toronto: Centre for Public Management, Faculty of Management, University of Toronto, 1997).



II

Major Policy Files

The Past Speaks to the Future: Lessons from the Postwar Social Union

Keith G. Banting

Ce chapitre s'appuie sur le passé pour informer le futur, en se demandant quelles aperçus peuvent être gagnées de la période après-guerre pour nos débats courants au sujet de l'union sociale. Il examine la structure de l'union sociale mise en place par la génération après-guerre, en mettant l'accent sur les instruments à travers lesquels le gouvernement fédéral appuya l'émergence de programmes sociaux à travers le Canada et les diverses relations fédéral-provincial qui les ont étayées. Le chapitre alors évalue le système après-guerre en termes de trois séries de valeurs de base: les valeurs de politique sociale, les valeurs démocratiques, et les valeurs fédéralismes. Il argumente que l'union sociale après-guerre a contribué fortement à l'accomplissement de valeurs politiques sociales clefs, que ses références démocratiques étaient plus ambiguës, et que le principal défi à l'union social était encre dans les valeurs fédéralismes. Par conséquent, l'histoire de la période après-guerre confirme la dure nature des échanges dont nous faisons face aujourd'hui. La question clef est à savoir quelle série de valeurs prédominera au moment où nous reconcevons notre union sociale pour le prochain siècle.

INTRODUCTION

During the postwar years, Canadians built their own version of the welfare state, establishing a new social contract between citizens and the state.¹ This process was underway throughout the western world, as all countries experienced similar pressures to protect citizens from the social insecurities inherent in industrial society. Canada, however, faced the additional challenge of fashioning its social programs in the context of a federal state and a society divided along linguistic and regional lines. Constructing the welfare state therefore also involved building what would now be called a *social union*, a set of understandings about the balance between federal and provincial social

programs, and a set of intergovernmental arrangements to give those understandings life.

The postwar generation had to decide whether there would be a *pan-Canadian* welfare state or a series of distinctive *provincial* welfare states. The social union that emerged in those years was a compromise between these two poles. The system was significantly more decentralized than that in many other federal systems, including countries such as Australia and the United States, but it did incorporate critical pan-Canadian dimensions. Major social programs operated across the country as a whole and established a set of social benefits that Canadians held in common, irrespective of the region in which they lived. In this way, Canadian experience reflected the larger historical trend identified by T.H. Marshall, who argued that the modern welfare state was adding a new dimension to citizenship in western nations, a new set of social rights that individuals hold, not because of their status, class, or region, but by virtue of their common position as citizens.²

In the postwar social union, the pan-Canadian elements of the welfare state were associated strongly with the role of the federal government. As the political and economic strength of the federal government has declined in recent years, and as our constitutional tensions have grown, the original social union has come under strain. Increasingly, Canadians are being forced back to first principles in social debate. What is the appropriate balance between pan-Canadianism and regional diversity in the construction of the welfare state? If pan-Canadianism is an important value, are there mechanisms other than federal power through which it can be sustained?

The purpose of this chapter is to draw on the experience of the postwar social union, and to ask what insights, if any, it offers for our current debates about the future accommodation between federalism and the welfare state. The following section examines the basic architecture of the postwar social union, focusing on the instruments with which it was constructed and the diversity of federal-provincial relationships embedded in it. The next section evaluates the postwar system in terms of three sets of core values: social policy values, democratic values, and federalism values. The final section then attempts to distil some tentative lessons from the history of the postwar system that might assist us as we redefine the social union for the next generation.

THE STRUCTURE OF THE POSTWAR SOCIAL UNION

The "social union" is a relatively new concept in Canadian political discourse. Not surprisingly, therefore, there is no consensus on its meaning, and the varied definitions that are emerging invite us down quite different pathways. For some analysts, the social union is essentially a broad social contract, a unifying vision of the social role of the state and a grand design for major social

programs.³ To be successful and durable over time, such a social contract would need to be grounded in a broad consensus on key parameters: the basic relationships among citizens, social groups, and the state; the values that should animate social programs; and the political processes through which social programs are to be designed. This definition of the social union suggests that the current challenge before us is to develop a new collective vision of our social future, a new blueprint for social policy which will replace the vision developed by the postwar generation.

There is no doubt that governance in Canada would be enhanced by a new consensus on social policy. However, a social union in this sense is a dauntingly ambitious project, requiring agreement on an enormous range of ideologically charged issues that go well beyond the relationship between federalism and the welfare state. Our recent constitutional history suggests that comprehensive packages can be sunk by the cumulative political damage inflicted by a wide range of interests each of which is primarily concerned about quite specific component of the total design. Defining a new social contract would certainly test Canadians' collective capacity for consensus and compromise.

For these reasons, this chapter adopts a narrower conception of the social union, one more analogous to the concept of the economic union which is already well established in our political discourse. The core issue from this perspective is the accommodation between the welfare state on the one hand and federalism on the other, and the focus is on the pan-Canadian reach of social programs and the federal-provincial relationships that structure the sector. As we shall see, the issues involved are complex, and securing a consensus on even this conception of the social union is a challenge, requiring hard choices among core values on which contemporary Canada is built.

To understand the basic architecture of the postwar social union, it is useful to examine its basic components: (a) the instruments that the federal government utilized to build a pan-Canadian structure, and (b) the diverse federal-provincial relationships that underpinned the key social programs.

FEDERAL INSTRUMENTS

The federal government utilized three critical policy instruments in developing pan-Canadian social programs: the provision of benefits directly to citizens, federal shared-cost programs in areas of provincial jurisdiction, and equalization grants to poorer provinces.

Direct Federal Programs

Although it is sometimes argued casually that social policy generally is a provincial responsibility, the federal government's own jurisdiction in social policy

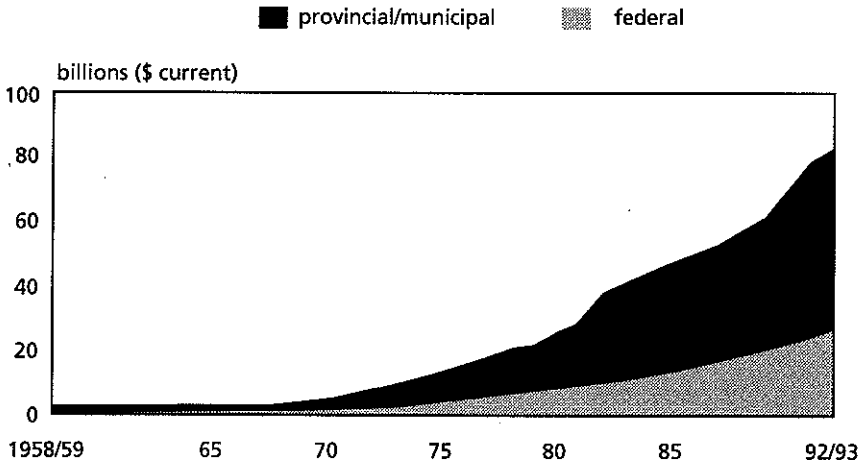
is substantial, especially in the area of income security. During the middle decades of this century, three formal amendments to the constitutional division of powers gave the federal government complete authority over Unemployment Insurance, and substantial authority in the area of pensions. In addition, under the doctrine of the spending power, the federal government claimed an untrammelled right to make payments to individuals, institutions or other governments for any purpose, and argued that such transfers do not represent an invasion of provincial jurisdiction as long as they do not constitute regulation of the sector.⁴ Finally, the federal role in taxation constitutes a powerful instrument in redistributive policies, especially with the development of a fuller array of refundable tax credits and benefits.

On these constitutional footings, the federal government developed a significant direct presence in social policy. In 1940, it introduced Unemployment Insurance, which was later complemented by training and other labour market programs. The federal government also established two universal programs: Family Allowances (1944) which were paid to all families with dependent children; and Old Age Security (1951), which provided a basic pension to all elderly Canadians. In the mid-1960s, the federal government enriched pensions with two additional programs: the Canada Pension Plan, a contributory plan providing earnings-related pensions, and the Guaranteed Income Supplement, an income-tested benefit for the elderly poor. Finally, a Spouse's Allowance for younger spouses of pensioners was added in 1975.

These initiatives established a direct federal presence in the lives of Canadians, and made Ottawa the dominant government in income security. Provincial governments delivered Workers' Compensation and social assistance programs; and Quebec chose to operate its own Quebec Pension Plan, which is closely aligned with the Canada Pension Plan operating throughout the rest of the country. Nevertheless, the federal role was dominant. Figure 1 measures the intergovernmental balance in terms of which government delivered income security payments to citizens. Even though these calculations ignore all federal contributions to the financing of provincial benefits, the preponderant role of Ottawa is clear: the federal government paid out between 70 and 80 percent of all income security dollars directly to Canadians for the entire period from the late 1950s to the early 1990s.

Direct federal delivery created pan-Canadian social programs that, with one significant exception, treated Canadians equally, irrespective of where they lived. Old Age Security, the Canada Pension Plan, the Guaranteed Income Supplement, the Spouse's Allowance, and Family Allowances established uniform benefits and conditions that did not vary from region to region. As such, they represented social rights of the type described by Marshall and other students of the social dimension of citizenship that was emerging in Western nations during the twentieth century. Canadians shared this network

Figure 1: Federal-Provincial Balance in Income Security Expenditures



Source: Data supplied by the Caledon Institute of Social Policy.

of benefits and obligations irrespective of the language they spoke or the region in which they lived.

Exceptions to the uniform application of federal income transfers did creep in over time. A minor exception emerged in the mid-1970s when the federal government agreed to vary Family Allowance payments among families of different sizes within a particular province at the request of the provincial government. However, average benefits were to remain equal in all provinces, and in the end only Alberta and Quebec took up this opportunity. The significant exception was Unemployment Insurance. In 1957, coverage was extended to self-employed fishermen, the only category of self-employment so covered, a provision that was particularly important to Atlantic Canada. Later the program was amended such that both eligibility criteria and benefit periods varied according to regional differences in unemployment rates. Although the definition of region for UI purposes did not correspond with provincial boundaries, in practice the level of generosity came to vary significantly by province, especially in later years when cuts to the program fell most heavily on areas with lower unemployment rates. By the mid-1990s, an unemployed person in Newfoundland was twice as likely to be receiving unemployment benefits as an unemployed person in Ontario.⁴ Unemployment insurance thus stood out

as a regionalized income-security program, and an exception to the general pattern of federal programs contributing to a pan-Canadian definition of the social rights of citizenship.

Shared-Cost Programs

In other parts of the welfare state, the constitution and political realities pointed to provincial responsibility and delivery. In such areas as health care, social assistance and postsecondary education, the federal government therefore relied on the spending power to make shared-cost grants to provincial governments. Under these programs, Ottawa provided substantial financial support to any province mounting a program that met conditions or standards specified in federal legislation. In this way, the federal government stimulated the expansion of key social services, and established a common framework for program design from coast to coast.

The pan-Canadian nature of these programs turned to a significant degree on the terms and conditions attached to federal funding, especially in their developmental stages. The level of specificity in shared-cost programs varied considerably, both over time and from program to program. For example, some of the early shared-cost programs, such as the categorical social assistance programs that were the precursors to the Canada Assistance Plan, did establish relatively detailed conditions, including maximum shareable benefit levels. However, provincial resistance, especially from Quebec, changed that practice, and federal conditions became less detailed. Nevertheless, the federal conditions that were attached to shared-cost programs were important in giving broad shape to provincial programs:

- The most specific and detailed conditions were reserved for medicare. Five principles were embedded in the legislation, requiring provincial health-care programs to provide comprehensive medical coverage, universality, portability, accessibility, and public administration. The federal role, especially when reinforced by the 1984 *Canada Health Act*, was most important in preserving equality of access to health care, and preventing the introduction of user fees in provincial plans. Otherwise, the federal principles left considerable scope for provincial variations in the range of medical services covered and the mix of delivery systems in place.
- In the case of social assistance and welfare services, the Canada Assistance Plan imposed fewer conditions. To qualify for federal support, provinces did have to establish a program that assisted all needy persons, a provision that prevented the exclusion of specific categories of poor people on the US model.⁵ Provinces were also required to create formal appeal procedures for beneficiaries, and to agree not to establish

provincial residency requirements for social assistance. Within this basic framework, however, there was substantial room for provincial discretion. For example, there were no national standards for actual benefit levels, and provincial generosity has varied significantly.⁷

- Postsecondary education represented the least intrusive federal program, as no conditions were attached to the federal transfer. Provinces were free to spend the money as they saw fit and, after the adoption of block funding in 1977, were even free to divert the money to other sectors. Nevertheless, the funding certainly facilitated the expansion of postsecondary institutions across the country, and it is difficult to believe that smaller provinces in particular would have established substantial university and college systems without the support. Some analysts have also argued that federal funding represented an implicit constraint on provincial discretion, for example, by forestalling the introduction of higher tuition fees for out-of-province students in universities and colleges.

Equalization Grants

Federal equalization grants to poorer provinces constituted the third instrument that sustained pan-Canadianism. These grants were designed to enable the seven poorer provinces to provide average levels of public services without having to resort to above-average levels of taxation. Equalization grants have always been unconditional, and in theory could be used to reduce provincial taxes rather than enhance provincial programs. In practice, however, the equalizing of fiscal capacity among provincial governments led to a more common level of public services generally across the country than would have been possible if provinces had to rely on their own revenues alone.

The power of the equalization system is illustrated by Tables 1 and 2. Table 1 shows the equalizing effects of these federal grants on the fiscal position of the provincial governments. Table 2 illustrates the implications of equalization for health-care, albeit somewhat indirectly. As the first two columns indicate, federal health-care transfers to the provinces are broadly similar across the country, both in per capita terms and as a proportion of provincial health expenditures. Moreover, as the third column indicates, actual provincial health expenditures are also reasonably similar in per capita terms; the differences between high- and low-spending regions are consistent with differences in the cost of providing services in different parts of the country. Yet the fourth column demonstrates that health expenditures represent a much larger proportion of the gross domestic product in poorer provinces than in rich ones, a difference that is only sustainable in the context of a strong equalization program that reduces differences in the fiscal capacity of provincial governments.

Table 1: Provincial Per Capita Revenues Before and After Equalization as a Percentage of the National Average for Own-Source Revenues, 1987-1988

	Nfld.	P.E.I.	N.S.	N.B.	Que.	Ont.	Man.	Sask.	Alta.	B.C.
Before	60	64	76	71	85	108	80	90	146	104
After	98	98	98	98	98	108	98	98	146	104

Source: R. Boadway and P. Hobson, *Intergovernmental Fiscal Relations in Canada* (Toronto: Canadian Tax Foundation, 1993), Table 4.7.

Table 2: Federal Health Transfers and Provincial Health Spending, 1994

Province	Federal Health Transfer: per capita (\$)	Federal Transfer: % of Provincial Health Spending	Provincial Health Spending: per capita (\$)	Public Health Spending: % of Provincial GDP
Newfoundland	553	34.3	1,613	10.3
Prince Edward Island	551	37.8	1,457	8.7
Nova Scotia	543	38.2	1,442	8.1
New Brunswick	541	34.1	1,589	8.6
Quebec	543	34.7	1,568	7.2
Ontario	541	31.8	1,702	6.6
Manitoba	535	34.5	1,553	8.3
Saskatchewan	535	36.3	1,474	7.6
Alberta	542	34.7	1,563	5.9
British Columbia	536	30.0	1,787	7.1

Source: Health Canada, *National Health Expenditures in Canada: 1975-1994: Full Report* (Ottawa: Minister of Supply and Services, 1996).

Thus three key policy instruments — direct federal programs, shared-cost programs, and equalization grants — contributed to a pan-Canadian structure of social programs in the postwar social union.

MODELS OF FEDERALISM IN THE POSTWAR SOCIAL UNION

The second basic component of the postwar social union was the complex set of federal-provincial relations underpinning core social programs. Canada did not develop a single, integrated philosophy of federalism to give shape to intergovernmental relations during the postwar period. Instead, the country proceeded in a quintessentially Canadian manner, through incremental, and often ad hoc arrangements for particular programs. In so doing, governments borrowed freely from a number of distinctive conceptions of federalism, and embedded a variety of different models in federal-provincial relations in the social union:

- *Classical federalism*: Some aspects of social policy were delivered by the federal or provincial governments acting independently within their own jurisdiction: Unemployment Insurance, Family Allowances, Old Age Security, and the Guaranteed Income Supplement at the federal level; Workers' Compensation at the provincial level. Historically, this model involved minimal efforts to coordinate the decisions of the two levels of government, even when decisions at one level had significant implications for programs at the other level.
- *Cooperative Federalism*: This term was associated with the traditional shared-cost model that was central to health insurance, welfare, and postsecondary education. Formally, this model involved each government making separate decisions: the federal government deciding to offer financial support to provinces on certain terms; and the provinces deciding whether to accept the money and the terms. In practice, considerable intergovernmental bargaining preceded the introduction of the major shared-cost programs, and the substance of many social programs was hammered out in the crucible of the federal-provincial conference. Nevertheless, these agreements are formally the result of independent decisions, and contain the potential for unilateralism, as became clear as the federal government began to cut its financial commitments to the programs from the mid-1970s on.
- *Co-determination*: In a co-determination model of federalism, the formal agreement of both levels of government is required before any action is possible. Unilateralism is not an option here. In the social policy sector, the strongest example is the Canada Pension Plan, which can be amended only with the agreement of the federal government

and two-thirds of the provinces representing two-thirds of the population of the country. This approach to formal rules-based joint decisionmaking reflects yet another model of federalism, one much more analogous to the German system. The institutions differ, since the provincial governments are not represented in the upper chamber of the national parliament, as in Germany. But the central dynamic is similar: nothing happens unless formal approval is given by both levels of government.

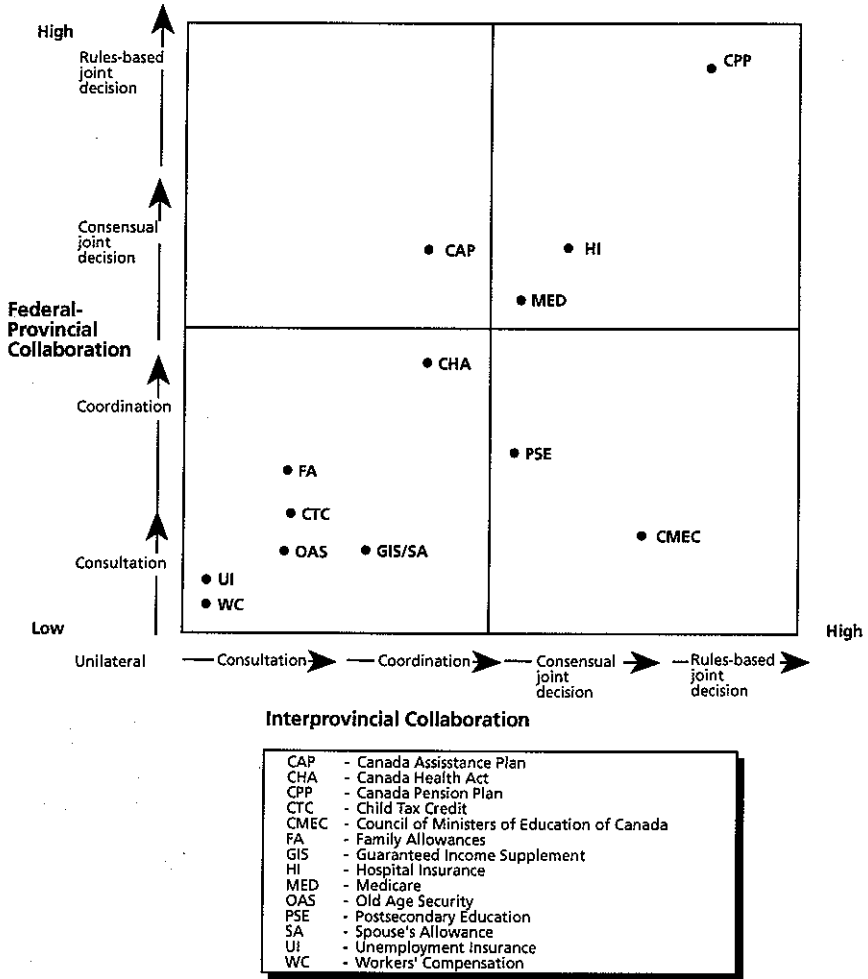
- *Confederalism*: This model is purely interprovincial. Although the federal government may play a facilitating role, final agreements are made and managed by the provincial governments. In the social sector, the initiatives of the Council of Ministers of Education of Canada on comparative testing and other matters reflect this basic approach.⁸

Thus at least four distinct models of federalism were embedded in the postwar social union. Another view of the diversity of intergovernmental relations in that period can be seen in Figure 2, which displays variations in the extent and nature of intergovernmental collaboration associated with different programs. The horizontal axis measures levels of agreement among provinces, while the vertical axis measures levels of agreement between the federal and provincial governments. The lower left corner represents unilateral decision-making by governments, as reflected in the classical model of federalism. The upper right corner represents the co-determination model of federalism, with its emphasis on formal joint decisionmaking by both federal and provincial governments according to established rules.

This figure not only highlights the considerable diversity in federal-provincial relations, but also their dynamic nature. Programs shift from one pattern of interaction to another over time. The case of health insurance is particularly revealing here, with the high level of intergovernmental collaboration that eased the introduction of hospital insurance in the mid-1950s fading somewhat into the more conflictual debate over the introduction of medicare in the 1960s, and dropping further with the introduction of the *Canada Health Act* in 1984 against the virtually unanimous opposition of the provinces. A similar figure capturing trends in the 1980s and 1990s would also reflect an evolutionary process, with further drift toward unilateralism in the context of federal budgetary reductions, followed by a reverse trend toward higher levels of intergovernmental collaboration more recently. Federal-provincial relations in the social policy sector are constantly being reshaped by the wider political and economic currents in the country.

In summary, the architecture of the postwar social union was complex. The federal government relied on three major instruments in building pan-Canadian social programs; and the federal-provincial relationships underpinning those programs reflected a range of models of federalism. This internal complexity makes any evaluation of the postwar social union a challenging undertaking.

**Figure 2: Intergovernmental Relations in the Postwar Social Union:
Forms and Levels of Collaboration**



Source: Adapted from M. Biggs, *Building Blocks for Canada's New Social Union*, Working Paper no. F-02 (Ottawa: Canadian Policy Research Networks, 1996).

EVALUATING THE POSTWAR SOCIAL UNION

A comprehensive evaluation of the postwar model turns on both the nature of the social programs that it sustained and on its implications for Canadian governance more broadly. Building on Biggs,⁹ one can identify three sets of values central to an assessment of the social union: social policy values, democratic values, and federalism values. Each of these values generates a series of questions that can be used to probe the strengths and weaknesses of the edifice of programs and intergovernmental agreements constructed during and after the Second World War:

- What were the implications of the social union for *social policy values*, such as equity and efficiency, in the design of social programs? In addition, did the social union enhance or frustrate coordination among different programs?
- What were the implications of the social union for *democratic values*? Did it preserve clean lines of accountability between individual governments and their electorates? Was the process sufficiently transparent to inform public debate? Did citizens and social interests believe that the process was accessible to them? Was the process sufficiently flexible to ensure that social programs could be responsive to changes in public preferences?
- What were the implications of the social union for *federalism values*? Did the social union strike an appropriate balance between regionalism and pan-Canadianism? Did the social union contribute toward national unity by building a common vision of the country, or erode that unity by imposing a centralized approach too rigid for its diversity?

This is clearly a sweeping set of questions and, as we shall see, different questions tend to point to different conclusions. In the final analysis, which set of values is to predominate becomes a critical issue.

In using these questions to assess the postwar accommodation between federalism and the welfare state, it is important to compare the results with the outcomes that would likely have flowed from the other historical choice available to the country at the time, which was a more decentralized system. As the Tremblay Commission in Quebec observed in the mid-1950s, expanding the role of the federal government was not the only possible response to at least some of the imbalances that constrained provincial governments during the interwar era. "It is no more difficult," the commission argued, "to add new taxes to the powers of the provinces than to transfer unemployment insurance and old age pensions to the central government."¹⁰ What, then, were the consequences of choosing a semi-centralized welfare state in the postwar period?

THE SOCIAL UNION AND SOCIAL POLICY VALUES

The strongest case for the postwar social union can be made in terms of social policy values. The pan-Canadian dimensions of the postwar social union contributed to higher levels of equity and efficiency in the design of the welfare state than could have been reasonably expected from a more decentralized regime.

Analysts of social programs normally distinguish between two dimensions of equity: *vertical* equity, which involves narrowing the range of inequality between rich and poor; and *horizontal* equity, which involves ensuring that individuals in similar circumstances are treated similarly by public programs. The postwar settlement enhanced both dimensions.

The social union contributed to stronger vertical equity by reducing economic and political obstacles that would have constrained the development of powerful social programs under a more decentralized regime. On the *economic* side, the stronger federal role reduced constraints implicit in fiscal competition among provinces. During the interwar era, provincial and municipal political leaders were very conscious of the implications of the mobility of both capital and labour for social programs. In 1927, for example, the premier of Manitoba wrote to the prime minister on the subject of unemployment in the following terms: "If any City or Province singly adopted plans to solve unemployment, that City or Province would become the mecca to which the unemployed in other cities or provinces would drift."¹¹ In 1933, the Quebec Social Insurance Commission argued that although family allowances were desirable, a provincial program "would perhaps place our manufacturers in a disadvantageous position with reference to other provinces."¹² The commission went on to argue that:

ordinary prudence suggests that unemployment insurance should be federal in character. It is very advisable to spread the social responsibilities over the whole country, for otherwise the provinces which participate will find themselves in a condition of inferiority with respect to the non-participants. It must not be forgotten that the expenses involved in social legislation would be incorporated in the net cost of production.... Moreover, the establishment of unemployment insurance in only one province would prove a great attraction to the unemployed in other provinces.¹³

The Rowell-Sirois Commission later summed up the case for federal action on unemployment insurance and old age pensions in almost identical words. "The principal reason ... lies in the readiness of industry in one province to complain if it is taxed for social services which are provided out of general taxation in other provinces or are not provided at all in other provinces.... The employer is placed in a position of competitive disadvantage in comparison with employers where there are not contributory social services."¹⁴

Clearly, policymakers at both levels of government were impressed by the logic of the mobility of the factors of production in the Canadian economy. The expansion of federal programs in the postwar period offset these constraints by creating the conditions for a broadly comparable tax and benefit regime across the country. None of this implies that provincial welfare states were an impossibility. The mobility of the factors of production did not prevent the diffusion of a number of provincial initiatives in the interwar years, such as workers' compensation and mothers' allowances, across much of the country. Nevertheless, it is unlikely that provincial diffusion would have created as complete or powerful a system as emerged under the postwar social union.¹⁵

The enhanced federal role also reduced *political* barriers to the expansion of social programs and their diffusion across the country. Throughout much of the postwar era, the federal government played a critical role in forging an ideological compromise among provincial governments on the main directions of social policy. In some cases, such as health care, Ottawa largely adopted a model already proven in one province, and became the instrument of its extension across the country; in other cases, federal leadership in program design was stronger. Its most important political role, however, was to force a pan-Canadian compromise. Although the outcome was not always as robust as more reformist provinces might have wished, it often went far beyond the initial preferences of more conservative provincial governments.

Pensions and medicare provide examples. In his analysis of federal-provincial diplomacy in the 1960s, Richard Simeon concludes that if contributory pensions had been an exclusively provincial jurisdiction in the 1960s, "it is most unlikely that a plan comparable to the CPP would have been enacted."¹⁶ Contributory public pensions were not a provincial priority at the time, and many provinces would undoubtedly have followed Ontario's plan to rely on regulation of the private sector, with employers of a certain size being required to provide occupational pensions.¹⁷ However, federal leadership catapulted a public plan to the top of the national agenda; and in the final bargaining, Ottawa played a critical role in forging a compromise between Quebec's preference for an expansive, redistributive plan and the more conservative design favoured by Ontario.¹⁸

Similarly, medicare would almost certainly not have spread from Saskatchewan across the country in the absence of federal action. Although Ontario's decision in 1956 to opt for universal coverage of hospital services was important in spurring Ottawa to action, Alberta, British Columbia, and Ontario opposed extending universal public insurance to include physician services in the mid-1960s. These governments sided with the private insurance industry and the medical profession in insisting that public coverage be restricted to the hard to insure, such as the elderly and the poor. Premier Robarts of Ontario

went so far as to denounce the new medicare program as "a Machiavellian scheme that is ... one of the greatest frauds that has ever been perpetrated on the people of this country."¹⁹ In the absence of federal action, these provinces would have opted for a more restricted public role in health insurance and, faced with the opposition of the medical profession, several other provinces would likely have followed their lead. However, once the federal shared-cost program was in place and their residents were paying federal taxes to support the program elsewhere, even these conservative governments had little choice but to join the national scheme.

Thus, the federal role overcame important economic and political barriers that would have faced a decentralized welfare state. Undoubtedly, regional pockets of radicalism would still have emerged in a decentralized system. However, diffusion across the country would have been more limited by fiscal and ideological constraints, and the resulting pattern would have not only been more regionally diverse but also less powerful on average. Almost certainly, programs such as the Canada Pension Plan and medicare would not have emerged on a country-wide basis. In effect, a decentralized Canada would have been a more conservative Canada.

The postwar social union also enhanced *horizontal* equity by increasing the extent to which citizens in similar situations were treated similarly by the public sector, irrespective of the region in which they lived. Powerful inter-regional transfers flowed explicitly through equalization grants and implicitly through direct federal benefits to individuals and shared-cost payments to provincial governments, narrowing regional differences in the quality of social benefits that would have emerged from a purely provincial system. The power of this dimension of the social union became apparent even in the early stages of the expansion of the federal role. Table 3 illustrates the impact in the late 1930s and the 1940s by comparing benefit levels in provincial programs that received federal support with provincial programs that did not. Mothers' Allowances, which were financed exclusively from provincial and municipal revenues, did not exist at all in two provinces, and average benefits where they did exist varied by a ratio of almost three to one. In contrast, pensions for the blind and elderly, for which Ottawa shared the costs and set a maximum shareable benefit level, existed in all provinces and average benefits across the country were much more equal. A more contemporary illustration of the importance of the interregional role of the federal government can be seen in the similarity in levels of inequality between rich and poor within the different provinces. As Table 4 indicates, the gini coefficients measuring income inequality within provinces were remarkably similar across the country, and became more so between the mid-1970s and the early 1990s. It is difficult to believe that a more decentralized system would have generated such a pan-Canadian pattern.

Table 3: Average Monthly Benefit Levels under Provincial Programs, 1938-1949

	<i>Mothers' Allowances</i> 1942	<i>Blind Pensions</i> 1938	<i>Old Age Pensions</i> 1938 1949	
Prince Edward Island	—	\$14.07	\$10.63	\$34.46
Nova Scotia	\$28.55	19.08	14.64	35.33
New Brunswick	—	19.34	13.68	36.01
Quebec	26.64	19.57	17.84	37.63
Ontario	28.91	19.48	18.43	38.05
Manitoba	35.79	18.68	18.66	38.36
Saskatchewan	13.77	19.79	16.45	37.29
Alberta	22.96	—	18.30	37.87
British Columbia	39.19	17.52	19.18	37.26

Source: K.G. Banting, *The Welfare State and Canadian Federalism*, 2d ed. (Montreal: McGill-Queen's University Press, 1987).

Table 4: Disposable Personal Income Inequality Across Provinces

	1975	1987	1991	% Change 1975-1991
Canada	0.293	0.289	0.286	-2.4
Alberta	0.328	0.288	0.284	-13.3
British Columbia	0.289	0.306	0.278	-3.9
Manitoba	0.288	0.279	0.278	-3.5
New Brunswick	0.288	0.283	0.266	-7.8
Newfoundland	0.300	0.284	0.265	-11.6
Nova Scotia	0.286	0.276	0.266	-7.0
Ontario	0.277	0.272	0.273	-1.4
Prince Edward Island	0.284	0.277	0.270	-4.8
Quebec	0.284	0.292	0.273	-4.0
Saskatchewan	0.342	0.298	0.286	-16.5

Note: Data are derived from the Luxembourg Income Study.

Source: T.M. Smeeding, "Trends in Income Inequality: New Evidence from the Luxembourg Income Study," presentation to Queen's International Institute on Social Policy, Kingston, 25-30 August 1996).

Horizontal equity contributes not only to a fairer distribution of public benefits across the country, but also to the *efficiency* of the Canadian economy. Pan-Canadian social programs should constrain economic distortions by reducing formal barriers to mobility in the form of residency requirements on one hand, and by reducing inefficient incentives to mobility in the form of sharply different benefit levels on the other. In effect, a strong social union reinforces the internal economic union. In the postwar version of the social union, formal barriers to mobility were reduced by the prohibition on provincial residency requirements for social assistance in the Canada Assistance Plan and the portability provisions of the *Canada Health Act*. In addition, the pan-Canadian application of federal programs such as Family Allowances, OAS and the GIS, as well as the close integration of the CPP and the QPP foreclosed residency barriers that might otherwise have emerged. Of course, the contribution of the postwar social union to economic efficiency was far from complete. As Courchene and others have argued, the social union established negative prohibitions of certain forms of provincial barriers, but it did not create positive incentives for integration in other areas more fully under provincial jurisdiction, such as the transferability of educational and technical qualifications.²⁰ Moreover, the increasingly marked regional discrepancies that crept into the federal Unemployment Insurance program over time have weakened the economic pressures for adjustment in labour markets in poorer parts of Canada, indicating that federal jurisdiction is not always a guarantee of equal treatment of Canadians from coast to coast. On balance, however, the postwar social union complemented and reinforced the Canadian economic union more completely than a purely provincial system is likely to have done.

The social union thus scores reasonably well in terms of the values of equity and efficiency. However, when attention shifts to other social policy values, such as the level of coordination among social programs, the record is less positive. Administrators and front-line social service officials regularly despair over the lack of a single, integrated *system* that is rationally designed and easy to administer. This professional orientation received an early expression in the 1943 Marsh Report, which insisted that "the task is to visualize the system as a whole, and to integrate the component units" in a unified structure through strong central leadership.²¹ Indeed, Marsh argued that it would be a "catastrophe" if the federal government dominated some programs and the provinces dominated others.²² However, Marsh's centralized blueprint crashed on the constitutional and regional realities of the country, and the divided jurisdiction described above fell into place.

As a result, problems of coordination and integration across programs were a recurring theme in the postwar politics of social policy. Some of the tensions in health care and other social services were eased in 1978 with the adoption of block-funding for health care and postsecondary education. However, the quest for closer integration of income security programs remained a

holy grail throughout the postwar period. Citizens faced a maze of programs offered by federal, provincial, and sometimes municipal agencies; and as a federal policy paper admitted, "somehow the poor citizen is expected to coordinate all of these bureaucracies — a degree of coordination which even governments themselves have been unable to achieve."²³ In addition, as governments increasingly sought to reform income security programs in the 1970s, divided jurisdiction became a major stumbling block.²⁴ Quebec emphasized the need for provincial control to ensure the *planification* of a single, integrated system. The theme was central to the report of a major provincial commission released in 1971, the Castonguay-Nepveu Report,²⁵ and the issue figured prominently in the political battles that led to the collapse of the constitutional package negotiated at the Victoria Conference in the same year. Frustration spread to other provinces as well during the subsequent decade, as federal waves repeatedly rocked provincial boats. In 1980, an interprovincial task force complained that provinces had spent most of the decade responding to repeated revisions to Unemployment Insurance, four changes in Family Allowances, the introduction of the Child Tax Credit, and the enrichment of the GIS — each of which had an impact on the management and costs of provincial social assistance programs.²⁶

Despite the recurring tensions, little progress was made in developing a mechanism for closer integration of the income-security system. As the interprovincial report emphasized, "there is no agreement on what level of government should co-ordinate and integrate social security programs."²⁷ In the context of a continuing struggle over jurisdiction, it was difficult to build a culture of intergovernmental collaboration, a step that would have implied the acceptance of the legitimacy of the role of both levels of government in the system. As a result, there was no intergovernmental mechanism in place to help manage the much more serious cuts and program changes in the 1980s and the first half of the 1990s. The resulting damage both to program design and to the federation more widely, as well as the more recent efforts to repair some of the damage through intergovernmental collaboration are discussed elsewhere in this volume.

On balance, the postwar social union contributed powerfully to critical social policy values. It facilitated the emergence of a stronger and more powerful welfare state, enhancing equity in both its vertical and horizontal dimensions; and it reinforced the efficiency of the internal economic union. The failure to develop coordination mechanisms was an important limitation, which became increasingly evident as governments sought to redesign the system they had created in earlier decades. In a wider social calculus, however, the contribution to social policy values was still a positive one.

THE SOCIAL UNION AND DEMOCRACY

The postwar social union also has implications for the democratic values of accountability, transparency, and openness. Here the evaluation is much more mixed, as the implications varied considerably with the different intergovernmental relationships embedded in postwar programs. The classical model of federalism generates fewest objections on democratic grounds: when each government operates independently in its own jurisdiction, accountability is less compromised than in other intergovernmental models. Admittedly, citizens in federal states are often confused about which level of government is responsible for any particular program, even when governments are operating independently in their own jurisdiction. Nevertheless, Family Allowances, the OAS and GIS at the federal level, and Workers' Compensation at the provincial level represented reasonably faithful approximations of the canons of parliamentary democracy. There is a continuing debate about which level within a classical federation is most responsive to its electorate. Some political theorists suggest that provincial governments are inevitably "closer" to the public; but many social groups, at least in English Canada, insist, often vociferously, that the federal government is far more open and responsive than the provinces. The response of disability groups to the Federal Task Force on Disability Issues is simply the most recent example.²⁸ The federal electorate is inevitably more diverse than that of any single provincial electorate, but there seems to be no particular reason for assuming that federal politicians are less attentive to their electors than their provincial counterparts.

In comparison to the clean lines of classical federalism, models involving stronger forms of intergovernmental collaboration generate tensions with democratic values. Many of the postwar social programs, such as the Canada and Quebec Pension Plans, medicare and the Canada Assistance Plan, were hammered out in the closed world of federal-provincial bargaining. As with international treaties, the resulting agreements represented complex sets of compromises that could not be changed without unraveling completely, and they were normally presented to legislatures, interest groups and the wider public as a *fait accompli*. Moreover, given their intergovernmental parentage, it was difficult for citizens to understand which government should be held accountable on a continuing basis. At the provincial level, priorities and design choices were constrained to some degree by federal policies. On the federal level, Ottawa was transferring substantial sums to provincial governments, for which it often received little visibility and credit, and over which it exercised a decidedly imperfect policy control. Only very knowledgeable citizens could understand the complex interplay of governments that shaped important social programs, and even they would have difficulty in deciding whom to hold accountable for policy failures.

Although these democratic tensions appear in the cooperative model of federalism, they are accentuated in the model of formal co-determination. The Canada Pension Plan is more difficult to amend than most parts of the constitution of the country. Under the existing rules, the federal government, the Ontario government, and a number of combinations of other provinces have a formal veto; moreover, the need for harmonization with the Quebec Pension Plan gives the province of Quebec a special role in the process.²⁹ As a result, amending the Canada Pension Plan requires a super consensus of the governments of Canada. The result has been a process that is partially insulated from the normal dynamics of democratic politics, and a program that is slow to adapt to changing conditions.³⁰

Clearly, one of the lessons that Canada learned in the postwar period is the tension between intergovernmentalism and democratic values. However, the weight of these criticisms should not be overstated. By its very nature, parliamentary democracy concentrates power, and most decisions made by governments within their own jurisdiction are hardly models of open, participatory policymaking. Indeed, in some cases, vigorous intergovernmental conflict over social programs probably enhanced public awareness and debate. Moreover, it is important not to impose contemporary concerns and standards on earlier historical periods. There is little evidence that the Canadian public was upset about the federal-provincial nature of the process that led to the Canada and Quebec Pension Plans, medicare and the Canada Assistance Plan. The danger that the intergovernmental bargaining might mute a wider politics raised few objections beyond the rarified confines of academic discourse; and the remarkably closed nature of the Social Security Review of the mid-1970s sparked remarkably little comment.³¹ The contemporary critique of intergovernmentalism is a more recent phenomenon, which was fueled by public reactions to the process of constitutional reform, not the politics of social policy. Overall, the theoretical tensions between collaborative forms of federalism and the canons of democratic theory did not unduly trouble either the Canadian public or their governments in the postwar period.

THE SOCIAL UNION AND FEDERALISM

The deepest challenge to the postwar social union did not flow from concerns about social policy values or democratic values but from the federal nature of the country. From one perspective, the social union seemed to be built on strong federalist foundations. Federalism is not only an instrument for accommodating regional diversity but also for reflecting commonalities; and there was considerable evidence in the postwar period that Canadians across the country shared increasingly similar values about the critical social issues that they confronted in their daily lives. The traditional divide on such issues between Quebec and the rest of Canada narrowed rapidly with the

secularization of Quebec society in the 1950s; and public opinion data provided evidence of a broad interregional consensus in public attitudes on social policy. Canadians were divided, to be sure, over the scope and generosity of social programs, but the distribution of opinion did not differ dramatically among regions. Further, the minor regional variations that did exist were not particularly surprising since, with few exceptions, the greatest support for social programs was found in Quebec and Atlantic Canada, the regions with the greatest needs.³² In effect, pan-Canadian social policy seemed to rest on a pan-Canadian consensus on the social role of the state.

However, the politics of Canadian federalism since the mid-1960s has taught us that a growing interregional consensus on policy does not guarantee agreement on jurisdiction. The last 30 years have been marked by recurring intergovernmental warfare over which level of government should be responsible for social programs. On the surface, some of these battles were about coordination and planning, as we have seen. At a more fundamental level, however, conflict was rooted less in differences over the substance of policy than in diverging conceptions of the nature of Canadian federalism and the appropriate balance between the federal and provincial governments in the lives of citizens. The real challenge was rooted in conflicting conceptions of community. An analysis of questions asked by the Canadian Gallup Poll organization between the years 1949 and 1975 found that regional differences in attitudes were much less pronounced on social issues than on issues relating to the nature of the Canadian community, such as language policy, relations with Britain, and federal-provincial relations.³³ These public orientations were reflected in, and reinforced by, the more general political conflicts within the federation. The rise of the sovereignist movement in Quebec and the wider conflicts among the regions of the country increasingly strained the sense of a common political community on which pan-Canadian social programs were premised.

The crisis of political community and identity gave a new significance to social policy, transforming it into an instrument of statecraft as well as an instrument of social justice. As the regional tensions built up in the federation in the 1960s and 1970s, the federal government argued that a strong federal presence in social policy was an instrument of national unity.³⁴ Medicare, pensions and unemployment insurance created a set of benefits and rights founded not on region or language but on a common Canadian citizenship. They represented spheres of shared experience in a society marked by considerable regional diversity, and they tied the interests of individuals across the country to the federal state. Given the economic structure of the country, monetary policy, trade policy, and energy policy tended to pit one region of the country against another; given the ethnic and linguistic structure of the country, cultural policies can generate similar conflicts. On social policy, however, Ottawa could fashion appeals that cut across territorial divides, reinforce the legitimacy

of the role of the federal government and strengthen Canadians' sense of attachment to their country. In addition, the interregional transfers embedded in the social union represented a shared commitment spanning the continent, serving much the same symbolic function that was served by the railroads in the nineteenth century.

The reaction of provincial governments to this dimension of social policy varied between Quebec and the rest of the country. Provincial governments other than Quebec did not evidence a strong interest in defending their jurisdiction in the postwar years. They lobbied the federal government throughout the 1950s and 1960s to expand its contributions to their social assistance programs, and they generally supported the expansion of the federal government's own income-security programs, which further eased provincial welfare burdens. As we have seen, there were conflicts, sometimes sharp ones, over the design of new social policy programs, such as Ontario's resistance to universal medicare in the mid-1960s; and the provinces expressed frustration over coordination problems in the income-security sector. In addition, provinces complained that federal shared-cost programs introduced rigidities into program design, although the shift to block-funding in 1977 eased many of the irritants, at least in the case of the health sector. In general, however, these conflicts did not congeal into fundamental battles over jurisdiction during the postwar years, and these provinces did not seek to recapture jurisdiction occupied by Ottawa in the heyday of federal influence.

This pattern remained largely intact as long as the federal government remained a substantial financial partner. The dynamic was seriously eroded in the 1980s and 1990s, however, when Ottawa began to reduce its financial transfers without significantly loosening the conditions attached to them. Indeed, the 1984 *Canada Health Act* tightened federal standards in the health sector by establishing penalties for provinces that allowed extra-billing. The legislation was passed in the face of almost unanimous provincial opposition and, although the popularity of the legislation with the public ensured provincial compliance, the tensions simply mounted. As the federal cuts continued year after year, Ottawa's share of the costs of critical provincial services such as health care fell from half to less than a quarter. Provincial governments were left to cope with the intense financial pressure on popular programs, and to face the political fallout from voters when benefits were cut. Not surprisingly, provincial leaders came increasingly to resent federal conditions supported by fewer and fewer federal dollars, and by the mid-1990s many of them began to challenge the basic legitimacy of the federal role.

In contrast, the primary issue for the government of Quebec has always been jurisdiction. Quebec never fully accepted the semi-centralized welfare state that emerged in the postwar era. In 1956, the Tremblay Commission described federal social programs as a form of "federal imperialism" that would erode the province's distinctive character,³⁵ and this view has been maintained

by virtually every provincial premier since then. Successive governments — federalist and sovereignist alike — have sought to capture the full domain of social policy from the federal government. This drive went well beyond the desire of other provinces for release from the constraints inherent in traditional shared-cost programs. Successive Quebec governments also demanded that a wide range of federal programs, including the full range of income-security programs, be transferred to Quebec jurisdiction, and constitutional negotiations from the Victoria Charter to the Charlottetown Accord have turned in part on this demand. Quebec has long been committed to the goal of a Quebec welfare state.

In effect, both the federal government and the Quebec government saw social programs as instruments of community-building and state-building. The political importance of these battles was highlighted by referendums on Quebec sovereignty conducted by the Quebec government in 1980 and 1995. During the 1980 campaign, federal ministers charged that independence would threaten the standard of living of Quebecers, and that a sovereign Quebec would not be able to sustain the social programs that Quebecers enjoyed as citizens of Canada. The federal minister of national health and welfare pointed to the interregional transfers implicit in federal programs that would be lost and told elderly voters that some of their pensions would probably disappear. The contrast with the 1995 referendum could not have been greater. The serious cuts to federal programs meant that federal ministers could no longer pose as defenders of popular benefits, and the separatist forces took the offensive. During the first weeks of the campaign, the *Parti Québécois* charged that only sovereignty could save pensions and other social benefits, and the leadership of the federalist forces in Quebec politics was left trying to explain why Quebecers should stay in a federation that reduced their social benefits. Obviously, the shift from a decisive federalist win in 1980 to a near loss in 1995 cannot be attributed solely or even primarily to the weakening of the federal role in social policy. However, the two battles highlighted the strategic role that social benefits play in some of the most intense moments in Canadian federalism.

MAKING THE PAST SPEAK TO THE FUTURE

Making the past speak to the future is never easy. History speaks with as many voices as there are listeners to hear, and each of us hears those parts of the story that resonate with our own concerns. We are unlikely, therefore, to draw conclusions that will answer definitively contemporary questions about how to build a new social union for Canada. Nevertheless, the history of the post-war social union does at least help to clarify the issues at stake in the current debates.

The basic architecture of the postwar social union leaves lessons. The simple recognition that there were multiple sources of pan-Canadian social policy in the postwar period reminds us that the issues go well beyond the traditional debate about national standards in provincial areas of jurisdiction. Shared-cost programs were only one of the arrows in the federal quiver. If the role of shared-cost programming is increasingly constrained in the future, the federal government can extend pan-Canadianism through the judicious use of other instruments, especially the direct delivery of benefits to citizens through the tax and transfer system. This option becomes increasingly plausible, at least in an incremental way, with the dawning of post-deficit politics in Ottawa. This is not to suggest that instruments are perfectly substitutable, and that direct transfers to Canadians can achieve precisely the same ends as shared-cost programs. But the multiple sources of pan-Canadianism in the postwar model stand as a reminder that the federal role in social policy does not rise and fall exclusively with the shared-cost mechanism.

The diversity of federal-provincial relationships embedded in the postwar social union points in a similar direction. As we have seen, the postwar generation did not elaborate an integrated philosophy of federalism, and the welfare state was undergirded by a diverse set of federal-provincial relationships, reflecting quite varied conceptions of the ideal federal state. Such complexity may be seen as a sign of confusion and weakness by those burdened with excessively ordered minds. But from the perspective of learning from the past, the diversity of relationships and models has important advantages. First, it suggests alternatives to which we might turn when individual approaches, such as cooperative federalism, fall into disfavour. Second, it creates a natural laboratory in which to assess the relative strengths and weaknesses of different approaches to federalism.

An evaluation of the strengths and weaknesses of the postwar social union also leaves lessons. Clearly, the strongest contribution of the postwar social union was in terms of social policy values. The semi-centralized system facilitated the development of a stronger set of social programs across the country as a whole than would have emerged from a decentralized system. Pockets of radicalism, such as Saskatchewan in the health-care sector, would presumably still have developed. But the diffusion of major innovations across the country would have been deeply constrained by the mobility of capital and labour, the ideological diversity of governments across the country, and the inequality in the fiscal capacity of rich and poor provinces. The expansion of the federal role facilitated a common tax and benefit regime across the country, forged ideological compromises among key provinces, and substantially equalized the fiscal capacity of provincial governments. Without that presence, major programs such as the Canada Pension Plan and medicare would not have emerged on a pan-Canadian basis. A decentralized Canada would have been a more unequal Canada.

In theory, one of the problems confronting a decentralized system — the inequality in the fiscal capacity of provincial governments — could have been offset by a system of equalization grants sufficiently powerful to compensate for the interregional transfers implicit in direct federal benefits to citizens and shared-cost payments to provinces. Indeed, the Tremblay Commission, which recommended the transfer of social programs to the provincial level in the 1950s, was quite sanguine about the prospects of such equalization emerging from a confederal compact among the provinces themselves.³⁶ Even if one sets aside that option as unrealistic, could federally-delivered equalization grants compensate for the transfers implicit in other federal programs? The problem here would be the political durability of one large, consolidated equalization grant. By making explicit all of the implicit transfers, such a grant would certainly attract much more political attention, and probably more criticism from citizens and politicians in rich regions receiving no significant social benefits from the federal government under the decentralized approach. Decentralization plus interregional transfers would have been a high risk strategy for poor regions in the 1950s, and would be today as well.

The only qualification to the largely positive relationship between the postwar social union and social policy values concerns the failure to coordinate federal and provincial programs. The institutional barriers to treating social policy as an integrated system were real, and became more obvious as governments sought to redesign postwar programs. The failure to establish an intergovernmental culture of collaboration in the postwar era is not an inevitable consequence of a federal state, as the current efforts to build a national child benefits program suggest. However, serious and continuing dispute over the division of power between levels of government does complicate the prospects, since the building of systems of collaboration does imply an acceptance of the legitimacy of the role of the two levels of government in social policy, something that Quebec has been unwilling to do.

Despite coordination failures, the overall contribution of the postwar balance in the federation contributed powerfully to social policy values. Not surprisingly, therefore, the weakening of the federal government has triggered anxious questions about the future. In part, the issue is how to preserve existing pan-Canadian social programs such as medicare; and in part, the issue is how to ensure that the country can devise equally effective responses to major social problems that emerge in the future. In the early 1990s, attention focused on the idea of a social charter;³⁷ and in the mid-1990s attention has shifted to the idea of a confederal model, represented by an interprovincial compact on social policy.³⁸ Debate on both of these options has been intense, focusing in both cases on the nature of the enforcement mechanism. Unfortunately, the history of the postwar social union offers few insights into instruments that were marginal or non-existent at the time.

In comparison to its contribution to social policy values, the postwar social union receives more mixed reviews in democratic terms. Programs reflecting the classical approach to federalism continued to approximate the canons of parliamentary democracy, but stronger forms of intergovernmentalism, such as cooperative federalism and co-determination, created problems for the openness, transparency, accessibility, and clear lines of accountability. The current shift toward stronger intergovernmental collaboration raises these issues once again. Informal forms of federal-provincial coordination, such as practised in the recent reforms to child benefits, are less problematic, although even here the process was marked by closed negotiations between governments.³⁹ However, the country may be inching toward the strongest form of executive federalism, the co-determination model. The commitment in the 1995 Speech from the Throne that the federal government will not initiate any new shared-cost programs without the formal support of a majority of the provinces represents a move in this direction, as does the pressure from provincial governments for a joint process of interpretation and enforcement of the *Canada Health Act*. The practical limitation on this approach is that it imports into the social policy sector all of the conflicts that have surrounded recent debates over the amending formula for the constitution as a whole. The formula governing reforms to the Canada Pension Plan was established in a period when such issues were much less charged, and it would be extremely difficult to get agreement on a similar formula today.⁴⁰ However, even if this practical limitation could be overcome, it is worth remembering the democratic critique of such potent intergovernmentalism.

Having said that, the seriousness of the democratic indictment of intergovernmentalism in social policy should not be overstated. Canadian governments are hardly paragons of openness even when operating exclusively in their own jurisdiction; and certainly in the postwar period Canadians were not particularly troubled by federal-provincial processes. Contemporary discontent with the elitist nature of executive federalism seems to focus primarily on the process of constitutional reform, and it is striking how few objections were raised to the largely closed negotiations that have moved forward the national child benefits program in recent months. In theory, the tension between intergovernmentalism and democracy is clear. In practice, it has not been the source of the primary challenges to the social union we inherited from the postwar generation.

The real challenge comes from the federal nature of Canada. The postwar social union has important lessons for the ways in which we debate the allocation of responsibilities between levels of government. Historically, theorists of federalism suggested that matters on which the population across the country largely agreed should be allocated to the central government, while matters on which regional populations tended to disagree should be allocated to provincial governments. More recently, theorists have also debated the question

in terms of the relative effectiveness of different levels of government. For example, advocates of decentralization often argue in terms of the greater flexibility of the system, with regional governments serving as sources of experimentation in the system; and opponents of decentralization have pointed to the dangers of triggering a race to the bottom, and so on.

The postwar tension between federalism and the welfare state points to a more complicated discourse. In the long term, substantial consensus in regional views on social policy was not enough to sustain the federal role at the heart of the postwar social union. The centrifugal pressures that weakened the postwar structure were not rooted primarily in regional differences over the substance of social policy. Rather they grew from two other sources: fragmenting conceptions of political community and political identity, most obviously in the challenge of Quebec nationalism; and the erosion of federal fiscal strength. Each of these crises had different but powerful consequences for the postwar social union.

The crisis of political identity transformed the debate about the division of powers from a discourse about effectiveness into a discourse about community and national unity. Social programs became cultural instruments, and controversies over jurisdiction took on a political symbolism that has made their resolution more difficult. Advocates of the decentralization of social programs see greater provincial jurisdiction as a means of accommodating centrifugal pressures and preserving the unity of the country. Critics counter that the decentralization of social programs diminishes the presence of the central government in the daily lives of Canadians, and erodes the underlying sense that, at some level, all citizens are part of a common political community with shared commitments and a collective future. Unfortunately, the postwar experience does not offer much evidence on the long-term effectiveness of either of these two strategies. Critics of the decentralist strategy might question whether successive past reductions in the federal role have actually undercut the appeal of sovereignty in Quebec, or whether a uniform decentralization to all provinces can really respond effectively to a challenge rooted in the need for a recognition of the distinctiveness of Quebec. Such critics might also argue that pan-Canadian social programs contribute to francophone Quebecers' sense of attachment to the country.⁴¹ Nevertheless, this is one issue on which history speaks with many voices, and different analysts hear different lessons.

History speaks more definitively about the corrosive effects of the erosion of federal fiscal strength. Provinces other than Quebec did not challenge the fundamental legitimacy of the expanded federal role as long as the federal government was a serious funding partner. It was the long series of reductions in federal financial transfers that slowly eroded provincial acceptance of the federal role. Deep and rapid cuts, such as those in the mid-1990s, were particularly deadly. In the long term, the fiscal crisis may not prove terminal to

the federal role, as Ottawa's financial position strengthens slowly in coming years. At a minimum, however, this experience speaks to the need for greater comity and predictability in funding arrangements, to be achieved through a set of ground rules concerning advance notice, consultation, transparency, and publicly discussed formula for the allocation of federal transfers among provinces.

In the final analysis, the experience of the postwar social union confirms the hard nature of the trade-offs before us. Strong pan-Canadian programs proved important to achieving key social policy values; the democratic credentials of the postwar social union were more ambiguous; and the primary challenge was rooted in federalism values. The central issue, therefore, is which set of values are to dominate as we refashion our social union. For some social policy groups, social policy values are fundamental, democratic values such as an accessible policy process represent a close second, and federalism ranks as a very distant third. From this perspective, federalism values should adjust to accommodate other social values. For other critics, federalism is the primary or primordial value, and other concerns must be adjusted accordingly. What is the purpose of a federal state, they ask, if we then create program structures that emulate a unitary state? There is no silver bullet, no magic solution that can easily reconcile such diverse views, and much will depend on the relative weight to be given to the three sets of values. History is silent on the balance that should give shape to a new social union for the decades to come, and the current generation of Canadians must find their own answer to this most fundamental of questions.

NOTES

1. This chapter builds on Keith G. Banting, "Institutional Conservatism: Federalism and Pensions," in *Canadian Social Welfare Policy: Federal and Provincial Dimensions*, ed. J.S. Ismael (Montreal: McGill-Queen's University Press, 1985); *The Welfare State and Canadian Federalism*, 2d ed. (Montreal: McGill-Queen's University Press, 1987); "The Welfare State as Statecraft: Territorial Politics and Canadian Social Policy," in *European Social Policy: Between Fragmentation and Integration*, ed. S. Leibfried and P. Pierson (Washington, DC: The Brookings Institution, 1995); and "The Social Security Review: Policy-Making in a Semi-Sovereign Society," *Canadian Public Administration* 38, 2 (1995): 283-90. The text has been significantly enhanced by excellent research assistance provided by Kate Brown, and by helpful comments on an early draft provided by Harvey Lazar and an anonymous reviewer.
2. Thomas H. Marshall, "Citizenship and Social Class," in *Class, Citizenship and Social Development*, ed. T.H. Marshall (New York: Doubleday, 1964).
3. Margaret Biggs, *Building Blocks for Canada's New Social Union*, Working Paper no. F-02 (Ottawa: Canadian Policy Research Networks, 1996).

4. Canada, *Federal-Provincial Grants and the Spending Power of Parliament: Working Paper on the Constitution* (Ottawa: Information Canada, 1970).
5. Timothy Sargent, *An Index of Unemployment Insurance Disincentives*, Working Paper no. 95-10 (Ottawa: Department of Finance, Fiscal and Economic Analysis Branch).
6. In the US, the AFDC program generally provided support to mothers with dependent children only, excluding single people and childless couples.
7. National Council of Welfare, *Welfare Incomes, 1995* (Ottawa: National Council of Welfare, 1996).
8. Tom Courchene's recent proposal for an interprovincial accord among provincial governments to sustain pan-Canadian social values represents another example of the confederal model. See Thomas Courchene, "ACCESS: A Convention on the Canadian Economic and Social Systems," Working Paper prepared for the Ministry of Intergovernmental Affairs (Toronto: Government Printers, 1996); and *Assessing ACCESS: Towards a New Social Union* (Kingston: Institute of Intergovernmental Relations, Queen's University, 1997).
9. Margaret Biggs, *Building Blocks for Canada's New Social Union*.
10. Quebec, Royal Commission of Inquiry on Constitutional Problems, *Report* (Quebec: Éditeur officiel, 1956), vol. 2, p. 320.
11. Banting, *The Welfare State and Canadian Federalism*, p. 64.
12. Quebec, Social Insurance Commission, *Report* (Quebec: Éditeur officiel, 1933), p. 108.
13. *Ibid.*, p. 203.
14. Canada, Royal Commission on Dominion-Provincial Relations, *Report* (Ottawa: King's Printer, 1940), vol. 2, pp. 36, 40-1.
15. For an analysis in terms of rational choice theory that points in the same direction, see Dan Usher, "How Should the Redistributive Power of the State be Divided between Federal and Provincial Governments?" *Canadian Public Policy/Analyse de Politiques* 6 (1980): 16-29.
16. Richard Simeon, *Federal-Provincial Diplomacy: The Making of Recent Policy in Canada* (Toronto: University of Toronto Press, 1970), p. 270.
17. Quebec was the only province to have shown any interest in contributory pensions, but such a program was not a priority of the Quebec government until Ottawa launched its initiative, see Simeon, *Federal-Provincial Diplomacy*, pp. 45-46; Kenneth Bryden, *Old Age Pensions and Policy-Making in Canada* (Montreal: McGill-Queen's University Press, 1974), p. 164.
18. Banting, "Institutional Conservatism"; Bryden, *Old Age Pensions and Policy-Making in Canada*.
19. Quoted in Malcolm G. Taylor, *Health Insurance and Canadian Public Policy: The Seven Decisions that Created the Canadian Health Insurance System* (Montreal: McGill-Queen's University Press, 1987), p. 375.
20. Courchene, "ACCESS."

21. Marsh, *Report on Social Security in Canada* (Toronto: University of Toronto, [1943] 1975), pp. 52-55 and *passim*.
22. *Ibid.*, p. 251.
23. Canada, *Working Paper on Social Security* (Ottawa: Information Canada, 1973), p. 15.
24. Rodney Haddow, *Poverty Reform in Canada, 1958-1978: State and Class Influences on Policy Making* (Montreal: McGill-Queen's University Press, 1993); Christopher Leman, *The Collapse of Welfare Reform: Political Institutions, Policy and the Poor in Canada and the United States* (Cambridge, MA: The MIT Press, 1980).
25. Quebec, Commission of Inquiry on Health and Social Welfare, *Report* (Quebec: Éditeur officiel, 1971).
26. Interprovincial Conference of Ministers Responsible for Social Services, *The Income Security System in Canada* (Ottawa: Canadian Intergovernmental Conference Secretariat, 1980), ch. 4 provided an excellent analysis of the administrative tensions among income security programs.
27. *Ibid.*, p. 113.
28. Canada, Federal Task Force on Disability Issues, *Equal Citizenship for Canadians with Disabilities: The Will to Act* (Ottawa: Minister of Supply and Services, 1996).
29. Although the Canada Pension Plan does not operate generally in Quebec, a number of Quebec residents do contribute to the fund, and the government of Quebec counts in the amending formula for the CPP itself. Thus, a combination of Quebec and another smaller province could conceivably also block a change.
30. Banting, "Institutional Conservatism: Federalism and Pensions."
31. The contrast with the process of the social security review initiated by the federal government in 1994 in the context of wider public dissatisfaction with intergovernmental elitism was dramatic. See Keith G. Banting, "The Way Beavers Build Dams: Social Policy Change in Canada," in *A New Social Vision for Canada: Perspectives on the Federal Discussion Paper on Social Security Reform*, ed. K. Banting and K. Battle (Kingston: School of Policy Studies, Queen's University, 1994) and "The Social Security Review: Policy-Making in a Semi-Sovereign Society."
32. For a review of public opinion data in this period, see Banting, *The Welfare State and Canadian Federalism*, ch. 8.
33. Donald Blake and Richard Simeon, "Regional Preferences: Citizens' View of Public Policy," in *Small Worlds: Provinces and Parties in Canadian Political Life*, in D. Elkins and R. Simeon (Toronto: Methuen, 1980).
34. See, for example, Canada, *Income Security and Social Services* (Ottawa: Information Canada, 1969), especially p. 68. For a wider discussion of social policy as an instrument of social integration, see Banting, "The Welfare State as Statecraft."
35. Quebec, Royal Commission of Inquiry on Constitutional Problems, *Report*.

36. Ibid., vol. 2, pp. 288-94.
37. Ontario, *A Canadian Social Charter: Making Our Shared Values Stronger* (Toronto: Ministry of Intergovernmental Affairs, 1991).
38. Courchene, "ACCESS."
39. Richard Zucker has labelled this form of collaboration "reciprocal federalism" in Richard Zucker, "Reciprocal Federalism: Beyond the Spending Power," 1995, mimeo.
40. The CPP formula gives a formal veto to Ontario but to no other single province.
41. Keith G. Banting, "Cultural Diversity, Citizenship and Social Rights," paper presented to the Conference on Citizenship, Diversity and Pluralism, University of Saskatchewan, 31 October – 1 November 1997.

Reducing the Muddle in the Middle: Three Propositions for Running the Welfare State

John Richards

Cet article essaie de répondre à la question à savoir comment mieux gérer les programmes sociaux dans un état fédéral. En résumé, l'article avance trois propositions.

La première insiste sur des budgets balancés en utilisant des procédures comptables crédibles. La politique sociale repose sur le consentement de la majorité. Une condition nécessaire pour le consentement est que les citoyens aient une idée juste au sujet des coûts des programmes, en termes des taxes qui devront être payées.

La seconde proposition concerne la responsabilité. Seul un niveau de gouvernement devrait en général être responsable pour un domaine particulier de politique sociale, et le gouvernement responsable devrait se procurer les revenus nécessaires selon ses propres sources de taxation. La responsabilité veut dire que le gouvernement responsable peut simultanément présenter de nouveaux programmes et enlever les vieux qui relèvent de son domaine, et que les citoyens par des élections démocratiques peuvent récompenser le gouvernement pour de bons résultats et punir pour les mauvais.

Un corollaire est de minimiser le rôle des cours et des agences coordinatrices intergouvernementales compliquées dans la politique sociale. Inévitablement, des programmes défieront l'affectation à l'un ou l'autre des niveaux de gouvernement. Par conséquent, il y aura toujours "un désordre dans le milieu." Un autre corollaire est que l'organisation de ce milieu sera compliquée, et sa taille devrait être gardée au minimum.

La troisième proposition concerne l'avantage comparatif. Ottawa a un avantage comparatif dans la livraison de programmes qui redistribuent le revenu selon des règles relativement directes, mais la plupart des programmes sociaux impliquent une administration complexe et, dans ces cas, la juridiction provinciale devrait primer. Qu'arrivera-t'il des provinces plus pauvres? Un programme d'égalisation fiscale à travers les provinces est une contribution fédérale valable à la politique sociale. À part l'égalisation, les transferts intergouvernementaux sont de façon générale à être évitées.

INTRODUCTION

From the beginning of civilized discourse people have disagreed, often passionately, over what mutual obligations they owe to their community — over what, in our secular age, is called social policy. This chapter contains little advice on what social policy should be. Instead, it provides advice on how to organize passionate disagreement. That advice is summarized in three propositions and the bulk of this chapter makes the case for these propositions which, in the interest of providing an outline, are listed below:

- *Proposition One: Never separate the case for generous social policy from the case for balanced budgets.* The welfare state rests on the democratic assent of the majority. A necessary condition for that assent is that citizens have a fair idea of both program benefits and their costs, in terms of taxes to be paid.
- *Proposition Two: Accountability matters. One — and only one — level of government should in general be responsible for any particular domain of social policy, and the responsible government should be required to raise necessary revenues via own-source taxation.* In a federation, as in any other form of government, accountability is crucial to the long-run success of government initiatives. Accountability means that the responsible government can simultaneously introduce new policies in its domain and scrap old ones, that citizens know the tax cost of social programs, and that citizens have a clear means — democratic elections — whereby they can reward their governments for good outcomes and punish them for bad. The first corollary is to minimize the role of the courts and of complex intergovernmental coordinating agencies in social policy. Successful welfare states require good politicians and administrators, not good judges or diplomats. They need good administrators to run a respectable welfare state, and good politicians to lead and heed public debate over social policy. Even the best of judges and intergovernmental diplomats are poor substitutes. Inevitably, some programs defy allocation to one or other level of government. Hence, there will always be a “muddle in the middle.” A second corollary is that organization of this middle will be convoluted, and its size should be kept to a minimum.
- *Proposition Three: Respect comparative advantage, and celebrate competitive federalism. Ottawa has a comparative advantage in delivery of programs that redistribute income according to relatively straightforward rules, but most social programs entail complex administration and, in such cases, provincial jurisdiction should prevail.* Reconciling provincial paramountcy in most areas of social policy with the requirements of accountability poses a problem: What about poor provinces

with insufficient fiscal capacity to raise sufficient revenue for a reasonable set of social programs? A program of fiscal equalization across provinces is a valuable federal contribution to social policy. Beyond equalization, intergovernmental transfers are generally to be avoided.

Before proceeding with the main argument, however, it is useful to digress briefly on the nature of social policy. It entails three dimensions.

THE THREE DIMENSIONS OF SOCIAL POLICY

The first and most obvious dimension of social policy is the extent to which the non-poor should redistribute income to the poor. Social assistance programs use general tax revenue to provide targeted benefits for the poor. Hence the first source of debate: how much redistribution to undertake? If social policy concerns only this dimension, and if people across the country give similar answers to this question, then the central government has a comparative advantage over subnational units. The central government can assure redistribution corresponds to citizen preferences. Furthermore, uniform tax and benefit rules avoid inefficient migration of people out of high-tax regions and into high-benefit regions.

Most social programs do more than redistribute income. Many simultaneously improve economic efficiency by overcoming a "failure" inherent in particular markets. To illustrate, in Canada, as in most industrial countries, health insurance is funded primarily from general tax revenue; citizens do not pay actuarially fair premiums. Accordingly, this is a social program that redistributes, in the form of health services, toward low-income and high-risk citizens. (These two groups overlap but are not identical.) It is also an example of using social policy to correct several market failures, one of which is the inefficiency associated with the buying and selling of private health insurance. In a private market, insurees want maximum coverage at the lowest possible cost and have a strong incentive to hide risk factors that point to a high probability of expensive claims. Insurers have a strong incentive to deny liability. The result is cheating by both parties, costly monitoring to discourage cheating and far-from-universal insurance coverage for high-risk patients. Pooling everyone into a universal health insurance plan can dramatically lower such costs. According to a US Congressional study,¹ the per capita cost of insurance overhead under the Canadian system, where provinces operate "single-payer" insurance systems for their entire populations, is approximately one-fifth the per capita cost in the United States where private health insurance is the norm.

That Canada has addressed the "failures" of health markets more aggressively than in the US is shown by the post-1960 divergence in health-care costs between the two countries. Prior to adopting "socialized medicine,"

Canada and the United States both spent about 6 percent of GDP on health care. By the mid-1990s, Canada was spending below 10 percent, and the US above 14 percent. Incidentally, by simple measures of health status (infant mortality and average life expectancy), Canada has maintained a slight but consistent edge over the US throughout the last three decades.²

Debating health policy accordingly entails debate over at least two dimensions: the extent to which government should redistribute, and the extent to which it can improve economic efficiency in an important sector of the economy.

That is not all. Health care is a social policy that embodies the third and most controversial dimension: use of government to realize certain widely shared values. The majority in most industrial countries insist everyone must have basic health insurance; they treat it as a "merit good." Regardless of the wealth or poverty of my neighbour, regardless of his or her preferences, regardless of the relative efficiency of market versus single-payer insurance systems and independent of whether the illness is communicable to me, I do not want him or her to face significant financial costs in seeking health care if and when it is needed. Accordingly, I am not prepared to let them choose to spend their money freely in this instance. I vote for a political party that obliges us to pay taxes that support a universal health insurance program.³

In summary, it is useful to think of social programs as government activities having one or more of the following goals: to redistribute income, to redress market "failures" where redress has a major redistributive effect, and to realize certain widely shared values concerning distribution of "merit goods." Once we allow that social programs entail the second and third dimensions, it is not surprising that social policy is contentious. It cannot be reduced to rules incorporated in an income tax system; it inevitably entails complex administrative and policy decisions that in turn require responsible politicians, professional administrators and dedicated service providers.

Proposition One: Never separate the case for generous social policy from the case for balanced budgets. It would have been far, far better for Canadian social policy if Canadian senior governments had engaged in fiscal restraint earlier — before the demand placed on social programs by the early 1990s recession forced spending up and, given high debt, also forced governments to raise taxes; and before debt-service costs became a cancerous growth squeezing the fiscal resources required for other programs. No one can be certain as to what would have happened had some particular event in the past been different. But, had the political leadership of the centre and left, federally and provincially, not succumbed so completely to an opportunistic Keynesian discourse that ridiculed the task of balancing the books, Canadian senior governments would probably have eliminated deficits much earlier, with less disruption to social programming.

For illustrative purposes, I pick on the federal Liberals. They are not the only set of Canadian politicians to have ignored this first proposition and, by 1997, the majority of Liberals had learned to respect it. The great irony of the 1997 general election is that many Canadians voted Liberal because the party did what, in 1993, it had ridiculed the Tories for having promised. Starting with the 1995-96 budget, Ottawa credibly set about the task of cutting its coat to the size of the available cloth.

I start with the Liberals' 1993 election manifesto, the famous *Red Book*. In it they quoted James Tobin, a prominent elder statesman among Keynesian economists, on the potential economic costs that deficit reduction might induce and they dismissed the Tory target for balancing the budget:⁴

the Conservatives have set another unrealistic target [in the 1993-94 budget] by promising to eliminate the deficit in the next five years.... Any responsible government must have as a goal the elimination of the deficit. That is our goal. Given the current state of the economy, a realistic interim target for a Liberal government is to seek to reduce the federal deficit to three percent of [GDP] by the end of its third year in office [i.e., by the 1996-97 budget]. To achieve this target, cutting expenditures alone, as the Conservatives are proposing, will not be sufficient. Faster economic growth and reduction of unemployment is a prerequisite for sustained deficit reduction.⁵

Were the *Red Book* merely election propaganda, such waffle would be unsurprising. But it was more than propaganda; it was an earnest attempt among policy-oriented Liberals to synthesize their ideas. On fiscal matters, this amounted to an opportunistic Keynesianism which, reduced to its core, goes roughly as follows. Faced with recession and unemployment, governments should stimulate demand by deficit spending and by expansionary monetary policy which lowers interest rates; a resurgent economy will generate the revenues necessary to eliminate the deficit. Cutting expenditures is inevitably counter-productive: it will lower aggregate demand, exacerbate unemployment and the demand for redistributive social programs.

The prevalence of this discourse distorted macroeconomic debate far too long. In 1993, John Crow (champion of restrictive monetary policy) and Ralph Klein (premier of a province actually engaged in fiscal restraint) were the personification of error for Liberals. The only other senior government which, at the time, had a credible fiscal program to restore balance was Saskatchewan, led by Roy Romanow. The anomaly of a NDP government reducing spending was beyond the ken of conventional wisdom; it was politely ignored.

I do not want to use irony to gloss over the complexity of debates surrounding appropriate macroeconomic policy. Here, I make a simple observation. Tight monetary policy becomes a logical outcome in a country whose political leadership refused the discipline required to balance budgets. Variants of this opportunistic Keynesianism were practised by most senior Canadian governments over the two decades prior to 1995.

Take as example the economic boom in the late 1980s. Both the federal and provincial governments — here the Liberal government at Queen's Park was the prime culprit — should have dampened aggregate demand by aggressive fiscal restraint. Had this occurred, inflation would probably not have increased in the final years of the decade, and the case for restrictive monetary policy would have been less convincing. Far from assessing the possibility of renewed inflation, the federal Liberals congratulated their provincial colleagues for new spending programs at Queen's Park, and did their utmost to undermine the modest exercise in fiscal restraint being practised by their Conservative opponents in Ottawa. John Crow's policies undoubtedly amounted to overkill; they unnecessarily increased interest rates in 1990 and deepened the ensuing recession. Intellectual honesty demands, however, that any critique of monetary restriction be accompanied by a critique of the failure of Canadian politicians to respect this first proposition.

Opportunistic Keynesians sin by omission. They ignore the politically painful half of fiscal stabilization: that governments must run fiscal surpluses to damp the inflationary potential of economic booms and to maintain the financial capacity to run deficits during recessions. When the majority of the political elite subscribe to some variant of opportunistic Keynesianism, the exercise of fiscal discipline becomes highly controversial. It requires more political courage than the typical government is capable of mustering. When, for whatever reason, inflation worsens and people call on governments for a response, most perceive monetary policy as the only feasible option.

The federal Liberals' 1995-96 budget marks a genuinely important break with past Canadian practice. We can trace the evolution of official Liberal thinking via a series of major documents, each identifiable by the colour of its cover. The appropriate point of departure is the scarlet-coloured *Red Book*. There followed the Grey and Purple Papers, the Green Paper, and the collected White Papers.

By the time the Liberals began preparing their first budget, 1993's scarlet maple leaves were buried beneath the snow. In January 1994 the Department of Finance published three sober documents on the state of the country's finances.⁶ These background documents and the 1994-95 budget⁷ were all bound in white covers. A neutral white symbolized that the Liberals' initial intent was, in aggregate, to change little. The Liberals projected an identical spending level for the next two years (1994-95 and 1995-96) to that undertaken by their predecessors in their previous two budgets.

Financial markets responded sceptically. Bankers discussed the possibility of a collapse in demand for bonds issued by Canadian senior governments (similar to what had occurred in Mexico in late 1994). Interest rates on Canadian public debt rose in spring 1994, and it became clear that debt-servicing costs would exceed budget projections. Finally, to use an appropriate image, the penny dropped. Cabinet agreed to abandon the *Red Book's* waffle and

actually balance the books. Given already high tax rates, this required lower program expenditures.

As was to be expected, the government was less than perfectly consistent in its conversion to fiscal rectitude. In the fall of 1994, for example, the Liberals continued with its major social policy review by publishing a Green Paper which contained a number of sensible reforms.⁸ But, in it, the Cabinet avoided costing social programs and establishing priorities appropriate to a smaller total budget. Shortly after the Green Paper, the Department of Finance published its Grey and Purple Papers.⁹ Here were two blunt policy statements, clothed in suitably subdued colours, intended to prepare Canadians for the 1995-96 budget.

Via the Grey Paper, the Liberals admitted that, using the Finance Department's base-case projection (the "prudent scenario"), realizing even the modest *Red Book* target of a deficit below 3 percent of GDP by fiscal 1996-97 required a combination of tax increases and program expenditure cuts not envisaged in the 1994-95 budget. The Grey Paper also undertook a useful disaggregation and description of the major categories of public spending. Using a definition consistent with the above discussion, social spending accounted for nearly two-thirds of the total.¹⁰ The message was clear: any serious exercise in deficit elimination meant cuts to social programs.

The most ambitious of all these documents was undoubtedly the Purple Paper. Here was a well argued attempt to provide what the title promised — "a new framework for economic policy." No one could accuse the Finance Department of opportunistic Keynesianism. It bluntly argued the antithesis, calling for an end to deficit spending as the prerequisite for good social policy:

The debt and deficit are often portrayed as issues primarily of concern to financial markets and ideologues. The truth is that those who suffer most immediately from Canada's fiscal deterioration are the unemployed, the poorer regions of the country, and the average young to middle-aged family with a mortgage and other debt incurred to raise and educate their children. The unease of financial markets in the face of Canada's debt spiral translates directly to higher loan and mortgage payments for the average Canadian. And the relentless compounding pressure of interest costs on the public debt is severely eroding the ability of the government to provide for Canada's less advantaged citizens and regions. The social consequences of debt are every bit as grim as the economic.¹¹

Beyond making the case to end deficit spending, the fundamental recommendation was that government policy be judged on its ability to help Canadians adapt to market change, as opposed to its ability to protect Canadians from change. For example, the Purple Paper stressed government's role in helping workers acquire new skills, as opposed to its role in providing passive income support. On the subject of UI reform, it stated bluntly: "more will be needed to return UI closer to insurance principles and to create programs that improve job readiness."¹²

The final document in this kaleidoscope is the actual 1995-96 budget, with its suitably sober dark grey cover.¹³ The budget reduced by a quarter inter-governmental transfers and transformed all remaining transfers into block grants; it cancelled the century-old Crowsnest Pass transportation subsidy to prairie farmers; it reduced the dairy subsidy and international aid; it required significant civil servant layoffs. It announced further cuts to UI and hinted at future reductions in pension benefits. Relative to the past generation of Canadian federal budgeting, all this was a radical departure. Admittedly, relative to the wrenching fiscal adjustments undergone by some other industrial countries — from Sweden to the UK and New Zealand — the changes were modest. And the net result was no more than a lowering, by 1996-97, of the projected federal deficit below the threshold of 3 percent of GDP.

One means to appreciate quantitatively the significance of the watershed 1995 budget is to compare the revenue and expenditure projection made by the Tories in their last budget,¹⁴ tabled in 1993, with actual outcomes. Here, in point form, are a few observations based on Figure 1 and Table 1 and the 1997 budget.¹⁵

- Relative to 1994-95 levels, the Liberals expect to have lowered (nominal dollar) program spending by 11 percent in 1998-99. The key break occurred obviously in 1995.

Figure 1.1: Overcoming Debt Denial, Program Spending

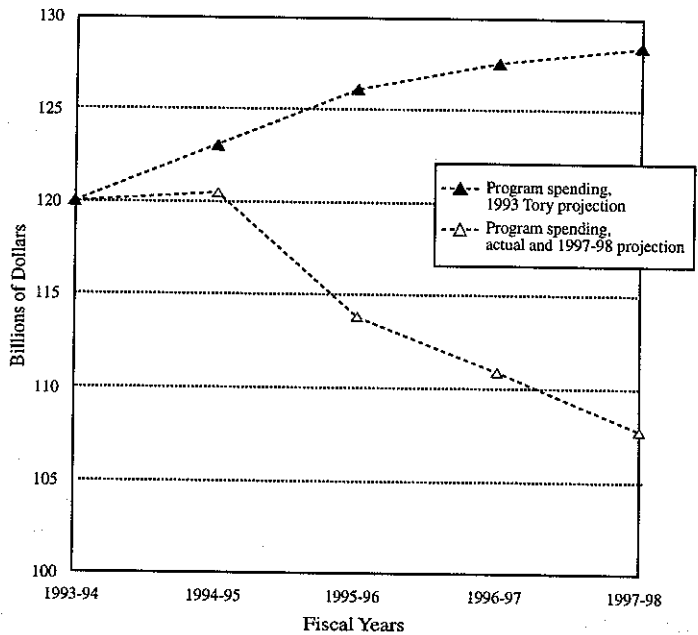


Figure 1.2: Overcoming Debt Denial, Debt-Service Costs

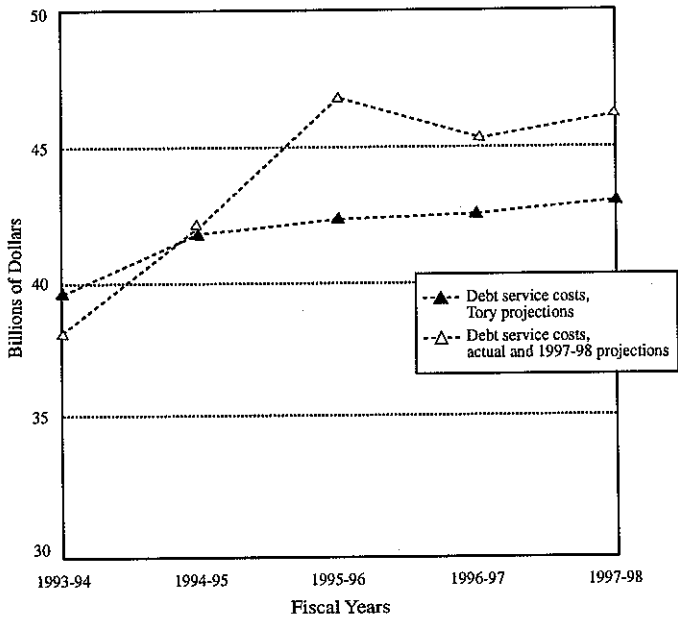
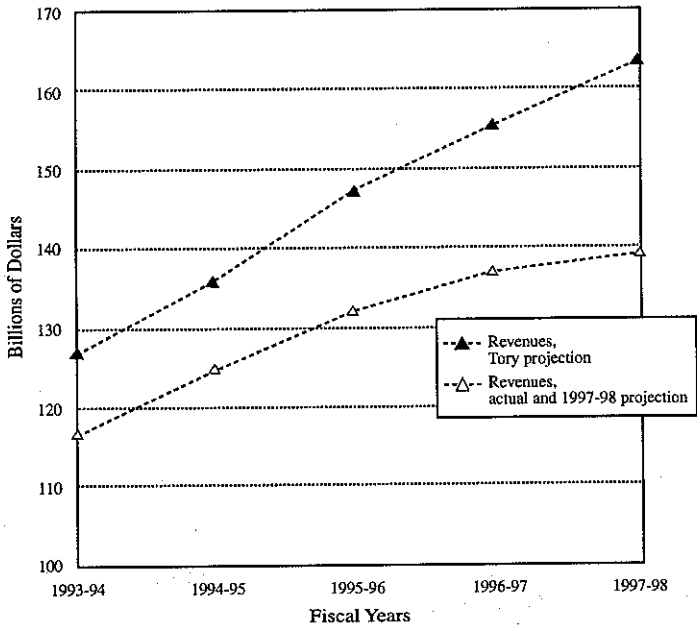


Figure 1.3: Overcoming Debt Denial, Revenues



- The Liberals accepted that public resistance to discretionary tax increases is sufficiently potent that federal tax revenues cannot be increased faster than GDP. The federal tax-GDP ratio accordingly remained constant throughout the Liberals' first term in office. It ranged between 16.5 percent and 17 percent of GDP.¹⁶
- Even with the recent decline in interest rates and federal expenditure restraint, federal debt-service costs are well above levels projected by the Tories in 1993, and are approaching one-half the total of all program spending. For 1997, federal debt-service costs are now greater than the value of all program spending by the Government of Ontario.
- Despite this exercise in fiscal redress, the net federal debt as a share of GDP continued to rise until 1996-97, at which point it reached 74.4 percent,¹⁷ four times the corresponding statistic in the early 1970s. Finally, in 1997-98, this ratio began to decline.

In concluding discussion of this proposition, a final argument is addressed to those who instinctively mistrust the linking of social policy to the setting of fiscal limits. If Ottawa balances its budget by fiscal 1998-99, as appears likely, and if Ottawa accepts that the tax-GDP ratio has reached a ceiling, does that mean such a large contraction in per capita program spending as to threaten the health of Canadian social programs?

By way of answer, I refer to a modest study published by the C.D. Howe Institute in 1994. With the inspirational title, "The Courage to Act," it was published after the Liberals' first do-nothing budget and before the do-something-serious 1995 budget.¹⁸ The study undertook a simple exercise to estimate the magnitude of federal program spending cuts required, assuming that Ottawa would balance its budget in fiscal 1998-99, (which is effectively the projection of the 1997 budget),¹⁹ and assuming that revenues would rise in proportion to GDP, that is, no increase in the tax-GDP ratio would take place. The conclusion was that program spending would need to be about 12 percent below 1994 levels, a reduction similar to current projections for fiscal 1998-99. (Table 1 shows the magnitude of program expenditures in 1994-95 and current projections for 1998-99. We shall return to the disaggregated figures below.)

If the Canadian population grows by 5 percent between 1994 and 1998, a cut of 12 percent in program spending implies an average per capita cut of 17 percent. This may appear draconian. It is not if placed in historical perspective. If both the federal *and* provincial governments reduce 1994 program spending by that amount by 1998, per capita program spending in constant dollars will be at levels prevailing in the early 1980s, hardly a time of the minimal state in Canada.

A corollary to this proposition is that governments must present budgets to their respective legislatures in a transparent manner that allows legislators

Table 1: The Liberals' Exercise in Fiscal Restraint: Changes in Federal Program Spending, 1994-95 to 1998-99

	1994-95	1998-99	Change	
	(\$ billion)		\$	%
1 Elderly benefits	20.5	22.9	2.4	12
2 Labour adjustment	14.8	14.1	-0.7	-5
3 Indian and Inuit	3.7	4.4	0.7	19
4 Canada Health and Social Transfer (CHST) ^a	19.3	12.5	-6.8	-35
5 Other transfers to territories and provinces	0.7	1.1	0.4	57
6 Equalization	8.5	8.4	-0.1	-1
7 Business subsidies and other transfers	16.3	10.1	-6.2	-38
8 Crown corporations	5.0	3.8	-1.2	-24
9 Defence	10.7	8.5	-2.2	-21
10 Other ^c	21.0	21.0	0.0	0
11 Total, program spending	120.5	106.8	-13.7	-11
12 Total, major program spending to individuals (1.+2.+3.)	39.0	41.4	2.4	6
13 Total cash transfers to other governments (4.+5.+6.)	28.5	22.0	-6.5	-23
14 Total, program spending less major program spending to individuals and transfers to governments (11.-12.-13.)	53.0	43.4	-9.6	-18
15 Total, program spending excluding CHST (11.-4.)	101.2	94.3	-6.9	-7
16 Debt-service charges	42.0	46.5	4.5	11
17 Budgetary revenues ^b	125.0	146.2	21.2	17
18 Deficit (-)/surplus (+) (17.-11.-16.)	-37.5	-7.1	30.4	

Notes:

- a. This figure includes cash transferred plus the value of Quebec's extra tax points which serve to lower what otherwise would be federal transfers to that province. The value of these extra tax points is deducted from the cash transfer to Quebec. Hence, the figures shown exceed actual cash transferred. The 1994-95 figure includes the cash transfers (plus value of Quebec's extra tax points) under the Canada Assistance Plan and Established Program Financing; the 1998-99 figure includes the cash transfer (plus value of Quebec's extra tax points) under the Canada Health and Social Transfer. The figure cited, \$12.5 billion, includes the electoral promise of an additional \$0.7 billion made by the Liberals during the 1997 election campaign.
- b. By an argument analogous to that in note a, this value exceeds actual revenues received by an amount equal to the value of Quebec's extra tax points.
- c. The figure cited, \$21.0 billion, includes \$0.3 billion, the estimated cost of electoral promises other than the \$0.7 billion increase to the CHST.

Source: adapted from Canada, Department of Finance, *Budget Plan* (Ottawa: Department of Finance, 1997), p. 64.

and citizens to engage in intelligent debate over levels of taxation and public expenditures. This may appear a banal matter, but it is not. Governments attempting to avoid fiscal discipline are always tempted to "cook the books." The devices used rarely confuse professional accountants engaged by bond rating agencies to assess government indebtedness, but they can readily frustrate public debate.

Proposition Two: Accountability matters. One — and only one — level of government should in general be responsible for any particular domain of social policy, and we should require the responsible government to raise necessary revenues via own-source taxation. Lord Durham and de Tocqueville made their respective observations on Canada and the United States during the 1830s. Had they returned from the grave a century later to observe once again the state of North American society, they would probably have concluded the United States would be more likely than Canada to generate a generous welfare state. Washington, with the blessing of the majority of Americans, was launching major new social programs. Prior to World War II, the United States enjoyed more generous social security legislation than did Canada. Central to the New Deal was the willingness of Americans at all levels — from the Supreme Court to ordinary citizens — to blur the fundamental principle of federalism, which is a sharply etched division of jurisdiction between levels of government. Washington was able to use a number of heads of federal jurisdiction to intervene in domains that formerly had been considered exclusive matters of state jurisdiction. In terms of the continuum Harvey Lazar constructs in his contribution to this volume, the Americans moved decisively from "classical federalism" in the direction of "federal unilateralism."

For Canada, the final arbiter of constitutional matters remained in London until appeals to the Judicial Committee of the Privy Council were abolished in 1947. Until then, this group of judges had the final say on Canadian squabbles over which set of politicians, federal or provincial, could intervene in any matter. The Judicial Committee represented the pinnacle of administrative wisdom distilled from British imperial rule and, in general, its members opted for strict accountability. If one level of government was responsible for a particular function, so be it. For example, inspired by the New Deal, Ottawa attempted to legislate on hours of work and minimum wage, matters generally deemed to fall under provincial jurisdiction. Ottawa justified its legislation on the grounds of implementing an International Labour Organization treaty to which Canada was a party. In 1937, the Privy Council overturned the legislation, refusing to allow Ottawa to use its treaty-making powers as means to blur provincial responsibility for labour law. In a famous line from his decision, Lord Atkin used a maritime image: "While the ship of state now sails on larger ventures and into foreign waters she still retains the watertight compartments which are an essential part of her original structure."²⁰

The sceptic's response to Lord Atkin's "watertight compartments" doctrine is to ask: Are contemporary elected governments — in particular provincial governments — worthy of such trust? Sceptics worry that allocation of particular social policy programs to the provincial level will result in a checkerboard of uneven social policy across Canada. Better to promote some variant of collaborative federalism that constrains provincial variation. Some prefer a model whereby Ottawa constrains the provinces by a set of conditional grants and imposition of national standards. Some want power in the hands of the courts — perhaps via an explicit social charter — to overlook the performance of both Ottawa and the provinces. But, having placed some agency in a position of overseer, the question then becomes, can we trust the overseer? The key problem is worth emphasizing: all variants of collaborative federalism entail shared jurisdiction and reduce political accountability of any one government for the quality of social programming.

Ultimately, the sceptic's question is an empirical one. Which generates better social policy: respect for "watertight compartments" or, on the other hand, the logic of collaborative federalism? The evolution of social policy north and south of the 49th parallel over the twentieth century has provided a prolonged large-scale social experiment. Canada and the United States are similar along many dimensions. Both are federations of continental size. Both are prosperous industrial societies whose dominant cultural roots are in Western Europe. At the end of the century, the conclusion is, I think, inescapable: the Canadian greater reliance on "watertight compartments" contributed to realizing a European-style welfare state, whereas the American emphasis on collaborative federalism retarded the Americans from making similar progress.

Canadians should not be smug about the better quality of our social programs. That we maintained a more precise division of responsibilities is due to a variety of factors having little to do with the search for good social policy. Overshadowing any other is the strength of the dual loyalty among francophone Quebecers. For reasons of culture and language, the majority among them want a powerful government in Quebec City. They have refused any Canadian equivalent to the New Deal transformation in American politics. While not as powerful as in Quebec City, other provincial capitals (such as Edmonton) also have a tradition of resisting an expanded federal role. And, so long as the Judicial Committee of the Privy Council was the final arbiter of our constitution, the courts played a role in preserving Canada as a classic federation.

The Americans, on the other hand, essentially abandoned classic federalism in the 1930s. During the Great Depression, the New Deal Congress established the pattern: those interested in active social policy concentrated on generating influence in Washington which, in turn, cajoled state and local governments via a combination of conditional grants, mandated programs and judicial overview. The strategy entailed the carrot of Washington's providing cash on a conditional basis, and the stick of intervention by activist courts in

the case of recalcitrance. The high point of American social policy innovation came in the 1960s, at the time of President Johnson's War on Poverty.

Undeniably, there have been successes. The courts played the lead role in obliging conservative states to desegregate within their jurisdictions. Washington shared in the cost of providing social assistance in poor states, and pioneered innovative programs such as early education for poor children. Washington successfully implemented programs of universal health care for the old (Medicare) and for the poor (Medicaid). And, despite the heavy hand of Washington and the courts, certain states (for example, Wisconsin) have established a reputation for continuous independent social policy innovation.

But, since the 1960s, there have been more failures than successes. Public enthusiasm for social policy has waned. Conservative Congressional leaders have damned the undeniable inefficiencies of many federally mandated social programs. They are right inasmuch as Medicare and Medicaid are inordinately expensive. In 1996, Congress abolished the long-standing Aid to Families with Dependent Children (AFDC) and substituted block grants to the states. AFDC contained many perverse incentives that perpetuated single parenthood and welfare dependency.

Among American liberals, some have been interested in rehabilitation of a Jeffersonian version of "states' rights" — the American equivalent of the watertight compartments doctrine. An example is the Democratic Leadership Council, an important lobby of senior Democratic politicians. But, it is fair to say the dominant view of social policy among US liberals remains the New Deal legacy.²¹

The natural instinct among social policy advocates is to refuse this second proposition. If one agency of government is, for whatever reason, resistant to social policy innovation, then lobby another. At this point, I introduce two cases. The first illustrates the value of strict accountability in generating good social policy; the second illustrates the damage done by lack of accountability.

Case One: Saskatchewan and the arrival of universal health insurance in Canada. In an evolutionary sense one can trace the origins of medicare back through the fossil remains of policy initiatives dating from the early twentieth century. But the key events all took place in a short space of time in the 1960s, starting with the 1960 provincial election in Saskatchewan. That election was effectively a referendum on the promise of Premier Tommy Douglas that, if reelected, his government would introduce a mandatory form of medical care insurance during its 1960-64 term of office.²²

The campaign was heated. The principal opposition party (the Liberals) adamantly opposed the idea of "socialized medicine," as did the province's physicians. Douglas won reelection, whereupon he launched a public enquiry on the matter, and his Cabinet and senior bureaucrats devoted their energies to the design and launch of an insurance agency capable of integrating the existing private insurance companies and of insuring all uninsured provincial

residents. Political controversy was intense. On the left, the government faced demands for more radical reorganization of ambulatory health care into a series of cooperatively organized community health centres. On the right, the physicians took their opposition to the point of calling a provincewide strike in the summer of 1962. In order to maintain health services the government found itself engaged in strike-breaking. It hired a hundred foreign doctors to practise on salary throughout the province. To mediate the strike, the government engaged a senior British Labour Party official who had participated in the launch of the British National Health Service in the late 1940s. After three weeks, the doctors and government came to an agreement. The doctors achieved a few concessions: a decrease in direct government control and increase in professional overview of the insurance agency but, on the essentials, the physicians conceded. They accepted that the government could introduce a mandatory form of medical care insurance. The government paid for the new service via general revenue and a premium which was, in effect, a poll tax varying by family size. There was no short-run prospect of federal cost-sharing.

Very quickly, the value of a universal medicare program became evident. The provincial government's insurance agency ran its affairs competently. The government did not interfere — any more than before — in the freedom of practice of physicians. Patients no longer had to concern themselves with the complexities of buying health insurance for basic services or, if previously uninsured, no longer worried about large medical bills. Doctors experienced higher incomes and simpler accounting procedures since their patients were, all of them, now insured and, all of them, able to pay for services. In 1964 Saskatchewan voters decided that, after 20 years, they had had enough of the socialists. They elected the opposition Liberals whose ideologically conservative leader (Ross Thatcher) had earlier vowed to dismantle medicare. He quickly realized the program's popularity and broke his vow.

Simultaneous with Douglas's initiative, John Diefenbaker's Conservatives had established the Royal Commission on Health Services (chaired by Judge Emmett Hall). The basic recommendation of this commission, delivered to Lester Pearson's newly elected Liberals in 1964, was to encourage adoption by all provinces of health insurance plans based on that in Saskatchewan. Ottawa utilized its spending power to inaugurate a highly popular cost-sharing venture that induced even the most conservative provincial governments to do precisely that. By the early 1970s, all ten provinces had set up equivalents to Saskatchewan's universal medical insurance plan.

The federal Liberals had promised universal health-care insurance from time-to-time since the end of World War I. It required, however, a successfully functioning provincial experiment before Ottawa and the other provinces acted. Cumulatively, Saskatchewan's health insurance reforms over the two decades of CCF rule (1944-64) demonstrated the feasibility of realizing in North America universal hospital and medical insurance systems comparable to those in Western Europe.

The case of medicare in Saskatchewan illustrates nicely the value of strict accountability: the freedom of a duly elected government to introduce and scrap social programs within its jurisdiction provided it pays for them with own-source taxation. Admittedly, Saskatchewan was in receipt of equalization and other intergovernmental transfers at the time, but the province had no means to transfer the cost of this program onto Ottawa. Its citizens paid via taxes on themselves. This induced within the provincial government a healthy attention to the complex managerial details of running a health insurance agency.

Medicare was a highly controversial social policy initiative.²³ The provincial government was obliged to contend with powerful hostile interest groups. Had jurisdiction over health policy been shared — either with the courts or Ottawa — displeased interest groups would probably have used these avenues in an attempt to block implementation. They might well have succeeded, at least to the extent of delaying implementation beyond the next provincial election. Strict accountability demonstrated its worth. It allowed a government to innovate despite strong interest group opposition, and placed evaluation where it belongs — in a general election among all citizens. The fate of medicare under the successor government in Saskatchewan should give the sceptics of provincial jurisdiction some reassurance. When a social program proves transparently popular, public preferences successfully manifest themselves — even when the government is ideologically ill-disposed.

Case Two: British Columbia and the welfare residency requirement. The Canada Assistance Plan (CAP) began in the 1960s, out of an admirable desire on the part of Ottawa to share the cost of provincial social assistance programs. Under CAP rules, both levels of government became responsible for social assistance. The provinces would undertake on-the-ground administration; Ottawa would establish appropriate national standards. The key national standard that the provinces agreed to respect was that financial need become the sole criterion for welfare eligibility, that is, that the provinces would not impose other requirements based on age, work/training requirements, or length of residency. Provided the provinces respected this national standard, Ottawa would pay one-half of all provincial costs of social assistance.

The availability of 50-cent dollars encouraged provinces with fiscal discretion to be generous. The most dramatic example was Ontario, which more than doubled its normalized caseload between 1983 and 1993. It passed from being the province with the lowest caseload in the early 1980s, to being the province with the highest by the early 1990s.²⁴ In 1990, Ottawa undertook an ad hoc initiative to constrain the generosity of provincial social assistance programs — Ontario's in particular — by imposing a "cap on CAP" payments to the three "have" provinces (Ontario, British Columbia, and Alberta). Alberta was not bound by the cap because, starting in 1993, it introduced a series of reforms which halved the provincial caseload. In 1995, Ottawa further curtailed its cost-sharing by scrapping CAP (and the Established Program

Financing transfer), substituting a new smaller transfer, the Canada Health and Social Transfer (CHST). This new transfer is a block grant with many fewer conditions attached. The one remaining condition is that provinces not impose a residency requirement on welfare applicants.

When, in 1991, the British Columbia NDP came to power, it launched a program of enhanced welfare generosity with little attention to either the likely effect on welfare use or the impact of the federal "cap on CAP" which prevented the province from shifting half the incremental cost to Ottawa. Between 1991 and 1995, the normalized caseload rose by 30 percent. Simple regression analysis suggests that this increase in welfare use is largely attributable to the NDP's introduction of a relaxed culture of provincial welfare administration. That, however, was an unpalatable conclusion for the NDP to accept.

A more palatable conclusion was to blame a Conservative provincial neighbour and a Liberal federal government. To symbolize this alternate explanation, the provincial government flouted Ottawa's one remaining condition on receipt of CHST funds and, in late 1995, imposed a three-month residency requirement on welfare applicants. Ottawa duly responded by withholding CHST funds and, thereby, the NDP was able to launch a very public partisan squabble. British Columbia would have been willing, provincial politicians claimed, to take Alberta's poor if Ottawa was not "offloading responsibilities and costs onto the provinces."²⁵ "Why is it okay," asked the provincial social services minister, "according to the Liberal government, that provinces [i.e., Alberta] who slash their welfare rates and cut and cut are allowed to do that, whereas British Columbia, who actually has strengthened their social safety net, is not allowed to have a residency requirement?"²⁶

Even if Alberta residents had been migrating to British Columbia welfare rolls in large numbers since 1993, the case for a residency requirement would have been weak. But the provincial government launched its residency requirement with no evidence to suggest Alberta's 1993 reforms had increased out-of-province welfare applications in British Columbia.²⁷

And, the accusation of federal "offloading" needs to be placed in context. Between 1990-91, the last full fiscal year under their Social Credit predecessors, and 1995-96, the NDP allowed the provincial welfare budget to increase by \$1.3 billion. This increase was nearly three times the magnitude of the cut in federal transfer revenue between 1994-95 and 1996-97. The cut, under \$500 million, was equivalent to 2.3 percent of provincial revenue for the 1996-97 fiscal year.²⁸

The growth in conditional intergovernmental transfers over the preceding two decades inevitably invited conflicts of this nature, particularly when Ottawa began to address its fiscal problems. Given the culture of fiscal unaccountability bred by large intergovernmental transfers, rancour becomes understandable. Which is not to excuse it. The provincial BC government exploited ambiguities surrounding responsibility for social assistance policy to

obfuscate accountability for its conduct of social assistance programs. To be blunt, increasing the normalized social assistance caseload by 30 percent during an economic boom is indicative of a poorly designed program.

None of this discussion implies that welfare residency requirements are good social policy. An important principle in free trade agreements is national treatment, the idea that host governments will not impose laws on foreign firms that are more restrictive than those imposed on domestically owned firms. It is even more important that governments apply this principle to their own citizens within a country. It is legitimate for British Columbia to vary the rules for welfare applicants, provided it does so for all applicants; it is not legitimate to use regulations as a device to impede interprovincial migration by Canadians in search of better opportunities. Had provincial politicians not obfuscated the matter by partisan attacks on Alberta Conservatives and federal Liberals, political discussion over residency requirements might have been more lucid.

Albeit I am loathe to puncture watertight compartments, I accept that residency requirements are odious and that it is important to eliminate them — by intervening on provincial jurisdiction if necessary. This constraint on provincial social assistance policy would probably be better couched in terms of the *Charter* mobility right than a condition attached to the CHST. Conditional grants utilizing national standards are simply too weak an instrument.

MINIMIZE THE MUDDLE IN THE MIDDLE: AVOID JUDGES AND MINIMIZE EXPECTATIONS FROM COMPLEX INTERGOVERNMENTAL COORDINATING MECHANISMS

Some social policy experiments succeed; some fail. A parallel exists between the chutzpah of business entrepreneurs and of political leaders. The former are essential to the success of capitalist economies, the latter to democracy in general and the welfare state in particular. Politicians engaged in persuading citizens to support their ideas with their votes — and to pay the requisite taxes — are not unlike entrepreneurs persuading potential financial supporters to risk their money in building the entrepreneur's better mousetrap. Many times the politicians' new ideas turn out to be less brilliant than originally touted; so too with the better mousetraps. Successful capitalist economies require the freedom of entrepreneurs and investors to make mistakes. Successful welfare states require an analogous autonomy on the part of elected governments.

The competitive process, whereby manufacturers of good mousetraps in the long run drive out bad mousetraps, is a time-consuming and messy one. So too is the electoral process whereby citizens select good social programs over bad. In neither case is there a feasible substitute. This implies we resist the temptation to construct elaborate mechanisms intended to oversee and coordinate social policy decisions of governments.

Unless governments are violating truly fundamental civil liberties — as I would allow was the case with the BC residency requirement — the courts should not intervene in this dynamic. Had the Charter been in existence in 1962, Saskatchewan physicians might well have used it to challenge introduction of a mandatory health insurance plan. The plan obliges physicians to accept payment from a government agency, and to abandon private contracting for payment between themselves and patients. A reasonable legal argument exists to the effect that this violates mobility rights under the Charter, one of which assures Canadians “the right ... to pursue the gaining of a livelihood in any province” (section 6.1.b). The Saskatchewan government, it could be argued, was taking to itself too much power to determine whether physicians could earn a living, and under what conditions. Presented with this argument, a sceptical Supreme Court might well have called upon the Saskatchewan government to come up with a less radical infringement on physicians’ freedom to contract with their patients.

Maybe I am guilty of overemphasizing the importance of precise jurisdictions and reliance on electoral accountability. Undoubtedly, Harvey Lazar thinks so. He observes that the federal approach to the social union has, in the last few years, been inching toward some version of “collaborative federalism.” From the perspective of provincial administrators, most probably perceive the decade to have begun with “collaborative federalism” (a large muddle in the middle) and to be groping toward the “disentangled federalism” pole of Lazar’s Figure 1.²⁸ Social programming has been “collaborative” over the last decade, in the sense that the provinces perceive themselves as leading on most dossiers in a context of (ambiguous) national standards, declining federal transfers, and complex Ottawa-designed fiscal incentives impinging on both provinces and individuals.

Admittedly, there will always remain elements of social policy that cannot be adequately given over to one or other level of government. For these elements, some form of collaborative federalism must be worked out. How should we organize this “muddle in the middle”? My basic conclusion is to keep such arrangements simple and few. Here is a brief critique of two important attempts to answer the question.

ACCESS

Tom Courchene, in an important paper released in 1996 by the Ontario government, has stated the ideal:

the provinces must have the flexibility to design and deliver their own vision and version of the socio-economic envelope.... The most cited exemplar here is the experimentation in Saskatchewan which led to Medicare.... The more general

point is that the on-going blossoming of provincial experimentation across a range of fronts is absolutely critical to recreating an efficient and viable social Canada. The policy challenge here is to ensure that this experimentation takes place within a framework of "national" (federal, federal-provincial or inter-provincial) norms or principles.³⁰

We should add that federal experimentation within its jurisdictions is also critical. Courchene is careful to insist that we cannot have our cake and eat it too: to allow more autonomy necessarily implies less restrictive standards or, to say the same thing another way, there is a price to be paid in terms of forgone experiments if we impose stricter standards. Courchene is sceptical of the ability of Ottawa to administer a set of national standards on the provinces but he is sanguine that, over time, it is feasible to construct an "enforceable interprovincial accord whereby the provinces jointly implement and maintain a framework of principles and standards/equivalences that will guarantee across Canada rights such as mobility and portability."³¹

I am less sanguine on this than is Courchene. Imposing standards on reluctant governments is tough to do, and we should attempt the exercise sparingly. The danger exists that, by overselling standards, we raise false expectations among Canadians about the potential of any coordination mechanism and, subsequently, generate confusion and disappointment when the standards are found not to work.

Second, we must keep clear the distinction between securing the economic union and what is, by analogy, often termed securing the social union. The essence of an economic union is establishing uniform rules over a market regulated by multiple governments. A central principle of any economic union is "national treatment," that governments treat all economic agents similarly, regardless of their state of origin. Having accepted the logic of national treatment in the context of NAFTA, Canadians are currently concerned — via the Interprovincial Trade Agreement, for example — to apply the principle more rigorously with respect to interprovincial trade.³² However, social policy is much more than setting rules or standards. The second and third dimensions of social policy (discussed earlier) mean it is often akin to running a large corporation. To the extent this is true, seeking appropriate national standards is an exercise in alchemy — one doomed to failure.

Attempting to build national social policy standards "from the bottom up" is often justified by reference to the attempts by members of the European Union to create a workable social charter. While the economic advantages from the European common market are undeniable, the benefits of a social charter remain nebulous. It may impose some very wide margins within which member states operate their social policy, but it will almost certainly remain at the level of the *Canada Health Act*, a statement of goals that provides a vague constraint on the social policy of member states but does not address

the ongoing tough trade-offs required to run a successful welfare state. Realistic European administrators do not entertain the illusion that there can be equally generous social programs in low-productivity economies (such as Portugal) as in high-productivity economies (such as Germany). Canadians should not expect that a poor province like New Brunswick be as generous as a rich province like Ontario in setting welfare benefit levels. (Even after the new Conservative government reduced Ontario benefit levels, they remain nearly two times higher than in New Brunswick.)

In a few instances, social policy overlaps economic policy so closely that the distinction between an economic union and social union becomes untenable. For example, all provinces are guilty of a variety of explicit barriers against employment of out-of-province workers. These clearly violate the spirit of an economic union. While nominally a social policy, a residency requirement on a welfare application is also a barrier against out-of-province workers. It has the clear effect of discouraging interprovincial migration among low skilled workers. Accordingly, in this instance, it is appropriate to generalize the concept of national treatment and seek a mechanism — interprovincial agreements, the courts imposing a Charter right, or some other — to constrain provincial welfare policy. By all means, a province should be able to tighten or relax administrative rules covering social assistance. The constraint imposed by “provincial treatment” is that all welfare applicants be treated equally. Whether the applicant originally lived in Fort St. John or across the border in Peace River, Alberta, should not affect his or her welfare eligibility in Vancouver.

Courchene optimistically concludes, “there exist plenty of opportunities for mutual gain [in social policy] arising from enhanced coordination, harmonization or even just from greater information sharing.”³³ Although sceptical about the potential for coordination and harmonization, I agree wholeheartedly on the value of information sharing. For the electoral dynamic to function adequately in generating accountable public policy, reliable information is essential. Generating good information about the outcomes of social policies is often expensive, and governments often restrict access to relevant potentially embarrassing information.

REPORT TO THE PREMIERS

Here is a second important attempt to organize the “muddle in the middle.”³⁴ This document, released in late 1995, reflects an attempt at consensus-building among nine provinces (Quebec excepted) to define federal-provincial responsibilities in an age where the provinces are, whether they like it or not, assuming more responsibility:

The Council [representing provinces plus territories] believes the following criteria should be used in clarifying federal-provincial roles and responsibilities in the social sector:

- federal activity in areas of sole provincial responsibility should occur only after federal/provincial-territorial consultation, and provincial/territorial agreement on how federal spending can be effectively applied;
- as responsibilities within the federation are clarified and realigned, commensurate resources can also be transferred;
- areas of joint federal-provincial/territorial responsibility be minimized in those instances in which this would improve the effectiveness of these programs;
- the use of federal spending power in areas of sole provincial/territorial or joint federal-provincial/territorial responsibility should not allow the federal government to unilaterally dictate program design;
- the federal government accept full responsibility for all programming for Aboriginal people, both on and off reserve, with a gradual transfer of authority to Aboriginal communities.³⁵

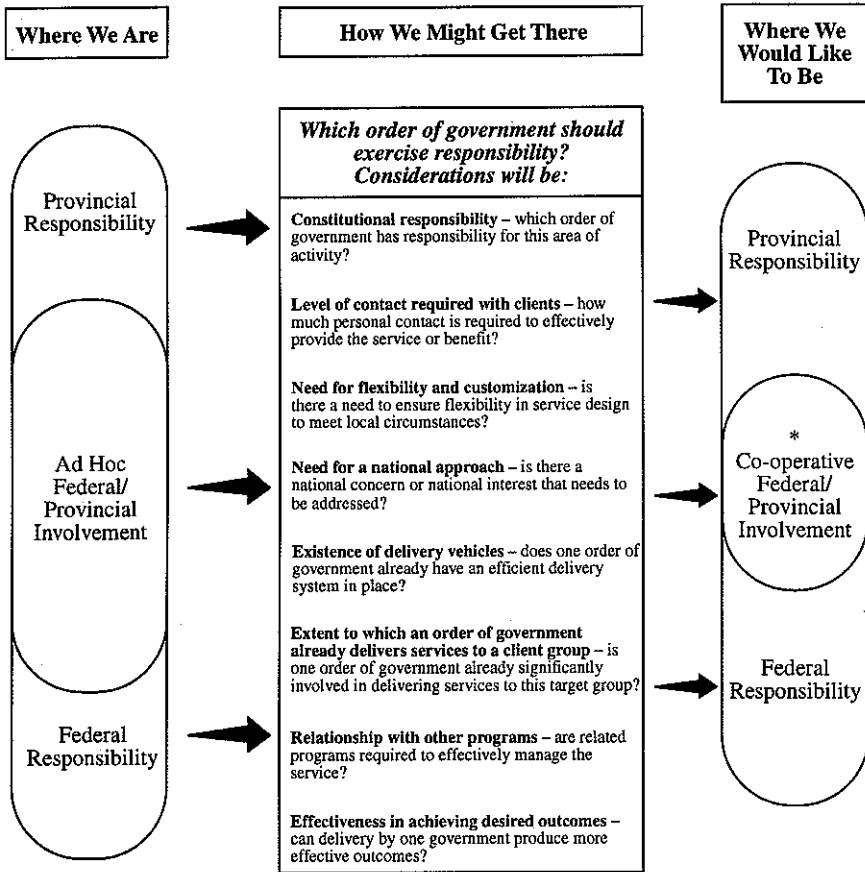
Figure 2, drawn from the report, envisions an evolution of social policy from the oval on the left — with a large area of “ad hoc federal/provincial involvement” — to the oval on the right — with larger areas of exclusive federal or provincial responsibility and a much smaller area of “co-operative federal/provincial involvement.”

The report displays a certain naïveté in its expectations for restoring the pre-1995 level of intergovernmental transfers from Ottawa. It also underestimates the difficulty of designing good social programs for Aboriginals. Since they are leaving reserves and increasingly living in cities like the rest of us, the potential for separate aboriginal programming is much less than implied here. That said, the report lays out a number of useful pragmatic guidelines. It wants an end to unilateralism in federal use of its spending power (e.g., no more unilateral adjustments in intergovernmental transfers). If Ottawa does spend in an area of provincial jurisdiction, provinces should be able to opt out of the federal program with full fiscal compensation.

Inspired by dispute resolution mechanisms in free trade agreements, the report's authors want an interprovincial mechanism for dispute resolution in matters of social policy. The first stage of such resolution would be provision of relevant accurate information. If that does not allow for a solution, the second stage would be mediation. If necessary, the third and final stage would be arbitration — perhaps via a panel appointed by the concerned senior governments.

Proposition Three: Respect comparative advantage, and celebrate competitive federalism. Ottawa has a comparative advantage in delivery of programs that redistribute income according to relatively straightforward rules, but most

Figure 2: Clarifying Federal-Provincial Responsibilities for Social Programs



*There will always be areas in which both governments should operate, and the aim should be for a process of effective and respectful cooperation in these areas. Cooperation means that major decisions on program design, financing and delivery should be made through agreement by both orders of government, with delivery of programs by one or the other.

Note: Federal-territorial cooperation should also address the need to clarify responsibilities as proposed in this chart, while reflecting the financial arrangements for the delivery of social programs to aboriginal residents of the territories.

social programs entail complex administration and, in such cases, provincial jurisdiction should unambiguously prevail. Much of the discussion of Proposition Two turned on the value of explicit provincial jurisdiction. That does not deny Ottawa's role in social policy. As stated in the introduction, the comparative advantage of Ottawa is most evident in programs that redistribute income among Canadians according to straightforward rules. Seniors' benefits are an example. If the goal of social policy is to redistribute income from rich to poor, federalism offers few advantages over a unitary state.

On the other hand, the two other dimensions of social policy entail political and administrative discretion. Here, the provinces have a comparative advantage. While the welfare state has the potential to be more efficient than the market in providing certain services and realizing some important collective values, it realizes that potential only if public sector "entrepreneurs" — that is, elected politicians and senior mandarins — actually undertake processes of creative destruction to adapt social programs to changes in society. Understanding the case for decentralized jurisdiction is the political analogue to understanding that decentralized property rights and free markets are a necessary (if far from sufficient) condition for realizing the productive potential of industrial technology.

Decentralization of jurisdiction creates competition within the public sector. At any point in time, different provinces may do things differently within their jurisdictions. The potential benefits should be considered both in terms of long-run innovation and short-term efficiencies. The long-run benefit is to increase experimentation, by enabling entrepreneurial provincial politicians in one province to innovate in social policy independent of the preferences of voters in other provinces. As in the market economy, voters favour some innovations; these are, with a lag, copied in other provinces. Other provincial innovations fail the test of popular support and are dropped. The short-run benefit has three aspects:

- *Reduce managerial scope.* The three most important spending ministries in all provincial governments are health, education, and welfare. Were these functions run out of three Ottawa mega-ministries, they would (as measured by annual revenues) be larger than any publicly traded private company in the country. However well intentioned, mandarins at the centre face more difficulty in assembling relevant information than their provincial equivalents, each responsible for a much smaller domain. Even after decentralizing to the provincial level, these ministries in large provinces manage revenues that place them among the top 20 of Canadian private companies, and they generate some opaque Kafkaesque bureaucracy.
- *Limit the dynamic of concentrated benefits and diffuse costs.* Decentralization is a partial solution to the problem of inefficient interest

group lobbying. Not all, but most, social programs are local inasmuch as the benefits accrue primarily to residents within the relevant province. Politicians have a universal tendency to advocate programs that confer concentrated benefits on identifiable local populations, while diffusing the costs over a larger population. Such tendencies encourage the accretion over time of inefficient programs. Decentralization does not eliminate this problem but lessens its severity. When provincial citizens choose by their votes to "buy" new programs, they must more-or-less agree to pay for them via provincial taxes. The per capita cost of any provincial program is larger than the cost of a program of equal absolute cost financed nationally. Hence, public debate of net benefits is likely to be more realistic.

- *Lower the cost to people of indicating their preferences as to what they want in terms of locally supplied public services.* Assembling and distributing information on policy options, and determining public preferences over some set of policy options is a complex social process. The larger the jurisdiction, the more complex and more inaccurate. People usually have more accurate analyses and more precise policy preferences about matters close to home than about matters far away. Decentralization can be seen, accordingly, as a means to lower the information requirements surrounding democratic decisionmaking.

This discussion leads to a simple but powerful insight on public policy: decentralization encourages a more efficient use of scarce resources because it encourages innovation, reduces managerial scope, constrains the ability of politicians and interest groups to shift costs, and lowers the costs of determining public preferences. The World Bank has repeatedly stressed this theme in recent "world development reports." An example cited is the value of decentralization to the quality of roads among 42 developing countries.³⁷ Centralized agencies come up with a few standardized road specifications, and this often results in overbuilt roads for rural areas. Also, centralized agencies underinvest in the hard-to-monitor activity of road maintenance. In those countries where responsibility for roads was decentralized to subnational governments, the World Bank concluded that the percentage of poorly maintained roads was roughly half that of countries with centralized responsibility. Roads may seem too humble an example from which to generalize. But the World Bank found similar results in its comparative analysis of many other local services — such as sanitary water systems.

In Canada a topical candidate for decentralization is labour market training. Here is a major area of social policy, one in which, given low employment-to-population rates among low-skill workers, there is a lot to do. On the other hand, the optimal set of training programs is far from obvious, and experimentation is highly desirable.³⁸ Ideally, Ottawa and the provinces

will agree to a clean exercise in decentralization. This may take the form of concurrent jurisdiction with provincial paramountcy. The large provinces will take up the jurisdiction; smaller provinces need not do so.

I conclude this section on an optimistic note. Poverty among low-income families with children is a major wound in Canadian society and, until now, social policy to address it has been inadequate. In this domain, at least, Ottawa and the provinces are each recognizing their respective comparative advantage. They are currently developing major, by-and-large sensible, policies.

Operating in pre-electoral mode, the Liberals announced in the 1997 federal budget their intention to enrich the tax benefits available for low-income families with children. Unlike years past, the Liberals did not claim that the federal role was preeminent. Instead, the budget displayed a refreshing humility:

This approach should assist lower-income families with children by allowing each order of government to focus on what it can do best. The federal government is best positioned to run large-scale programs through the tax system. Provinces and territories are better placed to run programs that include regional variations and that respond quickly to changes in the needs and circumstances of individual families.³⁹

Ottawa is restricting its intervention to what it can do well: provide a straightforward transfer of money via the income tax system. It is not presuming to dictate the design of what the provinces "build" on this "platform."

The provinces in turn are building anti-poverty programs reflecting their respective strategies. They are currently designing and implementing programs intended to increase reliance on employment earnings as opposed to transfers, and to supplement the after-tax rewards from low-wage employment. Which province has the best building? Which plans are flawed? At this stage, one could give highly tentative responses based on the various blueprints, but more important is to wait, see the buildings in place and being lived in and, at that stage, undertake some rigorous evaluation.⁴⁰

DECENTRALIZATION HAS ITS LIMITS

The comparative advantage of Ottawa lies in programs that redistribute income among Canadians according to straightforward rules. A related idea is that administrative economies may militate in favour of centralized program administration. For example, the federal child tax benefit is administered at minimum cost by use of the federal income tax system. If left to their own devices, provinces may undersupply services with a positive spillover effect. Provinces may undertake insufficient training because trained workers are

mobile, and the benefits of their higher incomes and tax revenues may accrue in provinces other than the one in which training takes place.

Avoidance of inefficient migration, realization of scale economies, and encouraging services where positive externalities exist are, all three, classic arguments on behalf of centralized social policy. By-and-large, in Canada, we have allowed for federal preeminence where these arguments are transparently important. The most problematic are labour training and (un)employment insurance.

Interprovincial labour mobility is an incentive for a province to underinvest in training its own citizens. But, there is little evidence of this. The prime goal at present is to raise the distressingly low employment-to-population rates among certain groups — including Aboriginals and low-skill youth — and many provinces are innovating. Given the inefficiencies embedded in EI(UI) programs over the last quarter century, an argument exists to decentralize it as well. However, Ottawa has unambiguous constitutional responsibility for this program, and has this decade begun the controversial reforms required to restore it to the status of a social insurance program — and eliminate those aspects which made it a supplementary social assistance program for the employable. The Liberals have incurred the political costs (not the least of which was loss of 20 Atlantic MPs in the 1997 election), and deserve some credit. Continuity is desirable here; transferring EI(UI) jurisdiction to the provinces makes little sense at present.

Another set of limitations to decentralization is inherent in the three dimensions of social policy. Decentralization may improve program efficiency but, if a poor province lacks an adequate tax base, it will lack adequate revenue to run a reasonable set of social programs. Hence, a good social policy case exists for equalization transfers that, in the language of the *Constitution Act*, allow provinces to “provide reasonably comparable levels of public services at reasonably comparable levels of taxation” (section 36(2)). Provided a province undertakes the average taxing effort among provinces, equalization transfers bring per capita provincial revenues to the average of the five provinces used as a benchmark. As befits the rationale, equalization in Canada takes the form of an unconditional block grant governed by five-year intergovernmental agreements that assure predictable funding over the medium term.

Beyond equalization, there are no sound policy arguments to make on behalf of major intergovernmental transfers. The CHST is a desirable innovation relative to the *status quo ante*. But it should be perceived as a transitional policy, as a means of phasing out the expensive conditional transfer model of social policy symbolized by CAP and EPF, and moving toward a greater respect for social program accountability and for the comparative social policy advantages of each level of government.

WHAT ABOUT THE CHST?

Phasing out the CHST is not a goal that is unanimously shared. Here is the case for doing so. By reducing the size of intergovernmental cash grants and removing conditions, the 1995 CHST reform implied acceptance by Ottawa of the value of clearer program accountability. Relative to the former regime of intergovernmental transfers, the CHST reduced the ambiguity surrounding responsibility for several major social programs — something much to be desired. It is now clearer than before: responsibility for social assistance and health care resides with the provinces and, if citizens don't like the results, they know whom to blame. But

The Liberals promised in their 1997 election campaign to restore some of the cuts in intergovernmental transfers. This promise was delivered in Halifax, in the hope of avoiding electoral losses in the Atlantic region. It was a promise that ran counter to all three of the propositions advanced here. Increasing intergovernmental transfers via the CHST retards realization of a balanced budget; it dilutes the trend toward clear accountability for social programs; it represents incremental federal social policy spending without reference to Ottawa's comparative advantage.

One misleading aspect of the CHST debate is the charge that it represents an immoral exercise in "offloading" program costs to the provinces. The prime piece of evidence in support of this charge is the contrast between the percentage cut in CHST cash transfers (relative to the now-defunct CAP plus EPF) and the percentage cut in all other programs. The former cut is 35 percent (line 4 of Table 1), whereas the latter is only 7 percent (line 15).

This comparison is dubious on several counts. First, the critics engage in highly selective accounting. Ottawa transfers revenues to the provinces via programs other than CHST, and these other transfers are also intended to support provinces in the financing of social programs. Adding together all such transfers, we find that Ottawa is proposing a cut of 23 percent (line 13) — not 35 percent.

A second consideration is that Ottawa directly provides social programs to individuals, the most substantial of which are seniors' benefits, labour market adjustment, and Indian and Inuit programs (line 12).⁴¹ The critics imply that an equitable exercise in fiscal restraint would have cut these programs at the same rate as other items. Given an aging population, the difficulties faced by unemployed Canadians and aboriginal poverty, equiproportionate budget cuts would have been immoral. If we exclude intergovernmental transfers and these major social programs, the projected reduction in all remaining program spending is 18 percent (line 14), a figure not far off that applied to aggregate intergovernmental transfers (line 13).

A final argument needs to be made on all this. An important means of restoring fiscal equilibrium at both the federal and provincial level over the next

decade will be to lower the public sector compensation advantage.⁴² The provinces spend a much higher share of their program dollars on salaries than does Ottawa. Accordingly, the provinces have a much greater potential than Ottawa to realize savings from better control over the public sector payroll. It is reasonable that Ottawa receive some benefit from provincial payroll savings in order to avoid excessive reductions in the social programs it directly administers. Reducing intergovernmental transfers is a means to do so.

Rather than seeking to placate Atlantic Canada, a preferable policy goal is to phase out the CHST entirely. Over a period of, say, five years, Ottawa could eliminate cash payments and simultaneously lower federal income tax rates by an equivalent amount. The provinces would be obliged to take up this tax room. This increase in provincial taxation would be subject to equalization and, to that extent, Ottawa would find itself engaged in some increase in the one remaining intergovernmental transfer.

Before we conclude, here are three arguments — none of which I find convincing — on behalf of Ottawa continuing to devote over 10 percent of its program spending on cost-sharing of provincial social programs via the CHST:

- *Dubious argument one. Cost-sharing provides Ottawa with a fiscal incentive with which to induce provinces to respect national standards.* We have dealt at length with this argument in the context of Proposition Two. At most, national standards operate on the fringe of social policy; it is very hard for one government to impose standards on another reluctant government.
- *Dubious argument two. Elimination of cost-sharing would aggravate the division between have and have-not provinces.* Probably the reverse is closer to the truth. The rationale for equalization enjoys widespread public support among Canadians. On the other hand, the arbitrary unequal per capita distribution of other intergovernmental transfers that emerged by the 1990s engendered political rancour. The majority living in Ontario and the west have concluded that fiscal federalism is an unfair set of programs that takes from them and gives to Canadians living in Quebec and the Atlantic. This thesis is most vigorously put forward by the Reform Party but, as shown by this selection from a major 1993 Ontario government report (written while the NDP was in office), support for the thesis is widespread:

In the period since 1985, there has been a series of discretionary moves by the federal government that have substantially increased the net burden on Ontario residents, through increased levies and reductions in the relative share of federal expenditures in the province. This redistribution of the fiscal burden has not occurred through programs designed for that purpose (e.g., equalization) but rather through unilateral reductions in federal transfers to

the provinces targeted on Ontario and other relatively well-off provinces, and through more subtle changes to spending patterns and transfers to persons.⁴³

This widespread public sense of unfairness about fiscal federal arrangements is a far more dangerous threat to the success of the Canadian welfare state than the short-term adjustment pains placed on provinces by elimination of the CAP and EPF, and a phasing out of the CHST.

- *Dubious argument three. Elimination of cost-sharing for social programs would further divide the two solitudes and encourage Quebec separatism.* Perhaps, but the historical evidence is hardly supportive of such an argument. For the last generation, Quebec politicians — operating out of both Ottawa and Quebec City — have negotiated skillfully within the intergovernmental transfer system, and realized for their province above-average per capita transfers. In effect, this has meant buying off Quebec nationalism. There has been no constitutional accommodation of that agenda and, instead, offerings of cash. It is an understatement to note that the cash has not had the desired effect of shifting the loyalty of francophone Quebecers toward the federalist cause.

NOTES

Portions of this chapter will appear in a forthcoming book on social policy, to be published by the C.D. Howe Institute.

1. United States, *Canadian Health Insurance: Lessons for the United States*, GAO/HRD-9190 (Washington, DC: General Accounting Office, 1991).
2. The ratio of insurance overhead costs comes from a 1991 study (United States, *Canadian Health Insurance*, p. 29). The OECD is the source for statistics on health-care costs relative to GDP, cited in Canada, "Striking a Balance: Working Group Synthesis Report," in *Canada Health Action: Building on a Legacy* vol. II (Ottawa: Canada Communication Group, 1997), p.12. The infant mortality and life expectancy statistics are from the World Bank, *The State in a Changing World*, World Development Report 1997 (New York: Oxford University Press, 1997), p. 225.
3. Many feel uncomfortable about government discriminating, in any way, on behalf of some group's values and against those of others. It is, however, in the nature of living together that some such discrimination takes place. The appropriate question is not whether to advance collective values, but to what extent and by what means. In a democracy, the majority can legitimately "impose" on others provided they obtain the sanction of an elected legislature — and provided the courts, as guarantors of fundamental civil liberties, do not object. When the Saskatchewan government first introduced mandatory health insurance, this

social program was — to understate matters — controversial. The majority of the province's doctors declared a strike and withheld services. The doctors did not oppose government subsidy of health insurance for the poor and, at the time, any efficiency savings from a "single-payer" system had yet to be demonstrated. The doctors' core complaint was that government should not impose its "socialist" values on those who preferred alternate insurance arrangements, either as health-care providers or as patients. The government insisted that, in this case, imposing a widely shared value was legitimate.

4. Liberal Party of Canada, *Creating Opportunity: The Liberal Plan for Canada* (Ottawa: Liberal Party of Canada, 1993), p. 17.
5. *Ibid.*, p. 20.
6. Canada, *Government Revenues in Canada. Federal Spending. Canada's Economic Challenges*, White Papers (Ottawa: Department of Finance, 1994).
7. Canada, Department of Finance, *The Budget Plan* (Ottawa: Department of Finance, 1994).
8. Canada, Department of Finance *Improving Social Security in Canada: A Discussion Paper*, Green Paper (Ottawa: Minister of Supply and Services, 1994).
9. Canada, Department of Finance, *Creating a Healthy Fiscal Climate* (Ottawa: Minister of Supply and Services, 1994); and *A New Framework for Economic Policy*, Purple Paper (Ottawa: Department of Finance, 1994).
10. I define social spending to include programs that are transparently redistributive — either to poor individuals or poor provinces — or correct market "failures" in a manner that redistributes. Deciding what programs to include and exclude entails some ambiguous choices. For example, the majority of program spending at the provincial level is for health, education, and welfare programs. Ottawa, in turn, provides equalization payments to "have not" provinces to assure that all can provide reasonably comparable social services at reasonably comparable provincial tax rates. However, not all provincial spending is for social programs and, accordingly, not all equalization should be considered social spending. In this simple exercise I have included equalization. Counted as social spending are \$41.5 billion in transfers to persons (elderly benefits, social insurance payments such as UI, veterans' allowances, aid to Aborigines); \$27.2 billion in transfers to other governments; \$1.6 billion in aid to farmers and fishers; \$2.6 billion in international assistance; and \$2.1 billion in housing assistance via CMHC. The sum of these items is \$75 billion, 63 percent of estimated total program spending of \$118.3 billion for fiscal 1994-95. Canada, *Creating a Healthy Fiscal Climate*, p. 36.
11. Canada, *A New Framework for Economic Policy*, p. 73.
12. *Ibid.*, p. 53.
13. Canada, Department of Finance, *Budget Plan* (Ottawa: Department of Finance, 1995).
14. Canada, Department of Finance, *The Budget 1993* (Ottawa: Department of Finance, 1993).

15. Canada, Department of Finance, *Budget Plan* (Ottawa: Department of Finance, 1997).
16. *Ibid.*, p. 44.
17. *Ibid.*
18. Thomas Kierans et al., *The Courage to Act: Fixing Canada's Budget and Social Policy Deficits*, Commentary no. 64 (Toronto: C.D. Howe Institute, 1994).
19. The 1997 budget (*Budget Plan*, p. 44) projects a deficit, net of the contingency reserve of \$6 billion for 1998-99. Given the Finance Department's overestimate of the federal deficit in recent budgets, this may turn into a modest surplus.
20. Quoted in Peter Russell (ed.), *Leading Constitutional Decisions*, 3d ed. (Ottawa: Carleton University Press, 1982), p. 130.
21. The most recent major example of liberal-inspired social policy reform is the abortive attempt, during President Clinton's first term, to introduce a system of universal health-care insurance. The proposal required Washington bureaucrats to set basic program parameters, to make complex administrative decisions, and to use extensive conditional grants to states. Unlike medicare in Canada, a system in which the provinces are independent "entrepreneurs" owning their respective plans, the Clinton proposal envisioned state governments as constrained "franchise operators." With justification, conservatives derided the proposal as a Rube Goldberg invention, and rhetorically asked: Could Washington bureaucrats specify the organizational structure for one-seventh of the US economy (that portion devoted to health care)? Would it not be a US equivalent of failed Soviet central planning? See A. Hacker, "The Medicine in our Future," *New York Review of Books* XLIV, 10 (1997) for a survey of why Clinton's health reform failed.
22. This discussion of the introduction of medicare to Saskatchewan is not footnoted. The best one-volume historical treatment is to be found in R. Badgley and S. Wolfe, *Doctors' Strike: Medical Care and Conflict in Saskatchewan* (Toronto: Macmillan, 1967).
23. In the 1990s, Canadians are wont to cite universal medicare as one of the criteria by which they distinguish themselves from Americans. In 1962 that was far from true. A footnote to this story is that Douglas resigned as premier to assume leadership of the New Democratic Party. His bid for election to Parliament from Regina in the 1962 election became another referendum on medicare, held this time at the height of the controversy over introduction of the program. Douglas lost, and was obliged to enter Parliament via a by-election in a British Columbia riding.
24. A simple regression using two variables explains most of the increase in the normalized Ontario caseload between 1983 and 1995. The two variables are, first, the unemployment rate and, second, the ratio of welfare benefits relative to a reference level of low-wage earnings. Increases in unemployment and a decline in the reference earnings level each explain a portion of the increase in caseload. The increase in welfare benefits are by far the most important component of the explained increase. A similar regression in the case of British

Columbia explains most of that Province's 30 percent normalized caseload increase between 1991 and 1995. The BC regression used the above two variables plus a third: a dummy variable to capture the effect of relaxation of the administrative culture determining access to social assistance upon election to the NDP. An increase in unemployment explains a small portion of the BC increase. The increase in low-wage reference earnings balanced the increase in welfare benefits and generated no net effect. The relaxation of administrative culture is overwhelmingly the most important among these variables. Regression results are available from the author.

25. British Columbia, *BC Benefits : Renewing Our Social Safety Net* (Victoria: Office of the Premier, 1995), p. 6.
26. Quoted in Edward Greenspon, "B.C. Fails to Sway Ottawa on Welfare," *The Globe and Mail* (Toronto), 8 December 1995.
27. Alberta introduced its welfare reforms in 1993. According to unpublished British Columbia government data, those who arrived in the province within the preceeding 12 months comprised 7.5 percent of the provincial welfare caseload in July 1992, and 8.1 percent in July 1994. The proportion of Alberta-origin welfare applicants among all out-of-province applicants has been roughly three-tenths since the province began collecting these data in 1993. (Data on province of origin do not extend back to 1992, before the Alberta reforms.) Introduction of the three-month residency requirement reduced out-of-province welfare applicants by more than half in 1996 relative to 1995, but had no effect on the proportion originating in Alberta.
28. British Columbia, *BC Budget '94* (Victoria: Ministry of Finance and Corporate Relations, 1994), p. 87; and *Budget '97 Reports* (Victoria: Ministry of Finance and Corporate Relations, 1997), pp. 80-81.
29. Harvey Lazar, "The Federal Role in a New Social Union: Ottawa at a Crossroads," in this volume.
30. Thomas Courchene, "ACCESS: A Convention on the Canadian Economic Systems" (Toronto: Ministry of Intergovernmental Affairs, 1996), pp. 9-10.
31. *Ibid.*, Table 2.
32. Daniel Schwanen, *Drawing on Our Inner Strength: Canada's Economic Citizenship in an Era of Evolving Federalism*, The Canadian Union Papers, Commentary no. 82 (Toronto: C.D. Howe Institute, 1996).
33. Courchene, "ACCESS," p. 22.
34. Discussion of this document is based on the text, plus discussions with several officials responsible for its drafting.
35. Ministerial Council on Social Policy Reform and Renewal, *Report to the Premiers* (Ottawa, 1995).
36. See, in particular, the world development reports for 1994 and 1997, World Bank, *Infrastructure for Development*, World Development Report 1994 (New York: Oxford University Press, 1994); and *The State in a Changing World*.
37. World Bank, *Infrastructure for Development*, p. 73.

38. Some provinces — Saskatchewan is the one with which I am most familiar — are trying to integrate labour training and social assistance much more closely.
39. Canada, *Budget Plan* (1997), p. 106.
40. By restraining from explicit answers to the questions in this paragraph, I do not want to leave the impression that I am neutral. I believe the provinces should render access to social assistance less automatic for able-bodied applicants. My preferred set of policies would integrate social assistance and training more closely, evaluate programs more rigorously, and introduce major employment supplements to low-income families with children.
41. Figure 1 ignores the fact that Ottawa delivers some social programs via tax expenditures (e.g., child benefits).
42. While any particular measure of the wage premium is subject to controversy, the public sector wage premium over comparable private sector workers was probably in the range of 10-20 percent by the early 1990s. This premium is concentrated among low-paid workers; at the upper managerial levels, public sector compensation is often below comparable private sector levels. See D. Brown, "No Sense of Direction," in *Paying Our Way: The Welfare State in Hard Times*, ed. J. Richards and W. Watson (Toronto: C.D. Howe Institute), for a survey of the evidence on this subject.
43. Ontario, "The Distribution of Federal Spending and Revenue by Province: Implications for Ontario and Other Provinces," Report prepared by Informetrica, Ltd. (Toronto: Ministry of Intergovernmental Affairs, 1993), executive summary, p. 3.

The Federal Role in a New Social Union: Ottawa at a Crossroads

Harvey Lazar

Ce chapitre discute de l'approche du gouvernement fédéral aux relations provinciales à l'égard d'une union sociale, depuis l'élection des Libéraux sous le mandat de Jean Chrétien en 1993. Il fournit une typologie des régimes fédéral-provinciaux en se basant sur deux séries de caractéristiques: jusqu'à quel point elles impliquent l'interdépendance ou l'interdépendance entre chaque paliers de gouvernement et jusqu'à quel point les relations entre les gouvernements sont hiérarchiques ou non-hiérarchiques. Définissant le fédéralisme-collaborationniste comme une relation basée sur l'interdépendance ou la non-hiérarchie entre gouvernements, le chapitre analyse les développements dans sept secteurs de politique sociale et suggère que Ottawa est devenu plus collaborateur ces dernières années. Aussi, le chapitre suggère que malgré les influences qui ont incité le gouvernement fédéral d'entreprendre cette ligne de conduite, elles vont peut-être être de longue durée. En particulier, la situation fiscale est en train de changer. Si le progrès est d'avantage atteint par le biais d'une approche collaborationniste, pour les quelques années à venir, alors cette façon de gérer les questions sociales à l'intérieur de la fédération pourrait couler les racines culturelles et le fédéralisme-collaborationniste pourrait devenir le nouveau status quo dans la capitale nationale. Mais, le gouvernement fédéral n'est pas encore là, et les prochaines quelques années, durant lesquelles Ottawa va probablement agir avec prudence vis-à-vis la fiscalité, vont être cruciales pour déterminer s'il va un jour être parfaitement confortable avec ce modèle de fédéralisme.

INTRODUCTION

The federal government is nearing a crossroads in its relations with the provinces in respect of the social union. For almost three years now, Ottawa has been inching toward a more collaborative approach to the provinces than had been its practice in previous decades. But whether the Liberal government in its second term will continue in this direction is not yet clear.

The uncertainty surrounding this question is not surprising. The Canadian polity is highly diverse, reflecting a broad range of regional, linguistic, ethnic, socio-economic and ideological interests and perspectives. Any political party that seeks seriously to form the national government has to include within its ranks much of that diversity. The result is that the federal government itself inevitably has to reconcile a wide range of opinion on many issues; and the federal role in the social union is one of those issues where opinion does vary.

This chapter discusses three sets of issues. The first has to do with the shift toward enhanced collaboration. In this regard, the chapter poses two related questions: What influences have prompted the federal government to pursue such a policy and are these influences likely to be long-lasting?

The second issue examined is the extent of the federal movement down the road of collaboration. To do this, the chapter defines collaboration as well as a number of other types of intergovernmental regimes, and offers a framework for mapping the regime changes that have occurred. It then uses that framework to judge the distance that Ottawa has moved in relation to a number of major social policy files since the election of the first Chrétien government.

Third, questions are raised about whether the new directions in federal policy are desirable. The chapter assesses the more collaborative approach to the social union in relation both to federal unilateralism, via the spending power, that has characterized many of the events of recent decades and the alternative of "disentanglement" or what is generally called classical federalism. The three criteria used in making this assessment are similar to those used by Keith Banting in his contribution to this volume. They are the effects on policy goals and outcomes, democratic values, and federalism principles.

Foreshadowing what is to follow, the chapter concludes that modest but significant shifts toward collaboration have occurred in the federal approach to the social union. It also concludes that where the shift toward collaboration replaces a regime that has previously been marked by federal unilateralism, there are likely to be more gains than losses in terms of the three criteria. As to the gains and losses associated with shifts between collaborative and disentangled models, they depend on the specific circumstances associated with the sector or program in question. When policy goals are being achieved with disentangled arrangements, there will be little reason to change; where policy goals are not being achieved, then there is a need for a case-by-case analysis of whether enough can be gained on the policy front through collaboration that will outweigh any losses in relation to the other criteria.

Two further points need to be noted by way of introduction. The first is how the term "social union" is defined here. In this context, the social union is the idea that Canadians have similar social rights and obligations of citizenship, wherever in Canada they may live; and the instruments of the social union are the constitutional provisions, federal government mechanisms (such

as the ability to tax, spend, and regulate) and intergovernmental arrangements (such as federal-provincial and interprovincial agreements, including intergovernmental transfers) that breathe life into this idea. As Banting notes in this volume, the extent of Canada's social union in the post-World War II years reflected a balance between the pan-Canadian notion of the welfare state and a series of distinctive provincial welfare states.¹

The other is to make explicit what this chapter is *not* about. In the main, it is not about provincial strategies relative to Ottawa or the factors that shape them. The purpose here is more confined: understanding and assessing trends in the federal government's relationship to the provinces in respect of the social union.

WHAT INFLUENCES HAVE LED THE FEDERAL GOVERNMENT TO BECOME MORE COLLABORATIVE? WILL THOSE INFLUENCES BE LONG-LASTING?

Five factors appear to lie behind the changes in the federal approach to the social union. One is the federal fiscal situation. When the first Chrétien government was elected, it inherited a string of more than 20 consecutive annual fiscal deficits and the accumulated debt was approaching 70 percent of Gross Domestic Product (GDP) and on a strong upward trend. There were concerns that Ottawa would soon be "hitting the wall" in financial markets. This is a point also emphasized by Richards.²

The result was strong federal action to restore its finances. As a part of the overall fiscal restraint program, federal transfers to the provinces were reduced very substantially in relation to previously planned levels, particularly through the introduction of the Canada Health and Social Transfer (CHST) in the 1995 federal budget. One consequence was that the political and moral authority of the federal government to determine unilaterally the terms and conditions under which provinces would receive these transfers was correspondingly reduced.³

A second factor that contributed to the change of attitude in Ottawa was the increased support for Quebec separation. In the aftermath of the 1995 referendum, all planned federal actions were reevaluated to give a greater weight to their possible effects on Quebec opinion including policies being advanced through the use of the spending power.

Third, the ongoing and determined demands from the westernmost provinces for a more decentralized federation were also being felt in the national capital. The prospects of ongoing squabbling with the governments of Alberta and British Columbia were a particular problem for a Chrétien government that was determined to show that the federation could reform and renew itself without constitutional amendment. In this context, a failure to improve relations

with Alberta and British Columbia would, at one and the same time, fuel on-going western alienation and provide ammunition to both the Parti Québécois and the Bloc Québécois regarding the alleged unworkability of the federal system.

A fourth influence was the high level of representation of two regionally-based parties, the Bloc Québécois and the Reform Party, in the Commons. The structure of the House meant that there were no significant pressures in the opposition benches for centralizing power whereas there was extensive pressure in the opposite direction. For Ottawa, making the federation work by reducing intergovernmental tension was one way of taking the sting out of opposition criticisms.

Finally, the federal government's approach to public management was undergoing change at the same time that these other influences were rising in importance. For some time the federal Public Service had been increasingly interested in the "steering," rather than "rowing," which was becoming part of the new public management literature and, with it, the variety of alternative approaches to program delivery — privatization, decentralization, arm's length agencies, etc. — with the objective of enhanced client service at a lower cost. Especially important in this context was a growing interest in "partnerships," a concept that was highly compatible with a more collaborative approach to federal-provincial relations.

This last factor might not have counted for much had the provinces been uninterested in partnership. Indeed, in the face of the CHST cuts, it would not have been surprising if the provinces had undertaken an aggressive political campaign against Ottawa. In fact, however, their response, in the form of the 21 December 1995 Report of the Ministerial Council on Social Policy Reform and Renewal was both moderate and thoughtful. That report recognized the national dimension in social programming and, in the circumstances of the very unpleasant fiscal medicine that provinces were being required to swallow, it offered a more than reasonable basis for further federal-provincial dialogue.

Given the very considerable weight associated with each of these influences, it is easy to understand what has driven the federal government to approach its relationship to the provinces in the social union in a more conciliatory fashion. On one side, the new environment reduced Ottawa's political room to manoeuvre as the political price of unilateralism rose. On the other, the government had to become more results-oriented and, in some situations, this could be best achieved through partnership arrangements with provinces; and, for their part, the provinces had left the door open to such a possibility. Thus, the Liberal Party's 1997 election platform proclaimed:

Our philosophy of federalism is that the best way for the various orders of government to meet the needs of Canadians is to work together. We know that is

what Canadians want. We will continue to improve the capacity of governments to collaborate.⁴

In turn, this raises a key question: How long will these influences last? And if not all of them are not long-lasting, will federal policy change as and when the pressures on Ottawa dissipate? Some of these influences do indeed seem likely to endure. The prospects of a large secular decline in support for separatism in Quebec are not, at this juncture, strong. The pressures from the governments of Alberta and British Columbia for a more decentralized federation show no signs of abating. To the contrary, as Sid Noel notes elsewhere in this volume, these two provinces have been joined by the Government of Ontario in seeking a different kind of federation than that which has characterized the post-World War II era. The 1997 federal general election has, if anything, made the new Parliament even more regionalized than the one that was elected in 1993. Finally, the new public management theory is receiving widespread attention across much of the industrialized world, suggesting long-term systemic change in approaches to public management, including in relation to social policy.⁵ Accordingly, important pressures will remain on Ottawa not to revert to federal unilateralism through conditional shared-cost programs in areas of provincial jurisdiction in the absence of a wide measure of provincial support.

But the 1997 federal general election also illustrates that the fiscal pressure that has constrained Ottawa is easing rapidly. The Liberals and New Democrats both talked about new shared-cost health programs. The Liberal Party undertook to eliminate more than a billion dollars in its previously announced cutbacks in cash transfers to the provinces under the CHST. By all accounts, the federal government's fiscal room to manoeuvre is likely to improve rapidly in the coming few years. Moreover, notwithstanding the above reference to the Liberal Party election commitment to federal-provincial collaboration, that same document indicated also that, in relation to the *Canada Health Act*, the "federal government must retain its authority ... to enforce these principles," suggesting a less collaborative approach in at least that one politically and socially important sector.⁶

What then can be concluded from this analysis? The first is that most of the influences that have driven the federal government toward greater collaboration appear destined to remain strong for at least the next few years. If, during that time, further substantial progress is made in developing and implementing a more collaborative approach, then a new culture may begin to develop in Ottawa under which federal politicians and public servants become more accustomed to meeting their objectives through a partnership relationship with the provinces. As this approach sinks roots in Ottawa, it will become the new status quo. Later, if and when the influences currently driving Ottawa toward collaboration ease, inertia will work in favour of the new collaboration.

If, on the other hand, there is little progress in the next couple of years on the social union front, or if it is confined to only two or three files, then the political and bureaucratic culture is more likely to change at the margins only. The status quo will be unchanged in its foundations. Hence, the suggestion at the outset of this chapter that Ottawa is at a crucial crossroads in relations with the provinces.

The analysis in this section indicates that Ottawa has been under a range of pressures that have helped steer it toward a more collaborative set of relationships with the provinces. The next section documents the nature and extent of movement.

ASSESSING CHANGES IN FEDERAL POLICY

Borrowing from Biggs, the starting point for the analysis is the idea that there is a continuum of intergovernmental regimes on which federal policy can be located.⁷ At one end of the continuum there is a federal approach which relies heavily on the use of the spending power in areas of provincial jurisdiction. At this point, federal transfers to the provinces require provincial acceptance of federal conditions. Although there generally is federal-provincial consultation prior to the establishment of these conditions, possibly extensive consultation, the formal decisions regarding conditions are made by the federal government alone and it is not bound to take account of provincial viewpoints. Although this approach is what Banting calls "cooperative federalism" in his chapter, it is referred to here as "federal unilateralism."

Federal unilateralism is characterized by a high level of interdependence among governments. On the one side, the federal government can only achieve its objectives if the provinces accept Ottawa's conditions and in that sense the federal government has to rely on the provinces. As for the provinces, each is dependent on the federal government for its appropriate share of federal revenue and, to that extent, may have to adjust its spending priorities or its preferred way of doing things to avoid losing financial transfers from Ottawa. This latter consideration points to the second characteristic of federal unilateralism: it implies that the federal government is the more senior government and that, therefore, the central government can effectively impose rules on the provinces, within their jurisdiction, without their approval.

The other end of the continuum is referred to here as disentanglement or "classical federalism" and is suggestive of the classical "watertight compartments." A precondition to successful disentanglement is a clarification of the roles and responsibilities of each level of government in relation to a particular grouping of citizens or a particular subject area. Whereas, under federal unilateralism, there is a high degree of interdependence between the central and the regional governments, under the disentangled model both levels of

government have a substantial measure of the *de jure* and *de facto* independence in the exercise of their constitutional powers (i.e., we have mutual unilateralism). A second distinction between these models is that, under disentanglement, neither jurisdiction is *de facto* subordinate to the other, as distinct from the hierarchical relationship implied in federal unilateralism.

In the middle is "collaborative federalism." With collaboration, the interdependence among governments remains but, as with the disentanglement model, there is no hierarchy among governments. Below we identify two kinds of fully collaborative models.

With rules-based collaboration, the intergovernmental arrangements reflect the fact that the constitution authorizes both orders of government to act in a particular subject area. (One example is the Canada Pension Plan, which is based on a constitutional provision, section 94A, that authorizes both federal and provincial legislation but with provincial paramountcy.) Alternatively, the constitution may divide authority between orders of government in a single subject area. (For instance, section 91 authorizes the federal government to legislate criminal law and section 92 authorizes the provinces to administer it.)

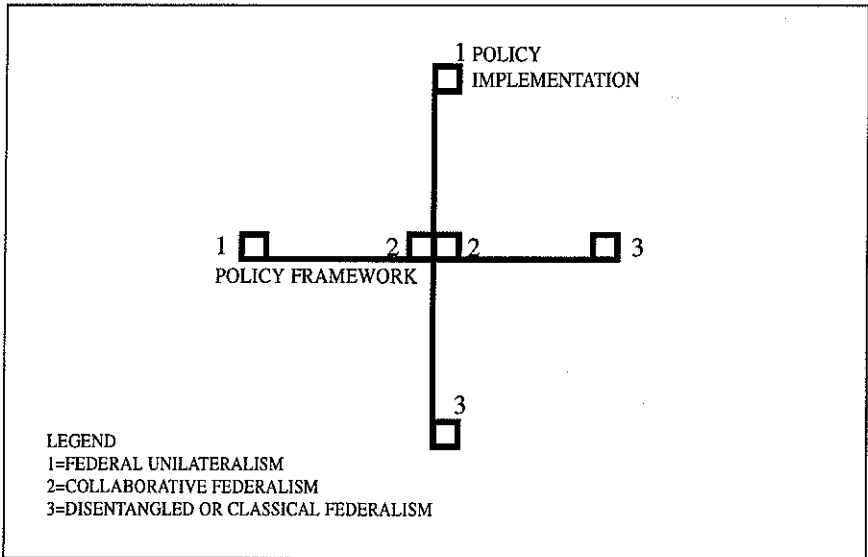
Consensual federalism is similar to rules-based collaboration but lacks its constitutional imprimatur. It includes political and administrative agreements among governments on how they intend jointly to deal with matters of public policy or public administration. Such agreements imply freely given political consent as there is no constitutional requirement to act in this way; and to qualify as consensual, one order of government cannot be effectively "forced" to agree to the dictates of the other by virtue of some form of financial or other dependence on the other order.

While by definition, consensual federalism and rules-based collaboration are different in significant respects, for our purposes they are similar in that they require a highly interactive process among governments and entail formal agreement in achieving results. For this reason, these are located at the same place in our diagrams below and are referred to hereafter by the term "collaborative federalism."

These models of federalism are relevant to the way in which broad *policy frameworks* are developed and how such policies are *implemented*. In this context policy implementation is being used in a very broad sense to include a number of different activities, such as program design, interpretation, monitoring and enforcement. Figure 1 below deals with both policy frameworks and policy implementation, thus enabling us to map changes in the federal approach to relations with the provinces in respect of the social union.

One qualification must be added here. It will seldom be possible to capture all aspects of the federal strategy by pinpointing a single location in Figure 1. More often, there will be elements in federal behaviour, in relation to a single subject area (e.g., health care) or a single client group (e.g., persons with

Figure 1: A Framework for Mapping Changes in Federal Strategy in Relation to the Provinces



disabilities), that fit on different parts of the diagram. For purposes of this chapter, the focus will be on the larger issues only (e.g., *Canada Health Act*) to avoid adding unnecessary complexity to this analysis.

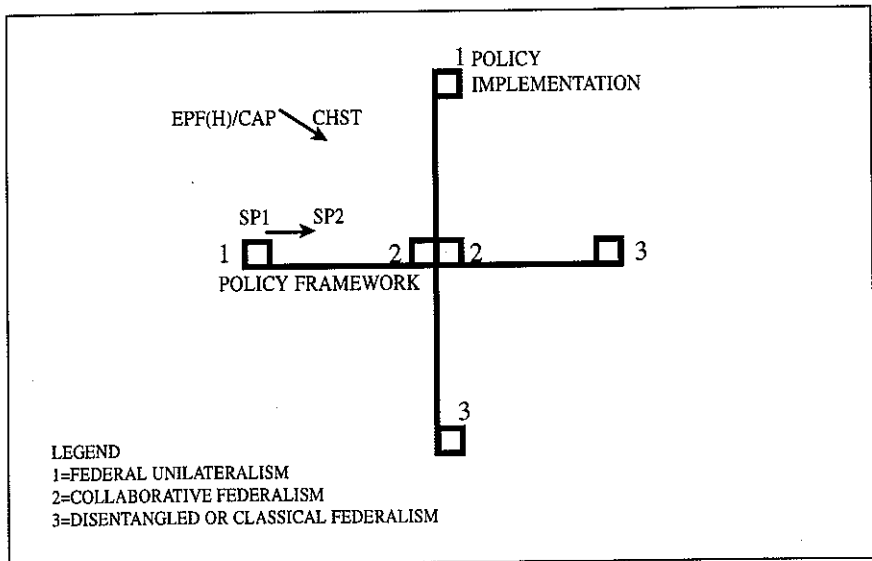
The above framework can be used in relation to both macrosocial and sectoral policy. Macrosocial policies are considered first. Under macrosocial policy are included those policies that condition a broad range of interventions affecting different groups of citizens (e.g., both children and seniors) and different subject areas (e.g., both labour markets and health care) — sometimes referred to as “horizontal” or cross-cutting policies. Here two examples are pertinent. The first is the provision in the Canada Health and Social Transfer (CHST) to the effect that additional “principles and objectives” (i.e., conditions) surrounding federal fiscal transfers to the provinces under that legislation would be implemented only if “mutual consent” among the provinces and the federal government is achieved. Prior to that enactment, the federal government had reserved to itself alone the power to determine what conditions were to be attached to transfers. For this reason, the CHST provisions entail some shift from the unilateral federal approach in terms of policy frameworks to a less unilateral approach. The elimination of all but one of the conditions associated with the Canada Assistance Plan (CAP) is also suggestive of less federal unilateralism (recognizing that not all of the CAP conditions were onerous).

But when the CHST was enacted, it was the federal government alone that decided to preserve the principles of the *Canada Health Act* (CHA), and the restrictions on the residency requirement for social assistance recipients, as conditions of that transfer. In part for that reason, and in part because the federal government has the exclusive effective authority to amend the provisions to the Canada Health and Social Transfer (including the "mutual consent" provision), although less unilateral than the federal programs it replaced, the intergovernmental regime implied in the CHST legislation is still closer to a federal unilateral than a collaborative model.

To date there has been virtually no change in the level of federal unilateralism associated with the implementation of the CHST. The federal government alone has the legal authority to interpret the five principles of the CHA and to decide whether penalties should be applied. This was illustrated most recently during the federal election campaign when Health Minister Dingwall threatened action against Alberta regarding the planned opening of a private health facility in Calgary.⁸ The same is true with respect to the interpretation of the no-residency requirements for social assistance.⁹

In Figure 2 below, the location of EPF (H)/CAP marks our assessment of the degree of unilateralism associated with major federal transfers to the provinces for health and social assistance and services prior to the 1995 Martin

Figure 2: Changes in Federal Strategy Relating to Macrosocial Policy, 1993-1997



budget. The positioning of CHST is our interpretation of the extent to which the federal government has moved in the direction of collaboration. In terms of policy framework (the horizontal axis), it is suggested that there has been a modest shift in the collaborative direction. But there is only slight evidence of enhanced collaboration regarding the implementation of the CHST (vertical axis).

The second macrosocial policy considered is the commitment in the 1996 federal Speech from the Throne not to use the spending power to create new cost-shared programs in areas of exclusive provincial jurisdiction without the consent of a majority of the provinces, and to compensate any non-participation if it undertakes equivalent or comparable initiatives. Since that announcement, no new federal initiatives have been implemented through the spending power. Further, although the Liberal Party indicated its interest in developing a new shared-cost program with the provinces for medically necessary prescription drugs in its 1997 election platform, the platform also suggested that these actions would not be taken without a significant measure of provincial support.

The line SP1-SP2 in Figure 2 above is our assessment of the extent of the federal government's shift. Since the federal commitment is not embedded constitutionally, or even statutorily binding, the shift is only halfway to the collaborative model.

SECTORAL POLICIES

In this section we consider developments in five sectors since the announcement of the CHST. In three of the five, federal strategy entails increased collaboration, albeit to varying degrees (labour markets, child benefits and disability). In a fourth, child care, the end result of a number of zigs and zags in federal policy entails an approach that is somewhere between disentangled and collaborative. In the case of the CHA, however, there have been no major shifts from a regime that is still largely unilateral. Each of these five files is considered further below

LABOUR MARKETS

During the life of the last Parliament, a new *Employment Insurance Act* (EI) was passed that involved a major restructuring of the provisions of the old *Unemployment Insurance Act*. The scope and depth of these changes qualifies as framework policy. Part I of the new legislation sets out the provisions relating to benefit entitlement. Part II deals with the role of active labour market programs to help the unemployed reintegrate into paid employment. Part II contemplates the possibility that provincial governments may be delegated the role of designing and administering programs that come within its scope.

Unemployment insurance is a federal responsibility under the constitutional division of powers between the federal government and provinces. It is unclear, however, whether active labour market measures are federal or provincial jurisdiction. In any case, a powerful argument can be made that active labour market measures are closely connected to heads of power that fit within both federal and provincial jurisdictions.

The processes leading to the enactment of the *Employment Insurance Act* involved no multilateral consultation between federal and provincial governments. While there was some bilateral consultation between federal and provincial governments, this was largely ad hoc. The governments of the Atlantic provinces were consulted most and made the most determined effort to influence the federal decisionmaking process; and they were major players in an aggressive Atlantic lobby that successfully persuaded the federal government to modify and soften some proposed benefit reductions that would have most affected Atlantic Canada. As to the inclusion of active labour market measures under Part II, with the provision for delegation to the provinces, this was exclusively a federal decision but heavily influenced by Ottawa's recognition that it might be "forced" by pressures from some provinces, especially Quebec, to retreat from labour market training and, perhaps, other active labour market measures.

Given federal jurisdiction for unemployment insurance, it would have been unreasonable to expect provincial governments to be an equal partner in decisionmaking in respect of unemployment insurance reform. But to the extent that federal decisions would have consequences for provincial expenditures on social assistance, more systematic consultation might have been appropriate.¹⁰

The other key development in the labour market area during the first Chrétien administration was the signing of bilateral labour market agreements between the federal government and eight provinces under which, to varying degrees, provinces have decided to assume greater responsibility for the design of programs under Part II of the EI Act and to deliver those programs to eligible persons (current recipients of benefits under Part I of the EI Act and others who are no longer receiving such benefits but who had such entitlements in the recent past).

Four of the eight agreements — with Alberta, Manitoba, New Brunswick, and Quebec (agreement-in-principle) — involve devolution from the federal government to the provinces. The other arrangements — with British Columbia, Newfoundland, Nova Scotia, and Prince Edward Island — entail co-management. To finance the active programs that the provinces will design and deliver, the four devolution agreements provide that the federal government will transfer an agreed sum of money annually to the provinces for five years. The four provinces have also been delegated the authority to deliver some of the services of the National Employment Service, such as

"service needs determination," employment counselling, and labour exchange services. As well, there is some expectation that there will eventually be single window delivery of federal and provincial programs. Around 1,600 federal officials are to be transferred to provincial employment. As for the co-management schemes, they entail federal and provincial governments working in concert in the design and implementation of the active programs, with continued federal delivery.

Overall, this amounts to a large transfer of responsibility from the federal government to the provinces. To the extent that there may have been significant duplication of federal and provincial activity, which was never demonstrated and almost certainly did not exist, it will be reduced. Nonetheless, there is the opportunity for improved client service in the sense that the agreements provide, to take two examples, for combined Canada-Alberta Service Centres and Canada-New Brunswick Human Resource Service Centres where clients can obtain both federal (including Employment Insurance payments) and provincial services (including the services and reemployment measures noted above) at co-located facilities. There are also arrangements for information and data-sharing that may enhance implementation of the programs operated by the two orders of government.¹¹

The agreements provide that the provinces will not require minimum periods of residency in their jurisdiction on the part of an individual as a condition of access to provincial benefits under the agreements. Thus, a potential barrier to mobility is proscribed by the agreements. The federal government has also explicitly retained its responsibility for a national system of labour market information and exchange to support interprovincial mobility of labour, for fostering interprovincial sectoral development and for responding to national economic crises.

There is another important signal that the federal government has not removed itself entirely from the promotion of reemployment measures and the strengthening of the national labour market, that is, the federal-provincial agreements on the "primary indicators" for evaluating the results of the program expenditures financed through the Employment Insurance Account that the provincial governments will be delivering.¹²

For those who see federal-provincial relationship as a zero sum competition for power, these agreements represent a victory for the decentralizers at the expense of the supporters of the status quo; and they were hugely influenced by federal concerns to defuse a Quebec-sensitive file and to a lesser extent to improve relations with a number of other provinces.

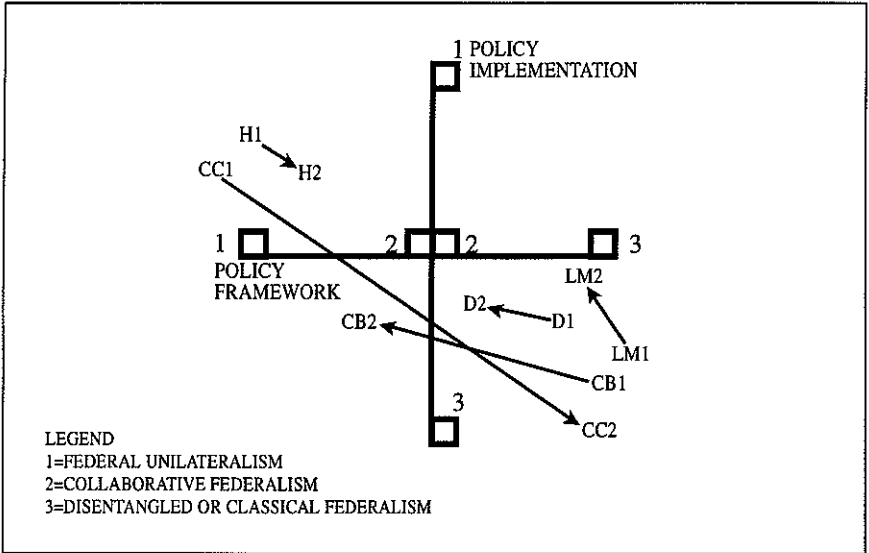
Although these influences helped to shape federal policy, the impact can be viewed through another lens. In this second perspective, a new partnership is emerging that better reflects the appropriate role of provincial governments in respect of local and regional labour markets and of the federal government in relation to the national and international labour market. This can be a positive

development from the viewpoint of clients' interests. First, since individual job seekers, and employers seeking workers, may wish to pursue their search activities on all fronts, from local to international, at the same time, one way for both levels of government to carry out their responsibilities in a client-friendly fashion is through a partnership arrangement along the lines of those that have been negotiated. The agreements also create the prospect that an unemployed person will be able to deal with both orders of government through a single office, and possibly even a single point of contact, even though for purposes of EI Part I they are federal clients and for purposes of EI Part II or social assistance they are provincial clients. In this perspective, the two orders of government have re-ordered their affairs to create a more "client-centred federalism."

Returning to our framework below (Figure 3), LM1 is an assessment of the federal-provincial relationship on labour market matters in the years immediately prior to the EI legislation. There had been little in the way of federal consultation with provinces on earlier unemployment insurance reforms, virtually no provincial-federal consultation on social assistance reforms related to the labour market and modest cooperation on active labour market measures with Ottawa transferring money to the provinces on the basis of a series of bilateral agreements or informal extensions of expired agreements. The relationship surrounding active labour market measures alone can perhaps be characterized as lying somewhere between the federal unilateral and collaborative models, perhaps a bit nearer to the collaborative. But in other and larger respects, on the basis of a number of citizens affected or dollars spent, the labour market, as reflected in the lack of intergovernmental consultation on reforms to unemployment insurance and social assistance, was more disentangled. The Forum of Labour Market Ministers was not meeting regularly and, when it did meet, the big issues were seldom on the agenda. That is, on the larger aspects of the policy framework, the two orders of government were acting independently of one another.

At the implementation level, prior to the introduction of EI legislation, useful federal-provincial cooperation had been started to lower barriers to internal mobility (under the framework of the Agreement on Internal Trade), there had been a long history of collaboration in respect of apprenticeship (the Red Seal program), and a number of interesting federal-provincial co-location experiments were being tried. Importantly, there was a working relationship on such issues as course purchase, for example, Ottawa buying training courses from the provinces for UI recipients. At the same time, the principal elements of federal unemployment insurance and provincial social assistance were disentangled. Thus, on issues of implementation, the model was perhaps halfway between collaborative and disentangled.

Figure 3: Changes in Federal Strategy Relating to Sectoral Policy, 1993-1997



Since the election of 1993, there has been no increase in collaboration at the policy framework level in relation to income support associated with employment insurance or the main features of social assistance and a modest increase only in relation to reemployment measures. Therefore, overall, we show relatively little movement on the horizontal axis over the last couple of years.¹³ But the eight recent bilateral agreements detailed above, which also allow for collaboration in implementing certain aspects of employment insurance, and the prospects for a single office delivery of federal and provincial benefits, as well as other examples noted above (including the reduction in barriers to mobility), suggest a substantial increase in collaboration at the implementation level.¹⁴ LM2 therefore shows a much more collaborative approach on the vertical axis. If all of the potential benefits of this enhanced collaboration at the implementation level are to be experienced, however, there will be need for further improvements and collaboration in policy frameworks in the years ahead.

CANADA HEALTH ACT

It was noted at the outset that there are ambiguities about the intentions of the federal government regarding the future of the social union associated with

the inevitable diversity of opinion that is normally contained within any federal Cabinet. This is reflected in the federal government's approach to CHA.¹⁵

Following the general election of 1993, the Chrétien government created a National Forum on Health. Provincial governments were leery of this federal initiative in an area of clear provincial jurisdiction and, for the most part, stayed well clear of that exercise. The advice Ottawa received from the National Forum on Health included a number of key points that are relevant in the context of this chapter. Declaring the health-care system to be "fundamentally sound," the forum's final report argued that the federal government should preserve and protect the current arrangements, including "public funding for medically necessary services..., the single payer model" support for the five principles of the *Canada Health Act* and, at the same time, strive for a strengthened federal-provincial-territorial partnership.¹⁶ The forum made clear that it believed that an essential element for achieving this end was the maintenance of stable and predictable flow of cash transfers to the provinces as a way of enforcing the Act. The intergovernmental partnership called for by the forum did not, however, extend to joint interpretation and enforcement of the five principles although it did suggest a "more open and transparent process."¹⁷

The CHA was originally enacted by Parliament in 1984, shortly before the federal election and without the explicit support of the provinces.¹⁸ Nonetheless, perhaps in part because the CHA enjoys widespread support among Canadians, provincial governments have endorsed it. Thus, the Conference of Provincial/Territorial Ministers of Health, in a January 1997 report entitled *A Renewed Vision for Canada's Health System*, stated: "All provinces and territories support the five principles of the Canada Health Act (universality, accessibility, comprehensiveness, portability, public administration) for insured hospital and medical services." Yet the 1996 Annual Premiers' Conference at Jasper also made clear that the provinces were seeking a new consensus with the federal government that would include "a vision document for Canada's evolving health system which would include goals and principles." The premiers also pressed for a clarification of roles and responsibilities between federal and provincial governments.

The Liberal Party's 1997 general election platform, although raising the possibility of new pharmacare and homecare programs, indicates that further extensions to the national health-care system, through the use of the spending power, will require a large measure of support from provincial governments. On the other hand, during the election campaign itself, and consistent with the above discussion, much of the Liberal rhetoric also suggested that Ottawa remains unswerving in its determination that the five principles of the CHA be maintained.¹⁹ Indeed, in commenting on the final report of the National Forum on Health, Prime Minister Chrétien had earlier declared: "Medicare is

a cherished legacy that we will never abandon as long as I am Prime Minister." The federal government also holds to the view that the preservation of this legacy requires that only one government can be legally accountable for the interpretation and enforcement of the CHA and that must be Ottawa. Polling data consistently indicate that a high proportion of Canadians want the principles of the CHA to be respected and these data no doubt serve to stiffen Ottawa's political backbone in maintaining its exclusive role, in a formal legal sense, in interpreting and enforcing these provisions. There may also be a federal concern that any opening up of these principles for debate, as provincial premiers have called for (even while supporting them), runs the risk of opening Pandora's box and that the outcome could be an "Americanization" of the system rather than a modernization.²⁰

At one level, it may be arguable that the federal unilateralism with regard to the five principles is unimportant since the provinces are on the record as endorsing them. Similarly, Ottawa recognizes that its unilateralism in cutting fiscal transfers to the provinces has been inappropriate, in terms of health-care policy and good intergovernmental relations, and it is seeking to provide greater stability in funding. While Ottawa's good intentions may be of small consolation to provincial administrations currently struggling to cope with reductions in transfers, there is, at least in principle, an awareness that such arbitrariness is wrong. For these reasons, it is suggested here that the policy framework is not entirely unilateral. But it is also much closer to unilateral than fully collaborative.

Perhaps more disturbing to provincial governments than the lack of explicit collaboration on the policy framework is that the federal government alone has the formal authority to interpret the CHA and to determine whether provincial health insurance plans conform with its provisions. Here it is important to observe that under the federal Progressive Conservative governments of Brian Mulroney, there was generally a *laissez-faire* attitude to CHA enforcement. In contrast, the Liberals were relatively quick to address violations when they took office in 1993, including the May 1994 penalties for extra billing by BC physicians.

This does not mean that Ottawa administers the CHA without consulting provinces. Rather, there is a history of the federal and provincial governments working together, including on controversial issues like unregulated private clinics and related facility fees, to reach a common understanding on the interpretation and application of the CHST provisions. Indeed, provinces have been among those "concerned that continued growth in the number of private clinics could lead to the development of a private system of health care in which people who can pay will get faster access."²¹

Notwithstanding this cooperation, provinces would prefer an arrangement under which the legal enforcement authority does not rest exclusively with

Ottawa and they call for a "joint administrative mechanism to interpret the Canada Health Act." To date, however, provinces have been unable to persuade the federal government to cede this formal authority.

Nonetheless, in a press release issued following the federal-provincial-territorial meeting of health ministers on 11 and 12 September 1997, it was announced that the ministers had agreed "to consider and develop a protocol for Federal, Provincial and Territorial governments to discuss issues of concern regarding interpretation of the Canada Health Act." Alan Rock added that "he would like to see a process that formalizes and makes more transparent the steps that should take place with provincial and territorial governments before the federal government makes decisions about violations of the Canada Health Act."²² Whether predictability and transparency in federal decision-making regarding interpretation and enforcement will be sufficient to satisfy provinces is doubtful. But it is encouraging that both orders of government have agreed to tackle this issue.

The placement of the short line H1-H2 in Figure 3 indicates two things. The first is that at the outset of the life of the first Chrétien government, the kind of federalism being practised in relation to the CHA entailed a significant measure of federal unilateralism, notwithstanding extensive consultation, especially in regard to implementation; and, second, that it changed little over the period.²³ At least for the time being, it appears that there is a fear that policy objectives of one-tier health care would be endangered by a more collaborative model for the CHA.

CHILD BENEFIT SYSTEM

At the sectoral level, perhaps the largest move toward the collaborative approach to the social union has been made in the area of child benefits. For many years, both levels of government delivered substantial programs aimed at supporting families with children. The federal government focused mainly on income support, both through the federal Child Tax Benefit and the cost-sharing of social assistance associated with the Canada Assistance Plan. Provinces helped such families both through their social assistance programs and various services, including child welfare services.

It was long recognized that the overlap, and weak coordination, between federal and provincial governments in the area of income support for families with children was unhelpful in meeting policy objectives related to the reduction of child poverty and the associated aim of improving work incentives for low-income families. For at least much of this period, federal policy was questionable since Ottawa typically exerted political pressure on the provinces to raise welfare rates for families with children whenever the federal government raised tax benefits for children. The result was an immediate improvement

in the income of those welfare families but, at the same time, no improvement in the incentive for individuals in such families to search for work or for working families with low labour market earnings to remain at work. Nor were these pressures appreciated by the provinces, since provincial law did not generally anticipate welfare rates being set indirectly by the federal government.

In the early years of the first Chrétien government, Ottawa was reluctant to put additional money into the reduction of child poverty despite a strong lobby that was critical of continuing high levels of child poverty and a growing body of evidence about the high long-term societal costs of such poverty. While federal reluctance to act in this way was, in the main, due to fiscal restraint, Ottawa also shied away from acting because it was open to provincial governments to reduce their social assistance payments, dollar for dollar, to offset the impact of any improvements Ottawa might make with the result effectively being no improvement in the income levels of poor families with children.

At the same time, the two orders of government had for awhile been signalling to one another their interest in a more collaborative approach. At the federal level, Lloyd Axworthy's social security reform process had alerted provinces to the federal interest by raising the integrated child benefit as a policy option and recognizing the issue of work incentives. Even prior to Axworthy's Green Paper, a number of provincial governments had made public their interest in a similar approach (e.g., Ontario and Saskatchewan).²⁴ Finally, at the June 1996 First Ministers' Meeting, there was an agreement to work together to achieve better integration of income support programs for children through a National Child Benefit System — a system that would replace needs-tested welfare benefits for children with income-tested benefits.

The essence of the agreement was that the federal government would provide a new Canada Child Tax Benefit, an enlarged and simplified child tax benefit, to strengthen the national foundation of income support to all low-income families with children. The initial federal commitment announced in the 1997 federal budget was to increase the more than \$5.1 billion being spent annually under the Child Tax Benefit, and a \$250 million increase that had been undertaken in the 1996 budget, into a \$6 billion commitment beginning in July 1998. Provinces would be free to reduce their social assistance payments on behalf of children by the amount of the increase in the federal child benefit and to reinvest the savings from their welfare budgets into complementary programs targeted at improving work incentives, benefits, and services for low-income families with children.²⁵

To fulfill the mandate of the first ministers, federal, provincial, and territorial ministers of social service have met on a number of occasions. Work has proceeded regarding ways of ensuring that increased federal income support would be reinvested, including the development of national reinvestment framework that would "flexibly guide" such reinvestments.²⁶ In September 1997, the ministers released a paper committing themselves to identify "performance

measures that will measure the National Child Benefit's success in achieving its objectives" and incorporating those outcomes into public reports to ensure public accountability.²⁷

Not all provinces waited for the intergovernmental negotiations to be completed prior to action. In 1996, for example, British Columbia replaced its existing welfare-based system of child benefits with a BC Family Bonus for "all low and modest income families — not just those on welfare."²⁸ Quebec, which has remained apart from the formal intergovernmental process, has also introduced a new integrated child allowance to cover the needs of children of low-income families and, in the process, also removed the benefits for children from its welfare programs.²⁹

Thus, the new intergovernmental arrangements for child benefits offer the prospects of significantly improved policy outcomes. They also entail a shift in intergovernmental regime — from one that was largely disentangled in terms of policy frameworks to one that is more collaborative. In this case, the collaboration has resulted in agreed policy objectives and a clarification of roles and responsibilities in relation to those objectives. Within that framework, provincial governments retain wide latitude to determine their reinvestment priorities and to design and deliver their own programs in relation to those priorities. At the implementation level, therefore, we have considerable disentanglement.³⁰

The line CB1-CB2 in Figure 3 reflects the shift from a somewhat disentangled system in relation to both policy framework and policy implementation — one that was falling short of agreed policy goals — toward a more collaborative policy framework. The overall result will be greater levels of income and other supports for families with children while, at the same time, improving incentives to work and facilitating welfare-to-work transitions. Moreover, it appears that this enhanced collaboration is only a first step. The provinces and Ottawa have also begun discussions regarding a wider National Children's Agenda — one that would involve provincial and federal health and justice ministries as well as departments concerned with social services and income support.

CHILD CARE

Child care is a provincial jurisdiction. In the period prior to the enactment of the CHST, the federal government influenced child-care policy principally through two instruments. It provided tax support to families that expended money on child care; and some provincial expenses on child care were eligible for federal cost-sharing under the provisions of the Canada Assistance Plan (CAP). With the termination of CAP, and its replacement by the CHST, the federal government ceased to share directly in child-care expenses. In this sense, the interdependence of the two levels of government in relation to child

care was reduced. But federal transfers under CHST were reduced sharply relative to previously planned levels under the combined CAP and Established Programs Financing and the arbitrariness of the action was suggestive of the old unilateralism. That is, there were contradictory messages for the provinces in relation to child care: federal action had components of both unilateralism and disentanglement.

There was less ambiguity, however, about the federal proposal to the provinces in December 1995 to create a new conditional shared-cost program for child care. Under that proposal, based on a 1993 Liberal *Red Book* commitment, the federal government would have cost-shared an expansion of child-care spaces. The proposal required provincial agreement. Whatever the intrinsic policy merit in the approach, it amounted to a federal effort to establish provincial spending priorities in an area of provincial jurisdiction. While several provinces appeared ready to discuss bilateral agreements with the federal government, the timing was awkward in that provincial social service ministries were under severe budgetary constraints; and soon after Doug Young replaced Lloyd Axworthy as federal minister, the initiative withered swiftly. A few months later, as noted above, the federal Throne Speech committed Ottawa to no further use of the spending power in areas of exclusive provincial jurisdiction without the support of a majority of the provinces.

More recently, child care has reemerged indirectly in the context of federal-provincial discussions of child benefits, as discussed above, under which enhanced provincial spending on child care can be, but is not required to be, part of the provincial *quid pro quo* for an enlarged federal income support to low-income families which children.³¹

It is too complicated to trace this checkered history. Instead only the start and end points are shown in Figure 3. Since provincial child-care systems were constrained by the cost-sharing rules of CAP, and these were determined formally by the federal government alone, the starting point for the inter-governmental aspect of the child-care system is reflected at CC1 (heavily unilateral) in that figure. CC2 reflects the new relationship that now appears to be emerging within the framework of the National Child Benefit System. In between, federal strategy on child care, in relation to the provinces, zigzagged. The current position is, however, much less unilateral than was the case at different points in the recent past.

There is one last observation that is relevant here. It is that the change in federal policy on child care relative to the provinces appears to have had less to do with a consideration of the policy merits or demerits of further federal encouragement for the expansion of child-care spaces and more to do with the kind of federalism Ottawa wished to practise in a period of restraint. Since the 1997 Liberal election campaign was also silent on child care, per se, it appears that child care has indeed been dropped by the federal government as a

major "stand-alone" social issue (although it may eventually re-surface in the context of the National Children's Agenda referred to earlier). This suggests that the intergovernmental regime in this area is now closer to disentangled than collaborative.

DISABILITY

As compared to child benefits, progress in better integrating federal and provincial support to persons with disabilities has been modest. The challenge here is huge. The federal government operates three large programs for persons with disabilities (the disability provisions of the Canada Pension Plan, the sickness provision of the *Employment Insurance Act*, and tax support under the *Income Tax Act*) and a number of smaller programs (e.g., the Vocational Rehabilitation of Disabled Persons Program). Provincial governments provide a wide range of services to disabled persons, income support through social assistance as well as the Workers' Compensation programs and, in some cases, automobile insurance. The overall package is poorly coordinated, at best. The result is very uneven levels of support for disabled persons, with some faring well financially and others poorly; and the coordination across governments concerning the weight to be attached to income support relative to services is also inadequately developed.

Provincial premiers decided at Jasper in August 1996 that priority should be given to overcoming the lack of coherence in federal, provincial, and territorial programs for people with disabilities and work has now been undertaken jointly by federal and provincial ministers of social services. A Federal/Provincial Working Group on Disability Income and Supports has been established and work is proceeding to "develop a shared vision and common agenda" to help Canadians with disabilities. Importantly, in this context, ministers have decided that their work will include the services that will enable people with disabilities to participate more fully in labour markets as well as income support.

Achieving substantial progress in this area will almost certainly take much longer than is the case for child benefits. For one thing, the two earnings replacement programs — Workers' Compensation and Canada Pension Plan — are financed either by employer, or combined employer-employee, contributions — and therefore any effort to integrate all of the income support programs into a single guaranteed income for persons with disabilities would inevitably be far more complicated than is the case in relation to child benefits (where only the general revenues of the federal and provincial governments need to be considered). Furthermore, there are substantial differences in purpose between the different categories of income programs. For these reasons, it is more likely efforts will be made to harmonize disability income programs,

perhaps by acting jointly to reduce work disincentives, improve information-sharing and encourage some joint activity (e.g., assessment of disability) rather than attempting a "big-bang" single integrated program.

Nonetheless, both orders of government have decided that a more collaborative approach is preferable to the current mutual unilateralism. The beginnings of progress in this area are reflected in the D1-D2 line. Whether these beginnings will generate concrete outcomes is still an open question. To date there is no high visibility initiative that parallels what has happened in child benefits or labour markets.

It is also arguable that there is a clear case for more collaboration in policy implementation in this area. The absence of a coordinated approach to large benefit programs (e.g., CPP Disability and Workers' Compensation) leads to efforts from one order of government to pass costs on to the other. This may be confusing for clients and costly for administration. Accordingly, it will be important to not only focus more on a collaborative approach to policymaking but also to get a greater coherence in program implementation.

SECTORAL CONCLUSIONS

In three of the five sectors noted, there is a move toward more collaboration either in policy framework, policy implementation or both. In two of the three — labour markets (implementation) and child benefits (framework policy and to a much lesser degree implementation) — the shift toward collaboration on the part of the federal government is significant. In the case of disability provisions, the direction appears similar, but it is premature to assess how much progress will be made in achieving improved policy outcomes. Given the technical complexity of the area, a strong political commitment will be required to advance the agenda in a large way although modest gains are a plausible outcome.

In the case of health care, the federal government is torn between a more collaborative approach and its interpretation of a public mood which appears to want Ottawa to continue to play a "strong" role to maintain one-tier health. What remains to be seen is whether it is possible for Ottawa to sustain a strong role while moving toward a more collaborative approach.

What has happened in child care is less the product of a conscious child-care strategy by Ottawa and more the outcome of the child-care file being swamped by concerns about the working of the federation and fiscal restraint. Nonetheless, the result is a shift away from a regime that had significant elements of federal unilateralism to one that is part-way between disentangled and collaborative but closer to disentangled.

IS MORE COLLABORATION DESIRABLE?

The analysis to this point suggests that, owing to changing circumstance, the federal government has been moving toward a more collaborative approach to the social union. In cases where there has been disentanglement between Ottawa and the provinces, as with child benefits, disability, and major labour market programs, there is a trend toward more collaboration. Where there has been federal unilateralism in macrosocial policy, it is being reduced, for example, restraint of the spending power and the reduction of conditions associated with social assistance. At least for the moment, something has changed. Ottawa appears to be taking the view that interdependence is a fact of life and that it needs to be managed. The reasons for this change were noted earlier. In this section we shift from the positive to the normative and ask two questions. Where we now have federal unilateralism, through the spending power, is collaboration to be preferred? Where we have had disentanglement, is collaboration better? Answering these questions involves a consideration of the effects of these alternative intergovernmental regimes on policy goals and outcomes, democratic values and federalism principles.

In relation to federal unilateralism, the three cases discussed above (child care, the *Canada Health Act*, and the elimination of most of the CAP conditions under the new CHST) do not allow any generalizations regarding any presumed benefits in terms of better social policy that might be seen as large enough to offset any costs such unilateralism might impose in terms of respect for federalism principles. In the child-care example, all that could be concluded was that policy objectives could not be achieved in the face of provincial irritations and fiscal shortfalls at both the federal and provincial levels. In effect, Ottawa's child-care policy has now been subordinated to the federalism and fiscal agendas.

As for the unilateralism associated with CAP, it is generally acknowledged that whatever benefits CAP provided in terms of common social citizenship (and these were relatively few), it discouraged provincial innovation. The current federal position on social assistance, as implied by both the virtual elimination of CHST conditions for social assistance and the new federal-provincial arrangements on child benefits, suggests that Ottawa too has come to recognize that any social policy gains associated with CAP were insufficient to offset the adverse effects on federalism principles (such as the respect for diversity that is implied in the division of powers).

As for the continued federal unilateralism associated with the CHA, it is difficult to form a definitive view since there is ambiguity around the counterfactual, that is, is it a two-tier Americanized system of health care or a modernized collaborative CHA?

The controversy surrounding the interpretation of the CHA is worth dwelling on because it highlights the different values that Ottawa has to weigh

— the trade-offs — in determining its position on the future course for the social union. If the Chrétien government were to follow the words of its own 1997 *Red Book* regarding the importance of collaboration, it would shift to a joint federal-provincial mechanism for interpretation and enforcement of the CHA. The rub here is that Ottawa is almost certainly convinced that this would increase the probability of a two-tier health-care system; and the Liberals also promised to safeguard the current set of CHA principles.

Alternatively, if interpretation of the CHA were assigned to an arm's length party, there is a concern that democratic values would be jeopardized since any such arm's length arbiter would not be directly accountable to voters. If such an arbiter functioned in a predictable and transparent fashion, then some of the potential criticism about its legitimacy might be softened; and if its interpretations drifted too far from federal commitments, it would be feasible for Ottawa to amend the CHA to better achieve the desired outcome. Such amendments could, however, offend some provinces who were supportive of the interpretations being given by the arm's length referees, re-igniting the concern about federal unilateralism. In short, there is no easy answer to the issue of CHA interpretation and enforcement that is a "winner" on all three fronts: achievement of policy goals, maintenance of democratic values and respect for federalism principles. The most recent federal-provincial-territorial initiative (announced in the September 1997 Conference of Ministers of Health) can be viewed, however, as an effort to seek out the optimal point in relation to these three criteria.

The CHA aside, there appears to be a significant measure of agreement concerning the potential benefits of federal-provincial collaboration relative to federal unilateralism. This is suggested by the position of all the provinces except Quebec. The message from the nine provincial premiers at Jasper in August 1996 indicates that provincial governments of all political shapes — from NDP to very conservative Progressive Conservatives — and provinces of varying wealth — from the richest to the poorest — are unanimous in their belief that the federal spending must be subject to some measures of provincial control. As for the current Quebec government, so long as Canada survives, it would scrap the federal spending power entirely and move to a fully disentangled model, with a minimal federal role in social matters. The necessity of enhanced provincial control of the federal spending power has also been acknowledged by recent federal governments including the Progressive Conservatives in the Charlottetown Accord and the Liberals, as noted earlier, in the 1996 Throne Speech. Indeed, it is difficult to find any commentators who would preserve the unfettered right of Ottawa to use the spending power.

The bottom line on federal unilateralism, even if preceded by extensive intergovernmental consultation, is that it entails a view about federalism that presumes that Ottawa is the senior order of government and that it knows more about areas of provincial jurisdiction than do the provinces. The fact

that there is a consensus to limit the spending power, as noted above, is an indication that federal unilateralism is increasingly seen as unacceptable in today's Canada. This suggests that the remaining controversy regarding the CHA may be an exception to the general rule.

It is more difficult to reach a conclusion about the merits of collaboration relative to disentanglement or classical federalism. Yet the factors leading to enhanced collaboration in the cases of child benefits and disability are suggestive of the kind of situation where collaboration may be desirable. That is, it may be desirable in cases where both levels of government have legal authority to act in respect of a particular group of citizens, or a particular subject area, and where there is dissatisfaction with policy outcomes.

There are risks in collaboration. As John Richards argues in this volume,³² collaboration, or what he dubs the "muddle in the middle," complicates political accountability, enabling federal and provincial governments to blame one another when programs are ineffective with the voter unsure about which order of government to hold accountable. Classical federalism avoids concerns about political accountability, eliminates the transaction costs of collaboration and respects federalism principles. Accordingly, in cases where the classical model generates satisfactory policy outcomes, it will be preferable to collaborative models.

In practice, however, both levels of government are legitimately involved in many areas of social policy. Several factors explain this overlap. One is the concurrent constitutional jurisdiction in relation to immigration and benefits for seniors. A second and more important factor is the role of the federal personal income tax system. It plays a key role in determining income distribution and therefore it inevitably impacts on many provincial programs, including those that are directly or indirectly concerned with income distribution. The income tax law also encourages some activities more than others (e.g., deductions or credits for postsecondary education) and these decisions also have implications for provincial programming. Moreover, there appears to be a view that the income tax system is an efficient instrument for delivering certain types of income support programs. Therefore, the role of the income tax system as an instrument of social policy may increase in the years ahead; and the fact that the federal government is planning to proceed with a Canadian Revenue Agency may increase the openness of provinces to use the tax collection system as a vehicle for implementing some of their programs. Finally, there are important interactions between provincial and federal legislative and spending decisions even when each government is acting in its own jurisdiction. For example, as noted above, federal EI decisions may affect provincial social assistance; and provincial decisions on Workers' Compensation may affect the costs of CPP Disability.

Policy collaboration involves costs. It requires financial and staff resources. It makes the task of any single government more complicated than would

otherwise be the case. The habit of policy collaboration is a constraint on any government's freedom of action. It can certainly slow decisionmaking. Pushed to an extreme, collaboration can be an excuse for inaction or lead to policies that constantly involve the "lowest common denominator" in policy. It can also complicate democratic accountability.

Yet the challenges to social policy in Canada are not mainly about difficulties associated within collaboration. For one thing, much of Canadian social policy is disentangled. Provinces and territories run the primary and secondary systems without any federal involvement (except on reserves). In the case of postsecondary education, the federal role is confined to facilitating access, through tax incentives, student loans, and support for research. As for the actual running of the hospital system, and practitioner-patient relationships, this too is largely disentangled. The CHA is mainly about insuring equal access to comprehensive services regardless of income. The provinces also design and deliver virtually all social services without any federal involvement. Conversely, the government has played the principal role in designing and delivering income support for seniors (recognizing that the QPP is separate).

Thus, in recent years, the difficulty in the ongoing interaction among federal and provincial ministers and officials has been less the so-called "democratic deficit," or the perception of such a deficit, that can exist with intergovernmentalism than the absence of an intergovernmentalism that has focused on solving concrete problems.³³ The evidence for this is in the fuss governments give to occasional efforts at collaboration (as has been the case recently regarding children). But if collaboration were normal in situations of significant overlap, there would be less need for fussing and, with more maturity, less bickering. Interestingly, ongoing work by Ekos Research indicates a desire among the Canadian public for both federal and provincial governments to be present in many areas of the social union, with a "desire for greater cooperation among governments."³⁴ For those who want to minimize disagreement among governments, of course, the obvious palliative is to minimize the intergovernmental process. But such an approach suggests that the role of government is to convenience itself, not to serve citizens.

It is by no means implicit in the above that more collaboration is always better: that on all files, the public interest is best served by gravitating to the centrepiece in the figures above. Where there is disentanglement and satisfactory policy outcomes, as already noted, the status quo may well be best. But where there are poor policy outcomes and significant overlaps exist, collaboration may be better. In cases where governments consider moving from a disentangled position to one of more collaboration, it will always be necessary to weigh the potential benefits in terms of policy coherence on a particular issue against the possible costs noted above — transaction costs, reduced political accountability, lowest common denominator, etc.; and there will certainly be a need to wrestle with ways of minimizing reductions in accountability

where collaborative models do emerge. In some cases, halfway to collaboration may be far enough or even too far; and that half-way point may be collaboration on the policy framework, as with child benefits, with both levels of government then free to design and deliver their programs with that framework on a disentangled basis. Interestingly, such an approach fits well with John Richards' proposition that provinces concentrate on services and the federal government on income.

CONCLUSION

The evidence from recent history suggests that the federal approach to the social union is becoming more collaborative. Ottawa is less inclined to use the spending power to provide conditional transfers to the provinces in areas of exclusive provincial jurisdiction without a wide measure of provincial concurrence. There is also less inclination on the part of the federal government to use the spending to transfer money to individuals without coordinating its activities with provinces if the provinces are also providing services or income support to the same target groups. In the first case, the limits on the spending power reflect a concern that federal action, while constitutional, runs counter to the broad political principles of federalism in Canada and creates too much tension in federal-provincial relations. In the second case, the readiness to coordinate reflects a belief that, in modern systems of government, it is impractical to build genuinely watertight compartments everywhere; and where such compartments are impractical, better policy may result from a serious effort at joint problem-solving.

Yet, it is by no means certain that this movement toward collaboration will continue. As federal finances improve, the temptation to "go it alone" could return. Going it alone is unlikely to involve further use of the spending power to create shared-cost programs with the provinces in areas of exclusive provincial jurisdiction without a substantial measure of provincial concurrence. The Chrétien Liberals have committed themselves too unequivocally against such actions to travel further down this road. Rather, if it does occur, going it alone is more likely to entail direct transfers to individuals, whether in the forms of cash, refundable tax credits, loans, or loan guarantees in situations where there are overlapping federal and provincial interests.

With the important exception of Quebec, which disputes the legitimacy of the spending power and prefers a classical model of federalism, the provinces have recently re-affirmed their commitment to collaboration. At their August 1997 annual conference, "premiers expressed their desire to strengthen the role of the Federal/Provincial/Territorial Council on Social Policy Renewal in coordinating and monitoring ... work on social policy renewal." The premiers also called for provincial negotiations with Ottawa on a "broad framework

agreement" that would add cross-sectoral issues like common principles, the use of the federal spending power and dispute resolution to the already large sectoral agenda that is being tackled by the council. In other words, Quebec excepted, it appears that there is a willing set of provincial partners if the federal government wishes to continue dancing. This openness of the provinces to collaboration should thus reduce the incentives of the federal government to act on its own.

The ability of Ottawa to stay the course on the collaborative model may also have implications for political reconciliation within Canada. Here, it is not necessary to be an insider to know the kinds of considerations that must be in the minds of federal Cabinet ministers. On the one side there will be concerns that in ongoing political battles regarding the future of Quebec, any new federal spending (or adjustments to existing spending) in social areas where the province is already active, or is even planning to be active, will be portrayed by the PQ and BQ as an "invasion" of presumed provincial jurisdiction. On the other side there will be concerns that if the federal government does not have some significant direct relationship with individual Quebecers, other than as a tax collector, it will make itself irrelevant to them. The former concerns speak to the desirability of the classical model, with Ottawa's watertight compartment within the social union being very small; the latter concerns presume the need for collaboration. In this regard, to the extent that the federal government is able to reach agreement with the provinces other than Quebec on social union issues, on a basis of genuine partnership and mutual respect, it may serve to strengthen the belief among federal ministers that they should be willing to continue making direct transfers to individuals, including in Quebec. In that perspective, such transfers might be seen as a win-win scenario, strengthening both the efficacy of the social union and the benefits to individual Quebecers in remaining part of a wider Canadian polity.

The social union reform agenda remains large. There are any number of issues on which the possibility of collaboration, at least at the level of policy frameworks, offers the prospects of improved policy outputs; and with a few more successful negotiations to accompany what has been achieved on child benefits and labour market training and development, the more likely it is that the habit of collaboration could become the new status quo in Ottawa. But the federal government is not there yet. Rather, we are at a crossroads in the working of the federation; and the next few years will be crucial in the direction that is taken.

One final observation: to the extent federal and provincial governments continue on the collaborative model, there is the risk of insufficient transparency and uncertain lines of accountability in the new social union. The greater the reliance on collaborative models, therefore, the more the two levels of government will have to address simultaneously issues of openness and democratic accountability.

NOTES

1. For a detailed discussion of alternative definitions of what is included in the social union, see unpublished conclusion from the Canadian Policy Research Networks' 24 March roundtable, Kathy O'Hara, "A Framework of Principles and Objectives for the Social Union" (Ottawa: Canadian Policy Research Networks, 1997), pp. 1-3. The definition used here is narrower than that in Margaret Biggs, *Building Blocks for Canada's New Social Union*, Working Paper no. F-02 (Ottawa: Canadian Policy Research Networks, 1996).
2. John Richards, "Reducing the Muddle in the Middle: Three Propositions for Running the Welfare State," in this volume.
3. According to *The Globe and Mail*, 31 May 1997, p. A4, Premier Clark of British Columbia stated at the end of the Western Premiers' Conference that the "federal government has been the principal cause in undermining medicare and so has lost its moral authority to tell the provinces what to do." The formal communiqué of the conference was almost equally blunt: "the federal government should be challenged to match its stated commitment to *Canada Health Act* principles with the financial commitment to support those principles in the delivery of health services" (p. 9).
4. Liberal Party of Canada, *Securing Our Future Together - The Liberal Plan* (Ottawa: The Liberal Party of Canada, 1997), p. 19. The Liberal Party's assertion that it knows that collaboration is what Canadians want is consistent with the Ottawa-based EKOS Research findings during ongoing public opinion surveys on this issue. The prime minister's speech of 25 March 1997 to the Laval Chamber of Commerce uses very similar language: "Our philosophy of federalism is that collaboration among the various orders of government in Canada is necessary to best meet the needs of Canadians."
5. Leslie A. Pal, "Alternative Instruments of Governance: Models, Trends and Implications for Income Security Policy," submitted to the federal government project on Governance Implication of Labour Market and Income Polarization (Ottawa: Statistics Canada and Human Resources Development Canada, 1997).
6. Liberal Party, *Securing Our Future Together*, p. 15.
7. Biggs, *Building Blocks for Canada's New Social Union*.
8. The premier of Alberta wrote to the prime minister on 16 May 1997 complaining about David Dingwall's "arbitrary and ill-informed deduction." Tabled in the Alberta Legislature, 20 May 1997.
9. There will be a fuller discussion of the CHA per se, in the sectoral analysis below.
10. It is also true that provinces do not discuss major amendments to social assistance law with the federal government, but there is no parallel uploading of costs to Ottawa when provinces restrict their social assistance programs.
11. Thus, the agreements require the provinces to undertake their activities relating to labour exchange services in a fashion that is "methodologically consistent" with the operation of the National Labour Exchange System. There is also

provision for a joint strategy in the gathering, production, and dissemination of local and provincial labour market information to be carried out in a way that is consistent with the National Labour Market Information System.

12. These primary indicators include the number of "active EI claimants" (a term that has a precise meaning under the agreements) that have access to provincial benefits and measures, the proportion of clients who are successfully reemployed, and the consequential savings to the EI account (e.g., section 7.1 of the Canada-Alberta Agreement). Targets have been agreed to and published by the two levels of government and provision is made for establishing mechanisms for jointly setting future targets and for jointly reviewing and assessing achievements. There is also provision that the measurement of primary indicators will be based on a methodology established by the federal government to allow for national results to be reported to Parliament. In addition, there is provision for a joint evaluation of results.

There are a number of good questions that can be asked about the accountability framework that the two governments have established for themselves (e.g., how can program effectiveness be judged when it is unclear whether the EI clients who will receive reemployment assistance from a province are those closest to or furthest from being "job ready?" What is the historical record that lies behind the current targets?). These questions should be pursued in public debate — by committees of the federal and provincial legislatures.

13. Note that this assessment understates, in one important respect, the increased collaboration relative to the policy framework. The new federal-provincial Child Benefit System, discussed below, helps improve labour market incentives.
14. As this chapter was being completed, there were still no signs of a federal-Ontario Labour Market Agreement. The principal obstacle is that the amount of money that the federal government is prepared to transfer to Ontario is substantially less than the amount considered fair by the Ontario authorities.
15. The CHA is, of course, only one element of Canada's health-care system(s). It bears noting that many other elements of the system(s) entail intergovernmental arrangements that are more collaborative or more disentangled than is true of the CHA.
16. National Forum on Health, *Canada Health Action: Building on the Legacy*, vol. I (Ottawa: Canada Communication Group, 1997), p. 21.
17. Ibid.
18. The principles can be traced back to the cost-sharing associated with the *Hospital Insurance and Diagnostic Services Act* (1957), the *National Medical Care Act* (1966), and their replacement through block funding, in 1977, via the *Established Programs Financing* legislation.
19. See, for example, the press release by Prime Minister Chrétien dated 4 February 1997. See also Liberal Party, *Securing Our Future Together*, p. 15, which states: "The federal government must retain its authority under the Canada Health Act to enforce these principles."

20. This possibility is hinted at in the final report of the National Forum on Health. As already noted, the starting point for the forum is its belief that the health-care system in Canada is "fundamentally sound" (*Canada Health Action* Vol. I, p. 11) and that this soundness is linked to the five principles. It rejects the practicability of relying on the "collective will of the provinces to develop and maintain a set of national principles" (*Canada Health Action* Vol. II, p. 28), and declares that there is "no viable alternative to federal-provincial transfers if we are truly serious about maintaining national health care principles as we know them."
21. Federal/provincial/territorial ministers of health, press release of meeting, dated 15 September 1994. Quebec and the Northwest Territories ministers were not present. Practices in four provinces — Nova Scotia, Newfoundland, Manitoba, and Alberta — have all been found, to one degree or other, to be non-conforming. The first three situations are still not resolved and remain subject to very small withholdings.
22. Press release, 12 September 1997.
23. It is recognized that huge changes are being implemented by the provinces in relation to the design and delivery of many health services. Almost all of these changes raise no issues concerning the five principles of the CHA. In that sense, much, but by no means all, of the health-care system can be seen as a disentangled model. The discussion here has been confined to the CHA.
24. In fact, the antecedents of this approach date back to the 1970s and even earlier (e.g., the 1943 Marsh Report, the system of federal Family Allowances that followed, the 1970 federal Family Income Support Plan proposal, Quebec's 1971 Castonguay-Nepveu Report, etc.).
25. See, for example, the communiqué from the 37th Annual Premiers' Conference, Jasper, 21 August 1996; and Canada, Department of Finance, *Working Together Towards a National Child Benefit System* (Ottawa: Minister of Supply and Services, 1997).
26. Federal/Provincial/Territorial Ministers Responsible for Social Services, press release, 19 February 1997.
27. Federal/Provincial/Territorial Ministers Responsible for Social Services, *The National Child Benefit: Building a Better Future for Canadian Children* (Ottawa: Minister of Supply and Services, 1997).
28. British Columbia, *British Columbia's Proposal for a National Child Benefit* (Victoria: Government of British Columbia, 1997).
29. Other premiers have also indicated planned actions, including an Alberta Family Employment Tax Credit, a Saskatchewan plan to create both an income-tested child benefit and an earnings supplement for the working poor, and an Ontario Child Care Tax Credit. New Brunswick is also starting a modest income-tested child benefit and working income supplement.
30. Even this conclusion is qualified in that one province, British Columbia, has asked Revenue Canada to deliver its BC Family Bonus.

31. The 1997 Ontario budget indicates that Ontario will implement a new child-care tax credit as a part of its commitment to the new intergovernmental agreements.
32. Richards, "Reducing the Muddle in the Middle."
33. See Robert Williams, "Without Mysteries or Miracles: Conducting Cultural Policy in the Canadian Federal System," in *Canada: The State of the Federation 1996*, ed. Patrick C. Fafard and Douglas M. Brown (Kingston: Institute of Intergovernmental Relations, Queen's University, 1996), pp. 189-212.
34. EKOS Research Associates Inc., *Rethinking Government* (Ottawa: EKOS Research Associates, 1996).

Economic Integration in Canada through the Agreement on Internal Trade

Robert H. Knox

L'Entente d'échange interne a deux ans. Cet article révisé ce que l'Entente a contribué à l'ouverture du marché domestique canadien et à l'amélioration de son efficacité. Il considère aussi comment l'Entente a fonctionné comme un arrangement qui a permis aux gouvernements canadiens de continuer à travailler de façon coopérative pour améliorer l'intégration économique dans le marché domestique.

L'article conclut que l'Entente a déjà contribué à améliorer l'intégration économique dans le marché domestique mais que cela est toujours en progrès. Le gouvernement fédéral et les provinces doivent continuer d'enlever les barrières à l'activité commerciale domestique et à améliorer la structure d'exploitation de l'Entente, notamment les procédés de prise de décision qui nécessitent le consensus et le système de résolution de conflit pour le rendre plus accessible, vite et transparent. Si les gouvernements sont en mesure d'utiliser les structures établies par l'Entente pour continuer un procédé d'intégration économique domestique coopératif, cela sera un accomplissement important dans la réforme non constitutionnelle.

The heart of the problem lies in the fact that the simplest requirements of provincial autonomy ... involve the use of powers which are capable of abuse ... the problem is to preclude or restrict abuses without interfering with legitimate and even necessary powers.

Rowell-Sirois Commission, 1940

Federalism justifies variation among provinces in response to local preferences ... the need to accommodate diversity ... must be balanced against the objective of gains from trade ...

Macdonald Commission, 1985

The Agreement on Internal Trade is now just two years old, yet it is a key avenue for tangible reform of the federation by "non-constitutional means." It is a complex and technically diverse intergovernmental agreement, attempting to deal with an ambitious range of issues affecting the integrity of the Canadian economic union.

Coming as it did in the immediate aftermath of failed attempts at constitutional reform (including reform to change constitutional provisions affecting internal trade), the agreement is among the more prominent examples of the kind of reform to which this volume is devoted. For this reason the agreement has come under considerable scrutiny — even though, as noted below, its potential for change is not yet realized and it has not been well understood or promoted among the community (i.e., Canadian citizens and businesses) it was meant to serve.

There is already a substantial body of analysis on what the agreement says. The purpose of this chapter is to document the extent and nature of the reduction of barriers to internal trade that have occurred since it was signed. By placing the agreement in its broader context and providing insight into its actual operations, more light can be shed on the pitfalls and promise of this area of ongoing reform of the federal system.

This essay argues that the Agreement on Internal Trade deals with two problems that Canadian governments had been unable to solve despite 15 years of trying. It allows provinces to adjust and develop policies and practices to improve national economic integration without compromising their policy capacity in other areas. Furthermore, it commits Canadian governments to an agenda and an operating structure to improve domestic economic integration progressively and cooperatively. The Agreement on Internal Trade has improved economic integration in the two years that it has been in place, but, as will be shown below, governments are not applying the Agreement to its full potential.

INTRODUCTION

Internal trade barriers and discriminatory commercial policies and practices are normal in any federation. Canada is no exception. Within the limits established by the constitution, provincial governments use their legislative authority to serve the interests of their constituents. This includes protecting and discriminating in favour of local businesses and using policies and practices to provide advantages to the provincial economy.

It is also in the interest of provinces to maintain the effectiveness and the integrity of the economic union. The advantages of this are less obvious and tangible. It is also difficult to accomplish this objective in the ambiguous Canadian constitutional framework that supports diversity and divides

responsibility for economic policy between the provincial and the federal governments. In Canada the rules for domestic trade derive from section 121 of the *Constitution Act, 1867* which says that articles of growth, produce, or manufacture of any province shall be admitted free into other provinces; and section 91(2) which establishes the authority of Parliament for regulating trade and commerce, including trade between provinces.

Generally section 121 has been interpreted as applying to goods and to tariffs and taxes, but not necessarily to non-tariff barriers and/or to the movement of people and investment and trade in services. Section 6(2) of the *Canadian Charter of Rights and Freedoms* now guarantees mobility rights and some recent judicial decisions have interpreted section 121 more broadly than before but the legal character of Canada's economic union remains unclear.¹ The federal government has not used section 91(2) to establish general rules and a regime for managing interprovincial trade and commerce. At this stage in the evolution of the Canadian constitution, it is uncertain whether the federal government could take this step without provincial consent and without changing the constitutional balance between federal and provincial jurisdiction.

Barriers to interprovincial trade and commercial activity were not a major issue until about 1980 when businesses, through their associations, began to focus on them as a factor that was having a negative impact on their efficiency, competitiveness, and growth potential.

Canada's economy expanded rapidly in the years following World War II, but trade was still largely resource-based internationally and the domestic market was still relatively protected and isolated. There was a national consensus regarding the value of markets and freer trade as an essential ingredient of economic growth, but this was understood to be an international not a domestic issue. Canada participated in successive rounds of trade liberalization under the General Agreement on Tariffs and Trade (GATT) starting with a tariff reduction on goods and expanding to include non-tariff barriers and, eventually, services and investment as part of the Uruguay Round in the 1980s.

As a result of the 1985 Canada-US Free Trade Agreement, (CUSFTA) later expanded to include Mexico as the North American Free Trade Agreement, Canada became part of a more or less open continental market by the early 1990s. The North American Free Trade Agreement (NAFTA) also produced a potential political problem. In effect, the availability of markets in the United States that were more accessible to Canadian exporters than their own domestic markets could eventually sap the integrity of Canada's economic union.

While all this was going on internationally, nothing much had happened to develop an open and efficient domestic market since the Rowell-Sirois Commission (the Royal Commission on Dominion-Provincial Relations) identified interprovincial trade barriers as a potential issue. For most of the period after World War II, Canadian businesses and most professional and skilled trade

groups generally accepted and even encouraged protectionist practices that gave them a local competitive advantage.

But in the face of more open international trade, and the development of new technologies and rapid economic globalization, it was increasingly difficult to ignore or justify local protectionist practices. This was particularly the case if these practices reduced the efficiency and competitiveness of Canadian business, limited the development of a productive and appropriately skilled workforce and constrained domestic employment growth and investment.

By 1980 the Canadian economy was less isolated, more diverse, and was beginning to anticipate the pressures of a more open and competitive global economy. Canadian business identified two particular problems in the domestic market. First were government policies and practices that discriminated against workers, goods, services, and investment from other jurisdictions. Second were the different regulations and standards and similar measures that made doing business in other provinces complicated and expensive.

Canadian business began to press governments to remove these barriers and to reduce regulatory burden and complexity. But, while there was an established apparatus and consensus for dealing with international trade issues, there was no similar system to manage domestic trade.

This chapter outlines the current status of the Agreement on Internal Trade reached in July 1994 and that came into force in July 1995. The second section provides a brief discussion of the protracted intergovernmental process leading up to the agreement. Section three provides an overview of the main principles and scope of the agreement. The fourth section discusses the implementation of the sectoral aspects of the agreement (ch. 4-15), while section five covers the implementation of the operating structure and institutions, including the dispute resolution process (ch. 16 and 17). The conclusion draws together comments on the extent and nature of the reform which the agreement represents.

THE INTERGOVERNMENTAL PROCESS ON THE WAY TO THE AGREEMENT ON INTERNAL TRADE

In 1980, the federal government proposed a reformulation of section 121 of the *Constitution Act, 1867* as part of the repatriation round. The proposed wording said that no Canadian government could discriminate on the basis of residence "in a manner that unduly impedes the operation of the economic union." Other parts of the proposal protected measures that might be inconsistent with this provision but were "in the interests of public safety, order, health or morals." Parliament (but not provincial legislatures) would also be allowed to continue policies for equalization and regional development.

This proposal was rejected by nine of ten provinces because it placed unacceptable constraints on provincial powers and extended federal authority and reserved regional development to the federal government. Consideration of this proposal was brief and not substantial.² This was nonetheless the start of a 14-year process that would lead to the *Agreement on Internal Trade* signed by all Canadian provinces and territories and the federal government in July 1994. During this time, a consensus on the importance of an open and efficient domestic market developed along with a commitment to make the necessary changes to accomplish this goal. Still, almost nothing of substance happened until 1993.

The fundamental problem remained the same through all the discussions and negotiations over this period. There remained a pervading concern by provincial governments that to remove barriers to domestic trade and to eliminate or harmonize other measures that make the economic union less efficient would reduce their economic jurisdiction and limit their policy and legislative flexibility and authority in other areas. Notwithstanding regular First Ministers' Conferences (FMCs) and meetings of committees of ministers, there was no formally mandated, cooperative process by which Canadian governments could jointly manage the domestic market in a way that would support continuing economic integration and respond to rapidly changing global economic conditions. All governments, the federal as well as provincial, tended to see the problem in "zero-sum" terms — any reduction in provincial authority would increase the federal government's jurisdiction and any formal cooperative arrangement for managing the domestic market would allow the national government to intervene in provincial affairs.

After 1980 there were a number of proposals and intergovernmental initiatives to resolve domestic trade issues. The issue remained prominent, sometimes near the top of the intergovernmental agenda and never far beneath the surface. The "Macdonald" Royal Commission on the Economic Union and Development Prospects for Canada was set up in 1982 by the government of Prime Minister Pierre Trudeau specifically to deal with economic integration. But while the Macdonald Report made recommendations for mechanisms to reduce internal trade barriers,³ its more prominent recommendations dealt with the need for a free trade agreement with the United States.

Over the subsequent period from 1985 to 1992, two issues eclipsed direct intergovernmental attention to internal trade as such. First, the negotiations with the United States over the (CUSFTA) and subsequently with the United States and Mexico over the NAFTA had priority over internal trade negotiations, although in many respects they subsumed them. Some barriers to internal trade also constitute international trade barriers, and some provisions of the CUSFTA and NAFTA eliminate barriers to internal trade or change the context of the regulation of the domestic market.

Second, from the first agreement at Meech Lake, federal-provincial relations were dominated for the next five years by attempts at constitutional reform. The economic union issue in general became a prominent part of the post-Meech, "Canada" round. Constitutional solutions to improving the economic union took a variety of forms, including a statement of general principles (e.g., the "Canada Clause" in the Charlottetown Accord); an improved section 121 (e.g., Government of Canada proposals, September 1991, and the "Charest" report of March 1992); and a new federal legislative power over the economy (the federal government's 1991 proposals for a new section 95A).

While the broader free trade and constitutional issues dominated, the federal and provincial and territorial governments pursued internal trade issues, first, through the Committee of Regional Economic Development Ministers starting in 1985, and then through the Committee of Ministers on Internal Trade (CMIT) starting in 1987. Successive Annual Premiers' Conferences (APCs), starting in 1986, and First Ministers' Conferences on the economy, starting in 1987, also discussed internal trade issues.

This process tried various options including voluntary "standstills" on new barriers to trade that failed almost as soon as they were accepted and negotiation of agreements on specific issues such as government procurement and liquor board marketing practices. Little of substance was accomplished.

By late 1992, with the failure to ratify the Charlottetown Accord, Canadian governments faced an internal trade agenda that was more urgent than ever. In trade policy terms, the differences between 1980 and 1992 were significant.

Economic globalization was now a reality. North American free trade was in place and the World Trade Organization was about to emerge from the GATT Uruguay Round along with further international trade liberalizing measures. Through extensive intergovernmental consultations with Ottawa over those international trade negotiations, most provinces now had knowledge of and experience with international trade policy. Similarly, major Canadian business associations had made the reduction or elimination of internal trade barriers a policy priority.

Although some provinces were more wary than others, making the domestic market more open and competitive was a priority and an objective for all Canadian governments, if they could find an acceptable way to do it. The years of work on domestic trade issues, particularly the recent constitutional discussions, had clarified the essentials of the problem and developed a cadre of informed and knowledgeable ministers and officials with clear negotiating positions.

In March 1992, at a conference on the economy, the first ministers agreed to accelerate the process to reduce internal trade barriers, to strengthen domestic trade linkages and to find ways to minimize competition for investment. They set a deadline of March 1995 for the Committee of Ministers on Internal Trade to achieve this objective. In May 1992, the Committee of Ministers on

Internal Trade approved three *Principles to Enhance Internal Trade in Canada* and a moratorium on new barriers.

By December 1992, as noted, the constitutional route had failed completely with the negative response to the referendum on the Charlottetown Accord. However, this result seemed to reinvigorate the non-constitutional process of internal trade negotiations, perhaps because public opposition to the Charlottetown Accord did not appear to be related to the issues of economic union or internal trade.

Michael Wilson, the federal minister of industry, tabled a proposed Statement on Canada's Internal Trade at a meeting of the Committee of Ministers on Internal Trade. The statement committed Canadian governments to negotiate a comprehensive agreement "to remove barriers and reconcile regulations, standards and administrative practices in all of the economic sectors and subject areas agreed to by governments." The negotiations would begin by July 1993. The agreement would be completed by 30 June 1994 and ratified by 30 June 1995. To the surprise of many officials, ministers agreed. They would recommend to their governments that they proceed as set out in the statement.

On behalf of their governments, ministers formally agreed to the process at their meeting in Montreal on 18 March 1993.⁴ The negotiations got underway in July 1993. A year later, at a conference in Ottawa on 18 July 1994, first ministers signed the Agreement on Internal Trade (AIT). It came into force on 1 July 1995.

THE AGREEMENT ON INTERNAL TRADE: OVERVIEW

The Agreement on Internal Trade has four components.⁵ First, it sets out objectives and general trade rules for domestic trade (Parts I, II, and III). Second, it contains chapters for each of the economic sectors covered by the agreement (Part IV). Third, there are Chapters defining an operating structure and dispute resolution procedures (Part V). Finally, it contains provisions of general application (Part VI).

The first component of the agreement sets out general objectives and, in Part III – General Rules, establishes operating principles for Canada's domestic market. These rules provide for non-discrimination,⁶ the right of entry and exit⁷ and a prohibition on measures that create obstacles to domestic trade.⁸ Other rules provide for the reconciliation of standards and regulations⁹ and require governments to ensure that measures and procedures relating to matters covered by the agreement are accessible.¹⁰ Effectively these last two rules establish a basis for positive economic integration through the agreement while the first three rules establish limits on government authority in relation to domestic trade.

Governments deal with the limits that broad trade rules might have on their capacity to act in other policy areas by applying the concept of "legitimate objective." Governments have further ensured the flexible application of the broad trade principles by limiting their application to matters covered in the specific economic sector chapters in Part IV.¹¹ To add suspenders to the belt, an article in Chapter Three¹² confirms that the agreement does not alter the legislative or other authority of Parliament or of the provincial legislatures or any other authority established by the constitution. Together these measures deal with one of the concerns that prevented agreement on internal trade after 1980. The question is do they make the principles for domestic trade contained in Chapter Four ineffective? In my view they do not.

Governments have undertaken to apply the agreement.¹³ If they respect the intent, spirit and substance of the agreement, they will use the principles in Chapter Four – General Rules, to guide the development and application of their policies and practices. The rules in Chapter Four apply to the specific sector chapters (in Part IV – Specific Rules) in one form or another. This allows for flexibility and restructuring to make the rules more effective and appropriate.

Part IV includes ten chapters on specific economic sectors that are covered by the agreement. Some of these chapters, such as those on government procurement, investment, labour mobility, and consumer protection, break new ground and should produce significant integration in Canada's domestic economy. Others, such as those covering transportation, communications, and environmental protection, reinforce and support economic integration processes already underway. Still others such as the one for agricultural and food products and, to an extent, the one for alcoholic beverages establish a schedule and a process for dealing with issues in the future.

Most chapters include a form of institutional structure and provisions for continuing consultation and review that are intended to promote continuing positive economic integration through the reconciliation and harmonization of policies and practices.

The details of the sectoral chapters (5-15) and the operating structure (16-17) are provided in subsequent sections of this chapter.

However, Chapter Eighteen – Final Provisions, includes articles that qualify the rest of the agreement by including a number of general exceptions. First, programs for regional economic development are exempted.¹⁴ (These exceptions are subject to constraints and reporting requirements. There are no reports yet on how much regional economic development exceptions have been used.) Also exempt are policies and programs for Aboriginal Peoples¹⁵ and measures to support culture or cultural industries.¹⁶ In addition, financial institutions and services are excluded.¹⁷ (The issue for governments was securities regulation, which was being negotiated separately.)

The final chapter also includes several other important provisions, including: a "standstill" on any new measures or amendments inconsistent with the agreement, or which decrease conformity with the agreement.¹⁸ It also contains a provision that requires an annual review of the scope and coverage of the agreement, that is effectively a commitment by governments to extend and expand the agreement.¹⁹ Finally there is a commitment to complete negotiation of the energy chapter.²⁰

THE SECTOR CHAPTERS AND THEIR IMPLEMENTATION

In assessing the results of the negotiation for the agreement and, more especially, its implementation, a few basic questions have been posed: What is the principal barrier to be removed by each part of the agreement, and how effective are the provisions in the agreement covering that barrier? Based on available evidence in the first two years, how has each part of the agreement been implemented and is it reaching its potential for improved economic integration in Canada? Are the operating structures and processes, including dispute resolution, adequate to the task of fulfilling the broader objectives of the agreement? To answer these questions, the following section summarizes the agreement, and its implementation thus far, particularly in the following areas: procurement, investment and business access (including incentives), labour mobility, and consumer protection.

PROCUREMENT

The Agreement on Internal Trade, through Chapter Five on Procurement, establishes a national open market for public sector procurement by establishing non-discriminatory rules and procedures for public sector procurement and developing a national electronic tendering system available to all governments and government agencies. Ultimately the terms of the procurement chapter will be extended to the broader public sector (municipalities, municipal organizations, school boards and publicly-funded academic health and social service entities, the so-called MASH sector as in municipalities, academic institutions, schools, and hospitals).

To date, a common electronic tendering system has been developed by an intergovernmental technical working group that was set up as part of the agreement.²¹ This working group has selected a supplier to provide a system that should be operational within the next two years. Eventually suppliers anywhere in Canada will be able to access most public sector tenders on this single system. As this chapter was being completed in September 1997, negotiations to extend the provisions of the procurement chapter to the broader public sector (the MASH sector) were incomplete.

The agreement called for negotiations on arrangements to include the MASH sector to be completed by 30 June 1995²² and to come into force on 30 June 1996.²³ These negotiations were nowhere near complete by either of these dates. Initially the main issue was concern by the groups and governments affected that they would be burdened with a complex, rigid, and expensive system. The health sector was particularly concerned that, if the procurement chapter applied to them, they would be unable to use strategic purchasing that allows them to engage their suppliers in hospital operations to reduce costs.

Most of the issues have been resolved in most jurisdictions. There is now a draft text that is acceptable to all provinces except British Columbia which, apparently, continues to believe that the provisions in the current procurement chapter are too complicated. The BC government is not prepared to require their MASH entities to apply them. They proposed another option based on a "best efforts" application of the open tendering principles in the agreement. Other governments believe this approach is unworkable.

Provincial governments (the federal government is not part of this negotiation because they do not have MASH entities within their jurisdiction) have been at a stand-off on this matter for more than a year. The agreement²⁴ requires that decisions be made by consensus. Since the Government of British Columbia has said that it will not accept what other provinces wish to accept there is an effective veto by BC and an impasse.

At their annual conference in August 1997, premiers directed internal trade ministers to meet as soon as possible and conclude "an arrangement to include open tendering provisions for MASH sector procurement, in a manner acceptable to all jurisdictions if possible."

Since BC is unlikely to agree, apparently other provinces are, reluctantly, prepared to proceed without that province. Excluding one jurisdiction is inconsistent with the economic integration objectives of the agreement. It could establish a precedent, which, if broadly applied in the future, would "fragment" rather than integrate the domestic market. Nevertheless, if used occasionally, it is an effective and flexible means to promote transition toward economic integration.

Critics believe that exclusions in the procurement chapter mean that it is less than comprehensive.

For example the agreement applies to purchases of goods \$25,000 and over and to services and construction contracts \$100,000 and over.²⁵ A number of government agencies and Crown corporations are excluded²⁶ as well as some services.²⁷ Procurement contracts can be excluded to support regional and economic development but only under certain conditions²⁸ and procurement procedures allow exclusions for such things as urgency or where issues such as confidentiality and public health and safety are involved.²⁹

Some of these exclusions are necessary to provide for efficient procurement. For example, the cost of the tendering process makes purchasing goods

by tender below \$25,000 inefficient. Other exclusions are currently under review as required by the agreement.³⁰ Reports are that governments are making progress in reducing the number of entities excluded, but have failed to come to terms on the services excluded.

So far there has been no move to change threshold levels, but, based on experience since negotiations on procurement started in 1988, further liberalization will begin once governments have an opportunity to adjust to the new environment and have a better understanding of how the agreement works.

Critics also believe that the procurement chapter must have an accessible, quick and transparent "bid-protest" system to be effective and that current procedures³¹ do not meet these criteria. Like most systems for dispute resolution in the agreement (and for that matter those proposed during the 1992 "Canada round" of Constitutional discussions) the bid-protest procedures for provinces (procedures for the federal government are different) are designed to be non-adversarial and to resolve issues through discussion and mediation. It is also, fundamentally, a government-to-government system and depends on the interest and energies of officials.

The federal government uses the International Trade Tribunal (ITT), which also handles procurement issues under NAFTA, to deal with bid protests. The virtue of this system is that ITT is a third party with quasi-judicial procedures dedicated to dealing with disputes. It also has the power to halt procurement proceedings and to reverse decisions as well as to recommend compensation. As an agency with a specific mandate to resolve disputes it is probably more accessible than provincial systems.

On the face of it, the best arrangement to deal with bid protests would be a single national system with the authority to intervene in procurement processes if necessary. But this was further than provinces were willing to go during negotiations.

As it stands, the provincial bid-protest system needs improvement in a number of areas. Unless provinces have taken the trouble to describe the bid-protest process and identify contact points in tender documents the process may not be particularly accessible. There is no capacity for the provincial contact point to intervene in the procurement process and no clear remedy for the complaining supplier unless provinces have defined one in their own procedures. As a result, a supplier is dependent upon the capacity of the "contact point," an official who usually has other responsibilities. There is no mandated third-party oversight of the process or the players. Furthermore, there is no formal public reporting of suppliers' complaints that have been resolved or dealt with in some other way. As a result it is almost impossible to tell if the process is working. Changes are possible. The chapter³² requires a review of the bid-protest system in 1998. Probably it is too soon for substantive changes.

The Internal Trade Secretariat recently started tracking complaints. Thirteen bid protests have been listed since 1995. Eight of these are through the

federal government system. Four of the protests were resolved or upheld, seven were denied or dropped and two are pending. It is hard to tell if this is a complete list or if a significant number of potential protests were never made because suppliers were unaware of the process or because they did not believe it would be worthwhile to use it.

Has the procurement chapter improved economic integration in Canada's domestic market? No doubt it has. Government procurement at the federal and provincial level is more open and accessible across the country and, imperfect as it may be, Canada has an undertaking in place for a national public sector procurement market that was not there before. Has the procurement chapter realized its full potential? The answer is no. It is disappointing, but not terminal, that governments are unable to meet negotiating deadlines and implement other obligations such as the reduction of excluded entities and services and that the review of the chapter, including the appropriateness of the existing thresholds, has not been done.

IMPROVING BUSINESS ACCESS

One of the issues for domestic commerce is the difficulty and the potential extra costs involved in doing business in other provinces. Each province has the power to regulate and set standards for business activities in its own region. There are two aspects of this issue examined below. First are the measures and practices that treat businesses from outside the province differently from those located inside. Second are the regulations, standards and other measures that are different from jurisdiction to jurisdiction even though they are intended for the same purpose. An example is the different corporate reporting and registration requirements that are in place in each province.

In some cases, the objective of discriminatory provisions and different regulations may be to exclude businesses from other provinces or at least to give an advantage to local business. In most cases, however, the problem is one of omission, or at least the absence of a compelling reason for change, and the want of a mechanism for resolving differences in practices and regulation.

The agreement deals with these issues in two ways. First, it seeks to resolve differences in standards and regulatory measures that create barriers to trade.³³ Most chapters — but most importantly those on investment, labour mobility, consumer protection, transportation, environmental protection, and natural resources — include specific obligations to reconcile these differences and require regular reviews to identify issues not already covered by the agreement. Second, it attempts to eliminate discriminatory practices altogether.

Chapter Six on Investment provides for non-discriminatory treatment of Canadian businesses regardless of where the head office is located, where the firm is incorporated or where the owners live. It also eliminates local presence and residency requirements as a condition for carrying on business or

making an investment³⁴ and restricts the use of local purchasing and local sourcing requirements.³⁵ Chapter Eight – Consumer Related Measures and Standards, prevents governments from requiring individuals to live in a province or territory as a condition of licensing, registration or certification as a supplier and allows local presence and residency requirements for businesses only where necessary for consumer protection.³⁶ It also eliminates any discriminatory fees or other requirements for the licensing, registering or certification of suppliers.³⁷

Within the next year, implementation of another provision in the investment chapter will ease the compliance burdens for firms conducting business in more than one jurisdiction. In the agreement, governments undertook to reconcile corporate registration and reporting requirements and agreed to produce an implementation plan by 15 July 1995.³⁸ They missed the deadline but last year, ministers approved an implementation plan that is now being applied.

In summary, these measures will undoubtedly improve domestic economic integration. However, Canadian governments have not yet come to terms with the need to reconcile different standards and regulations even though the agreement provides the structure and the obligation. Probably the problem is a lack of specificity to provide focus. Either businesses and associations, in cooperation with government, will have to develop a menu of issues to be resolved or governments will have to look to new mechanisms, such as cooperative national institutions for standard setting, for regulation, and for inspection. This approach is being implemented in the securities industry and in agriculture, and it will probably happen elsewhere if and when the need becomes acute.

THE CODE OF CONDUCT ON INCENTIVES

In the initial discussions of barriers to interprovincial trade in 1985, competition for investment among provinces became a collateral issue. Its main proponent was British Columbia. They were concerned that neighbouring provinces, particularly Alberta, were enticing operating companies away from BC with subsidies and other incentives. In other words, provinces were “poaching” businesses with jobs that would not have relocated otherwise.

There was also the situation in which companies that were interested in moving or investing would “subsidy hunt” or auction their investment to the highest bidder. For the larger provinces — Ontario, Quebec and British Columbia — the competition was with American states that could offer attractive packages of municipal and state tax relief and infrastructure incentives as well as subsidies. These provinces were not anxious to change their practices. Smaller provinces, on the other hand, frequently found themselves competing against one another for the same investment.

The Agreement on Internal Trade includes a Code of Conduct on Incentives in the investment chapter as an annex.³⁹ It prevents governments from giving incentives or subsidies, of any kind, to businesses to lure them away from other Canadian jurisdictions and rules out incentives that would allow an enterprise to undercut a competitor from another province for a specific contract.⁴⁰

The code commits governments to use their best efforts to avoid incentives that sustain uneconomic operations, that increase capacity that is not warranted by market conditions or that is excessive and to avoid bidding wars.⁴¹ The annex also requires an annual report on incentives that will describe the incentive programs offered by governments, the amounts of incentives paid by type and amount of individual grants over \$500,000 and loans or loan guarantees and equity over \$1 million. So far this report has not been produced by the Working Group on Investment that is responsible for it. The working group itself only started meeting regularly in 1996.

The Code of Conduct on Incentives has already been tested twice but inconclusively. In the spring of 1995, about four months before the agreement came into effect, United Parcel Services (UPS) announced that it would consolidate its administrative and call centre operations in Moncton, New Brunswick. The consolidation involved 900 jobs including about 300 from British Columbia. British Columbia protested that New Brunswick used subsidies to attract UPS. They said that these kinds of subsidies were prohibited by the Code of Conduct on Incentives and that, according to Article 1807, New Brunswick was committed to a standstill on measures or actions that were inconsistent with the agreement after it was signed by the first ministers in July 1994.

New Brunswick's position was that UPS had already decided to consolidate its administrative activities somewhere in North America and decided on New Brunswick and that the commitment was made, but for the details, before the agreement was signed in July 1994. Therefore, any incentives provided were consistent with the agreement. New Brunswick also maintains the Code of Conduct on Incentives is incomplete. Before the agreement was signed the parties had agreed to clarify how incentives would apply in cases where a business was consolidating its activities. This had not been done.

The agreement provides for consultation among parties who disagree. Although BC and New Brunswick took their positions to the media first, there was eventually consultation under the terms of the agreement. These went on for about 18 months during which British Columbia asked for information and New Brunswick provided some information but withheld some to protect commercial interests. Ministers were consulted twice but were unable to resolve the issue.

Finally, in September 1996 *The Globe and Mail* reported that: "New Brunswick will not submit to the scrutiny of a new interprovincial trade tribunal

looking into the province's acquisition of 900 United Postal Service jobs last year." *The Financial Post* reported that: "[The] B.C. Industry Minister [said] that he will recommend repudiation of the [internal] trade deal to his cabinet colleagues ... B.C. charges that New Brunswick is unwilling to participate in the formal dispute settlement process under the terms of the *Agreement*." There it stands. Both British Columbia or New Brunswick could ask for a panel but neither has.

Meanwhile, around the same time it was reported that in May 1995, nine months after they signed the Agreement on Internal Trade, Saskatchewan decided to provide a \$5 million forgivable loan to a BC meat packer to consolidate its operations in Saskatchewan. It appears from these reports that the Saskatchewan government knew that its decision was inconsistent with the agreement but decided to go ahead anyway. BC has not protested this issue.

Probably both New Brunswick and Saskatchewan legitimately thought their initiatives to attract business were not yet covered by the agreement. It is at least arguable. British Columbia, for its part, has a right to feel frustrated. For the BC government, the Code of Conduct on Incentives was an essential part of the agreement and one of the main reasons it could support it. It made this clear during negotiations. Now it appears that the code is ineffective.⁴²

It is likely that the problem lies with the dispute resolution process that cannot resolve issues quickly and with some kind of satisfaction for the protagonists (dispute resolution is covered in more detail below). On the other hand, the agreement's dispute resolution process may be more effective than it appears. It is based on the premise that, generally, governments will avoid doing things that require them to publicly defend policies that are inconsistent with the agreement and that might be politically embarrassing. Maybe governments will ensure that their programs are consistent with the Code of Conduct on Incentives in the future.

LABOUR MOBILITY

Provinces have the constitutional responsibility for regulating the workplace and determining occupational standards and qualifications in their jurisdiction. In most provinces much of the administration of professional standards has been delegated by legislation to professional associations. Effectively there are different occupational and professional licensing bodies in every province. Over time this has resulted in different provincial requirements to qualify or to be certified, some tending to protect a profession or trade, but most to meet what are understood to be local conditions and to meet their statutory obligation to protect standards and ensure adequate qualifications for practitioners or workers.

Now, because of increased mobility and improved communication, the practical differences in occupational and professional training and competence

across Canada have been reduced. However, the fragmented structure for developing and applying standards and qualifications remains. Mobility for Canadians is guaranteed by section 6 of the *Canadian Charter of Rights and Freedoms*. This means that Canadians cannot be refused entry or work or the right to practise their trade or profession because they have come from another province. This has been confirmed by the Supreme Court in a ruling on a case of a lawyer qualified to practise in Alberta who was refused the right to practise because he was not associated with a firm of practising in Alberta.

Section 6 of the Charter does not override the requirement to be qualified so that, even though Canadians have the right to move to and work in other jurisdictions, the problem of different and sometimes onerous and restrictive occupational standards and licensing practices still exist.

Chapter Seven of the agreement is intended to reduce these practical barriers to mobility and includes three measures to accomplish this objective. First, it removes residency as a condition for access to employment opportunities, for licensing, certification or registration or for eligibility for an occupation.⁴³ Second, it establishes that requirements for licensing, certification or registration of workers must relate principally to competence, must be published and must not result in unnecessary delays or burdensome costs.⁴⁴ Third, the agreement requires that qualifications of workers from other jurisdictions must be recognized and differences in occupational standards reconciled.⁴⁵

The key requirement is the commitment to reconcile occupational standards and recognize qualifications. Accomplishing this objective has eluded Canadian governments for years. The main problem is the number of professions and skilled trades and the number of organizations involved in setting and administering standards for them. For example, the Labour Market Coordinating Group, the officials responsible for implementing the chapter, has identified and contacted more than 400 non-governmental trade and professional groups who are required to change their policies and practices to be consistent with the agreement.

An annex to the chapter⁴⁶ requires provinces to begin this process within 12 months after the agreement came into force. Governments met this deadline and work is now underway to mutually recognize qualifications and reconcile standards. The problem is that there is no deadline for completing this process.⁴⁷ Even though governments have taken steps to notify the 400 or more non-governmental occupational licensing bodies of their obligations and to set out procedures, little has changed. Premiers acknowledged this at their annual conference in August 1997.⁴⁸

In February 1997, the federal government announced a program to provide funding to consortia of provincial occupational groups to help them develop harmonized standards and qualifications. Four groups have been funded and 12 applications are being considered. This program is likely to produce results but it is possible that governments will have to consider ways to bring

closure to the process for occupational groups and to speed up the process of harmonizing occupational standards for trades. They plan to do this in the spring of 1998.

In the meantime, governments are using the procedures for consultation in the chapter⁴⁹ to identify and resolve issues while the process of reconciliation is underway. Some of the issues raised through this process are illustrated in the examples that follow:

- An Emergency Medical Technician from Alberta found that his qualifications were not recognized in Ontario and that he would have to go through the Emergency Medical Care Assistant Challenge Eligibility process at Humber College to assess his prior training, knowledge, and skills against the current program curriculum. He believes that Ontario is violating the agreement by not recognizing the equivalency of his Alberta qualifications. Ultimately the technician was successfully qualified in Ontario and Ontario has said that it is reviewing its procedures. The case remains open because the professional association in Alberta remains concerned that the Ontario Eligibility Challenge process violates the agreement.
- Many residents of Sparwood, British Columbia work in Crowsnest Pass, Alberta. They were being charged higher fees for various work and business permits. BC complained, citing Article 707: Licensing, Certification and Registration of Workers. The issue was resolved when Crowsnest Pass passed a by-law expanding the area of residency for workers and business, but the discriminatory practices have not changed.
- The owner and operator of a funeral chapel on the Alberta side of Lloydminster wanted to open a chapel on the Saskatchewan side of the city. He was trained in Saskatchewan but only licensed in Alberta. The Saskatchewan Funeral Services Association requires all out-of-province licensed embalmers to take a one-year internship program under a Saskatchewan licensed embalmer to be accredited. Although he was trained in Saskatchewan, the Saskatchewan Funeral Services Association would not waive the internship requirement. The issue has not yet been resolved.
- A graduate in Occupational Therapy from McGill University worked in occupational therapy in Ontario for 13 years before moving to Alberta in 1996 and applying to practise there. The Alberta Association of Registered Occupational Therapists requires applicants to write the Canadian Association of Occupational Therapist (CAOT) certification exam. Following a complaint, the Alberta Professional Examination Board in Occupational Therapy agreed that, based on her education

and currency in practice, she qualified to be licensed under a "grandparenting" clause in the Alberta Occupational Therapy act.

These examples demonstrate the effective use of the consultation process in the labour mobility chapter in the agreement. It is interesting to note that the complaints, though sometimes successful, do not necessarily lead to changes in policy or practice. Nor does the chapter solve all outstanding labour mobility issues.

For example, it is not clear how the agreement would resolve the hiring hall and licensing practices of Quebec construction unions that, by legislation, are allowed to grant permits only to workers in specific regions of Quebec. This generally excludes qualified workers from outside Quebec as well. The agreement also may not resolve the long-standing problem of Certified General Accountants (CGAs) who are allowed to sign financial statements in some provinces but not in others. This issue might be resolved when provinces go through the process leading to the mutual recognition of qualifications and the reconciliation of standards.

In summary, the labour mobility chapter is clearly promoting domestic economic integration in an area that has been a problem for Canadian governments for some time. It is also an example of how the agreement and, potentially, any other domestic intergovernmental agreement, can be used to implement and reinforce constitutional provisions and principles. In this case, section 6 of the *Charter of Rights and Freedoms* guarantees mobility for Canadians. Chapter Seven: Labour Mobility, extends the effectiveness of the mobility principle in the Charter by reconciling occupational standards, qualifications, and regulations.

CONSUMER-RELATED ISSUES

All Canadian governments have measures to protect consumers. The federal government's interest is with goods and services that are traded interprovincially. Therefore, the federal government has labeling and packaging regulations and is responsible for such things as weights and measures (legal metrology). Provinces are responsible for protecting consumers in relation to commercial activities that happen within their jurisdiction and in areas of provincial responsibility.

Chapter Eight deals specifically with commercial activities. Since all provincial governments occupy the same legislative and policy space there is significant overlap, duplication, and inconsistency in consumer measures. The scope of the chapter is broad. It establishes that the chapter applies to all "consumer related measures and standards adopted or maintained by a party."⁵⁰ It also eliminates discriminatory fees for licensing, registration, and certification.⁵¹ And it removes residency or local presence as a requirement for

licensing, registration or certification except measures to establish a legal presence for consumer protection.⁵²

Beyond that, governments have chosen to deal sequentially with a number of specific measures. Three specific issues were identified to be reconciled immediately.⁵³ With respect to *Direct Sellers Harmonization*, governments agreed to harmonize cancellation rights and contract content requirements that will apply to direct sellers and provide the same consumer protection across Canada by June 1996. In the area of Cost of Credit Disclosure, governments agreed to standardize minimum disclosure requirements and the methods by which cost of credit is calculated and reported. A legislative "template" has been drafted to assist governments in preparing legislation that is expected to be passed in all jurisdictions by July 1998. Measures concerning *Upholstered and stuff articles* have been harmonized in the remaining jurisdictions that regulate these matters.

The chapter also specifies a second tranche of measures to be assessed and reconciled as appropriate after July 1997, including: reciprocal investigative powers, enforcement of revocation rights, financial compensation for consumers, and enforcement of judgements.⁵⁴

In summary, the consumer-related measures chapter is an example of a step-by-step approach to economic integration that is appropriate to the diverse nature of the issues involved. As is the case with other obligations in the agreement, governments have had problems meeting the deadlines specified in this chapter. Nevertheless, even 12 to 18 months behind schedule, harmonizing direct selling measures and introducing legislation to standardize the disclosure of the cost of credit in Canada are significant for domestic economic integration.

OTHER SECTORS

Other sector chapters also support economic integration to a greater or lesser degree depending on the policy issues. Without exception, however, they all include a commitment to the objectives and general principles of the agreement and a structure and a program to identify and resolve issues to increase domestic economic integration.

The agriculture and food sector probably is more regulated and government managed than any other in Canada. Much of it is for health, safety, and environmental reasons. But much of it, including supply management, is also intended to protect national and local producers and processors.

Chapter Nine on Agriculture and Food consists of commitments to study and to a rigorous work program. These include a commitment to review supply management, the *Western Grain Transportation Act* and the "agricultural safety net programs"⁵⁵ and to a review of the scope and coverage of the chapter by 1 September 1997 to "achieve the broadest possible coverage and further (liberalize) internal trade in agriculture and food goods."⁵⁶

Agriculture ministers have postponed this last obligation until December 1998. They will develop a revised chapter based on stakeholder consultations to be completed by July 1998. The chapter will be based on "principles" which means that they will devise a set of rules, probably similar to the General Rules in the agreement, that will apply to all aspects of the agriculture and food sector.

Still, there are small changes in the agricultural sector and signs that the industry is beginning to prepare for greater changes to come. An example is the dairy industry. To start with, dated and unnecessary colouring restrictions for margarine have disappeared in most of Canada and the remaining regulations in Quebec are now subject to the general rules of the agreement.

The industry is changing rapidly, partly as a result of international trade agreements but also in anticipation of an open domestic market in dairy products. Specifically: licensing of fluid milk distribution has disappeared in western Canada; Ontario is reviewing similar regional regulations; there is substantial consolidation among domestic milk processors particularly in Quebec and Ontario and large international processors have acquired domestic companies; milk producers from Manitoba east have established a common market in fluid milk; and milk distribution regulations in the Atlantic region are under pressure as at least one company, Farmers Cooperative Dairy, seeks to improve its competitiveness by establishing an integrated regional operation.

In effect, the agreement has, in some cases, stimulated economic integration even though the issues are not directly covered. For example, liquor regulation and Liquor Board marketing practices have been recognized for a long time as a source of barriers to interprovincial trade. In the 1980s the main issue was rules that required a beer to be brewed in most provinces where it was sold. Most, but not all, of the barriers to interprovincial trade in beer disappeared in 1992. Chapter Ten on Alcoholic Beverages will complete the process of integration over the next few years. The sector will remain highly regulated and some provinces, like Newfoundland, will continue to protect their industry as long as possible.

Chapter Eleven on Natural Resources is intended to deal with measures that require natural resources to be processed in the province where they are produced. Some measures remain but there are provisions for consultations to resolve these issues over time.

The communications industry is probably one of Canada's most technologically advanced and competitive sectors. The industry has also been integrated on a national basis for some time. Chapter Thirteen – Communications, confirms this open domestic market and establishes a process to monitor the sector and deal with practices that may be inconsistent with the agreement should they arise in the future.

In the motor vehicle transportation sector, intergovernmental committees of ministers, officials, and technical experts have been in place for more than

20 years, integrating the industry in Canada. The industry has been deregulating for about ten years, since the federal *Motor Vehicle Transportation Act* was revised in 1987. The object of this process has been to develop harmonized standards and to mutually recognize and harmonize licensing and inspection. Chapter Fourteen on Transportation commits governments to continue this process of integration and establishes a tighter time table and more specific commitments and allows for complaints to provide discipline.

The process to harmonize environmental measures that may limit trade and increase business costs unnecessarily was in place before the Agreement on Internal Trade was negotiated. The Canadian Council of Ministers of the Environment (CCME) has the responsibility to manage this process. Chapter Fifteen on Environmental Protection confirms this process to resolve trade issues that result from environmental regulation and puts it in the context of the principles of the agreement.

THE OPERATING STRUCTURE

Chapter Sixteen establishes a Committee on Internal Trade to implement and operate the agreement and to assist in resolving disputes.⁵⁷ The terms, scope and coverage of the agreement defines the mandate of the committee. The committee is also required, annually, to review scope and coverage and to make recommendations to expand the agreement.⁵⁸ The committee is to be composed of "cabinet-level representatives ... or their designates."⁵⁹ Alberta and Saskatchewan are represented by ministers of intergovernmental affairs. Other governments are represented by ministers responsible for industry and economic development. In other words the committee can consider any issue related to the domestic market and should be an effective vehicle to oversee and promote economic integration in Canada.

Some of the architects of the agreement thought that the Committee on Internal Trade would operate like the GATT or WTO governing council. In this view, the committee would become the central forum for negotiating and resolving all domestic market issues across all economic sectors. Normally governments would be represented by a minister with broad responsibility for domestic trade and intergovernmental issues related to the domestic market. On specific matters, governments would be represented by the minister with the appropriate responsibility for the issue being discussed. All negotiating or work groups would report to and through the Committee on Internal Trade.

The Committee on Internal Trade has not functioned this way and is unlikely to do so. This is because of the competing jurisdiction of a network of ministerial level intergovernmental committees that has evolved in Canada since the 1960s. These committees are in place for almost every chapter/sector in the agreement (Labour Mobility, Consumer Affairs, Transport, Natural

Resources, Agriculture, Environment, Communications) and will continue to operate independently of the Committee on Internal Trade. The internal trade related issues in these portfolios will probably not be considered directly by internal trade ministers. As a result, many issues, and therefore a large part of the internal trade and economic integration agenda, will remain outside the agreement's institutional structure. In effect, an intergovernmental mechanism with a broad responsibility for promoting economic integration in the domestic market has not evolved yet in Canada, although the mandate and structure exist in the Agreement on Internal Trade.

The agreement establishes that the chair of the Committee on Internal Trade will rotate annually among governments.⁶⁰ In fact, the joint federal/provincial sharing of the chair that started in 1987, when the Committee of Ministers on Internal Trade was first established, remains in place. Furthermore, the province sharing the chair, Manitoba, has not changed since 1990.

There are probably practical reasons for continuing the arrangement of federal/provincial co-chairs. First the federal government's interest is national in scope. The federal priority and responsibility is to promote an open and efficient domestic market. The federal minister is, therefore, able to focus resources and time, as well as a national perspective, on the public policy issues involved in the proper functioning of the domestic market and of the agreement. Second, continuity has been an important factor in starting up the agreement. Having the same ministers in the chair through the negotiation and during the first years of operation probably has improved the odds that the agreement will get off the ground.

Finally, rotating the chair annually requires a strong and experienced secretariat with sufficient staff and resources. To provide continuity and consistency in the operation of the agreement, the executive director of the secretariat should have a clear and accepted mandate to provide technical and policy advice to the chair on national domestic trade issues as well as on the effective functioning of the agreement. The Internal Trade Secretariat is in place but still evolving. It is not clear that it has these attributes yet or that all governments accept its policy function in relation to the chair of the Committee on Internal Trade. An annually rotating chair is probably the most effective and appropriate arrangement in the long run but, until the agreement is understood and accepted by both governments and the private sector and is operating effectively, a shared federal/provincial chair with tenure of three to four years is probably the most effective arrangement.

Chapter Sixteen establishes that the committee's decisions will be taken by consensus.⁶¹ There was no consideration of alternatives during negotiations. Decision by consensus now seems to be a problem for the committee in implementing and operating the agreement. Since concluding the agreement in July 1994, the Committee on Internal Trade has met about every six months, sometimes more frequently. During this time the committee has been

preoccupied with the extension of the procurement chapter to the MASH sector and this has been delayed because provinces have been unable to find an approach acceptable to all.

During this period the committee also dealt with a number of other issues including the dispute between British Columbia and New Brunswick concerning the relocation of UPS. The committee was unable to mediate this dispute successfully. The work program set up under the agreement is behind schedule in almost every respect. Work has not started on obligations such as the review of the scope and coverage of the agreement except in a cursory way. Simple administrative matters like producing the first annual report are behind schedule. A draft of the annual report for the period to the end of March 1996 has been on the table since March 1997. It is still under discussion. As well, reporting requirements under most articles and chapters have not been honoured.

The problem in maintaining momentum on the agreement's work program is partly the result of the requirement for consensus on even straight forward issues. It is also partly that internal trade ministers do not control the full agenda and rely on other ministers, and the officials reporting to them, to meet the obligations of the agreement. These groups have the same problem of motivation, resources, and consensus as internal trade ministers and their officials.

The third problem is the organization of the committee of officials — Internal Trade Representatives (ITRs) — that supports the committee of ministers, and the role and resources of the Internal Trade Secretariat. The agreement establishes a national Internal Trade Secretariat to support the Committee on Internal Trade.⁶² It is located in Winnipeg. The Executive Director of the Secretariat is the senior official and reports to the co-chairs of the committee of ministers and takes directions from the committee.

The executive director is also, effectively if not officially, the chair of the committee of Internal Trade Representatives (ITRs) from each government. Internal Trade Representatives are informally responsible for making the agreement work. Although the ITRs committee has no formal standing in the agreement and no specific terms of reference, they work with the executive director of the Internal Trade Secretariat to carry out the directions of the Committee on Internal Trade, to negotiate and resolve issues, and to monitor and oversee the agreement.

The original idea was that ITRs would take responsibility for specific issues such as liaison with specific sectors or the operation of specific chapters, chair working groups, and provide resources to carry out specific projects. The reality is that most Internal Trade Representatives have other jobs and most governments have not provided specific resources to support the internal trade process (only Alberta and the federal government have officials working full time on the internal trade file).

The Internal Trade Secretariat has a restricted budget. During negotiations, some governments were clear that they would provide only limited resources to a national secretariat. One issue was a desire not to be seen to be expanding public administration when there was a concern about the size of government and most governments were cutting back. An unspoken issue may be the concern on the part of some governments that a strong national internal trade bureaucracy would reduce governments' control over the internal trade agenda and the functioning of the agreement.

The operating structure and processes supporting the agreement are changing gradually as those involved develop greater mutual trust and a better understanding of the problems in its implementation and operation. In the meantime, it is difficult to maintain the agreement's work program on schedule, to maintain effective links with sector groups, to communicate and consult with the private sector, and to carry out the operational tasks and research necessary to make the agreement effective.

In summary, The agreement notionally provides a standing intergovernmental process with the operating infrastructure that Canadian governments need to integrate the domestic market: the Canadian version of the GATT Secretariat or the European Community Commission. But the Committee on Internal Trade and the Internal Trade Secretariat are still evolving. The committee needs to reconcile the requirement for consensus with the need for a more effective decisionmaking process. It also needs to consolidate the internal trade issues in all economic sectors into a concerted process to improve domestic economic integration; and finally, it must provide adequate resources to meet the provisions of the agreement and develop a responsive organization to support its activities.

DISPUTE RESOLUTION

Resolving disputes and enforcing commitments is an issue in all trade agreements. Generally speaking, international trade agreements rely on government-to-government consultations, mediation and panels to resolve disputes, and the withdrawal of benefits or retaliation to enforce decisions and the agreement generally.

The situation within a national structure, dealing with non-tariff barriers that arise from day-to-day government operations is different. First, disputes often result from specific problems for specific companies or individuals that require immediate solutions rather than extensive changes to government policy or protracted government-to-government discussion. Second, retaliation in relation to non-tariff barriers within a federation governed by a constitution is difficult and destructive to the domestic market and the economic union. Finally, in a national structure, the justice system is the usual means of dealing with disputes and fines or financial compensation are the normal remedy to

satisfy civil issues. Courts can also force changes to government measures if they do not conform to laws or the constitution. Still, the justice system is not really a satisfactory way to promote economic integration.

Although Canadian governments can apply the normal trade policy model to dispute resolution, they need to find creative ways to make it work effectively in a domestic context. The private sector, which was pressing for an agreement on internal trade, wants an accessible, transparent, inexpensive, non-adversarial process that is enforceable and would resolve its problems quickly and practically and eliminate the offending policy or practice in the future. Most provincial governments want a system that is inexpensive and allows them some control over the issues to be considered and that does not allow third parties, namely the courts, to define policy. The federal government prefers a system that the private sector, as well as governments, could use, ideally a single, third-party system such as a national commission or tribunal whose decisions could be enforced by the courts.

The system in the agreement emphasizes consultation and encourages dispute avoidance at a number of levels. Most sector chapters (Part IV) provide for consultation and reference to the ministers responsible for that chapter before resort to the agreement's general system set out in Chapter Seventeen – Dispute Resolution Procedures. The general process in Chapter Seventeen allows parties to proceed through further consultations or, by agreement, to refer the matter immediately to the Committee on Internal Trade or to a panel for consideration.

In addition, a person or a company can make a complaint if a government declines to act on their behalf, and if a neutral "screener" appointed by each government agrees that the complaint is legitimate. After that, the process includes consultation, reference to the Committee on Internal Trade and eventually a panel if the issue cannot be resolved at an earlier stage. Governments have agreed to implement the recommendations of panels.⁶³ If governments do not comply the panel report is published and referred back to the Committee on Internal Trade for action; including, in the case of complaints by governments, retaliation. If the system is effective in dealing with complaints through consultations there will be few panels. There may also be little policy integration resulting from a process that does record or follow-up issues with policy change.

According to information gathered by the Internal Trade Secretariat, which may be incomplete given the informal and dispersed character of the first consultation stage of the dispute resolution process, 36 complaints have been made since the agreement came into effect on 1 July 1995. Of these, seven were dropped, seven were denied, six were resolved or the complaint upheld, five were cases where there was no basis for the complaint, and eleven are pending. The average length of time for dealing with the complaints that have been concluded one way or another is seven months. But the average in the

second year of operation, 1996-97, was three months. Performance may improve with time.

Although the main dispute resolution processes in Chapter Seventeen have not been used the first issue may now be pending. Early in 1997 the federal government passed legislation to ban the use of the gas additive MMT by banning interprovincial trade in the product. The basis for this policy was technical evidence that MMT contributes to pollution. It has been banned in the United States for this reason. The refining industry disputes the technical evidence and contends that the ban is not justified.

In April 1997, Alberta and Saskatchewan, with Nova Scotia and Quebec as intervenors, launched a complaint under the agreement.⁶⁴ Presumably the basis for the complaint is that the federal government, even though it has the constitutional authority to regulate interprovincial trade, cannot, under the terms of the Agreement on Internal Trade, use this authority to create an unjustified barrier to interprovincial trade.

The federal government will probably argue that it passed the legislation to meet a "legitimate objective" as defined by the agreement and will refer to the article in the environment chapter that says "an environmental measure shall not be considered to be inconsistent with this agreement by reason solely of the lack of full scientific certainty regarding the need for the measure."⁶⁵

It may be difficult for either party to back away from this dispute so that consideration by a panel may be the only way to resolve the issue. It is now going through the consultation process prescribed by the dispute-resolution chapter and that, depending on the wishes of the parties, can be a protracted process.

Effective issue identification and dispute-resolution procedures are as important as anything else to promoting economic integration. Governments tend to be blind to weaknesses in their policies and practices and naturally, and correctly, disinclined to change without reason. An arrangement that encourages those affected by government measures to raise issues is essential to a process of continuing and relevant change and improvement and an effective process for this purpose is one that is accessible, responsive and not arbitrary.

Those who negotiated the agreement were aware of these considerations and developed a system for dealing with complaints based on consultation and mediation rather than on an adversarial approach.

Unfortunately the result for an outsider, however, is like dealing with a black box and it is not clear that the process even serves the interests of governments. First, the agreement has not been well publicized so only the well informed or those with time and money will know how to raise an issue under the agreement, who to contact and under what conditions. Second, for most people making complaints, the best solution to a problem is a quick, clear answer either way so that they can get on with their business. The procedures set out in the agreement process takes time, as long as 18 months if there is

any difference of view and probably a minimum of two or three months even for simple issues. Third, the dispute resolution should lead to changes in policies and practices. Identifying issues, keeping records and following up on the policy implications of issues raised through complaints is essential for continuing policy change and improvement. It is not certain that this kind of process is in place.

For the Internal Trade Agreement, the best dispute-resolution process is likely to be a well-publicized, single national system, accessible from anywhere in the country, with people dedicated to resolving issues using techniques similar to those used by ombudsmen and with panels available to deal with complex disputes or those that cannot be resolved through normal mediation processes. No complaint process should take longer than 90 days. This arrangement would also provide a database of issues and problems that would help to adjust the agreement and improve domestic market integration.

CONCLUSION

The Agreement on Internal Trade solves the problems that prevented Canadian governments from dealing with domestic trade issues through 12 years of constitutional and other types of negotiation after 1980:

- it allows provinces to change their policies and practices to remove barriers to trade and increase national economic integration without compromising their policy capacity in other areas;
- it provides an intergovernmental operating structure that allows Canadian governments to identify issues and adjust policies and practices cooperatively and responsively.

The question is: Does the Agreement on Internal Trade accomplish real economic integration? Critics say no. They say the agreement is too complex, that it has substantial exceptions that confirm, rather than remove, trade barriers, that it defers issues and is unenforceable with an inaccessible, opaque and toothless dispute-resolution process.

The other view is that the Agreement on Internal Trade has helped, and is helping, to integrate the Canadian economy.

- The General Rules in the agreement, accepted by all Canadian governments, are now the benchmark for trade and economic relations between provinces and territories.
- Through a range of initial measures, the agreement has improved economic integration by establishing a national public sector procurement

market, resolving labour mobility issues, establishing rules for subsidies and incentives and dealing with long-standing consumer issues.

- There is a program and a process to deal with outstanding issues, to reduce and remove exceptions and to expand the coverage, and improve the functioning of the agreement. Even if the process is slow and erratic it is probably also irresistible and change will inevitably happen at a time and in a way that reflects the interests of all Canadians.
- There is an institutional structure — the Committee of Ministers on Internal Trade, the Internal Trade Secretariat, and the compliance and dispute-resolution processes — that Canadian governments can use to manage, cooperatively, trade and economic relations. If these institutions are not fully effective yet, the potential for use exists for governments.

The agreement is not perfect and some of these imperfections in its substance and its implementation could be terminal. Most could be fixed with sufficient interest, goodwill, and ingenuity.

In summary, the parties to the agreement need to go the extra distance to reach its potential as a major breakthrough to an effective Canadian economic union. Specifically:

- Governments have to give the agreement profile. Unless individuals and businesses use the agreement to deal with domestic trade issues that affect their business and governments are seen to be using it to improve economic integration, the agreement could disappear without a trace. It is not clear that there is an alternative to the agreement;
- Governments need to consider an alternative to the requirement for consensus as the basis for all decisionmaking;
- The Committee on Internal Trade should be responsible for managing economic integration in the domestic market;
- Consultation and dispute-resolution processes have to be more accessible, effective, and quick and contribute to changing and improving the agreement.

In conclusion, governments and critics should remember that the agreement does what could not be done by other means, including constitutional reform. Indeed as one of the more prominent of attempts by Canadian governments to reform the federal system without constitutional amendment, the Agreement on Internal Trade deserves special scrutiny. It achieves its results through a complex intergovernmental agreement that is still stymied by the consensus-only decisionmaking of Canadian intergovernmental relations. Yet it also achieves its results with diversity and flexibility and in a way that does

not appear to interfere with the sovereignty of the federal and provincial legislatures, which is the federal balance in Canada.

The agreement is also a work-in-progress with an important amount of unfinished business as governments negotiate workable rules affecting procurement, agriculture, and energy among other areas. Thus there is much continuing opportunity for governments to improve upon and extend the Agreement on Internal Trade. The framing of an effective ongoing process may be the important achievement of such non-constitutional reform.

NOTES

1. Among the judgements usually cited are La Forest J.'s comments in the *Law Society of Alberta v. Black et al.* This case was a Charter challenge based on mobility rights guaranteed by section 6(2) of the *Canadian Charter of Rights and Freedoms* and *Morguard Investments Ltd. v. De Savoye* and the tests used by Dickson C.J. in *City National Leasing*, *supra*.
2. See Robert Howse, *Economic Union, Social Justice and Constitutional Reform: Towards a High But Level Playing Field* (Toronto: York University Centre for Public Law and Public, 1992), pp. 61-72.
3. Royal Commission on the Economic Union and Development Prospects for Canada *Report*, Vol. III (Ottawa: Minister of Supply and Services, 1985), pp. 135-40.
4. Meeting of Ministers of Internal Trade, *Communiqué*, Montreal, 18 March 1993.
5. The *Agreement on Internal Trade* is available on the Internet at the Internal Trade Secretariat web site (www.intrasec.mb.ca/) or the Industry Canada web site (strategis.ic.gc.ca/IPTrade). Detailed commentary on the provision of the agreement is provided in Michael J. Trebilcock and Daniel Schwanen (eds.), *Getting There: An Assessment of the Agreement on the Internal Trade* (Toronto: C.D. Howe Institute, 1995); see also Bryan Schwartz, "Assessing the Agreement on Internal Trade: The Case for a 'More Perfect' Union," in *Canada: The State of the Federation 1995*, ed. D.M. Brown and J.W. Rose (Kingston: Institute of Intergovernmental Relations, Queen's University, 1995).
6. Article 401.
7. Article 402.
8. Article 403.
9. Article 405.
10. Article 406: Transparency.
11. Article 400: Application.
12. Article 300: Reaffirmation of Constitutional Powers and Responsibilities.
13. Article 101: Mutually Agreed Principles.
14. Article 1801: Regional Economic Development.

15. Articles 1802: Aboriginal Peoples.
16. Article 1803: Culture.
17. Article 1806: Financial Sector.
18. Article 1807: Measures Subject to Transitional Provisions; and 1808: Non-Conforming Measures.
19. Article 1810(4).
20. Article 1810(2) & (3). Negotiations of the Energy Chapter are not complete. The problem has been to define an acceptable commitment on the transmission of electricity across the territory of another province and how to open provincial markets to competition in electric power given the heavy debt obligations of Crown producers and monopolies. The sector is changing rapidly, however, particularly in Ontario, which is now considering unbundling the production, transmission, and retailing of electricity, and privatizing some elements of the industry. A recent ruling by a US energy regulating agency has closed off exports to the US unless exporting provinces reciprocate by opening their markets to imports. Apparently agreement on an energy chapter is now close and premiers, at their annual meeting in August 1997, agreed to complete these negotiations within the next 12 months.
21. Article 516(3).
22. Article 517(1).
23. Article 502(4).
24. Article 1601(5).
25. Article 502: Scope and Coverage.
26. Annexes 502.2A and 502.2B
27. Annex 502.1B
28. Article 508: Regional and Economic Development.
29. Article 506(11) and Article 507: Non-Application.
30. Articles 516: Future Reviews; Article 517: Future Negotiations.
31. Articles 513 and 514.
32. Article 516(4).
33. See Article 405: Reconciliation; and Annexes 405.1 and 405.2.
34. Article 604: Local Presence and Residency Requirements.
35. Article 607: Performance Requirements.
36. Article 806: Residence and Local Presence Requirements.
37. Article 805: Licensing, Registration and Certification Fees.
38. Article 606: Corporate Registration and Reporting Requirements.
39. Annex 608.3.
40. Annex 608.3, paragraphs 4-7.
41. *Ibid.*, paragraphs 4-7.

42. In the news release on internal trade issued at their annual conference in August 1997, premiers directed internal trade ministers to "examine, as a major priority, potential clarifications and improvements to the *Agreement's* Code of Conduct on Investment Incentives."
43. Article 706: Residency Requirements.
44. Article 707: Licensing, Certification and Registration of Workers.
45. Article 708: Recognition of Occupational Qualifications and Reconciliation of Operational Standards; and Annex 708 that establishes the process for implementing the terms of Article 708.
46. Annex 708, paragraph 10.
47. Governments are obligated to complete this process "within a reasonable period of time." Ministers responsible for this chapter, the Forum of Labour Market Ministers (FLMM), recognize that this obligation is too broad and, in the next few months, will recommend to internal trade ministers a more specific commitment.
48. The Annual Premiers' Conference news release on the *Agreement on Internal Trade* identified "compliance of regulatory bodies with labour mobility provisions" as one of the agreement's outstanding issues that they directed their internal trade ministers to resolve.
49. Article 711: Consultations.
50. Article 801: Scope and Coverage.
51. Article 805.
52. Article 806.
53. Annex 807.1.
54. Article 808: Cooperation on Consumer-Related Measures and Standards.
55. Article 903.
56. Article 902(4).
57. Article 1600: Committee on Internal Trade.
58. Article 1810(4).
59. Article 1601(1).
60. Article 1601(4).
61. Article 1601(5).
62. Article 1603: Secretariat.
63. Articles 1708 and 1719.
64. Chapter 15: Environmental Protection.
65. Article 1505(8).

Canadian Regardless of Origin: “Negative Integration” and the Agreement on Internal Trade

Daniel Schwanen

Dans cet article, Daniel Schwanen passe en revue les dispositions de l'Accord sur le commerce intérieur qui ont pour but d'éliminer les mesures qui font discrimination sur la base de l'origine provinciale des biens, services, personnes ou entreprises. L'auteur a trouvé que, malgré un progrès réel dans certains domaines, plusieurs étapes concrètes prévues par l'ACI et dont le but était de rendre ces dispositions effectives, n'ont pas été franchies. De plus, il estime que le mécanisme de règlement des différends de l'Accord n'a pas été pleinement utilisé. L'auteur discute des raisons possibles de cette mise en oeuvre incomplète de l'Accord, et propose nombre de mesures qui pourraient en accélérer le processus et en réaliser les promesses.

INTRODUCTION

In this chapter, I will examine some of the progress accomplished so far under the Agreement on Internal Trade (AIT), signed in 1994 between the Canadian provinces and territories and the federal government. Specifically, I will be concerned here with whether the commitment made in the AIT to remove laws, regulations, or practices in effect in one province (or territory) that discriminate against out-of-province persons or businesses, has been fulfilled.¹

Attempts at removing discriminatory barriers often come under the rubric “negative integration,” because getting rid of the barriers in these cases usually involve banning an offending set of behaviours. However, to give practical effect to negative integration, it is not enough just to agree to refrain from certain practices. Specific steps must also be taken, such as, in the AIT, the

disclosure of information necessary to ensure transparency in the treatment of out-of-province entities, the publication of reports monitoring compliance with the agreement, and the creation and operation of mechanisms, such as the one governing dispute settlement, necessary to enforce the commitments.

Much of this chapter will be concerned with whether such actual steps as Canadian governments promised to do under the AIT in order to remove inter-provincial discrimination have been fulfilled. But first, I will briefly review the purpose of negative integration and the various tools which can be used to secure the non-discriminatory behaviour which it entails. Following this, I will review the commitments made in the AIT, both in general and in specific sectors, and assess whether the steps that were to have been taken under the agreement have in fact been taken. I will then look at whether and how the dispute settlement process has been used to ensure that the parties to the agreement² stick to their obligations not to discriminate. Some thoughts will then follow on what is left to be desired in the process of negative integration undertaken with the AIT, and on what can be done to improve it.

My conclusion regarding the achievement of the goal of non-discrimination under the AIT is that significant progress has been made toward it, but not always at the pace that signatories were pledged to follow under the agreement. The continued elimination and avoidance of discriminatory barriers would be greatly helped by governments making at least as much information public as they had promised to do when they signed the AIT, including on the progress of trade disputes. In addition to giving greater public profile to the agreement, I would favour strengthening the AIT's institutional structure, in order to accelerate the pace of outstanding negotiations, and would urge governments to implement legislation that would steep their day-to-day operations in the principles of the agreement, in order to enshrine the latter's status as a fundamental tool of the common citizenship of Canadians. Finally, the federal government should contemplate a more interventionist role in areas where implementing the agreement is meeting serious stumbling blocks.

PURPOSE AND TOOLS OF NON-DISCRIMINATION OR NEGATIVE INTEGRATION

The benefits of an integrated economic area can initially be understood in terms of a more efficient allocation of resources within the area, with individuals and regions being allowed, through their participation in a wider market, to specialize in what they are relatively better than others at producing, and thus generating higher incomes. In order to achieve this better allocation, it is necessary that goods and services providers, and people and capital, be able to seek business or employment across regions. Non-

discrimination on the basis of origin, or negative integration, is in turn essential to such dynamics being allowed to take place.

For Canada, evaluations of the dollar amount of additional national income that would result from a more efficient allocation of production, compared with the pre-AIT situation, have indicated that these gains would be significant, although not overwhelming since the Canadian market was already well-integrated in many sectors even before the agreement came into effect.

But the gains from a more open market exceed those which can be evaluated simply by looking at how production across the country might be reallocated on the basis of comparative advantages, once the removal of remaining barriers allowed firms and individuals to do so. Many economists have pointed out that the benefits from a more completely integrated market also include higher economies of scale (with a larger sized market lowering the average cost of output), the dynamic effects of increased competition (due to the incentive to adopt the best processes and technologies), and the reduced deadweight cost of lobbying for protection.³

In any of the above senses, the rationale for integration is not different than that existing for entering into larger free trade areas (and some of the same caveats, such as the danger of diverting trade away from other, potentially lesser-cost trade partners, exist as well). Indeed, on all of the above counts, free trade with the United States since 1989 would have generally reduced the relative advantage of a more integrated Canadian market. However, while access to the US market has become much easier for many Canadian firms, it remains strewn with barriers in a number of sectors, particularly in agriculture, in most services, in construction, for firms bidding on public sector contracts, as well as for small- and medium-sized businesses in virtually all sectors, because of the administrative costs of qualifying for tariff-free status and the risk of attracting trade "remedy" action across the border.⁴ For these firms among others, maintaining or increasing access to the Canadian market constitutes an important, even vital, underpinning to their growth and investment strategies.

Another benefit of an integrated market is that, apart from its positive effect on national and individual incomes, it also reduces individual and corporate risk through the creation of a reciprocal economic citizenship, in that it requires people and firms to be treated, if not always the same everywhere (a matter of "positive integration"), then certainly to be treated everywhere as a citizen (the essence of "negative integration"). Thus, tools that ensure negative integration across a wide area reduce the risk from having to operate within the confines of smaller, more specialized economies, and this benefit accrues even to those who never actually take advantage of opportunities to expand or move beyond provincial borders.⁵

Within a political union, negative integration is all the more valuable in that it allows the benefits of both income gains and reduced risk to take place within an institutional structure that all regions hold in common. As a result, the economic gains from integration need not occur at the cost of having to adopt a foreign institutional (e.g., legal) structure, or of people having to move to a foreign country and lose the benefits of citizenship (e.g., public pensions) if, for example, their skills are not easily marketable in their province of origin. The advantages of an economically integrated political union can also extend to international bargaining, since when representatives of the union "speak with one voice" on issues of common interest (or support each other's position on a reciprocal basis), each constituent unit can leverage its bargaining power to that of the whole.

Of course, any of these benefits will obtain within the union provided that the political compromises involved in maintaining the economic union — especially with respect to basic reciprocal rights and obligations, and to who is responsible for making decisions for the whole — can be struck and adhered to by the members of the union.

In Canada, attempts to remedy shortcomings with respect to the legal and institutional basis of economic union led to the creation of an intergovernmental Committee of Ministers on Internal Trade (CMIT) in 1987, produced some regional and sectoral trade agreements in the late 1980s and early 1990s,⁶ and culminated in 1994 in the more comprehensive AIT.

Although the federal government is a signatory to the AIT on par with the provinces, it is important to note that this does not mean that it has let go of any of its other options for removing discriminatory practices or otherwise strengthening the Canadian economic union. This is important to note, because unlike the European model, the AIT itself has little or no judicial "backstops," available to citizens, businesses or governments, should a signatory decide to ignore some of its provisions. The AIT does have a dispute settlement mechanism (DSM) which is admittedly more open to citizens than equivalent international procedures, but there is little that can be practically done if governments decide not to comply with them. Legislations implementing the agreement, introduced in some provinces and at the federal level, fail to make the AIT directly applicable in law.⁷ It has little non-political supporting structure, save for a Secretariat established to provide administrative and operational support and "such other support" as the Cabinet-level Committee on Internal Trade (CIT), which replaced the CMIT and which ultimately supervises the implementation of the agreement, "may direct" (article 1603). Given the current terms of the AIT, all that can be done to ensure its implementation, apart from appealing to the DSM or applying direct political pressure on the signatory governments, is to expose any violation or lack of progress, and suggest ways of improving the process in order to make it easier to achieve its promises, as I will attempt below.

NON-DISCRIMINATION IN THE AIT: COMMITMENTS AND RECORD TO DATE

In this section of the chapter, I will review two kinds of promises made by governments in the AIT to eliminate discriminatory barriers to the Canadian economic union. It should be noted that the practices targeted by this promise need not only be provincial: federal measures that discriminate against the movement of goods, services, people, and investment between provinces⁸ are considered equally reprehensible under the AIT, as indeed they should be.

The first type of promise concerns agreements to adopt on an ongoing basis a certain behaviour, for example, non-discrimination toward another province's suppliers, or to follow transparent procedures. It is difficult to judge on the face of it whether actual behaviour has conformed to these promises, especially since, as we have seen, the implementing legislation in the provinces and federal jurisdictions involved mostly housekeeping items, and hence did not result in the AIT becoming directly applicable in law. The best indicator of whether the agreement is being followed on this general "good behaviour" score may lie in the record of the complaints that have been brought under its dispute avoidance or dispute settlement mechanisms. I will leave an examination of this record for the next section of the chapter.

The second type of promise made in the AIT concerns specific steps that governments promised to take, often within a stated deadline, to deliver on a certain administrative procedure, to make recommendations, or even conclude negotiations on certain specified issues in order to complete the coverage of the agreement. These are commitments to act and to deliver a product, even if it is only a report, the progress of which is relatively easy to track. In this section of the paper, I will review the status of these specific commitments to act, listed according to the sector or activity to which they apply. First, however, a short review of the AIT's general principles and rules as enunciated by the signatory governments is in order.

GENERAL PRINCIPLES AND RULES

Apart from the general undertaking enunciated in the AIT to reduce and eliminate barriers to the extent possible, the parties to the agreement have also agreed, under the heading of "mutually agreed principles" (article 101), to be guided by two broad rules of behaviour that speak most directly to the question of eliminating interprovincial discrimination, namely that of not establishing new barriers to internal trade, and that of treating persons, goods, services, and investments all equally, irrespective of where they originate in Canada.

The "reciprocal non-discrimination" principle is in turn made operational by the rule on reciprocal non-discrimination (article 401). Under this rule,

governments (including the federal government) agree to grant out-of-province goods, persons, services, and investments of another province at least the best treatment they accord to those originating within a particular province ("provincial treatment," akin to national treatment in international trade agreements), and also, at a minimum, the best treatment it accords goods coming from another province or country (equivalent to a "most-favoured-nation" clause). The rule is meant to apply to goods that are "like, directly competitive or substitutable" and to the treatment of persons, services, and investments "in like circumstances."

There can be exceptions to the above rule, and these exceptions are defined in such a way as to provide a balance between the principle of non-discrimination, and "legitimate" public objectives that may require the existence of measures that are on their face, or could be construed as, discriminatory. Contrary to previous attempts at entrenching exceptions in rules governing trade within Canada, however, (notably those contained in the early drafts of what became the Charlottetown Accord) a discriminatory measure must pass a severe test before it can be considered admissible under the agreement (article 404 -see below).

Box 1: General Acceptability Test for Discriminatory Measures

Even if it discriminates on the basis of provincial residence, a measure is still acceptable under the terms of the Agreement on Internal Trade if:

- a) Its purpose is to achieve a legitimate objective, defined as either:
 - Public security and safety
 - Public order
 - Protection of human, animal or plant life or health
 - Protection of the environment
 - Consumer protection
 - Protection of the health, safety and well-being of workers
 - Affirmative action programs for disadvantaged groups
- b) If goods, services or investments meet the legitimate objective of a measure, then the measure must not operate so as to unduly impair their access to the jurisdiction imposing the measure.
- c) The measure is not more trade restrictive than necessary to achieve the legitimate objective.
- d) The measure does not create a disguised restriction on trade.

The AIT also contains transparency provisions, which are very much complementary to the non-discrimination requirements, because they allow verification of whether specific practices actually conform to them. Among specific undertakings concerning transparency, governments must ensure that relevant information, ranging from laws to guidelines to administrative rulings, are made readily accessible; that parties to the agreement notify the other parties in advance of any measure they are proposing to adopt that may affect the operation of the agreement; and that they maintain enquiry points to answer enquiries and provide information required under the agreement (article 406).

Certain provisions in Annex 405.1 of the agreement directly relate to the objective of ensuring non-discrimination in how standards and standards-related measures are set or implemented (in addition to those aimed at reconciling a number of standards and standards-related measures across Canada, the scope of which falls under "positive integration" rubric). These provisions require that the parties "shall" specify their standards in terms of performance or competence, "shall" ensure that procedures to assess the conformity of goods to their standards are non-discriminatory and expeditious, and with respect to persons, services and investments "of all other Parties," "shall endeavour to ensure such non-discriminatory and expeditious treatment."

If these rules had been governing trade within Canada from the time the accord officially came into effect; if, for example, they had been entrenched in the constitution or otherwise made enforceable before the courts and any derogation been transparent, it is fair to say that today individuals and businesses would be facing no discriminatory barriers between different parts of the country. However, despite or perhaps because of the clarity of the general rules, *almost all* of the AIT's sectoral chapters begin with an article stating that the general rules apply only to the extent specifically allowed by the chapter! This means that, in effect, it is left to the specific chapters not only to expand on or, conversely, circumscribe the application of the general principles, but even in some cases to start from scratch in the application of those general principles to the sector. Thus, the reach of the agreement cannot be understood without reference to its sectoral chapters, to which I now turn.

SECTORAL COMMITMENTS

The very idea of sectoral exceptions opens the door to serious gaps between the general rules and their practical application to specific sectors. I will now detail both how the rules are to be applied and what the key exceptions are in six of the sectors covered by the AIT, and the extent to which governments are meeting specific sectoral steps as agreed to in the AIT. With respect to the latter, I have attempted to give an idea of progress accomplished under the agreement in a series of tables. For each sector or group of sectors, the tables

show, in summary form, the specific steps undertaken by governments toward removing discriminatory barriers, and the status of these commitments according to whether they have been acted upon, tangible progress has been made toward them, or conversely nothing of substance has been achieved.

Public Sector Procurement

As with many of the other chapters of the agreement, chapter five on public sector procurement begins by stating that the "general rules" of reciprocal non-discrimination and of transparency do not apply in this case. However, this is redeemed by article 504, also titled reciprocal non-discrimination, which states that non-discriminatory treatment is to be given in any province to goods and services and suppliers from another province. This provision also applies to the federal government, that is, it cannot discriminate between goods, services or suppliers of a particular province and those of another. There are also detailed provisions respecting the valuation of procurement and the procedures for procurement, including the use of source lists, which together are meant to ensure a very transparent system for both suppliers and governments (articles 505 and 506). As part of these measures, all governments were to have designated, by 1 January 1995, an electronic tendering system or newspaper(s) accessible to all Canadians in which it will issue its calls for tenders. As well, a working group on electronic tendering was formed, with the objective of developing a common, or at least fully compatible, electronic tendering system between the parties.

The agreement not to discriminate means specifically, but not exclusively, that practices such as inviting only local suppliers to bid on contracts, the biasing of technical specifications in favour of local suppliers, or the use of preferential margins in order to favour particular suppliers, are generally forbidden for the type of contracts covered under the agreement. The contracts covered by the commitment are those above a certain threshold (\$25,000 for goods, \$100,000 for services and construction), and only those issued by certain entities listed in Annex 502.1A, which includes government departments as well as a large number of public boards, agencies, commissions, councils, offices, centres, foundations, cultural institutions, tribunals, etc. of the public service. Only a few provincially-owned commercial enterprises are listed in this annex. Even then, however, many types of services are excluded from the AIT regardless of the procurement entity, including the purchase of many professional services and of advertising and public relations services.

Other publicly-owned entities, listed in Annexes 502.2A and 502.2B, are at least temporarily excluded from the AIT's procurement chapter. The first of these annexes lists a number of "entities that are not accountable to executive branches of governments of the Parties, entities whose object is national security, businesses of a commercial nature or in competition with the private

sector, and state monopolies involved in the transformation and distribution of goods and services," in particular a number of publicly-owned electric utilities and liquor boards. With respect to these entities, negotiations are to be completed by 30 June 1996 that would list them definitely into 502.1A (i.e. covered by the non-discrimination provisions of the chapter), or in 502.2B. The latter annex lists entities covered by non-intervention commitment, that is certain "entities that are businesses of a commercial nature or in competition with the private sector, and state monopolies involved in the transformation and distribution of goods and services" for which we are pleased to learn that governments "shall not direct those entities to discriminate" against out-of-province suppliers, "including those related to construction."

In the meantime, governments may not direct the procurement of those entities remaining in 502.2A, except in accordance with the provisions of the chapter concerning regional and economic development. These state that a government may "under exceptional circumstances" exclude a procurement from the applicable provisions of the AIT for regional and economic development purposes, although notice must be given of the exceptional circumstances. Governments may challenge the extent or effect of the use of this exception by another government (article 508).

Annex 508.3 contains a list of regional and economic development policies and programs at the federal level and in BC, the two territories, PEI and Newfoundland, that will be allowed to continue even though they would otherwise not conform with the procurement chapter. But provinces maintaining such policies or programs must prepare an annual written report on them, and must submit these to review by 1 January 1998 "to ensure that they meet their regional and economic objectives" (article 508.4). In general, each government must report annually on the number and aggregate value of procurements equalling or exceeding the above-mentioned threshold values, as well as an estimated total value of procurements falling below the threshold for the three broad categories of goods, services, and construction (article 511.1). As well, governments must report on the value of procurement above the threshold but excluded from the provisions of the chapter for various reasons (including regional and economic development).

Each party must also provide, annually, basic information on its procurement procedures, such as names of contact points that each party must designate under the agreement and how to register on a source list. The Secretariat is to compile this information into similar format for each government, and this information is then to be published as an annual advertisement (article 511.6).

As well, before July 1996 and each March thereafter, the parties are to review whether the procurement chapter is meeting its objectives, assess and if necessary adjust threshold levels, and otherwise review the chapter and assess opportunities to include procurements that it does not cover. These findings

and any recommendations are to be presented to the CIT for inclusion in the agreement's annual report (article 516.1).

The provinces also agreed to extend coverage of the AIT's procurement chapter to municipalities and municipal organizations, schools and publicly-funded academic, health, and social service entities by 30 June 1996, with negotiations to be completed by June 1995 (article 517).

Finally, the procurement chapter also contains a bid protest procedure, which will be reviewed below in the discussion on dispute settlement. However, I will note here that the bid protest procedures will initially be different for provincial and federal contracts, and that the parties committed themselves to issue recommendations toward harmonizing or reconciling these procedures "no later than three years" after the AIT came into effect, that is, by July 1998 (article 516.4).

As Table 1 indicates, some progress has been made on the AIT's procurement undertakings, particularly with respect to establishing a national, electronic contract tendering system. Regarding the incorporation of the MASH sector into the agreement, the deadline originally envisaged has come and gone, although we can be encouraged by the fact that a draft proposal to this effect is circulating. Governments obviously do not agree on this draft proposal, and it would probably be valuable to circulate it or a summary of the issues outstanding, so that the process in this instance may be spurred by public debate. A more bothersome issue to me, although less immediately important in terms of potential economic benefits, is that some of the key reports mandated by the agreement with the goal of fostering the emergence of non-discriminatory and transparent procurement practices, have either been issued sporadically, or have not yet been approved for public consumption. This is difficult to understand, because these undertakings do not involve negotiations between provinces, where deadlines may be missed because of disagreements among governments, but only require each to report on their current procurement practices. If the time or funds allocated toward the release of these reports are not realistic, then they should be reappraised, but it is vital for the success of the procurement portion of the agreement — which relies a lot on accurate and transparent information — that the information which was to be issued be produced and made public.

**Table 1: Non-Discrimination in Public Sector Procurement,
Status of Steps to be Taken under AIT**

<i>Measure</i>	<i>Completed</i>	<i>Progress/ Partial</i>	<i>Not Done</i>
Designate contact points for complaints by suppliers and other governments	Yes		
Establish working group on electronic tendering	Yes		
Designate common electronic or newspaper tendering system by January 1995	Yes, late		
Annual report on value of procurement		1995/96 done, but not approved by ministers	
Annual written report of non-conforming regional development policies and programs		1995/96 done, but not approved by ministers	
Review of non-conforming regional development programs by January 1998			Still within deadline
Information on basic procurement procedures to be advertised annually			X
Annual report to CIT on the operation of the chapter and recommended changes		Only one report issued	
Extend to MASH by June 1996		Draft proposal only	
Definite listing of certain entities as covered or not		Proposals have been submitted	
Recommendations to reconcile provincial and federal bid protest procedures by July 1998			Still within deadline

Investment

The general non-discrimination principles of the AIT are being superseded, in chapter 6 on investment, by a slightly differently worded article which states that an investor from across Canada will, in any province, receive at least the best treatment given to any other Canadian investor in that province (article 603), although measures inconsistent with this undertaking are still permissible if they meet a "legitimate objective" test which is also worded slightly differently than the general test described above (essentially making it more consistent with investment instead of trade issues). Article 603 also specifies that there will be no difference in the treatment accorded, in "like circumstances," to out-of-province firms established and carrying their activity in that province relative to that accorded to local firms. Furthermore, under article 604, governments cannot impose local presence or residency requirements as a condition of establishment, acquisition or carrying on business in a province.

The investment chapter's commitments regarding local presence and residency requirements did not, however, apply immediately to measures contravening them at the time the agreement was implemented. Respecting these, governments were to have listed by 31 December 1995 any existing measure inconsistent with the agreement, and governments were to have made recommendations to the committee regarding the appropriateness of retaining, removing or replacing these measures by 31 December 1996.

Other parts of the chapter forbid governments to condition the receipt of an incentive (e.g., a subsidy) on the recipient achieving a certain level of local content or on purchasing goods and services locally, and forbid discrimination in the receipt of incentives based on ownership or location of head office (within Canada) in the availability of incentives. Article 612 also builds on the AIT's general transparency provisions, by requiring the parties to promptly make relevant measures available, to simplify any reporting requirements, and to facilitate the development of electronic databases on investment-related programs and measures.

An important annex (608.3) contains a code of conduct on incentives (ranging from cash grants to price support, but excluding general investment promotion activities such as market information) adopted as part of the AIT negotiations. Under the code, the parties promise not to use such incentives to induce the relocation of an enterprise's existing Canadian operation from one province to another, or to undercut a Canadian competitor in obtaining a specific contract within Canada, and in general to agree that they will try to avoid incentives that "harm the economic interests of other Parties," such as sustaining non-economically viable operations in one province that compete with facilities in another province.

Finally, in order to carry out the obligations of the chapter such as the listing of incompatible existing measures and helping parties through consultation procedures in the event of disputes, the parties have established a Working Group on Investment. The WGI must also prepare an annual report on incentives for submission to the committee, including a report on any matters that have given rise to consultation between the parties.

As indicated in Table 2, partial progress has been accomplished on a few steps agreed to in the AIT's investment chapter which concern negative integration, but the key outcomes, the elimination of local presence and residency requirements and the publication of an annual report on incentives, have not yet been achieved, and are clearly past their deadlines. Particularly as some disputes have erupted with respect to the code of conduct on incentives (see below), the absence of an authoritative report on such incentives is an impediment to the well-functioning of the agreement.

Table 2: *Non-Discrimination in the Treatment of Investors, Status of Steps to be Taken under AIT*

<i>Measure</i>	<i>Completed</i>	<i>Progress/Partial</i>	<i>Not Done</i>
Set up Working Group on Investment	Yes		
List existing presence and residency requirements by December 1995	Yes, list awaits CIT approval		
Recommend steps re: presence and residency requirements by December 1996		Awaiting approval of ministers	
Annual report on incentives		1995/96 reports submitted. Await ministers' approval	

Labour Mobility

As with many other chapters of the AIT, chapter 7 on labour mobility begins by stating that the *general* rule of reciprocal non-discrimination is not applicable to this specific chapter, although the general rule on transparency applies. Instead, as I will detail here, there are specific commitments not to discriminate in certain key practices affecting labour mobility.

The chapter's obligations apply to measures such as occupational standards, licensing, certification, registration and residency requirements of workers,⁹ which create barriers to labour mobility (article 702). Governments are also committed to seek compliance "within a reasonable period of time" with the obligations of this chapter with other public sector and non-government bodies (such as professional corporations, regulatory bodies, trade unions or industrial associations) falling under their jurisdiction and exercising an authority delegated by government over the establishment, assessment and recognition of standards related to licensing, certification or registration.

Much of the AIT's labour mobility provisions concern the mutual recognition and reconciliation of standards (on this, see article by Robert Knox in this volume), but as I have said the chapter also makes explicit commitments not to discriminate. Under article 706, governments cannot impose residency requirements as a condition for access to employment opportunities, licensing, certification or registration of workers, or eligibility for a worker's occupation. More broadly, workers from across the country are to be accorded in any province a treatment at least as favourable as that awarded to that province's own workers. Article 707 contains some detailed commitments that have the effect of strengthening the non-discrimination provision with respect to licensing, certification, and registration measures. These include an understanding that they will relate principally to competence, that there will be no unjustified delays or cost differentials for out-of-province workers and, regarding transparency, that these measures be "published or otherwise accessible."

In keeping with the agreement's general philosophy, measures that do not conform with these non-discriminatory provisions are still permitted, where the purpose of the measure is to achieve "a legitimate objective," and meet certain tests ensuring, notably, that it is not more trade-restrictive than necessary and does not create a disguised restriction to mobility (article 709.1). However, the definition of "legitimate objective" specifically as it applies to the labour mobility chapter is broader than that generally in effect through the agreement. It includes "provision of adequate social and health services to all geographic regions" of a province, and the more nebulous category of "labour market development."

Under the AIT, the Forum of Labour Market Ministers ("the forum," which predates the AIT) is responsible for developing a framework permitting governments to "establish and review annually" a list of discriminatory measures falling under the "legitimate objective" rubric and meeting the tests just mentioned, that is, a list of permissible discriminatory measures. Governments are to participate in this exercise by giving written notice of all discriminatory measures adopted or maintained under the "legitimate objective" exemption. The notice "shall indicate the Party's justification for the measure and the anticipated duration of the measure" (articles 709.2 and 709.3). In

addition, compliance with the AIT may be suspended for a period of six months (renewable), but only under exceptional and tightly controlled (by the other parties) circumstances. A contact person is to be designated by each party to receive complaints from other governments concerning the interpretation or application of the labour mobility chapter, and complaints from persons (workers, employers, etc.) regarding a party's actual or proposed measure (article 711). The forum also established a Labour Mobility Coordinating Group (LMCG), composed of the contact points, in order to coordinate the chapter's implementation on the FLMM's behalf.

In addition to these specific steps, the AIT also requires the forum to "develop a workplan for the implementation" of governments' obligations under the labour mobility chapter, and to "produce an annual report on the operation" of the chapter. The annual report is specifically to include (under article 712) an assessment of the chapter's effectiveness — and recommendations to remedy any concerns with respect to the effectiveness — as well as a report on any disputes on the interpretation and application of the chapter, and on steps to resolve them. Governments are to report on such compliance through assessments and the annual report prepared by the forum.

The status of specific steps to be taken under the AIT's labour mobility chapter toward the removal of discriminatory barriers is shown in Table 3.

As explained above, the ability for individuals to move where they perceive their best earnings opportunities to be, without sacrificing certain basic tenets and advantages of Canadian citizenship, is one of the principal advantages for Canadians of the economic union. Even if they did not move in search of opportunities across the country, the ability to do so is still worth something to each individual, in that it reduces his or her economic risk of engaging in a particular occupation. In the event, hundreds of thousands of Canadians move across the country every year, with every province experiencing significant two-way population flows.

In that light, it is gratifying that some significant progress on removing discriminatory barriers has been accomplished under the labour mobility chapter of the AIT. In fact, the LMCG has initiated some key measures not expressly called for under the "priority for action" guidelines for developing the workplan (outlined in Annex 712.2). These include notably a survey of practices (which was answered by 300 of the 400 occupational regulatory bodies asked to participate), guidelines to assist regulatory bodies to comply with the chapter, and a communications strategy designed to implement the chapter. In addition, the federal government is offering financial support to help regulatory bodies comply with their obligations.¹⁰

Clearly, section 6 of the Charter will remain the cornerstone of individual mobility rights across Canada, but actions taken under chapter 7 of the AIT have also advanced the cause of mobility in a proactive fashion, as it relates to skilled workers and regulatory bodies by bringing most relevant non-

Table 3: *Non-Discrimination in Occupational Standards and Requirements, Status of Steps to be Taken under AIT*

<i>Measure</i>	<i>Completed</i>	<i>Progress/Partial</i>	<i>Not Done</i>
Framework to list and review all discriminatory measures	Framework in place		
Governments give notice of all discriminatory measures, justification, and anticipated duration			No measures to be listed
Annual review of discriminatory measures		Ongoing – part of annual report	
Develop workplan to implement chapter	Yes, initial workplan and subsequent workplan (1996/97)		
Seek compliance with wide public sector and non-government bodies			Four hundred regulatory bodies invited to comply on 1 July 1996
Parties to designate contact points to receive complaints	Yes (turned into Labour Mobility Coordinating Group)		
Annual report by Forum of Labour Market Ministers			1995/96 Report has been published

government bodies into a process similar for all, and where all are working under the same guidelines and toward clearly established objectives. The caveats here are that such work is still very much in progress, and that, when the provinces feel they have the power to threaten another with retaliation for measures to which they object, they will do so, as demonstrated in the case of the dispute over the right of Ontario construction workers to work in Quebec, which flared up again shortly after the entry into force of the AIT. Nevertheless, in the latter case, the dispute was resolved along lines compatible with

the obligations of the labour mobility chapter, and recourse to the dispute settlement mechanism would clearly have been available in the event a similar dispute involved a complaining province which did not have the economic clout necessary to retaliate.

Consumer-Related Measures and Standards

With respect to consumer-related measures and standards (chapter 8 of the AIT), the agreement's general rules of non-discrimination and transparency are meant to apply in their integrity. Much of this chapter is concerned with the harmonization of standards (i.e., positive integration) in three specific areas. Provisions related to negative integration include the elimination of differences in licensing, registration, and certification fees in any province between suppliers based in that province and others in Canada, except to the extent that the difference reflects actual costs (article 805, taking effect on 1 July 1996). The AIT also forbids requiring residency as a condition for awarding licensing, registration, or certification in a province (article 806). Likewise, any requirement imposed on suppliers as a condition of licensing, registration, or certification, (such as maintaining a place of business or an address for service, post a bond, etc.) is only allowed to the extent necessary to achieve a legitimate objective.

As with the labour mobility chapters, the definition of "legitimate objective" differs from the one given under the agreement's "general" principles, but in this case seems more restricted, focusing on the right of parties to establish the level of consumer protection it considers "appropriate," when this is done to achieve "the protection of the personal safety of consumers or the economic interests of consumers [including contractual fairness, protection of privacy, etc. as defined in the agreement]" (articles 803, 804 and 810).

In addition, article 809 requires the establishment of a Consumer Measures Committee, which is enjoined, under article 808, to report, "no later than 1 July 1997" on agreements concluded by governments on mutual enforcement of standards (e.g., reciprocal investigative powers and enforcement of judgments), and under article 810 to develop dispute resolution mechanisms specific to the chapter (to be used, as with all chapter-specific dispute resolution procedures, before a dispute can proceed to the overall agreement's dispute settlement mechanism, see below).

The status of steps to be taken under the AIT's chapter on consumer-related measures and standards is shown in Table 4 below. The table shows that, even with these straightforward requirements not to discriminate, and the relatively narrow range of harmonization measures contemplated under the chapter, it appears that certain steps required under the agreement are still posing some difficulty, although progress has been made in all areas.

Table 4: Non-Discrimination in Consumer-Related Measures and Standards, Status of Steps to be Taken under AIT

<i>Measure</i>	<i>Completed</i>	<i>Progress/Partial</i>	<i>Not Done</i>
Establish committee on consumer-related measures and standards		Yes	
Develop appropriate DSM before July 1995		Approved by ministers, but not yet adopted	
Eliminate discriminatory fees by July 1996	Yes		
Report on cooperation and mutual enforcement by July 1997		Preliminary report out	
Submit annual reports for transmittal to committee	Yes		

*Agricultural and Food Goods*¹¹

General rules of non-discrimination and transparency apply to this chapter of the agreement (chapter 9). However, because the chapter explicitly applies to measures identified as "technical barriers to trade" by the federal-provincial Agri-Food Inspection Committee (the "inspection committee"), the reach of the chapter is determined in practice by the various agriculture ministries represented on the committee. By "technical barriers," it is meant such things as differences in product, process or packaging standards or transport regulations, and not policies such as supply management and financial assistance programs (many of which are contentious but, according to an annex to the chapter, are currently being addressed through the Agri-food Policy Review).

Few provisions of this chapter deal with specific discriminatory barriers. There is a prohibition on "arbitrarily or unjustifiably" discriminating in the application of sanitary and phytosanitary measures (article 904). With respect to other measures, the signatories agree more generally not to amend an existing measure, or adopt a new one, so as to restrict trade in an agricultural or food good (article 905), that is, a standstill provision.

Under article 902, the inspection committee provided the CIT, before the entry into force of the AIT, with a written notice of measures identified as

**Table 5: Non-Discrimination in Agricultural and Food Goods,
Status of Steps to be Taken under AIT**

<i>Measure</i>	<i>Completed</i>	<i>Progress/Partial</i>	<i>Not Done</i>
Inspection committee to list technical barriers to trade before July 1995.	Yes		
Include barriers "with policy implications" in the coverage of the AIT by September 1997	Yes		
Ministers to review chapter coverage by September 1997		Delay requested by ministers	
Public notice of all new measures and amendments ahead of implementation	Yes		

technical barriers, following which specific measures to remove those "with policy implications" were in the "scope and coverage" of the agriculture chapter. Some clearly discriminatory measures have fallen under this provision of the AIT, including Ontario, Quebec, and Prince Edward Island regulations on coloured margarine designed to keep out-of-province producers from the domestic market. By 1 September 1997, the agriculture ministers were also to have reviewed the chapter and any recommendations for change, with a view to achieving "the broadest possible coverage" under the chapter, but this deadline was extended at their request.

It is striking that, unlike other sectors covered by the AIT, the obligation of agriculture ministers to report to the CIT is minimal in the case of agriculture. Along with other provisions of this chapter, this suggests that the process is to be squarely controlled by the various departments of agriculture.¹² Furthermore, no periodic report on any of the operation of this chapter seems to be required. On the plus side from the point of view of eliminating discriminatory practices, the chapter does build quite a bit on the AIT's general transparency provisions with respect to new measures or amendments to existing measures that may affect trade in agricultural or food goods. These changes are to be published and submitted to other agricultural ministers at least 20 days prior to the adoption or amendment of the measures, and other governments and any interested persons are entitled to have their comments on the measures taken into consideration (article 907).

Included as a barrier with "policy implications" in the AIT's coverage has been Quebec's regulation prohibiting margarine sold in the province to be coloured like butter. However, it seems clear that the province, despite initial promises to act on this matter under the AIT's agricultural chapter, will not comply in this case, which, while not imposing huge costs on other provinces as a whole, is a major irritant for the (mostly Ontario-based) margarine producers involved.¹³ It appears that this particular trade restriction will be challenged under the DSM provisions of the AIT, which would be a major step in removing discriminatory barriers in the agri-food sector in Canada.

Alcoholic Beverages

The general rules of reciprocal non-discrimination and transparency, as well as the general definition of legitimate objective, are said to apply to the AIT's chapter on alcoholic beverages (chapter 10), in particular with respect to listing, pricing, access to points of sale, distribution, merchandising, and cost of service fees and other charges (article 1004) levied by the competent authorities overseeing the alcoholic beverage market in each province.

In practice, however, many provinces have reserved the right to continue certain measures that do not conform with these general rules. The hope for improvement here results from promises made in the AIT that all these measures will be reviewed before a certain date, namely 1 July 1996 for differential floor pricing mechanisms for beer maintained by Nova Scotia, the differential cost of service or other charges maintained for beer by New Brunswick and Quebec, and Ontario's application of its Canadian grape content requirement; and 1 December 1999 for Newfoundland's measures denying access for out-of-province beer to its outlets of brewers' agents. However, governments will still be able to apply certain measures specifically authorized by international trade agreements, such as measures in Ontario and British Columbia requiring private wine store outlets to discriminate — to an extent — in favour of provincial wines, and measures in Quebec requiring any wine sold in grocery stores to be bottled in Quebec (although the province must open other outlets to wine bottled outside the province). In this light, however, British Columbia and Quebec have agreed to negotiate reciprocal equivalent access for wine and wine products by 1 July 1996. Table 6 shows that progress on these promises to review or remove even partially the remaining discriminatory barriers to trade in alcoholic beverages has been slow, or has not lead to the hoped-for result.

Governments also agree to report annually to the CIT on whether there have been any complaints made under the chapter's dispute settlement procedures, on whether there are any changes proposed to the chapter, and on any "arrangement proposed or entered into under article 1800 (Trade Enhancement Arrangements) relating to trade in beverage alcohol products."

**Table 6: Non-Discrimination in Alcoholic Beverages,
Status of Steps to be Taken under AIT**

<i>Measure</i>	<i>Completed</i>	<i>Progress/Partial</i>	<i>Not Done</i>
Review Nova Scotia differential floor pricing for beer by July 1996		Review done, but no change	
Review New Brunswick and Quebec differential cost of service and other charges by July 1996, where other parties also effectively maintain higher charges		Ontario still working on its charges; NB said it will not remove its charges	
Ontario Canadian grape content requirement to be reviewed by July 1996	Ontario will meet 1999 removal deadline		
Quebec and BC to negotiate equivalent access for wine by July 1996		Still at discussion stage	
Newfoundland's measures denying access to its brewers' agents outlets to be reviewed before December 1999			Still within deadline
Parties to report annually to the committee		First draft of 1996/97 report	

DISPUTE SETTLEMENT: THE PROOF OF THE PUDDING

ROLE AND COVERAGE OF THE AIT'S DISPUTE SETTLEMENT PROCEDURES

As we have discussed, the observance of many of the commitments entered into by governments in the AIT with respect to "negative integration" involves not specific actions or steps, but rather refraining from acting in a non-discriminatory way. It is difficult for an outside observer to judge whether this last commitment is being honoured on an ongoing basis. However, governments can be taken to task, through the agreement's dispute settlement process, by those (governments or persons) who feel that existing or proposed measures discriminates against them on the basis of provincial residence or

place of business, and are therefore contrary to undertakings made in the agreement.

Although other institutions set up under the AIT, either at the ministerial decisionmaking level (e.g., the Committee on Internal Trade) or at the technical level (the Secretariat), allow for ongoing informal discussions of potentially contravening measures, the AIT's dispute settlement mechanism (DSM), set out in chapter 17, is the only available venue for formal testing of a particular measure by a government against the promise it has made not to discriminate. In particular, it is the only available forum in which the "legitimate objective" defence, which governments can raise in order to justify an otherwise discriminatory measure, can be formally tested.

Indeed, the dispute settlement mechanism of the AIT is focused almost entirely on enforcing the negative integration or non-discrimination aspects of the agreement. The agreement's DSM cannot, in general, be invoked in cases where governments allegedly fail to comply with their "positive" obligations or undertakings under the agreement, such as commitments to harmonize standards in a number of areas. And even this enforcement ultimately relies not on a legal obligation to remove an offending measure — since the agreement is not a legal document — but in large part on the willingness of governments to heed the decisions of the independent panels, which are the last possible stage of adjudicating a dispute under the AIT (the agreement also contains provisions for applying various degrees of moral suasion and even retaliation on governments not conforming with panel decisions, but retaliation is not likely to be an effective weapon in most cases, mostly because the type of simple retaliatory measures available between countries would, happily, be unconstitutional within Canada, while other types of retaliatory action authorized under the AIT might be more administrative trouble than they are worth).¹⁴

Within these limitations, there are two types of general dispute settlement procedures under the AIT. One concerns disputes brought by governments against other parties to the agreement, including on behalf of citizens or businesses having a "substantial and direct connection" with it (such as a place of business or residence). The other concerns disputes brought up by citizens against any government. The main difference between the two is that citizens can only bring up cases which their own government is unwilling to take up, and are obliged to go through an independent "screener," a type of ombudsman who will make sure there is some substantial basis to the case, before a complaint can proceed to the DSM.

There is considerable emphasis in the AIT, as indeed increasingly in international agreements, on dispute "avoidance" mechanisms, in the sense of requiring the complainant and the party complained against to endeavour, within a certain period, to settle a question amicably, and if needed, to seek expert advice before taking more confrontational steps. Thus, in the AIT,

complaining provinces are expected to make use of the specific procedures for consultation, mediation, and conciliation contained in sectoral chapters and in chapter 17 itself, before moving to intervention by trade ministers in the dispute, and ultimately, to public adjudication of a dispute by an impartial panel (private complainants are expected to follow a similar route after receiving approval from the screener, and may be awarded costs if successful, but not damages or injunctive relief).¹⁵ However, even the consultation step can be considered part of the dispute settlement process from the moment it is invoked, and parties are to notify the Secretariat of their use of this and other successive steps involved in the DSM.

As is the case with international agreements such as the NAFTA, the government procurement provisions of the AIT are subject to a "bid protest" procedure separate from the agreement's overall DSM. Under this procedure, bidders may enlist their provincial government to challenge the way contracts have been awarded in another province, and their complaint may ultimately be examined by a bi-provincial review panel, which will assess whether the procurement practices conformed with the AIT (article 513). In the case of federal procurement, suppliers may lodge a protest directly with an independent reviewing authority (article 514). However, when a supplier's government is unwilling to take up its case against another province's entity, the supplier may use the chapter 17 procedures for person-to-government complaints. A provincial government may also use the government-to-government dispute settlement procedures in chapter 17 when it takes up a complaint against a federal government entity on behalf of one of its residents.

To give effect to the DSM, governments agreed to take a number of steps, including naming contact points for receiving complaints under certain chapters (article 512 for procurement, article 711 for labour mobility), naming rosters of panelists to sit on procurement disputes "before the entry into force of this agreement" and deliver notice of the roster to the other parties (article 513.7), and, with respect to the general dispute settlement, maintain a roster of panellists (article 1705) and establish "before the date of entry into force of this Agreement," model rules of procedures for the panels (article 1706). The seriousness with which governments view the prospect of any measure being overturned by an independent panel can be gauged by the fact that many of these panelists are well-known Canadians whose decisions in these matters would, if they were asked to pronounce on an internal trade issue, likely be respected by the public at large.

THE EXPERIENCE WITH DISPUTE SETTLEMENT TO DATE

The exact number of recourses to the AIT's dispute settlement process and current status of complaints has not been published, unlike what is available, for instance, through the WTO or the NAFTA for disputes pertaining to these

agreements. Therefore, the numbers I will cite below result from a compilation based on data which are possibly incomplete or subject to revision. I have not been able to distinguish between those complaints that concern discriminatory measures, and others concerning a failure to harmonize. But as noted above it is almost impossible to lodge a complaint against a government for not fulfilling a promise to harmonize ("positive integration"), whereas they can be taken to task for instances of discrimination as defined by the agreement.

Some analysts have described the AIT's DSM as "dormant,"¹⁶ and headlines concerning the few disputes that have made a public impact have on occasion suggested that the process was easily stalled, in turn putting the entire agreement in jeopardy.¹⁷ In fact, while it is true that no dispute has yet reached the crucial stage of being adjudicated by a panel, if one considers that any complaint passes through an obligatory stage of consultation as part of the DSM, it appears that both governments and private agents have made substantial use of the dispute provisions of the agreement. In the first two years since the coming into effect of the AIT:

- There have been close to 40 complaints made under the agreement's provisions, of which a dozen or so were entered into by governments against other governments, and the rest were entered into by private parties against governments.
- The party complained against most often under the provisions of the AIT has been the federal government (all but one of these complaints has come under the procurement chapter), followed at a distance by Ontario and Saskatchewan, then British Columbia, Quebec, New Brunswick, and Alberta. Only Nova Scotia and the Yukon have never been complained against under the agreement.
- Complaints have arisen most often under the labour mobility and procurement chapters, followed as a distant third by the investment chapter. Together, complaints arising under these chapters have made up about 80 percent of the cases. There have also been complaints under the alcoholic beverages, transportation, and environment chapters.
- An important indicator in my view is that most provinces have intervened at one time or another in the government-to-government dispute settlement process. This is important, because, once a province begins to rely on the DSM to secure compliance with the AIT by others, it can hardly deny other provinces or individuals the use of the same mechanism with respect to its own policies.

However, there are also troublesome facts regarding the use of the DSM, which probably account for its reputation of ineffectiveness:

- Few of the complaints have actually been resolved by changes in the practice complained against. Partly, this is because a significant number of complaints (about a third) were found at an early stage to be without foundation, either because they were not falling under the purview of the AIT, because the complainant lacked standing, or because the measure complained against had already expired. But most of these cases occurred in the first year of operation of the agreement, suggesting that perhaps a learning curve was involved. In fact, the 25 percent or so drop in the total number of cases between 1995-96 and 1996-97 is entirely due to the drop in the number of such "non-starter" complaints, and a plausible explanation for this is that complainants have started "picking" their cases better.
- More worrisome is that many complaints identified as legitimate rarely seem to be resolved quickly. Another third or so of the complaints, some dating back almost two years, seem to be stuck at the "chapter consultation" stage, or such other low intergovernmental stage of the DSM. In fact, over the entire history of the DSM, only one dispute has ever required consultation among CIT ministers, the last possible stage before adjudication by a dispute settlement panel. That complaint (by British Columbia against New Brunswick against incentives provided to UPS to expand its New Brunswick operations) was eventually dropped. The fact that more complaints have not reached higher levels of confrontation is not an indication of ineffectiveness per se of the DSM, since some complaints actually have been resolved at the lesser ("chapter") levels or, in the case of complaints against federal procurement practices, by an independent reviewer. But the number of complaints still pending and the lack of use of either the CIT or panels to resolve them also suggest the possibility that parties may try to avoid an impartial adjudication of the disputes altogether.
- Of the other third or so complaints that were allowed to proceed and that have come to a conclusion, almost as many have been dropped by the complainant as have resulted in corrective action. Although this may well mean that the party complained against was able to justify its measures vis-à-vis the complainant without having to go to a dispute settlement panel, which in principle is the more advisable route if indeed the measure did not contravene the AIT, it also means that the DSM has been pretty limited as a force of actual change in government practices.

Thus, while it cannot be concluded that the AIT's dispute settlement provisions have been ineffective — too many cases remain pending to form such a

judgement yet — they certainly have had a very limited impact on reforming measures affecting internal trade. The fact that disputes involving the provinces have usually ended at some low level of intergovernmental consultation suggests either that problems can genuinely be solved at these levels, or that governments are reluctant to bring impartial advice to bear in complaints against them, an interpretation that seems bolstered by the large number of yet unresolved disputes.

CAUSES OF SHORTCOMINGS AND OPTIONS FOR IMPROVEMENTS

WHY CERTAIN UNDERTAKINGS WERE NOT MET

Shortly after the AIT was signed, severe criticisms were published of the very idea of relying on such an intergovernmental agreement to promote a more open and integrated internal market in Canada.¹⁸ Since then, unflattering comments have appeared from both critics and supporters-in-principle of the AIT, regarding progress accomplished so far under its auspices, as measured against the agreement's own promises to remove barriers. For example, the authors of a study published last year by the Organization for Western Economic Cooperation wrote that the AIT "held the potential to move towards a Canadian common market, but has seen only limited success." The Canadian Chamber recently issued a report which said that the AIT required "political will" in order to be "transformed into an effective instrument to seize the opportunities for enhanced internal trade."¹⁹ And by the AIT's Secretariat own admission, "A number of administrative matters, required by the Agreement, remain to be completed [as of 31 March 1997], including rosters of potential panellists, lists of contact points and some information reports." The Secretariat adds that "Governments are committed to dealing with these matters during the next year or reconsidering their function within the Agreement."

As we have seen, the implementation of the provisions of the AIT has indeed been slow, relative to the pace which the signatories had set for themselves at the time the accord was signed. In addition, implementation has not been as transparent as one might have hoped based on promises to release reports on the implementation of various chapters and on remaining barriers.

Abundant speculation, as well as logic, suggest what the reasons for these delays and lack of transparency might be, although little discussion of them can be found in the sparse literature on the topic. Before recommending avenues for improvement, it is worth listing these possible causes. They are:

- *Costs of money and time.* It is conceivable that certain promises made under the accord were unrealistic in terms of the budgets of people and money which governments were willing to lend to the project.

Part of this may be due to the large differences in population and economic size between the partners, the smaller partner tending to have a difficult time finding the resources to issue, or respond to, challenges under the agreement and fulfil their reporting and other obligations. The fact that, according to the Secretariat, governments may "reconsider" the function of some of the agreement's undertakings suggests that for some, the benefits are not worth the costs involved.

- *The political calendar.* Another reason may be that, following the major negotiating exercises of 1993-94, which preceded the agreement, governments considered the main job done and devoted attention to other priorities. The AIT was signed in July 1994, and although both the Conservative government defeated in 1993 and the succeeding Liberals were equally supportive of the agreement, the period since its signature was rich in changes to the Canadian political landscape, ranging from politically absorbing fiscal and social reforms in many provinces to the events related to the close Quebec sovereignty referendum, which may have left the single Canadian market far behind in terms of priorities.
- *Lack of political pressure.* A more serious problem than the political calendar itself may be the lack of pressure on the part of business people, professionals, tradespeople, and others potentially affected by the barriers existing within the Canadian market. It is true that large business organizations and some professional groups, as well as economic think tanks and many individual academics, have periodically voiced their concerns that unnecessary barriers — including most existing discriminatory barriers — were impeding the well-functioning of the Canadian economic union and denying fundamental rights of citizenship. These accumulated concerns were probably the main intellectual force behind the AIT negotiations. However, governments would implement the agreement far more vigorously if they were submitted to ongoing political pressures to do so: if, for example, they were faced with a steady stream of delegations of firms and individuals urging that this be done. But clearly they are not. A possible reason for this, in my view, includes lack of knowledge of the opportunities and reduced economic risks which a truly well-functioning agreement would confer on many Canadian firms and individuals, perhaps combined with a general impression, engendered by the very existence of an agreement, that the issue is already being dealt with.
- *A flawed bargaining mechanism.* An even more serious obstacle to the implementation of the AIT may arise from flaws in the agreement itself, in particular in its decisionmaking structure. Instead of adopting the

model used to complete the Single European market, that is, use a qualified majority voting procedure to decide on specific technical measures to implement the goals *which have already been unanimously agreed upon*, the principle of consensus is carried into each minute, technical negotiations, which gives an extraordinary leverage to a single province wishing to hold onto a particularly sensitive barrier. The latter can just say no, as seems to have happened in a number of cases already. This flaw is exacerbated by the fact that there are no independent experts or body (as with the EU's Commission) recommending technical measures to be adopted to fulfil the AIT's obligations. This means that in many cases it is left entirely to the very officials previously in charge of maintaining the barriers to propose ways to remove them, or to explain why it cannot or should not be done, a process that clearly runs the risk of generating only minimal progress.

- *Fear of legitimizing the AIT.* Finally, and not unrelated to the previous point, it is not inconceivable that governments fear legitimizing the agreement by aggressively demanding that other provinces or the federal government submit to their AIT obligations, or by pursuing disputes through the AIT's settlement mechanism, even if they had a legitimate trade complaint against another government. Clearly, if one signatory begins to do so, its own policies will likely come under closer scrutiny by others and members of the public, a situation that governments may not want to face. In this respect, it will be interesting to see whether the Government of Ontario takes up the case of its margarine producers against Quebec restrictions on margarine colouring by using the government-to-government provisions of the DSM, or whether it will prefer that the producers involved take up the person-to-government dispute route available under the AIT.

Keeping these possible obstacles in mind, I will now turn to options for improving the pace of implementation of the accord.

OPTIONS FOR IMPROVEMENT

Because of the genuine, if very slow, progress accomplished so far, and the number of issues reportedly at the "progress" stage and disputes at the "consultation" stage, it seems way too early to call the AIT a failure. There is, however, a danger that the agreement, which became possible because it was a comprehensive, carefully balanced package, will unravel if all of its parts are not made to function properly and promptly. I will discuss here some options which have been put forward for giving a new impetus to the AIT itself, and to the process of removing barriers to trade more generally using the AIT as a centrepiece.

Increased Public and Business Awareness and Participation

It is difficult to judge what awareness of the AIT and of its market-opening provisions the public and individual businesses have in general. Perhaps nothing short of a publicity campaign, explaining rights under the agreement, focusing on specific real-life examples, and listing provincial contact points as well as supporting business and professional associations, would drive home the point. In the meantime, it seems absolutely crucial that documents registering both the pace of progress under the AIT and the road left to fulfil the agreement, be published and receive widespread circulation and discussion, as did the annual European Commission review of progress on the White Paper agenda.

It would be well within the mandate of the Secretariat to issue an annual report on the implementation of the AIT's various chapters, including an evaluation of the reasons for missed deadlines and an assessment of outstanding issues. This report should subsume or summarize all other reports which governments are committed to provide under the terms of the AIT, including those on progress toward harmonizing labour standards and on the operation of their regional development programs. In sum, it seems to me that the Secretariat should be given sufficient resources for a one-time campaign of information on the agreement, and commanded directly to get on with the business of producing an overall report on the progress — and failings, including failures to file required reports — under the agreement. Governments should be able to see and comment ahead of time on this document, but not to veto it.

Strengthening the Agreement's Institutions

The federal government should convene a "three-year summit" in June of 1998, to review the functioning of AIT's institutions. In my view, proposals being discussed at the summit should include a clarification and strengthening of the Secretariat's mandate, along the lines of a mini-European Commission (that is, not a decisionmaking body, but with strengthened policy advice and reporting role), and a temporary one at that, focused only on the task of ensuring that all commitments under the agreement are fulfilled.

Specifically, the Secretariat should be able to play a much greater role in monitoring and reporting on obstacles to implementation of the agreement, as well as seeking expert advice in proposing solutions. It could translate this advice into proposals for specific measures. A key reform would be that the CIT should have to formally vote on measures proposed by the Secretariat (or by other governments) to ensure completion of the AIT, with the votes being publicly recorded.

In addition, governments should consider adopting a rule of qualified majority voting, again referring only to those issues which they have agreed to in

principle.²⁰ The point, again, being that since governments have agreed to the principles contained in the agreement, no one government should be able to block implementation.

Finally, governments should commit to have all the promises of the AIT fulfilled by the end of the fifth year of implementation, or 1 July 2000.

The federal government, constitutionally responsible for maintaining the economic union, should be willing to help certain jurisdictions to meet the costs of implementing the agreement and meet the necessary reporting requirements. In addition, since the agreement allows for the recovery of costs but not damages, the federal government should set up a one-off program of challenges designed to help firms, organizations and individuals, test the dispute settlement system, in the public interest, at a reasonable cost to them.²¹

Legislative Options

One key institutional weakness of the AIT is that its provisions have not been made generally applicable through implementing legislation in the various Canadian jurisdictions, unlike the way the European Single Market initiative and the NAFTA, for example, were implemented in their respective member countries. That is to say, AIT implementation remains almost entirely a matter of administrative fiat. Provinces have either passed minor changes to existing statutes or have passed implementing legislation covering mostly housekeeping provisions. Likewise, the federal legislation does not make the AIT directly applicable in federal law.²² As Robert Howse explained, one way of making all or at least some of the AIT's obligations directly applicable would be to embody them in federal and provincial statutes. Of course, these could always be rescinded by the legislatures but, as Howse pointed out, this would attract more attention than flouting the provisions of a non-legally binding accord.²³ Some provinces could take the initiative by passing such laws which would take effect if a critical mass of others did the same thing.

While it is understandable that governments may not want to make all the provisions of this relatively new and untried agreement into law yet, a start could nevertheless be made in certain key areas, perhaps with legislation requiring that governments comply with the key reporting requirements provided for under the AIT.

A bolder avenue would be for the federal government to use its constitutional authority under sections 121 and 91(2) of the constitution, in order to seek the implementation of specific provisions of the AIT, where provinces cannot agree to do so.²⁴ Howse in particular has argued that the legitimacy of the federal government taking such action is actually reinforced by the existence of an AIT: that is, all the federal government would do in this instance is take action for ensuring that what has already been agreed to between it and the provinces is actually implemented. Clearly this is an important option,