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From the Editor

Thirty-five years ago, a small group of people from Vancouver, British Columbia, had an idea. The idea was to create an organization that would conduct independent economic and social research and disseminate its findings, thus offering policy makers better alternatives and stimulating demand for better policies among the populace. In 1974, that idea became a reality and the Fraser Institute was born.

To commemorate the Fraser Institute's 35th anniversary, there will be a special feature in each issue of *Fraser Forum* this year, chronicling the Institute's history while focusing on a number of important milestones. (The first of these articles, which tells the story of the Institute's founding, can be read on pgs. 14–15).

Doing research for these articles has been a fascinating exercise. Over the years, the Institute has produced hundreds of publications; hosted numerous distinguished economists and speakers (including Milton Friedman, Margaret Thatcher, and Steve Forbes, to name just a few); and taken on many other creative projects to promote free market ideas. For example, in the early 1980s, the Institute created its own version of Monopoly called Poleconomy, a game in which players buy, sell, and take over real companies. And in the late 1980s and early 1990s, the Institute actually sponsored a hockey team made up of economics and business students from Simon Fraser University in Vancouver. The team, which won its divisional championship in 1990, was called "The Fraser Institute Right-Wingers."

Looking back, it is easy to see why the Fraser Institute is one of the top think tanks in the world. In fact, in a recent *Foreign Policy* magazine article, which ranked 5,465 think tanks from around the world, the Fraser Institute was ranked:

- 1st of all non-US North American think tanks;
- 3rd of all international economic policy think tanks;
- 7th of all domestic economic policy think tanks;
- 8th of all health policy think tanks; and,
- 11th of all non-US think tanks.

It's difficult to say what 2009 will bring. The world is bracing for difficult economic times. The United States, Canada's most important trading partner, now has a new president. As I write, the fate of Canada's current Conservative government is unknown.

But however the year unfolds, the Fraser Institute will be here, measuring, studying, and communicating the impact of competitive markets and government interventions on the welfare of individuals.

— Kristin Fryer (kristin.fryer@fraserinstitute.org)

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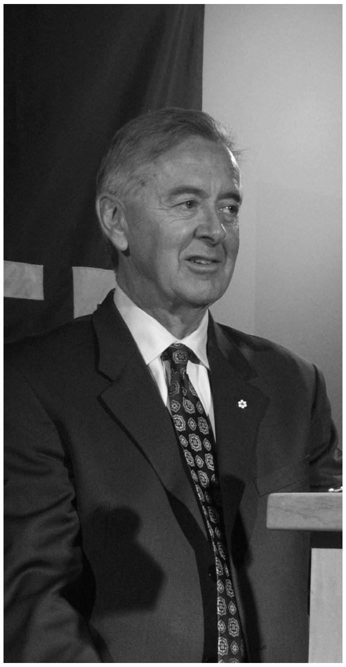

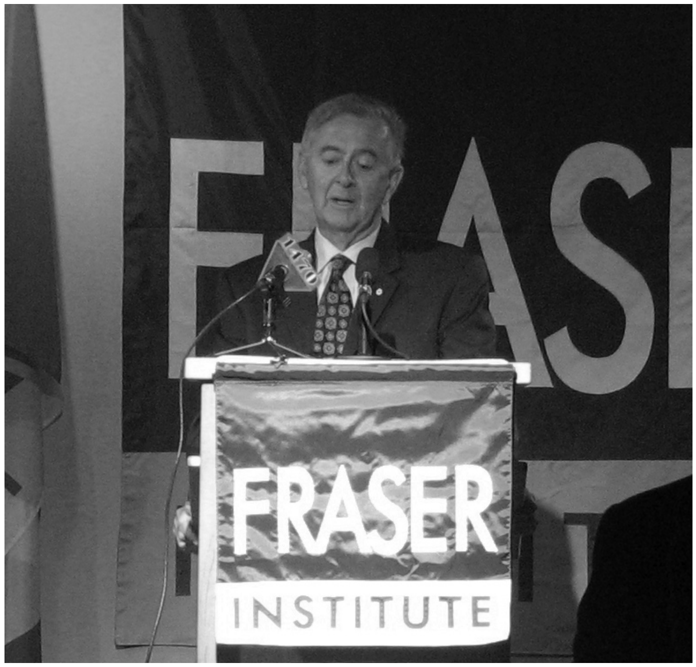

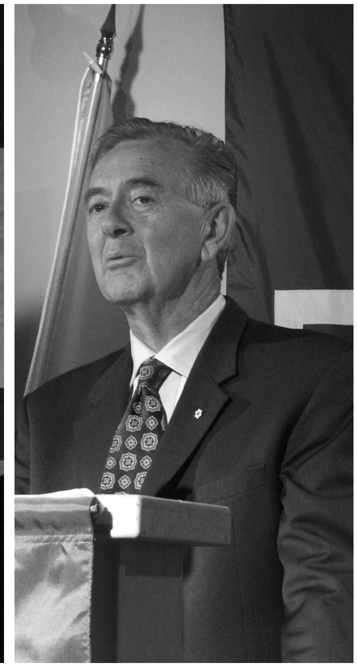

Public policy in tough times

Preston Manning stresses the importance of avoiding deficits

On January 16, veteran politician and Fraser Institute Senior Fellow Preston Manning spoke to a full house at the Institute's Vancouver office, sharing his thoughts on the recent Parliamentary crisis and possible outcomes of the federal budget. This event followed a similar policy briefing held in Calgary in December.

In a FraserTV interview following his Vancouver presentation, Manning expanded on his speech, emphasizing the importance of creating a balance between the role of government and the role of the market.

"Making the rules and creating the macroeconomic framework in which individuals, corporations, and not-for-profit organizations make decisions is the rightful role of government," he said. "The actual creation of wealth and jobs is the challenge of the private sector." Manning added that in this time of economic difficulty, the government should not overstep it role, but should avoid nationalization, protectionism, over-regulation, and deficit spending.

"The orthodoxy that many people are clinging to today is that stimulative spending by governments is the silver bullet that will cure the recession," said Manning, noting that government spending is "not the answer." However, if governments are going to engage in deficit spending, he added, then they must have a concrete "exit strategy," so that deficits do not become chronic or systemic.

He further advised that if governments do decide to invest in infrastructure, then they should do so on the basis of possible return, investing in projects that yield "the fastest and highest socio-economic return."

In his speech, Manning also touched on the future of Canada's relationship with the United States, now that Barack Obama has been sworn in as President.

"A number of observers feel that the new American Congress and administration is going to be more protectionist than the previous one, and that may create problems for Canada as one of the biggest exporters to the United States," he said. Manning believes that Canada's greatest strength in terms of countering such protectionism is its energy resources.

"The United States is quite concerned about continental energy security and is trying to reduce its dependence on offshore petroleum, in particular," he noted. "Canada, with its oil and gas and its hydroelectric exports, can be part of the solution for American energy sustainability."

Manning believes that if Canada emphasizes its ability to supply the United States with these resources, it may be able to gain an exemption from any protectionist measures the US adopts. ◻

A FraserTV video of Preston Manning's interview is now available at www.fraserinstitute.org/frasertv.

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Beware of bailout

"Stimulus" is just another word for corporate welfare

Mark Milke

Just before Christmas 2008, the American and Canadian governments announced a series of "stimulus" packages for the North American automotive industry. Then-President George W. Bush announced that automakers would receive US$17.4 billion (McKinnon and Stoll, 2008, Dec. 20), despite Congress' explicit rejection of any bailout package. President Bush said the money would come instead from the already-authorized $700 billion fund set up to "rescue" or provide bridge financing to the financial sector.

On December 20, 2008, Canada's federal and Ontario governments promised $4 billion in aid to the auto sector. The Canadian aid came in the form of 91-day renewable loans, which will be stopped if the automotive companies fail to submit adequate restructuring plans. General Motors of Canada was given $3 billion in aid, while Chrysler Canada was given $1 billion. Prime Minister Stephen Harper said that the loans were a "regrettable but necessary step to protect the Canadian economy" (Tibbetts, 2008, Dec. 23).

Canadians should be prepared to write off that $4 billion. The government's record with respect to recouping loans to any business, let alone a business in trouble in the midst of a recession, is poor. The best example of how government loans to business turn out badly for those holding the IOUs (i.e., taxpayers) comes from the province of Alberta, which incurred billions of dollars in losses after its government attempted to bail out risky businesses before, during, and after the two 1980s-era recessions.

Between 1980 and 1994, in an effort to diversify Alberta's economy and combat unemployment, the Progressive Conservative governments of Peter Lougheed and later Don Getty loaned or provided loan guarantees to a number of Alberta-based businesses. The results fell far short of what was hoped for. One recipient, Novatel, cost the provincial government $646 million through a failed loan guarantee; the Swan Hills waste treatment plant cost the province $410 million; and Millar Western cost Alberta another $199 million. These and other companies with loans or loan guarantees from the province of Alberta cost taxpayers an astounding $2.3 billion between 1980 and 1994, according to the Canadian Taxpayers Federation (Milke, 2002: 197).

The stimulus packages or bailouts promoted by the American and Canadian governments are not any different from past attempts to "fix" the economy, and they will likely end with similar results: some companies will likely go bankrupt anyway or they will shrink severely after undergoing a bankruptcy process that temporarily protects the firms from creditors, but not taxpayers from losses. In either event, governments will have thrown good money at bad management.

Just as alarming about the current stimulus approach is that the justifications for the aid have all been heard before: to save a company or industry, or to save jobs and the economy. But these reasons just do not stand up to scrutiny.

Even if some automakers went out of business, there would still be an auto industry in North America, one that would likely be more attuned to what consumers want to buy.

Insofar as the automotive industry is concerned, the apocalyptic claim that the North American automotive industry will disappear if Washington and Ottawa do not use public funds to prop up ailing firms is without merit. As the recent bailout reveals, only certain firms are in dire straits: General Motors and Chrysler. And even if GM and Chrysler entered bankruptcy, that would not necessarily cease manufacturing vehicles. Firms in both the United States and Canada have entered bankruptcy voluntarily in order to buy time and renegotiate contracts with unions and debts to creditors. In the past, companies such as Air Canada have done precisely that and have later emerged and are still flying; the once-mighty tech company, Nortel, also entered voluntary bankruptcy in January of this year (McNish and Avery, 2009, Jan. 14).

The larger point is that even if some automakers went out of business, there would still be an auto industry in North America, one that would likely be more attuned to what consumers want to buy. As of early January, Ford was not taking bailout money in order to survive the current downturn, nor were "foreign" automakers such as Toyota, Honda, or Hyundai. While some of those companies have received grants from American and Canadian governments in the past—as provinces, states, and federal governments have bribed automotive companies to locate plants in certain jurisdictions—it is clear that many automakers will survive the recession without public money.

So why are American and Canadian governments picking favourites among automakers? After all, the $3 billion delivered to General Motors will not create demand for a single new car sale. It will only allow some firms to continue to produce automobiles, automobiles that would otherwise be purchased from other firms. The reality is that the billions of dollars that are being thrown at failing automobile companies will only shift job losses from one company to another. Employees at GM's plants and dealerships will not lose their jobs, but some employees at Ford, Honda, or Hyundai plants and showrooms probably will.

Corporate welfare is pernicious precisely because it circumvents the market remedy: consumers who choose—who substitute—one automaker for another, and do so voluntarily. Corporate welfare forces all consumers and taxpayers to support one or two automotive companies.

Many of the stimulus packages now being rolled out by governments around the world are nothing new; they are old-fashioned corporate welfare packages that may save one business—and perhaps only temporarily. Furthermore, keeping alive some auto manufacturers may dilute the market and actually handicap healthier competitors.

Whatever form it takes, "help" for failing businesses takes money from taxpayers and businesses and delivers it to specific firms, most often with disastrous results (see Milke, 2007). During this budget season, beware of governments bearing stimulus packages.

Whatever form it takes, "help" for failing businesses takes money from taxpayers and businesses and delivers it to specific firms, most often with disastrous results.

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The wrong answer to high drug prices

Drug rationing hurts patients, discourages innovation

Philip Stevens

Around the world, tax-funded health systems are facing pressure from many directions. Populations are aging and consuming more health care, often for expensive, chronic conditions such as cancer. The latest treatments are becoming more expensive, as governments introduce ever more regulations into the drug development process. At the same time, increasingly consumerist patients in countries with state health monopolies are becoming less tolerant of government attempts to restrain access to these expensive medicines in order to contain costs.

This has led to enormous tensions between patients who want the latest drugs, and governments that are forced to ration those drugs in order to maintain some semblance of financial integrity for their state health systems. Such tensions underline the damaging absurdity of massive state intervention in both the drug development process and the health care systems that deliver those drugs.

Not so NICE

In state-run systems, cost pressures typically prompt governments to ration access to treatments for patients, often via waiting lists or low usage of medical technology. As the pharmaceutical industry has limited leverage over governments (as compared, for instance, to medical unions), it is politically easier for cash-strapped governments to limit the number of new treatments available to patients. In order to provide a veneer of scientific rationale for these restrictions, governments often employ cost-benefit analyses, known as "health technology assessments" (HTAs), before new treatments can be procured within the state health care system. Though these assessments may save money in the short term, they unleash a number of hidden but noxious economic consequences and create undue distress for dying patients.

Many countries are increasingly turning to these types of "comparative effectiveness" reviews to restrict access to expensive new drugs. Canada first instituted a Health Technology Assessment program in Quebec in 1988, and HTAs are now widely used at the national and provincial level. In 2004, Germany instituted the Institute for Quality and Economic Efficiency in the Health Care Sector (IQWiG), which provides "comparative effectiveness" information to health care insurers. Even the United States is poised to give more prominence to HTAs, as President Barack Obama has proposed to "establish an independent institute to guide reviews and research on comparative effectiveness" (Obama, 2008).

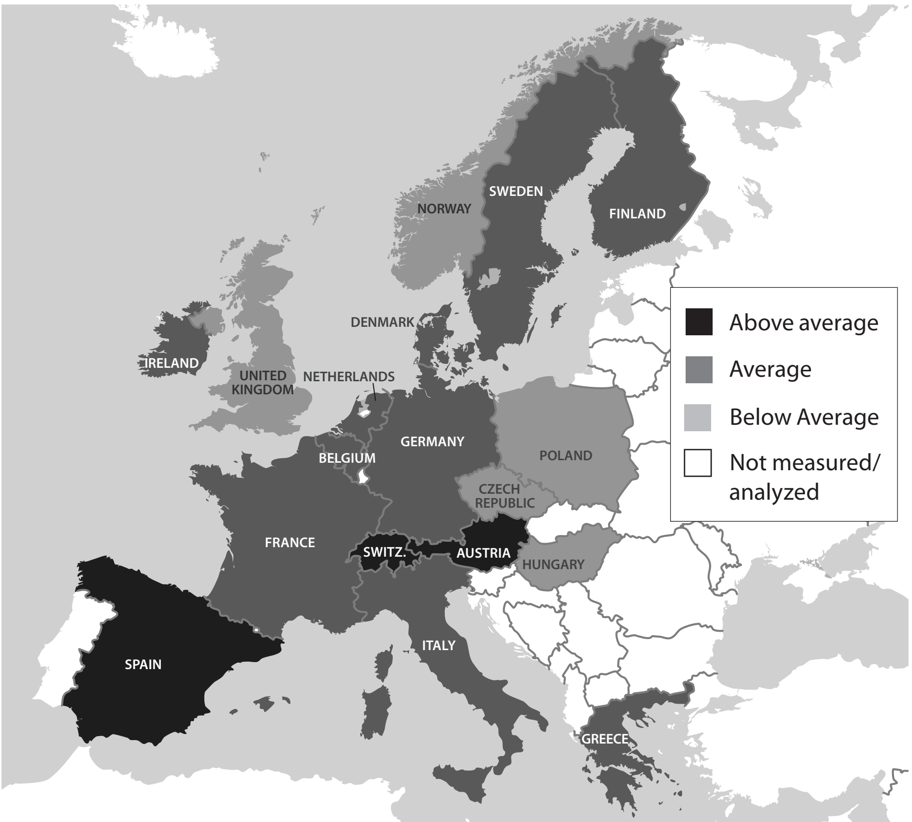
While many European countries make some use of HTAs, many other countries throughout the world, particularly in Asia and Latin America, are looking to the British health system for ideas about how to cut costs. All local providers within the British National Health System (NHS) are legally obliged to fund treatments recommended by the National Institute for Health and Clinical Excellence (NICE), created by the government in 1999. Conversely, if NICE deems a new treatment not to be cost effective, then all NHS providers will be prohibited from offering it to patients.

The National Institute for Health and Clinical Excellence comes to its decisions by reviewing a range of evidence submitted by parties such as drug manufacturers, independent academics, and patient groups. It typically considers a new drug's clinical effectiveness; cost per quality-adjusted life year (QALY)[1] saved; and impact on costs borne by the NHS (Raferty, 2001). Bearing in mind that the NHS constitutes 83% of the UK's expenditure on health (Klein, 2005), the blessing of NICE is absolutely vital if the vast majority of British patients are to benefit from a new treatment.

Judging from Britain's comparative international performance, NICE does a thorough job of keeping innovative drugs from patients covered by the NHS. According to Sweden's Karolinska Institute, for instance, the United Kingdom is below average for the uptake of innovative oncology drugs (Wilking and Jönsson, 2005) (figure 1). Rarely a week goes by without media coverage of a terminally ill patient denied access to a new medicine readily available in other European Union countries or in the United States. Most recently, NICE refused to recommend a drug for aggressive bone marrow cancer, despite the fact that the drug can extend the lives of patients for up to three years (Smith, 2008, Oct. 28).

NICE effectively serves as a nuclear weapon in the government's cost-containment arsenal. If a drug does not meet its criteria, it will simply be unavailable to NHS patients, no matter what their need.

Figure 1: Cancer drug uptake in Europe, 2005



Source: *BBC News*, 2005, Oct. 6.

Unfortunately, the criteria that form the basis of NICE's cost-benefit analyses are somewhat suspect. Most obviously, NICE takes a static view of the cost-effectiveness of new treatments, through which the expense of a drug is weighed against its immediate benefit to patients measured in quality-adjusted life years (QALYs). Although NICE does not publish any price cut-offs, it has tended only to approve drugs that cost less than CA$52,000 per QALY saved (Raferty, 2001). As a result, many innovative drugs are excluded.

This static approach ignores the long-term opportunity costs of not using a newer, more expensive treatment. In particular, not using innovative drugs sends a clear signal to research and development companies that future products are unlikely to be rewarded, meaning that there will likely be fewer innovative drugs in the future. Chronic or terminal conditions that could be made curable by future innovation will remain a burden on humanity (Jena and Philipson, 2008). Moreover, in countries that do not rely on these kinds of health technology assessments, such as the United States, the greater use of newer prescription drugs has limited the number of people on disability rolls, thereby creating huge downstream cost savings for both individuals and governments, as well as increasing general economic productivity (Lichtenberg, 2008).

There are also ethical questions regarding the withholding of approved treatments from patients—especially in Britain, where new treatments are available to private patients, but not to those enrolled in the public National Health Service.

The drug approval process

State-funded systems with pressurized budgets have been forced to limit the use of new technology because new drugs are expensive. But state intervention is largely responsible for the high cost of new drugs. Most new drugs gain approval either through the US Food and Drug Administration (FDA), the EU's European Medicines Agency (EMEA), or Health Canada. Before these regulators can grant marketing approval for a drug, the drug must pass through four phases of clinical trials. Less than one in one thousand molecules makes it past the first, pre-clinical stage, which lasts 42 months on average. The chances of a drug making it to approval are less than 0.03% (Abrantes-Metz et al., 2004), and the process can take between 8.5 and 13.5 years (FDA, 2002; Dranover and Meltzer, 1994) (table 1).

Every year, regulators add more mandatory tests. As a result, the average cost of bringing a new drug to market has risen from US$119 million in 1975 (Hansen, 1979) to almost US$900 million in 2003 (DiMasi et al., 2003). In many European countries and Canada, further delays are caused by the need for government-controlled health systems to determine whether the drug will be reimbursed, and, if so, at what level.

Clinical trials have become ever more expensive because of the increasing demands of regulators, an observation made by Sir Michael Rawlins, chairman of the National Institute for Health and Clinical Excellence. According to Sir Michael, regulators have adopted a precautionary approach to regulation that is characterized by a myopic focus on safety, which comes at the expense of efficiency and speed. Every year, regulators create further

Table 1: Duration and success rate for new chemical drugs

	Pre-clinical	Phase I	Phase II	Phase III and FDA approval	Total
Probability of success	0.1%	80.7%	57.7%	56.7%	0.03%
Successful duration	42 months	19.7 months	29.9 months	47 months	96.6 months

Source: Abrantes-Metz et al., 2004.

hurdles within clinical trials, which achieve little other than adding millions to the final cost of a drug (Rawlins, 2004). This is hardly surprising given that drug regulators are public monopolies. They do not have to compete for clients, and their main incentive, therefore, is to avoid politically embarrassing safety scandals.

Aside from driving up the final cost of drugs, the monopoly in drug regulation has a number of other perverse consequences. For example, in order to ensure that they can recoup their initial investment and turn a profit, manufacturers have strong incentives to concentrate their resources on developing "blockbuster" drugs—drugs that achieve extremely high levels of sales. This approach deters research into rarer diseases because companies are less able to recoup their enormous development costs from small patient populations. When drugs for rarer diseases are produced, their price has to be extremely high in order to turn a profit during the limited time before patent expiry. The same is true for tropical diseases, which afflict fairly large populations, but with extremely limited purchasing power.

To solve the problem of high drug prices, it is necessary to radically overhaul the drug approval process. Several commentators have proposed injecting a degree of competition into the drug approval process, for instance, by creating a market for private drug certification bodies that compete on speed and efficiency (Tollison, 1996; Sauer and Sauer, 2007). Others have suggested the more politically realistic idea of creating a "dual track" approval process by which informed patients would be free to purchase drugs that have passed only initial testing by the FDA (Madden, 2004). Bringing competition into the approval process could liberate innovation, speeding up the development of new generations of medicines that could extend life, remove the need for expensive surgery, and limit the need for costly in-patient care. This would be good for patients and health care funders alike.

The drug approval process is largely responsible for the high price of new medicines. With greater competition in this area, there could be a greater number of cheaper drugs, available more quickly. Politicians try to justify drug rationing by claiming that health care systems cannot afford expensive new treatments. But if every health care system in the world ceased purchasing new treatments, innovation would rapidly grind to a halt. If medical progress is to continue, then the government needs to loosen its grip on both health care provision and the drug approval process.

Note

1 QALY is a pharmo-economic evaluation of the extent of the benefits gained from a health intervention in terms of health-related quality of life and survival for the patient. It takes into account both the quantity and quality of life generated by a health intervention or technology.

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Tolls, not taxes

BC should increase, not reduce use of tolls

Niels Veldhuis & Charles Lammam

"The interior," as locals call it, is a vast playground for outdoor enthusiasts located in the central/southern non-coastal area of British Columbia. Many Lower Mainland residents travel to the interior to enjoy various summer and winter activities. One of the key routes into the southern part of the interior is the Coquihalla, a toll highway between Kamloops and Hope.

Late last year, the BC government suddenly decided to eliminate the Coquihalla toll. Unfortunately, its removal had little to do with sound infrastructure financing. With mounting opposition to BC's unpopular carbon tax and a provincial election looming in the spring, the government presumably felt it had to do something for voters who use the highway, many of whom reside in BC's interior or use the highway for business purposes (i.e., trucking).

Of course, we have always sympathized with people and businesses that frequently use the highway. After all, users have been funding transportation twice over since the highway opened, paying tolls on top of taxes. However, the decision to axe the tolls was ill advised. A better way to increase fairness and finance transportation infrastructure is to increase the use of tolls and to offset them with reductions in taxes.

Whether it is the original building costs, ongoing maintenance and upgrade costs, or emergency services costs, mobility has to be paid for on a continuing basis. The question is how. We suggest that tolls administered by private entities are superior to tax-based approaches for several reasons.

First, tax-based funding of transportation is inequitable: taxes take money from people who may not drive, or never use certain roads, and subsidize other people who do. Sometimes that subsidy is quite regressive, with lower-income people funding mobility for higher-income people. For example, why should people who primarily drive to work in the Lower Mainland pay to send skiers and campers into the interior? And why should a motorist who cannot afford a new, better-mileage car (and who will, therefore, pay more gasoline tax per km driven) subsidize someone who can afford a newer, more fuel-efficient car?

Tolls can also be used to better manage traffic flow. While non-toll roads regularly become overloaded during peak hours, bringing traffic to a halt, toll roads more effectively price road use and optimize traffic flow. Variable toll pricing is the key to using road capacity more efficiently and preventing stop-and-go driving. Variable toll rates increase when roads are heavily congested (i.e., during rush hour) and decrease when they are not.[1] By sending price signals, tolls manage the flow of traffic and reduce the number of vehicles idling on the road, thereby saving valuable time and reducing auto emissions in the process. Real-world case studies show that the benefits of so-called “congestion pricing” are genuine, cutting peak period traffic volumes by between 7% and 30% in places like London, New York, and California (Replogle, 2006: 15).

In the past, toll collection was a cumbersome and expensive way to collect revenue, as well as a nuisance to drivers, but technological innovations have made variable toll collection easier, cheaper, and less of a hassle. Drivers no longer need to stop to pay as modern electronic toll collection systems allow payments to be made without toll booths. Vehicles are now outfitted with wireless radio frequency transponders, which are read by overhead antennas that detect and bill drivers according to use. To deter violators, cameras record the license plates of drivers who use the roadway unlawfully. Far from being a theoretical ideal, we need only look to Toronto’s Highway 407 as an example of this technology in practice.

Finally, a major advantage of tolls over taxes is that tolls present an opportunity to upgrade and expand transportation infrastructure at minimal cost to taxpayers. Public budgets are increasingly strained by program spending in areas such as education and health care, and have largely neglected infrastructure, letting it age and slowly deteriorate.

Through public-private partnerships (P3s), private partners can invest in neglected infrastructure, provided that they would be able to earn a reasonable return on investment. Tolls are critical in this sense because they supply a dedicated and self-generating stream of revenue, allowing private financiers to recoup and profit from up-front expenditures on designing, building, operating, and maintaining facilities. In the end, toll-financed P3 projects may lead to better investment decisions: if prospective toll revenues cannot cover project costs, then perhaps it would be best to think twice about the project.

There is no doubt that removing tolls on the Coquihalla will provide relief for many users who have been double-charged for over two decades. However, a more effective way to finance transportation is to have more tolls and lower taxes. Unfortunately, the BC government’s decision to remove tolls on the Coquihalla was based on politics rather than sound policy.

Note

1 Toll rates may be set for different time periods in advance, or they may be set “dynamically”—that is, they may be increased or decreased in real time to ensure that the lanes are fully utilized without a breakdown in traffic flow.

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Generic drugs in Canada

Overpriced and underused

Brett J. Skinner &
Mark Rovere

Generic drugs are often an economical alternative to brand-name medicines. As the World Health Organization notes, generic drugs are "usually intended to be interchangeable with an innovator product … [and] are frequently as effective as, but much cheaper than, brand-name drugs" (WHO, 2008). In Canada, however, generic drug prices are quite high relative to prices in the United States. Due to various pharmaceutical policies in Canada, Canadians pay much more for generic drugs than they otherwise would if prices were determined by competitive market forces.

Our annual study, *Canada's Drug Price Paradox*, compares Canadian and American prices for an identical group of the 100 most commonly prescribed brand-name drugs and the 100 most commonly prescribed generic drugs in Canada.[1] The most recent edition of the study found that, although brand-name drugs were more expensive in the United States, generic drugs were significantly more expensive in Canada in 2007 (Skinner and Rovere, 2008). This is the third year the study has been performed, and these results are generally consistent with the previous two reports.

After adjusting for the purchasing power parity[2] of the US and Canadian dollars, Canadian retail prices for identical brand-name drugs sold in 2007 were on average 53% lower in Canada than they were in the United States (figure 1). This is slightly different from relative prices in 2006 and 2003, when average prices for brand-name drugs in Canada were 51% and 43% lower, respectively. This means that average Canadian prices for identical brand-name drugs have decreased over the last five years relative to American prices.

However, Canadian retail prices for generic drugs in 2007 were, on average, 112% higher than retail prices in the United States for identical generic drugs (figure 1). In 2006, generic drug prices in Canada were on average 115% higher than American prices. This means that the difference in the average price of generic drugs in the two countries narrowed slightly from 2006 to 2007, but prices remained much higher in Canada.

The gap between prices for identical generic drugs in Canada and the United States has widened significantly since 2003.

However, the gap between prices for identical generic drugs in Canada and the United States has widened significantly since 2003, when generic drug prices were 78% higher, on average, in Canada. In 2007, Canadians paid more than twice as much as Americans paid for the same generic medicines.

Generic utilization

Our study cited data from IMS Health Inc. (2008), which shows that Americans use generic drugs at a much higher rate than Canadians do. In 2007, generic drugs accounted for 48% of all prescriptions dispensed in Canada, while brand-name drugs accounted for 52%. In contrast, generic drugs accounted for 67% of all prescriptions dispensed in the United States, while brand-name drugs accounted for only 33%.

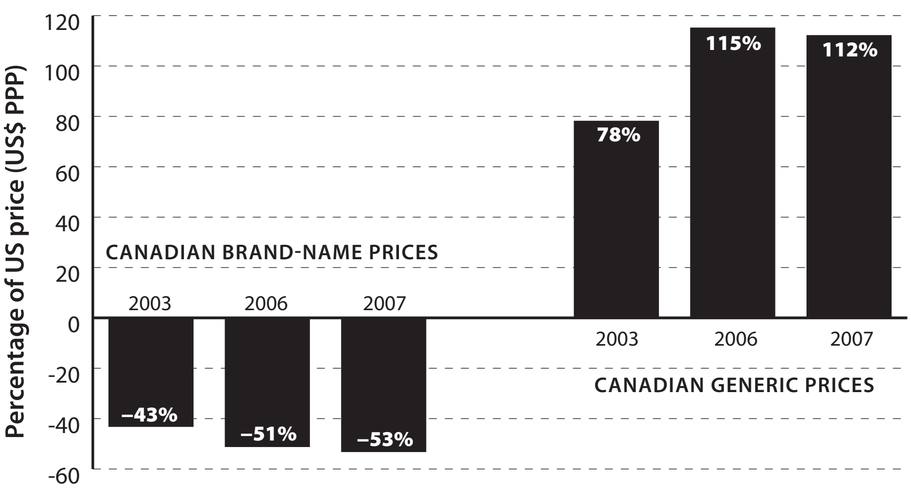
Our findings suggest that higher generic substitution rates in the United States are probably the result of larger generic discounts relative to the prices of brand-name drugs. Bigger discounts have created a stronger incentive for Americans to voluntarily substitute generics.

Indeed, recent innovations by some large retailers have increased competition in the sale of drugs, further discounting generic prices in the United States. For example, through its pharmacy operations, Wal-Mart has introduced drug plans through which consumers can purchase a 30-day supply of generic drugs for a flat fee of $4, or a 90-day supply for a flat fee of $10. These plans apply to any drug listed on the retailer's formulary, which is comprised of approximately 361 generic products (Wal-Mart, 2008).

Policy distortions

The evidence suggests that generic retail drug prices are higher in Canada than they are in the United States because

Figure 1: Differences between estimated average prices in Canada and the United States for the 100 most commonly prescribed brand-name drugs, and the 100 most commonly prescribed generic drugs, 2003, 2006 and 2007, stated as a percentage above or below the US price



Source: Skinner and Rovere, 2008.

of various provincial and federal policies in Canada that are not found in the US (Skinner, 2005; Skinner and Rovere, 2008). In particular, there are three policies that are chiefly responsible for distorting retail price competition for generic drugs in Canada.

Provincial and federal drug programs direct public reimbursement of prescriptions to pharmacies instead of consumers, insulating consumers from the cost and removing incentives for comparative shopping that would put downward pressure on prices (Skinner and Rovere, 2008: 23).

Public drug programs also reimburse generics at a fixed percentage of the price of the original, brand-name drug. Under fixed-percentage reimbursement, there is no incentive for retailers to undercut each other to win sales. This is because the buyer (government) offers every seller the same price and the price is known in advance (Skinner and Rovere, 2008:23).

Federal price controls on patented drugs unintentionally prevent brand-name companies from reducing prices on these products once a patent expires. This is because Canada's price-control policy uses the highest price of the existing drugs in the same therapeutic class as a reference for establishing the maximum allowable price for new patent-protected drug formulations entering the market. Therefore, makers of brand-name drugs are extremely reluctant to reduce the price of the original drug when it goes off patent for fear of inadvertently lowering the maximum allowable entry price for new drugs in the same class. In fact, after the entry of generic competitors into the market for an off-patent drug, the price of the brand-name drug tends to remain high. Thus, Canadian price controls create an artificial incentive for brand-name companies to resist competing on the basis of price with generic firms for sales of off-patent drugs (Graham, 2000; Skinner and Rovere, 2008: 23) Thus, when governments use public reimbursement policies that set prices for generics at a fixed percentage of the brand price, then the price paid by governments for generics is higher than it would be if the off-patent brand price was free to adjust to generic competition.

As we explain in our study (Skinner and Rovere, 2008: 24), large, established generic companies take advantage of the system of direct-to-pharmacy, fixed reimbursement to offer rebates to retailers that are "bundled" across many products in exchange for exclusive distribution rights. This frequently results in these companies having a virtual monopoly within particular retail pharmacy chains for a particular generic label. Yet, because pharmacies are reimbursed directly by public drug programs, discounts are not passed on to consumers or insurance payers. Exclusive distribution and direct-to-pharmacy reimbursement allows retailers to push the generic prices paid by public drug plans onto private sector insurance payers and uninsured consumers as well.

It is important to note that under any set of pharmaceutical policies, it is economically rational for generic manufacturers and pharmacies to maximize the prices of generic drugs. Due to Canada's particular set of pharmaceutical policies, generic drug prices are higher than they would be in a competitive market, but the cause is government interference in the market, not the behaviour of generic drug manufacturers or retail pharmacies.

In order to estimate the scale of the total savings that could be achieved by repealing the government policies identified above we conducted a cost-benefit analysis using expected prices and generic drug utilization rates for the United States as a proxy. We estimated that Canadians could save between $2.9

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35 YEARS OF IDEAS AND IMPACT

This year, the Fraser Institute celebrates 35 years of studying market solutions to public policy problems. To commemorate the Institute's many years of success, each issue of *Fraser Forum* in 2009 will look at a different milestone in the Institute's history. This first feature tells the story of the founding of the Institute.

The year was 1974. The world was in the midst of a severe economic downturn, and the general consensus in Canada was that increased government involvement in the economy was necessary to ensure the economic well-being of Canadians.

In British Columbia, voters had recently elected the province's first-ever New Democratic Party (NDP) government, led by Dave Barrett.

"Dave Barrett was in the process of creating a socialist paradise in British Columbia," explains Michael Walker, founding Executive Director of the Fraser Institute. "And in the course of doing that, he established a government think tank" to advise the new government on economic priorities and policies.

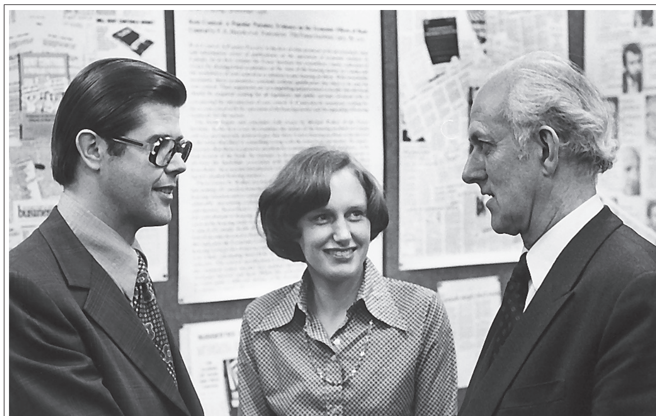
"The ideological orientation of the economic think tank alarmed me and others," recalls Csaba Hajdu, co-founder and current Senior Fellow at the Institute. "We realized that there was no organization that could be called upon to express a balancing view to the public. There was no champion of free market principles."

"We initiated the Fraser Institute to fill that void."

The founding

T. Patrick Boyle, a senior industrial executive and then Vice President, Financial Planning, at MacMillan Bloedel, was also watching with unease. Not content to watch from the sidelines, he and Hajdu, who was then Chief Economist at MacMillan Bloedel, worked together to think about how to respond to the changes the government was making.

Michael Walker gives a speech at the 1977 AGM, Royal York Hotel, Toronto.



John Raybould, Sally Pipes and Sir Anthony Fisher at the 1977 AGM, Royal York Hotel, Toronto.

At this time, Walker was working as an in-house consultant with the federal Department of Finance, following a four-year stint at the Bank of Canada. Concerned about the policies of the federal government under Pierre Trudeau and their implications for Canada, Walker had already decided to leave this position.

"The more I lived in Ottawa, the more I came to understand the frailties of government involvement in the economy," Walker says.

Walker was contacted by Hajdu, a former classmate at the University of Western Ontario who shared similar views, and agreed to meet with Boyle and Hajdu on his next trip to British Columbia.

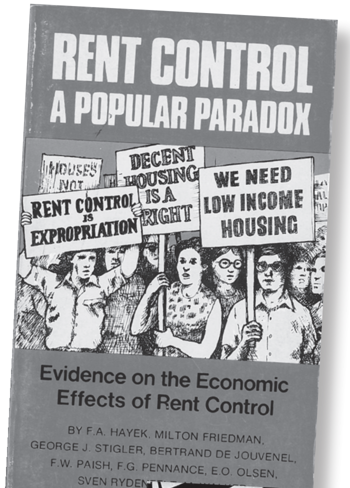
Out of these discussions, Boyle conceived the idea of creating an economic and social research institution that would educate Canadians about matters of public policy.

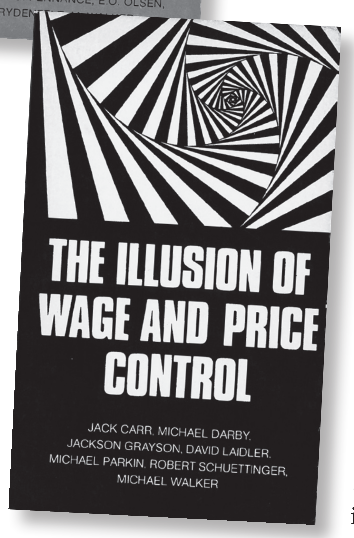
"We decided to take a different approach than was being taken, for example, by the Economic Council of Canada and other economic analysis organizations," says Walker. "We decided that our target audience had to be the general public, that we had to get the 'fog index' down in our publications so that we could communicate to people."

In the autumn of 1974, Boyle, Walker, and Hajdu got together with Sally Pipes and John Raybould, and began developing a mission statement and operating plan for the Institute. On October 21, 1974, the Charter of the Fraser Institute was granted by the government of Canada, and the Institute was officially born.

The challenge

The most significant challenge for the Fraser Institute after its founding was financial survival.





"Right out of the gate, we had financial problems, and within two years of being formed, it looked very much like we were not going to make it," says Walker.

"This was a new idea," says Pipes, an economist with the Institute from 1974 to 1991, "and the challenge was how do you get people to take a risk on funding something early on?"

At times, the Institute's strict adherence to sound market principles made raising funds more difficult. In 1976, the Institute published *The Illusion of Wage and Price Control*, in response to the Trudeau government's proposal to impose wage and price controls across Canada. This stance ran contrary to the wishes and expectations of some financial supporters.

"That did not please some initial supporters who apparently wished for or expected a short-term pro-business public relations effort, rather than a permanent institute based on sound market principles," recalls Hajdu.

In its early years, the Institute received help from Sir Anthony Fisher, founder of the Institute of Economic Affairs in London, England, who came over to take the position of Acting Director of the Fraser Institute between 1975 and 1976.

The impact

In 1975, the Institute published its first book, *Rent Control: A Popular Paradox*. The book was a huge success, selling more than 6,000 copies in its first six months—a best-seller by Canadian standards.

"We faced a situation where rent controls were starting to be talked about—it looked like a lot of provinces were going to adopt them," says Walker. "British Columbia had already adopted a form of rent regulation and we could see this was a disaster."

The book, which took a historical and international look at the economic effects of rent controls, was the first North American book to provide a careful analysis of this policy. Authors of the book included intellectual giants such as Milton Friedman and F.A. Hayek, who was also a member of the Institute's Editorial Advisory Board at the time.

Rent Control was followed quickly by *The Illusion of Wage and Price Control*, the Institute's second best-seller. The book may not have been popular initially among the business community, but it received a warm welcome elsewhere.

"*The Illusion of Wage and Price Control* was reviewed in some of the top academic journals in the world and with favourable comment," says Walker, earning the Institute both national and international renown.

This acclaim only grew following the Institute's first conference in 1976, which focused on another hot topic of the day: unemployment insurance. The conference, held in Vancouver and developed with the assistance of Senior Fellow Herbert Grubel, was sponsored by Liberty Fund, enabling the Institute to bring many top economists to Canada from around the world. It was a defining event that led to a major change in attitudes toward unemployment insurance regulations in Canada and abroad, Walker notes.

The conference was also a defining event for the Institute itself, allowing it to establish relationships with economists and other think tanks from around the world at a relatively early stage in its development.

"These linkages would prove over time to be very important, both to our own development and to the development of economic policy in the world," says Walker, "because right from the beginning, we were engaged in the global discussion of economic policy problems."

The influence

The year is now 2009 and that discussion of economic policy problems continues as the Fraser Institute enters its 35th year in operation.

With over 70 publications, 127 events, and more than 7,000 media hits in 2008 alone, the Institute continues to grow and expand its influence each year, building on the foundation of many past ideas and successes.

As Walker says, "It really has been a wonderful progression from one level of accomplishment and success to the next."

— *Kristin Fryer*

The future of NATO

At 60, the alliance faces a time of change and challenge

Alan W. Dowd

After doing one thing—and one thing well—for its first 40 years, the NATO alliance now seems to be a work in progress.

In fact, the alliance has tweaked its mission three times in the past 15 years. After the collapse of the Soviet Union, NATO turned to stabilizing Eastern Europe and pacifying the Balkans. After 9/11, it added counter-terrorism and counter-proliferation of weapons of mass destruction to its list of responsibilities. As one NATO ambassador put it in 2002, "We're deconstructing the old NATO to build a new one to meet the threat of terrorism and weapons of mass destruction" (NATO, 2002). Finally, in recent years, NATO has been focused on the war in Afghanistan.

Perhaps this search for a new mission is a function of how fast the world is changing, or perhaps it's happening because NATO's record of late is decidedly mixed.

Caveat emptor: Allies beware

First, the good news: In 1999, NATO officially adopted a plan to stabilize Eastern Europe and "build an undivided continent" (NATO, 1999).

That vision for post-Cold War Europe has been largely fulfilled. NATO offered security to most of the orphan states of Russia's receding empire, smothered Slobodan Milosevic's wars, and gave Europe time to rebuild the links that were severed by the Iron Curtain. Thriving with commerce, free from the daily threat of war, and no longer divided by an occupying army, today's Europe is unrecognizable from the one we knew in 1989. And NATO deserves much of the credit.

But NATO's mission in Afghanistan is another story, and this brings us to the bad news.

The war-torn country is no longer under the control of the Taliban and its al-Qaeda partners. Yet after seven years of NATO nation-building, it does not appear that Afghanistan is under anyone's control.

Thanks to sanctuaries in Pakistan, remnants of the Taliban and al-Qaeda are waging a bloody guerilla war against NATO and the Afghan people. In fact, insurgent attacks jumped 50% in 2008 (Gopal, 2009, Jan. 2). Although NATO's 51,000 troops in Afghanistan—2,500 Canadian troops among them—are doing their best to smother the insurgency, the same cannot be said of some of their governments.

Many members of NATO have been short-changing the International Security Assistance Force in Afghanistan (ISAF) from the very beginning. This is partly a function of their paltry investment in defense.

For example, while the United States spends about 4% of its GDP on defense—a GDP that is enormous compared to that of other NATO nations—only six of NATO's 26 members have mustered the will to meet the alliance's standard of investing 2% of GDP on defense. Although Canada is still under the 2% threshold (at just 1.2%), it has made significant contributions to ISAF—some $8.1 billion as of the end of the 2008 fiscal year. Ottawa expects to spend $14 to $18 billion by the end of Canada's commitment in Afghanistan, which is set for 2011 (Clark, 2008, Oct. 9).

As a consequence of this low level of investment in defense, most NATO members have to hitch a ride with the US Air Force or rent Soviet-era transports to deploy troops and equipment to Afghanistan (Sieff, 2006, May 30; NATO, 2004). They lack helicopters to move within Afghanistan. They "are not trained in counterinsurgency," in the blunt words of US Defense Secretary Robert Gates (Spiegel, 2008, Jan. 16). And they aren't fulfilling their troop commitments. For example, in 2006, alliance members only contributed 85% of the forces they pledged to ISAF.

Not much has changed since then. In fact, in early 2008, Canada threatened to withdraw its 2,500 troops if NATO failed to muster 1,000 more personnel for operations in Afghanistan's restive south. At NATO's 2008 summit in Bucharest, some allies were cajoled into action: France sent 1,000 additional troops, Britain 800 more, and Poland another 400 (Baker and Tyson, 2008, Mar. 31).

Even so, a January 2009 analysis by the *New York Times* concludes, "NATO has not met its pledges for combat troops, nor for the vitally important transport helicopters, military trainers and other support personnel" (Shanker and Cooper, 2009, Jan. 3).

Predictably, the United States will fill the gaps, deploying as many as 30,000 more troops to Afghanistan this year (in addition to the 32,000 American personnel already there).

However, the extra troops will only solve part of the problem. NATO still allows members with military forces in Afghanistan to opt out of certain missions. These "caveats," as they are euphemistically called, have been used by Germany, Italy, and Spain, for example, to steer clear of combat in southern Afghanistan. Other nations have played the caveat card to limit the use of air assets or the deployment of personnel near Pakistan (Reuters, 2006, Nov. 26).

Caveats not only make it difficult to field an effective combat force, but they also strike at the very heart of NATO's cohesiveness. After all, an ally that promises to help only when the guns are quiet and where the scenery is serene is not much of an ally.

"We must not—we cannot—become a two-tiered alliance of those who are willing to fight and those who are not," Defense Secretary Gates warned last year, adding that such a development "would in effect destroy the alliance" (Gray, 2008, Feb. 10).

The will to prevail

Of course, if the Afghanistan mission is any indication, the alliance is already two-tiered, with the Americans, British, Canadians, Dutch, and Danes doing most of the fighting and dying.

That explains why at the Bucharest Summit NATO members were implored to "support each other in sharing the burden in Afghanistan" and to "provide maximum possible flexibility of use of our forces by the ISAF Commander" (NATO, 2008a).

Perhaps the most disheartening aspect of the failure of major European nations to send more troops to Afghanistan—and to send them with no strings attached—is the fact that NATO's European contingent fields some 2.3 million active-duty troops and another 3.04 million reserves (Coonen, 2006). The United States, by comparison, has 1.4 million troops on active duty and less than one million reserves.

Several retired NATO generals grimly conclude that NATO "lacks capabilities, and its constituent nations are showing a marked lack of will for it to prevail" (Shalikashvili et al., 2008). The generals are so concerned that they issued a paper on the eve of the Bucharest Summit calling for sweeping reforms.

Among other things, they propose the "abolition of the system of national caveats"; recommend that NATO jettison consensus-based decision making at the operational level in favour of majority voting to "enable NATO to take quick decisions in crises, when minutes matter"; argue that "only those nations that contribute to a mission—that is, military forces in a military operation—should have the right to a say in the process of the operation"; and call on the alliance to maintain the option of pre-emptive and even preventive war (Shalikashvili et al., 2008).

Thanks to sanctuaries in Pakistan, remnants of the Taliban and al-Qaeda are waging a bloody guerilla war against NATO and the Afghan people.

Along with these reforms, there must be a renewed awareness on the part of governments and populations alike that NATO is not attempting to keep peace in Afghanistan, but waging war.

NATO's fighting forces know that they're at war. More than seven years after intervening in Afghanistan, NATO has lost 636 Americans, 142 Britons, 107 Canadians, 25 Germans, 25 Spaniards, 23 French, 21 Danes, 18 Dutch, 12 Italians, and a number of others (as of January 23, 2009) (CNN, 2009).

For those watching at home, the cost of Canada's mission in Afghanistan may seem too great, both in terms of lives lost and dollars spent. However, it is important to remember that the protection of society, which Adam Smith called "the first duty of the sovereign," can be performed only by means of military force (Smith, 1776/1991: 689). Thus, the state has a responsibility to provide for defense, Smith writes, even as the cost of that defense "grows gradually more and more expensive" (Smith, 1776/1991: 707).

There should be no free-riders in the alliance because being a member of NATO comes with certain responsibilities. The main responsibility of every NATO member is to rise in defense of another who has been attacked. Specifically, Article V declares that "an armed attack against one or more of them in Europe or North America shall be considered an attack against them all," and obliges members to come to the aid of an attacked ally "to restore and maintain the security of the North Atlantic area" (NATO 1949).

NATO is in Afghanistan because that country spawned an armed attack against a NATO member, which prompted NATO to invoke Article V for the first time in history.

If NATO's own members do not take Article V seriously, then neither will NATO's enemies. For NATO to work, it cannot be a "one-for-all" public good; it must be an "all-for-one" alliance.

NATO's future

Given all the headaches and half-measures, is NATO still worth the time, trouble and treasure? Yes.

From Kosovo to Kandahar, the past decade reminds us that alliance warfare is never easy, but it is preferable to the alternative—fighting alone. And thanks to NATO, America has not been alone in its campaign against terror.

Immediately after 9/11, NATO invoked Article V, the alliance's collective defense clause. Europe soon became a key jumping-off point for the war on terror. Operations in the Middle East, Central Asia, Africa, and beyond depend on NATO infrastructure in places like Lakenheath, Ramstein, Aviano, and Incirlik.

Of course, Canada was the first NATO ally to stand with America after the 9/11 attacks. In fact, Canadian personnel at NORAD in Colorado and the Northeast Air Defense Sector in New York were standing with their American counterparts during the attacks, first trying to make sense of what was happening on 9/11 and then securing the skies over North America (Hograth, 2006).

Ever since, Canada has contributed heavily to post-9/11 missions, both within and outside the NATO context. The Canadian navy, air force, and commando forces were deployed during the initial counterstrikes against the Taliban and al-Qaeda in October 2001. Canada later commanded peacekeeping and combat operations in Afghanistan, and there are many Canadian troops in Afghanistan today.

Those who say that Afghanistan is NATO's Waterloo forget that equally dire diagnoses were made when NATO watched Yugoslavia tear itself apart in the early 1990s, when the United States deployed Pershing missiles along the NATO-Warsaw Pact line in 1983, and when France withdrew from NATO's military command in 1966.

Yet NATO has found a way to survive. In fact, it turns 60 this year. The reason for its staying power is simple: Despite all its shortcomings, NATO still serves an important purpose—or more accurately, a number of important purposes. Since the fall of the Berlin Wall, NATO has evolved into a ready-made structure for building military coalitions of the willing. These alliances within the alliance helped to liberate Kuwait and Kabul, wage war and keep peace in the Balkans, and topple Saddam Hussein's regime. Plus, NATO has taken on other new missions—such as tackling cyber-defense and deploying missile defenses—and continues to carry out its oldest mission—keeping an eye on Moscow.

In fact, the alliance that once focused on defending Western Europe from a Soviet invasion is now playing a role in several global hot spots:

NATO has evolved into a ready-made structure for building military coalitions of the willing.

- NATO has supported African Union peacekeepers with training and transport.
- Built around a strong NATO core, the Proliferation Security Initiative is an ongoing naval operation that intercepts weapons of mass destruction and their precursors while in transit. Similarly, NATO task forces patrol the Mediterranean to deter terrorist activity and have been deployed off the Horn of Africa to fight piracy.
- NATO has trained 10,000 Iraqi security forces and is developing what the alliance calls "a long-term relationship with Iraq" (NATO, 2008b).
- NATO's membership invitations to Albania and Croatia, pending invitation to Macedonia, 16,000-person peacekeeping force in Kosovo, and entreaties to Serbia are proof of its determination to make Europe whole. And Russia's foray into Georgia, a former Soviet republic, serves as a grim reminder that NATO may be the only source of real security in Europe's borderlands.

Mind your business

In 1993, when NATO leaders were debating whether to intervene in the Balkans, US Senator Richard Lugar predicted that NATO would either "go out of area or out of business" (Lugar, 2002). In other words, the middle-aged alliance would have to reorient itself for new missions outside of what NATO's founding document calls the "North Atlantic area."

NATO heeded Lugar's counsel and cautiously intervened in Yugoslavia. Sixteen years later, it appears that NATO has more "business" than it can handle. But to extend Lugar's metaphor, NATO's CEOs need to invest more in human resources and training, acquire new equipment, and refine the organization's mission if they hope to keep pace with the challenges of today—and tomorrow.

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*A version of this article appeared in **The American Legion Magazine**.*

Generic drugs in Canada
continued from page 13

billion and $7.5 billion (in 2007 Canadian dollars) annually on generic and brand-name drugs if Canada repealed public policies that distort prescription drug prices (Skinner and Rovere, 2008).

Notes

1 In 2007, this sample of drugs represented approximately 70% of the entire brand-name market and approximately 55% of the entire generic market. Most, but not all, drugs were available in both markets for comparison.

2 Purchasing power parity compares the prices of similar goods and services in different nations, including the prices of non-tradable goods and services, which better reflect the purchasing power of different currencies. Purchasing power measures the amount of goods and services that can be purchased for a unit of currency.

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The problem with central planning

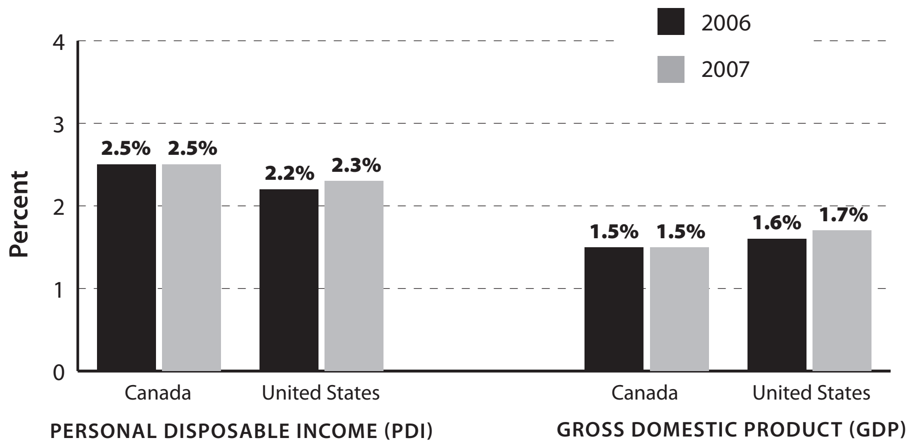
How successful are Canada's drug policies?

Brett J. Skinner & Mark Rovere

There is a common misconception that the cost of new patented drugs is the primary cause of escalating health care costs (Picard, 2006, May 11; Sanger, 2006). In response to such concerns, Canadian governments have regulated the prices of new patented medicines and have, in general, substituted centrally planned rationing for consumer choice in public drug insurance plans.

In order to determine whether government intervention in the prescription drug market has actually made prescription drugs more affordable for Canadian consumers, a recent Fraser Institute study compared prescription drug spending in Canada with that in the United States. In the United States, governments are less prone to intervening in pharmaceutical markets than Canadian governments. Thus, comparing prescription drug spending in Canada and the United States gives some indication as to how successful the Canadian government's interference in the prescription drug market has been.

Figure 1: Annual change in the personal prescription drug cost burden in Canada and the United States, 2006 and 2007



Source: Skinner and Rovere, 2008b.

Incentives versus regulation

The study, *Cost Burden of Prescription Drug Spending in Canada and the United States: 2008 Edition*, compared average per-capita prescription drug spending in Canada and the United States (total spending on prescription drugs divided by total population), in order to determine whether Canada's prescription drug policies result in lower drug costs for Canadians. The study examined per capita Canadian and American prescription drug spending as a share of both per capita national income (gross domestic product [GDP]) and per capita personal after-tax income (personal disposable income [PDI]). As with the 2007 edition of our report, the findings of the 2008 report suggest that Canadian prescription drug policies do not result in lower drug costs for Canadians.

In both 2006 and 2007, Canadians (on average) spent approximately 2.5% of their PDI per capita on prescription drugs (figure 1). Americans spent less than Canadians did in both years, but the US figures were up slightly in 2007 relative to the previous year. On average, Americans spent 2.2% of their after-tax income on prescription drugs in 2006 compared to 2.3% in 2007.

When comparing the proportion of per capita GDP spent on prescription drugs in Canada and the United States in those same years, the data indicate that Americans spent slightly more of their per-capita national income on prescription drugs than Canadians did. On average, Canadians spent about 1.5% of their per capita GDP on prescription drugs in 2006 and 2007 (figure 1). By contrast, Americans spent approximately 1.6% of their per capita GDP on prescription drugs in 2006 and 1.7% in 2007.

It is important to note that the number of prescriptions dispensed per capita in

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Raising BC's minimum wage

Good intentions, bad policy

Niels Veldhuis

Despite British Columbia's slowing economy and rising unemployment, unions and other activists continue to advocate for a significant increase in BC's minimum wage. For example, the BC Federation of Labour, among others, wants raise the minimum wage from $8 per hour to $10 per hour, a 25% hike (BC Federation of Labour, 2009).

Minimum wage advocates argue that increases are needed to reduce poverty for the "working poor," and that these increases can be implemented without negatively impacting employment. The reality, however, is that increases in the minimum wage come with serious negative costs, particularly for those workers whom the increases are intended to help.

The most damaging consequence of minimum wage increases is that employers respond by reducing the number of workers they employ and/or the number of hours their employees work. In other words, minimum wage increases result in higher unemployment for low-skilled workers and young people.

This unpleasant reality is well documented in the research. A review of academic studies from Canada and around the world demonstrates convincingly that high minimum wages lead to lower employment levels. For example, a recent, comprehensive study by renowned minimum wage experts Professor David Neumark of the University of California and Dr. William Wascher, an economist with the US Federal Reserve Board, reviewed more than 100 studies covering 20 countries over the past 15 years. They found that the "overwhelming majority" of studies, especially the most credible, consistently show that minimum wage increases result in decreases in employment (Neumark and Wascher, 2007).

Closer to home, 14 studies have specifically examined the impact of minimum wage increases in the Canadian provinces, including British Columbia. The Canadian research indicates that a 10% increase in the minimum wage is likely to decrease employment by 3% to 6% among all young workers (those aged 15 to 24). For the young workers who are most directly affected—those earning between the current $8 per hour minimum wage and the proposed $10 per hour wage—the impact is more acute, resulting in employment losses of 4.5% to 20% (Godin and Veldhuis, 2009).

Increasing BC's minimum wage to $10 per hour would lead to a loss of 11,000 to 52,000 jobs for workers aged 15 to 24.

Using the evidence from past minimum wage increases across Canada, a recent Fraser Institute study, *The Economic Effects of Increasing British Columbia's Minimum Wage*, estimated that increasing BC's minimum wage by 25% to $10 per hour would lead to a loss of 11,000 to 52,000 jobs for workers aged 15 to 24.

Workers lucky enough to retain their jobs if the minimum wage were increased to $10 would likely to see reductions in their hours, fringe benefits, and/or training. Again, these effects have been widely studied. For example, a study in the *Journal of Labor Economics* found that a 10% increase in the minimum wage reduced the proportion of minimum wage workers (aged 20 to 24) who received on-the-job training by two percentage points. This means that even if low-skill workers retain their jobs, they actually may not be better off, depending on changes to their benefits and training (Neumark and Wascher, 2001).

In addition to those negative effects, higher minimum wages have also been associated with increased school dropout rates. When minimum wages increase, more young people leave school in search of employment.

Less education, fewer employment opportunities, and less training is a poisonous cocktail of results, given that experience, education, and skills development are critical drivers of higher wages and thus improved living standards.

Though some minimum wage earners would benefit from a wage increase, the typical minimum wage earner is not the person depicted by advocates of higher minimum wages (adults supporting families). In reality, the majority of minimum wage workers are young people, often students living at home.

The latest available data from Statistics Canada reveal that only 3.4% of workers in BC earn the minimum wage. Of these, 56% are between the ages of 15 and 24, most of whom (87%) are living at home with family. Many of the remaining individuals earning minimum wages are adults supplementing their family income with part-time work during child-rearing years or after retirement. This means that any changes to the minimum wage would mainly affect younger workers and would have negligible impacts on working adults or those supporting families (Statistics Canada, 2008).

Finally, it is important to note that minimum wage work is largely a temporary experience. The vast majority of minimum wage earners experience upward income mobility rather quickly. Research shows that after one year, more than 60% of minimum wage workers earn more than the minimum wage, with a typical wage gain of about 20%. Over 80% of workers who earn minimum wage go on to earn more than the minimum wage within two years. With experience and growing skills, minimum wage workers increase their productivity and thus garner higher wages.

Minimum wages are seen by politicians, and indeed most in the general public, as an effective method of ensuring that the "working poor" can earn a livable income. Despite these good intentions, minimum wages are incapable of alleviating poverty and can actually make matters worse for the people they are intended to help. If the government wishes to raise the incomes of and improve economic opportunities for British Columbia's low-income workers, they would be wise to steer clear of increasing the minimum wage.

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A version of this article appeared in the ***Vancouver Sun****.*

The problem with central planning
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each country is approximately the same. In 2007, 13.7 prescriptions were dispensed per person in Canada compared to 12.6 prescriptions per person in the United States (IMS Health, 2008; IMS Health Canada, 2008; Statistics Canada, 2008).

Canadian prices for brand-name prescription drugs are lower than US prices for identical drugs (Skinner and Rovere, 2008a).Thus, if brand-name drugs are priced higher in the United States than they are in Canada, then why do Americans spend approximately the same percentage of their personal income on prescription medicines? There are two important reasons for this paradox: (1) average prices for generic drugs in Canada are more than double the average prices for identical drugs in the United States; and (2) Americans tend to substitute cheaper generic versions of drugs for the relatively more expensive brand-name originals to a greater degree than Canadians do (Skinner and Rovere, 2008a).

Conclusion

Our findings indicate that the Canadian government's intervention in the prescription drug market does not produce a lower drug cost burden for Canadians relative to the cost burden for Americans, who enjoy much freer markets.

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The need for worker choice in BC

Union members should not be forced to support their unions' political battles

Niels Veldhuis

SEVEN of British Columbia's biggest unions are currently in BC's Supreme Court fighting a new law that restricts their ability to spend on advertising during election campaigns. Bill 42 limits spending by third-party groups to $3,000 per riding and $150,000 overall. To put this into perspective, these unions allegedly spent $3 million on anti-Liberal Party of British Columbia advertising in the run up to the 2005 BC election.

The unions are certainly right to fight Bill 42. Engaging in the political process, whether financially or through other means, is a cornerstone of our democratic process. Unions, businesses, associations, and individuals should be free to spend as they wish.

The real crime is not that unions attempt to influence election outcomes through advertising, but rather that union leaders are able to use mandatory union dues to fight political battles that their members may not support. Rather than limiting union spending on election campaigns, the BC government should give workers the right to choose whether or not to financially support their union's political activities.

In British Columbia, as in all provinces, workers can be forced to join a union as a condition of employment, in accordance with the Labour Relations Code. In addition, workers covered by collective bargaining agreements have no choice but to remit full union dues.

This stands in stark contrast to the choice afforded to workers in other countries. In the United States, for example, workers in some states enjoy significantly more choice. Workers in some states cannot be forced to join a union, and they have the ability to opt out of union dues that are not related to their representation (i.e., collective bargaining, arbitration proceedings, etc.), such as political activities (Palacios et al., 2006). Further, there are 22 US states that afford workers even more choice by allowing them to opt out of all union dues payments.

Research has shown that this striking difference in worker choice between Canada and the United States explains in part why unionization is so much higher north of the border (Taras and Ponak, 2001; Moore, 1998). In 2007, total unionization was 31.5% in Canada and 13.3% in the United States (Statistics Canada, 2008; Hirsch and Macpherson, 2008).

The lack of worker choice in British Columbia is exacerbated by the fact that unions are not required to publicly disclose detailed financial information. While BC unions are required to disclose some financial information to unionized workers upon request, the information is limited.

Most importantly, there is no requirement for unions to disclose to their members even the most basic breakdown of financial information, such as money spent on activities directly related to representing workers as opposed to expenditures unrelated to representation, such as political support and activism.

Again, this is in stark contrast to how workers in the United States are treated. In every US state, all unions are required to submit detailed financial statements to the Federal Department of Labor (DOL). Large unions—those that spend over $250,000—are required to provide information for 47 financial items and another 21 informational items (Palacios et al., 2006). Perhaps the most important requirement, representing a striking difference from British Columbia, is that spending on collective representation must be reported separately from spending not related to representation.

In addition, large unions in the United States must disclose every financial expenditure that is $5,000 or larger. Similar but less onerous requirements are imposed on medium-sized unions ($10,000 to $250,000 expenditure) and small unions (less than $10,000 expenditure).

Another important aspect of union financial disclosure in the United States is the fact that union members and the public have equal access to all this information on the DOL website. This anonymous access allows workers to make decisions without being influenced by union representatives.

In British Columbia, any such request for information must be done formally, meaning that no request is anonymous. Without anonymity, there is a serious risk that workers' confidentiality and ability to draw conclusions without intimidation from union leaders and co-workers may be compromised.

The unfortunate reality is that American workers have a choice regarding union membership and full dues payment, and have anonymous access to detailed information on union finances; British Columbia's workers do not. At a minimum, BC workers should at least have the same level of financial disclosure accorded to their counterparts in the United States.

Rather than limiting the ability of BC unions to engage in the democratic process by capping their spending, the provincial government should prohibit the use of mandatory union dues to fight political battles without workers' expressed support. It's high time the provincial government ended unions' free ride on workers.

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High costs for seniors

Generic drugs significantly more expensive in Canada than in US

Brett J. Skinner &
Mark Rovere

A recent Fraser Institute report, which estimated the differences in brand-name and generic drug prices in Canada and the United States for the drugs most commonly prescribed to seniors (i.e., people aged 60 years and older), found a significant price discrepancy: in 2007, Canadian seniors paid more than twice as much as their American counterparts paid for identical generic drugs (Skinner and Rovere, 2008a).

The high prices of generic medicines in Canada are the result of various ill-conceived public policies that shield retail pharmacies and generic drug manufacturers from competitive market forces (Skinner and Rovere, 2008b). Because of these policies, Canadians, in general, and seniors, in particular, are paying too much for generic drugs.

Studying the prices of the drugs most commonly prescribed for seniors is important because most publicly funded drug programs in Canada base eligibility for benefits on age. As a result, the cost burden of these inflated generic drug prices is largely borne by taxpayers.

Detailed findings

In 2007, prices for the generic drugs that were most commonly prescribed to Canadian seniors were, on average, 101% higher in Canada than they were for identical drugs in the United States (figure 1). By contrast, prices for the brand-name drugs that were most commonly prescribed to Canadian seniors were, on average, 57% lower in Canada than they were for identical drugs in the United States (Skinner and Rovere, 2008a).

A similar analysis using 2006 data found that, on average, the prices of the generic prescription drugs most commonly prescribed to seniors were 118% higher in Canada than they were in the United States. Prices for identical brand-name drugs were, on average, 52% lower in Canada than in the United States. Although generic drug prices in Canada declined relative to American prices from 2006 to 2007, the most recent analysis indicates that generic drug prices in Canada have increased significantly relative to US prices over the past five years.

In 2003, prices for identical brand-name drugs were, on average, 36% lower in Canada than in the United States, while prices for identical generic drugs were 64% higher in Canada (figure 1). This means that over a five-year period (2003 to 2007), the average cost of the generic drugs most commonly prescribed to seniors living in Canada rose substantially relative to US prices, while prices for the brand-name drugs most important to seniors have decreased.

Prices paid by public drug programs affect all of us

As most publicly funded drug programs in Canada base eligibility for benefits on age, these findings are relevant to taxpayers. The results of our study show that prices for the generic drugs most commonly prescribed to seniors living in Canada are significantly higher than American prices for identical drugs, which means that Canadian drug policies are failing to provide better outcomes with respect to generic drug prices than more free market-based policies could produce. Taxpayers would be better off if prices for generic drugs were determined by competitive market forces.

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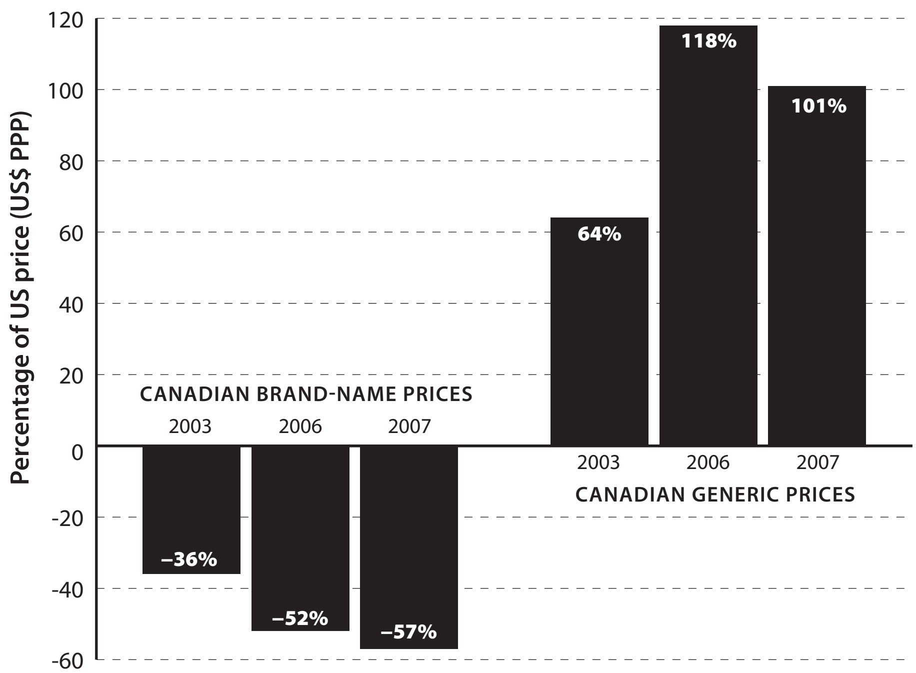
Figure 1: Average Canada-US price differences for the brand-name and generic drugs most commonly prescribed to seniors, 2003, 2006, and 2007



Source: Skinner and Rovere, 2008a.

Combating AIDS in Africa

Poor policy prevents Africans from getting medicine

Thompson Ayodele

Twenty-five years after the disease was first discovered, AIDS remains an epidemic, claiming over two million lives each year.

As an African, I've witnessed first-hand the suffering caused by this disease. Although sub-Saharan Africa accounts for only about 12% of the world's population (Population Reference Bureau, 2007), it accounts for two thirds of those infected with HIV and 75% of all AIDS-related deaths (UNAIDS, 2008).

Western activists continue to blame the high price of drugs for the continued prevalence of the disease in Africa. They argue that poor countries should be permitted to violate pharmaceutical patents to produce cheap knock-off versions locally.

Unfortunately, the activists are not just wrong; their policy proposal is flat-out dangerous. The real causes of restricted access to AIDS drugs are Africa's derelict transportation systems, widespread corruption, and poor utility infrastructure.

Most of the high-quality AIDS drugs that Africa imports must be transported over vast distances and stored for extended periods of time before they can be distributed. But the roads and warehouses in most African countries are poorly maintained. Electricity, which is necessary to keep drugs refrigerated, is scarce. Corrupt officials often exploit weaknesses in the supply chain, and extort hefty bribes from aid personnel.

On April 26, 2001, African leaders pledged to invest 15% of their budgets in health care infrastructure. Seven years later, very few have come even close to meeting that commitment. Nigeria, for example, devotes less than 6% of its budget to health (Nigeria, Federal Ministry of Finance, 2008). Most of Africa's impoverished people still lack health insurance. Medical workers earn low wages, which has led to low morale and a dearth of qualified personnel. The National Association of Nigerian Nurses and Midwifes says that the country's hospitals urgently need 300,000 additional nurses (Onwuemenyi, 2008, May 13).

The trade policies of African governments often make the AIDS problem worse. For example, all pharmaceuticals (except those containing insulin) imported into Uganda and Tanzania are subject to a 10% tariff.

The trade policies of African governments often make the AIDS problem worse. For example, all pharmaceuticals (except those containing insulin) imported into Uganda and Tanzania are subject to a 10% tariff (Olcay and Laing, 2005). The rate jumps to 40% in Sierra Leone and up to 34% in Nigeria (European Commission, 2003: 7; Stevens, 2007: 149). These countries should follow the lead of Kenya, which eliminated its 10% import tariff on necessary medicines in 2005.

Giving African governments the power to manufacture patent-protected pharmaceuticals locally would likely result in patients receiving inferior or ineffective drugs. In Thailand and India, for example, locally produced AIDS drugs are often of such low quality that they're actually fuelling drug resistance.

Western drug companies have already gone to great lengths to make their drugs affordable to the world's poorest patients. Many use tiered pricing models, in which Western customers pay substantially higher prices than people in poor countries do. And just last year, GlaxoSmithKline, Merck and Pfizer donated hundreds of millions of dollars worth of drugs to Africa (Adelman and Norris, 2004).

Now more than ever it is important to look at how the West can better assist the developing world in its battle against this deadly disease. But we cannot forget that governments in the developing world need to play their part as well. Instead of violating patent protections, without which there would be no drug innovation, they need to clean up their policies.

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A question of balance

Unionization policies in Canada and the United States

Jason Clemens &
Niels Veldhuis

Labour relations laws are intended to balance power between employers and employees, who are represented by unions. Changes to labour relations laws that tilt the balance too far in either direction impose serious costs on workers and the economy.

A number of significant changes to American labour relations laws are likely to be made now that President Barack Obama and noted pro-union Secretary of Labor Hilda Solis are in government. The proposed Employee Free Choice Act would not only restrict worker choice, but would also throw labour markets out of balance, creating negative consequences for the American economy.

The proposed changes in the United States are a marked shift from its historical approach to labour relations laws. Currently, the United States enjoys a relatively balanced set of labour laws that provide unions with an opportunity to convince workers of the benefits of collective representation while retaining worker choice and freedom with respect to that decision. One way that the United States ensures this balance is by maintaining relatively low and equal thresholds to trigger a union vote for certification and decertification.

Unions wishing to represent workers only have to obtain signatures of support from 30% of workers in order to have the National Labor Relations Board (NLRB) institute a secret-ballot vote to certify a union. By comparison, Canadian provinces require an average of 40%, with one province, Prince Edward Island, requiring a majority of workers (50% plus 1).

Once the NLRB has issued a vote, workers are able to obtain information regarding the costs and benefits of unionization and then are free to cast a secret ballot as to whether or not they wish to be represented by a union. There are many penalties that the NLRB can impose for improper behaviour, in order to ensure a fair process.

By contrast, the grossly misnamed Employee Free Choice Act would allow unions to be certified without a secret-ballot vote if enough workers (50% plus 1) support certification by signing union cards in the first step (referred to as a card check). This would significantly tilt the balance of power in favour of unions, and would negatively affect workers, employers, and the economy.

The experience of several Canadian provinces demonstrates just how dire the consequences can be. Over the last three decades, several provinces have changed from secret-ballot voting to automatic certification.

Professor Christopher Riddell of Queen's University in Kingston, Ontario, has completed pioneering work on the effects of different certification mechanisms. In a 2004 study published in *Industrial and Labor Relations Review*, Riddell examined unionization rates in British Columbia between 1978 and 1998. In 1984, the province implemented secret-ballot voting and then reverted to automatic certification in 1993. Professor

Riddell found that unionization success rates fell by 19% after mandatory secret-ballot voting was introduced, and then increased by nearly the same margin when it was eliminated.[1]

Similarly, Professor Sara Slinn (2004), also of Queen's University, investigated the effect of Ontario's change from a card-check system to secret-ballot voting. Her research, published in the *Canadian Labour and Employment Law Journal*, showed that the introduction of secret-ballot voting in 1995 reduced the likelihood that a union would be certified by 21%.[2]

In 2007, the unionization rate was 31.5% in Canada and 13.3% in the United States. One of the reasons offered for this marked difference in unionization rates—which were almost identical in the mid-1960s—is the difference in how unions are certified. A 2004 study by Professor Susan Johnson, published in *Industrial Relations*, examined unionization rate differences between Canada and the United States. She concluded that "17 to 24 percent of the density gap in 1998 can be attributed to the widespread use of mandatory votes in the United States." In other words, Canada's unionization rate is higher than the American rate because Canadian labour laws do not require secret-ballot voting to the same extent.

Eliminating secret-ballot voting in the United States will undermine the balance of the current system, and key drivers of a dynamic and prosperous labour market. A growing body of scholarly research confirms that flexible labour markets outperform regulated ones in terms of job creation, investment, and general prosperity.

For example, Harvard Professor Rafael Di Tella, along with his Princeton counterpart Robert MacCulloch (2005), looked at 21 industrialized countries from 1984 to 1990 to ascertain the influence of labour market flexibility. They found that flexible labour markets enjoyed lower rates of unemployment and, in particular, lower rates of longer-term unemployment. There are literally hundreds of supporting studies that verify the benefits of balanced, flexible labour markets.

More specific to the issue at hand, professors Timothy Besley and Robin Burgess (2004) examined the influence of changes in labour laws in the manufacturing sector. They concluded that changes moving the balance of power towards collective representation (through unions) resulted in lower output, less employment and investment, and lower productivity.

Eliminating the ability of workers to vote privately and anonymously represents a significant shift in the balance of power towards unions. Like the Canadian experience attests, the cost of such changes would be substantial for American workers, who would bear the burden of higher unemployment rates, less investment, and a less prosperous economy. These costs would be widely dispersed while the benefits would be largely concentrated among union leadership and union members whose jobs would be protected. This is not likely to strike most Americans as a reasonable balance of power.

Big unions and several Democrats are pressing hard for the Obama administration to champion this shift in the balance of power. It's critical for the sake of American workers and indeed the American economy that Obama look north and learn from the Canadian experience with this un-democratic and economically destructive policy.

Notes

1 In 2001, British Columbia reverted back to the more democratic method of secret-ballot votes.

2 In 2005, the Ontario government removed the requirement for secret-ballot voting for the construction sector and replaced it with a card-check system. A new study published in *Canadian Public Policy* found that the 2005 changes are already having an impact on the volume of union-organizing attempts and their success rates. Specifically, these changes have led to an average increase of seven new bargaining units certified per month. This translates into an overall increase in certification success rates of 10.2 percentage points.

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