



THE Quarterly

SUMMER 2014

Canadian Government Indebtedness

\$1.2 trillion
Direct debt

The image shows a large iceberg floating in the ocean. The top part of the iceberg is above the water, and the bottom part is submerged. The submerged part is much larger than the visible part, illustrating the concept of hidden debt. A small white figure is sitting on the water surface near the submerged part of the iceberg.

\$2.9 trillion
Other types of debt

\$243,476
per taxpayer

CANADIAN PUBLICATION MAIL SALES PRODUCT AGREEMENT NUMBER 40069269

ALSO INSIDE

Government meddling to combat obesity

School choice in Canada

Air pollution and economic freedom



Niels Veldhuis
President, Fraser Institute

Dear Fraser Institute Friends and Supporters,

I hope you are all enjoying the early days of summer. Here at the Institute we have had a busy year thus far, tackling the most pressing policy issues in the country.

One of those issues is the increasingly high levels of debt accumulated by our governments. In March we released *Canadian Government Debt 2014* which calculated the total amount of debt racked up by federal, provincial, and municipal governments.

While politicians usually focus on how much direct government debt (debt that constitutes a direct legal contract) has been accumulated, direct debt is just the tip of the debt iceberg as the picture on the cover highlights. It does not include the unfunded liabilities of government programs like Old Age Security, Canada Pension Plan, and medicare.

As Charles Lamnam, Milagros Palacios, and Hugh MacIntyre highlight in their article on page 18, when a government promises to provide certain benefits for a specific period but lacks the necessary resources to do so, the program is said to have an unfunded liability. When all of the debt and unfunded liabilities are added up, Canadian governments have produced a \$4.1 trillion fiscal hole.

Across the provinces, Quebec and Ontario are in the worst shape when it comes to government indebtedness. On page 15, Sean Speer and I respond to the CIBC's criticism of our work highlighting Ontario's worrying level of indebtedness by comparing it to that of California. Sean also summarizes the Institute's recent study on Quebec's indebtedness on page 6.

This spring the Institute was pleased to publish two commentaries by Philip Cross, former chief economic analyst for Statistics Canada. You can read a summary of his study *Economic Consequences of the Lower Canadian Dollar*, which details the negative effect of a weaker loonie on individual Canadians and businesses, on page 8.

On a more positive note, Joel Wood and Ian Herzog's recent study (page 10), released as the world celebrated Earth Day on April 22, finds that higher levels of economic freedom lead to cleaner air.

We hope you enjoy this issue of *The Quarterly*. As always, if you have any feedback, please don't hesitate to call or email.

Best,

A handwritten signature in blue ink, appearing to read 'Niels Veldhuis'.

Niels Veldhuis

New Research



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The Fraser Institute, 4th Floor, 1770 Burrard Street, Vancouver, British Columbia Canada V6J 3G7

How Much School Choice Do Parents in Canada Enjoy?

Jason Clemens, Milagros Palacios, Jane Loyer, and Frazier Fathers

More and more research is showing that in general, education improves when parents can choose the schools their children attend and when schools are forced to compete with each other for students. Education is decentralized to the provinces in Canada, meaning that the degree to which parents enjoy school choice is heavily dependent on the province as well as the city they reside in.



However, this does not mean that the public education systems in Canada do not provide some level of choice to parents and competition between schools. For example, one source of choice is second language schools—French in all provinces except Quebec, and English in Quebec. Enrolment in these public schools ranges from 0.4% in Newfoundland & Labrador to 28.2% in New Brunswick. In addition, many principal language schools offer language immersion programs, which further the level of choice.

PUBLIC EDUCATION

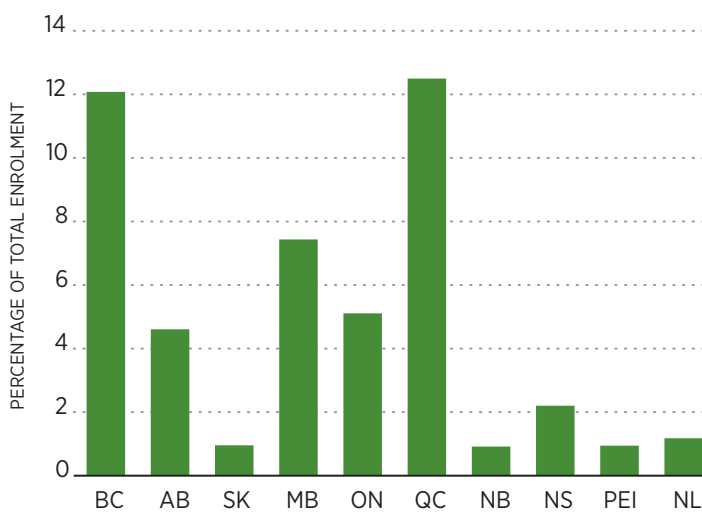
Unfortunately, there is a lot of misunderstanding about school choice and competition. Between 87.5% (British Columbia and Quebec) and 98.8% (Newfoundland & Labrador and Prince Edward Island) of Canada's K-12 students attend public schools. Many Canadians see these statistics as a sign of a lack of choice and competition.

But the reality is much more complicated as our study, *School Choice in Canada: An Update*, by Jason Clemens, Milagros Palacios, Jane Loyer, and Frazier Fathers shows. Principal language public schools—Anglophone in all provinces except Quebec, which is Francophone—dominate public school enrolment: between 63.3% (Ontario) and 98.5% (Newfoundland & Labrador) of all students attend such schools.

Another source of choice and competition within the public education system comes from separate, religion-oriented schools. Alberta, Saskatchewan, and Ontario provide full funding for religious schools, principally Roman Catholic, within the public education system. Between 21.1% (in Saskatchewan) and 30.3% (in Ontario) of students in these provinces are enrolled at religiously-focused, fully funded public schools.

Finally, charter schools also provide parental choice and competition between schools. Charter schools are autonomous, not-for-profit schools within the public system. They provide alternative education programs and generally have more flexibility in their curriculum, teaching style, and approach to learning than do public schools. Currently Alberta is the only province offering charter

INDEPENDENT SCHOOL ENROLMENT BY PROVINCE, 2009-10



schools. While only a small share (1.3% of all Alberta students) attends charter schools—these schools do, nonetheless, increase parental choice and competition.

All told, enrolment in public schools—including principal language schools, alternative language schools, immersion language programs, separate religious public schools, and charter schools—ranges from 87.5% in British Columbia and Quebec to 98.8% in Newfoundland & Labrador and Prince Edward Island. The choice available to parents within the public education system ranges widely depending on the province and city.

INDEPENDENT SCHOOLS

Every Canadian province has an independent school system that is separate and distinct from the public system. The nature of the independent school sectors, and their funding and regulations vary by province. Student enrolment in independent schools also varies by province, ranging from just 0.9% in New Brunswick and Prince Edward Island to 12.5% in Quebec. British Columbia (12.1%), Manitoba (7.4%) and Ontario (5.1%) also have relatively high levels of independent school enrolment.

HOME SCHOOLING

Home schooling, whereby parents educate their children on their own, offers parents another alternative. All 10 provinces permit home schooling, though the degree

to which it is supported varies greatly. Alberta offers the most support; it gives parents resources, funding, and helps facilitate mechanisms for home schooling. Even in that province, however, at 1.6 percent of student enrolment, home schooling enrolment remains marginal. In most provinces, enrolment rates are below 0.5 percent of total school enrolment.

CONCLUSIONS

Alberta currently offers the most school choice in Canada. It has six different, fully-funded public school choices (depending on residential area), provides substantial funding to students attending independent schools, helps parents who are educating their children at home, and gives some support to charter schools. At the other end of the spectrum, there is less choice for parents and less competition among schools for students in the Atlantic Provinces. This includes no public support for religiously-oriented schools and no public funding for independent schools. School choice and competition in the other provinces fall in the range between these two limits. Ontario, for instance, provides a fair degree of choice within the public education systems but fails to provide any support for independent schools. [FI](#)



JASON CLEMENS



MILAGROS PALACIOS



JANE LOYER

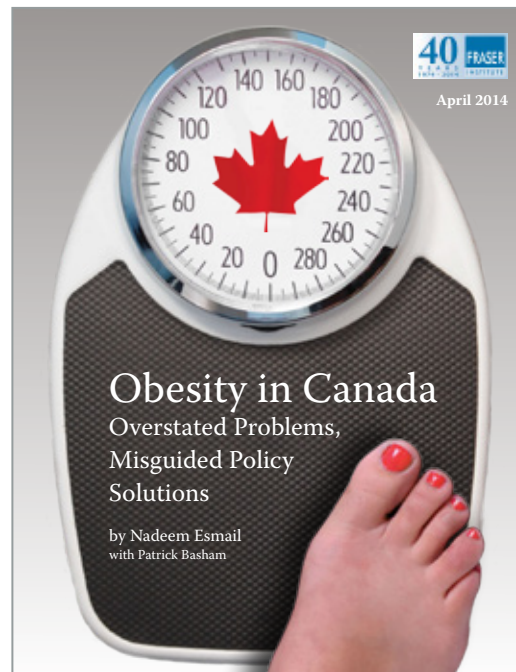


FRAZIER FATHERS

Jason Clemens, and Milagros Palacios are economists with the Fraser Institute. Jane Loyer and Frazier Fathers were 2013 Fraser Institute interns.

Obesity in Canada No Cause for Panic

Nadeem Esmail with Patrick Basham



Contrary to the prevailing wisdom of many Canadians, measurements of overweight and obesity among the Canadian population from Statistics Canada suggest that Canadians should not be particularly worried about an obesity “epidemic” overtaking the country. Among Canadian adults, there has been no statistically significant change in the rate of overweight (Body Mass Index between 25 and 30) between 2003 and 2012. For those considered obese (with a Body Mass Index greater than 30), the rate among Canadian adult males appears to have stabilized or even begun to decrease. For adult females, however, there has

been a steady increase in the prevalence of obesity since 2003. Among Canadian youth (aged 12 to 17), the rates of overweight and obesity between 2005 and 2012 are largely unchanged (2003 data were not available).

The health consequences of excess weight might also be overstated in the popular debate. A number of studies of the relationship between overweight, obesity, and early mortality have suggested that the risks associated with obesity lie at the higher end of the scale, above a BMI of 35 (known as Class II or Class III obese). They also suggest those who are classified as

overweight, with a BMI between 25 and 30, may have lower rates of premature mortality than those who are “normal weight,” while those who would fall into the Class 1 obese range with a BMI of 30 to 35 face similar risks to those in the normal weight range.

This suggests that the health-based justification for obesity interventions may only exist among a small section of the population with very high excess weight: a much smaller proportion of the population than is commonly claimed to be at risk.

While much of the focus on obesity relates to the health consequences of carrying too much excess weight, there is also the important concern about the costs obesity imposes on the economy. Indeed, many advocates justify their desire to intervene by pointing to the increased burden on Canada’s tax-financed health system. However, a closer examination shows that the majority of the costs of obesity are borne directly by the individual—in terms of lower income, reduced employment opportunities, reduced enjoyment of life, greater illness, and a potentially shorter lifespan. The data also show that the justification for intervening to save the tax-funded health care system from the costs that the obese allegedly impose is weakened by the possibility that obese individuals may in fact not be a net burden to taxpayers over their lifetimes.

There is also little solid evidence that commonly proposed government policy interventions could systematically reduce the prevalence of excess weight and obesity.

There is also little solid evidence that commonly proposed government policy interventions could systematically reduce the prevalence of excess weight and obesity. To the contrary, even if concerns about poor consumer decision making are correct, commonly recommended interventions (e.g., fat taxes or junk food taxes, menu labeling requirements, reduced availability

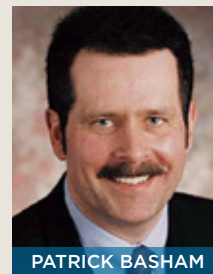
of particular foods, simplified or directive food labels, graphic warning labels, vending machine bans, zoning restrictions, and advertising restrictions) are likely unable to reduce obesity. Private solutions may be more effective in helping individuals reduce excess weight.

While government interventions may not be effective in reducing obesity prevalence, they would impose costs indiscriminately (and potentially regressively) on both non-obese and obese Canadians, not to mention inappropriately vilifying particular foods and food manufacturers. Increased costs for individuals and families might come from reduced choices, increased travel times, increased costs from taxation, increased costs of goods and services as a result of regulation, or taxpayer funding of programs and of the increased bureaucracy that may be required. Interventions may also create barriers to entry for smaller businesses or artificial constraints on growth, and generate higher business costs from regulation.

In total, a review of the facts about the prevalence of obesity, the risks associated with obesity, and the efficacy of commonly proposed policy interventions suggests a very different truth about obesity. While there still may be too many expanded Canadian waistlines, the number appears to have stabilized and may even be turning a corner. Further, health concerns associated with obesity may affect fewer Canadians than is sometimes suggested by advocates of government intervention. Finally, commonly proposed government interventions would not be likely to change behaviours in ways that systematically lead to a lower prevalence of obesity. [FI](#)



NADEEM ESMAIL



PATRICK BASHAM

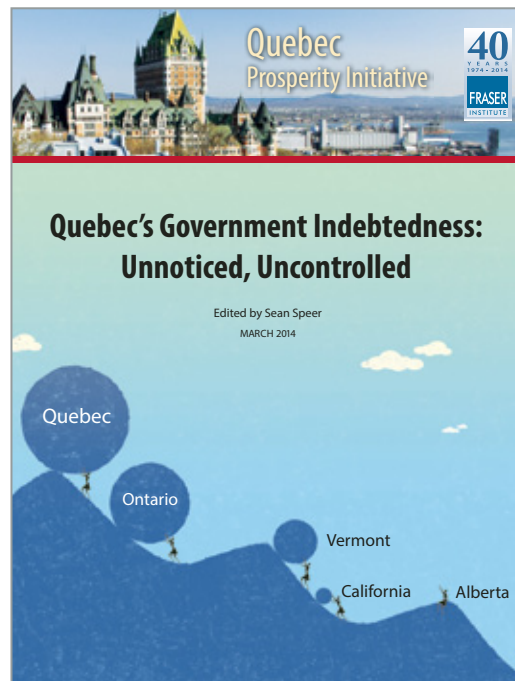
Nadeem Esmail is a senior fellow of the Fraser Institute. Patrick Basham is founding director of the Democracy Institute and was an adjunct scholar with Cato’s Center for Representative Government in Washington, DC.

Quebec: Most Indebted Province

Sean Speer

Quebec's recent election was fought over a range of important issues, including the province's place in confederation and the ongoing debate about how to accommodate the traditions and cultures of those new to the province. Quebec's budget deficit and high government debt also received considerable public attention during the campaign. The Fraser Institute study, *Quebec's Government Indebtedness: Unnoticed, Uncontrolled*, contributed to this public discourse.

The purpose of the study was to show Quebecers that the province is not only the most indebted in Canada, but even among US states, such as California and New York, that have received considerable attention for their lack of fiscal discipline and high government debt. These comparisons enable readers to better understand where the province's indebtedness stands



today, what it can expect for the future, and what the cost of inaction might be.

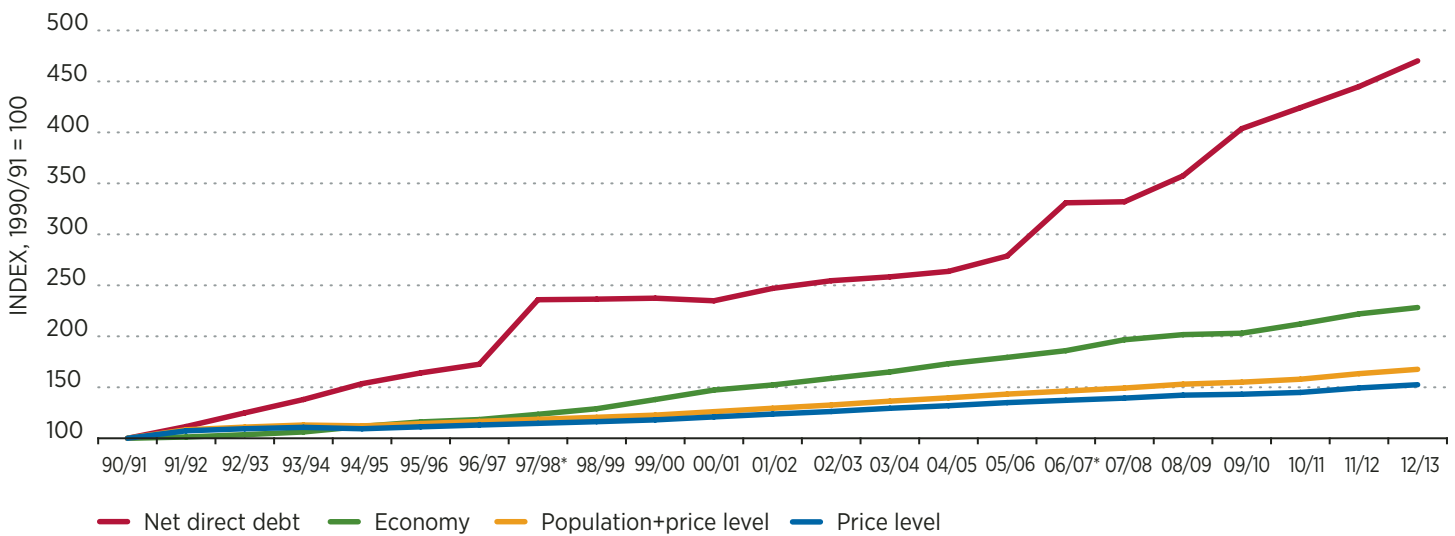
Some of the data are staggering and ought to serve as a wake-up call for *la belle province*.

Quebec's net direct debt has grown in nominal terms, that is, without adjusting for the effects of inflation, from \$37.6 billion in 1990/91 to \$175.5 bil-

lion in 2012/13. This growth in government debt has significantly outpaced growth in Gross Domestic Product (GDP), population, and inflation. And it is slated to continue to grow; the province's return to a balanced budget is projected to be a few years away.

This level of indebtedness now represents 49 percent of Quebec's GDP and in 2012/13 required debt interest payments of \$9.8 billion or 11 percent of government revenue. Both measures, it is important to note, are the highest among all Canadian provinces.

**INDEX COMPARISON BETWEEN NET DIRECT DEBT, GDP, POPULATION, AND PRICE LEVEL
1990/91 - 2012/13, WHERE 1990/91 = 100**



But the study went beyond Canada and sought to compare Quebec’s indebtedness with a broad cross-section of US states. The comparison shows that Quebec’s government debt is higher than the 24 states to which we compared it.

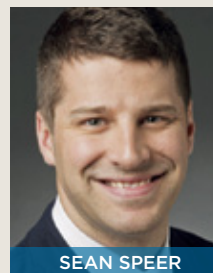
Quebec’s bonded debt for 2011 (the last year for which we have data) was \$160.8 billion, representing approximately 47 percent of the province’s GDP, which greatly exceeded the levels found in US states, including Vermont, which at 17.1 percent has the highest bonded debt-to-GDP ratio. Quebec’s bonded debt per capita is more than double the amount borne by the worst American case—\$20,162 for Quebec and \$8,691 for Alaska—and 65 percent higher than New York’s, which has been called a “crisis” in recent years and the subject of a major task force review.

Strikingly, these figures only account for the Quebec’s direct and bonded debt. Its indebtedness is driven even higher once municipal debt in the province (for which Quebecers are ultimately responsible) is accounted for, along with its share of the federal debt, and indirect debt such as future liabilities including debt guarantees and unfunded obligations under the Quebec Pension Plan.

If Quebecers are concerned by the current situation, they should be very alarmed at the future, which will be

even bleaker without decisive short- to medium-term action. If the Quebec government continues to tax and spending at current levels, this study estimates that the province’s debt-to-GDP ratio could exceed 57 percent in the next ten years.

Quebec’s new government is now responsible for addressing these challenges. If it is to succeed in getting the province’s debt under control, it will need to participate in a full debate about the role of government in the province and the types of major reforms needed to improve the efficiency of its services and the competitiveness of its economy. The Fraser Institute looks forward to building on the recent study and contributing to this important public debate. [FI](#)



Sean Speer is the associate director for the Centre for Fiscal Studies at the Fraser Institute.

Consequences of a Lower Canadian Dollar

Philip Cross

After hovering around parity with the US dollar for three years, Canada's loonie fell sharply in 2013 to near 90 cents (US), where it still hovers. Initially, the lower dollar was greeted with relief, especially for our manufacturing exporters. However, as the dollar continues to languish, awareness grows that the benefits of a weaker loonie are small compared with its costs.

Our lower exchange rate automatically raises the Canadian price for goods where an integrated North American market sets one price in US dollars—mostly gasoline and home heating fuels. The lower Canadian dollar already has opened up a gap between the price for these goods in the US and in Canada. In January 2014, for example, the price of gasoline in the US edged up 0.1 percent from January 2013, while in Canada it was up 4.6 percent. Prices will rise soon for



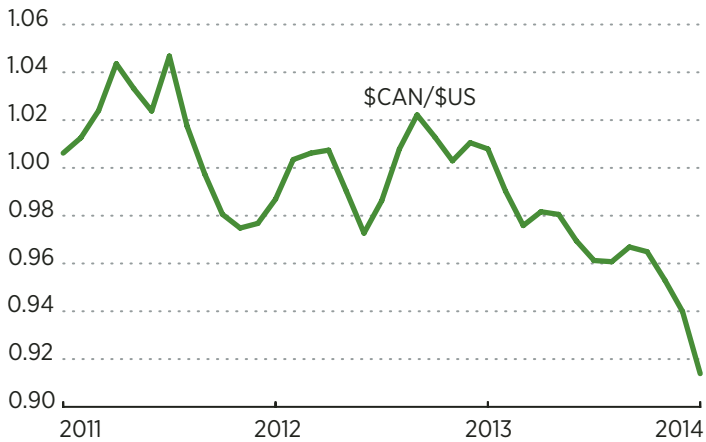
products that consume a significant amount of energy, such as air travel.

Prices for some other products are sensitive to the exchange rate. The cost of fresh fruit and vegetables, mostly imported during our winter months, was up an average of 4.1 percent in Canada from a year earlier, compared with a slight decline in the US. Of course, cross-border shoppers face large price increases, since they automatically have to pay more to buy US dollars. The same increase

will face Internet shoppers buying products priced in US dollars.

Not only consumers will pay higher prices. Businesses import most of their machinery and equipment. Faced with higher prices, firms will trim their outlays for machinery and equipment, which ultimately will depress productivity and wages in the future. Meanwhile, governments will feel an increased burden of their debt that is denominated in US dollars.

CANADIAN EXCHANGE RATE



The benefits of a lower exchange rate go primarily to exporters. Firms that earn US dollars from exports will profit from a lower exchange rate, as these US dollars buy more Canadian dollars when they are repatriated. Even here, the benefits are likely to be limited to prices, since the volume of exports shows little sensitivity to the exchange rate. The volume of Canada's exports is largely determined by the trend and composition of demand in our major export markets.

Some may view a lower dollar favourably out of hope it will shift growth from natural resources to manufacturing. They will be disappointed. The most stimulus to exports from a lower dollar is for natural resources, which need it the least, and the least stimulus is for manufacturing, which needs it the most. This reflects how manufacturers adapted to the higher dollar over the past decade. When the dollar was near parity with the US greenback, firms hedged their exposure to the high dollar by reducing their reliance on exports and increasing their use of imported inputs. This "natural hedge" reduced the net exposure of manufacturing firms to exchange rate fluctuations by almost ten percentage points in the past decade. Meanwhile, our natural resource industries have the highest net exposure to a lower dollar, because they export most of their output while importing few inputs. With prices already high for most commodities, this will further tilt our economy towards natural resources.

The other major beneficiary of a lower exchange rate is to Canadians invested abroad, who pocket more Canadian dollars when they repatriate these investments. This is a dubious benefit for our economy. It rewards

people for not investing in Canada at the cost of lowering the value of all assets in Canada. The losses foreigners will feel on these investments will make Canada a less attractive place to invest in the future, while encouraging Canadians to invest more abroad. The myth that a low exchange rate encourages economic growth took hold in Canada in the 1990s. Canada's manufacturing growth was led by low-wage industries such as clothing, textiles, and furniture, where employment rose 29.7 percent from 1992 to 2000. The flimsy basis for this allocation of resources was fully revealed when a rising dollar and China's exports devastated these industries. In retrospect, one can only look back with wonder and astonishment that Canada acted as if our future lay in investing in low-wage industries predicated on a chronically low exchange rate. Even the 1990s boom in autos and high tech was partly a figment of a low exchange rate, which enabled these exporters to reap export earnings in US dollars while paying their Canadian workers the equivalent of 63-cent US dollars. It was a business model doomed to fail when the exchange rate started to appreciate.

Devaluationists should be pleased that the boost to manufacturing indeed seems to be happening. Factory jobs have risen 1.5 percent since last October, while investment in manufacturing is projected to rise further in 2014. However, there is no sign this is boosting the overall economy, as both total employment and business investment have stalled. Apparently, there is something more to economic growth than just revving up factory output. At least we no longer have to listen to the acrimonious and tiresome debate about Canada's manufacturing sector suffering from "Dutch Disease." But what do you call an economy where manufacturing prospers and the rest of the economy languishes? Perhaps "Asian Disease," where exports flourish but domestic demand retards growth. [FI](#)

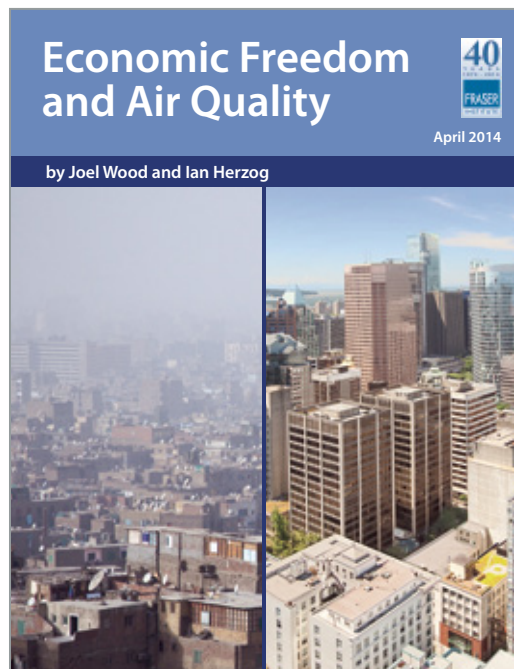


PHILIP CROSS

Philip Cross is the former Chief Economic Analyst for Statistics Canada and the author of Fraser Institute commentaries on a wide range of economic issues.

Air Pollution Declines as Economic Freedom Rises

Joel Wood and Ian Herzog



It is well established that economic freedom is one of the main drivers of economic prosperity. Economic freedom is the extent to which you can pursue economic activity without government interference as long as your actions don't violate the rights of others. Pollution is generally given as an example of a situation where the economic actions of one person violate the rights of others, thus justifying government intervention. However, the same economic institutions that contribute to economic freedom may also lead to a cleaner environment.

Property rights, open markets, and a vibrant private economy are critically important economic institutions that affect environmental outcomes. Ever since the seminal work of Nobel laureate Ronald Coase, secure property rights and a strong justice system have had a recognized ability to protect people and their property from pollution. Inappropriate government regulation can impede negotiations between those benefiting from and those being hurt by a polluting activity, preventing an efficient distribution of the right to the environmental resource and causing inefficient levels of pollution. In contrast, openness to trade is key to

ensuring that new, cleaner technologies can be adopted across borders. Bureaucratic inefficiency, the influence of special interest groups, and the prevalence of state-owned enterprises can all hinder the ability of a government to effectively improve the environment. All of these economic institutional factors are captured in the index published in the Fraser Institute's annual report, *Economic Freedom of the World* (see freetheworld.com).

The results lend support to the proposition that economic freedom creates the incentive to abate local air pollution.

In a dataset giving concentrations of fine particulate matter for 105 countries around the world (taken from the World Bank's *World Development Indicators*), the 20 countries rated the most economically free by the *Economic Freedom of the World* index experience much cleaner air quality than the 20 countries with the lowest scores for economic freedom. Indeed, in 2010, the 20 countries that were most economically free had average concentrations of fine particulate matter that were nearly 40% less than those in the 20 least-free countries. Of course the story is more complicated than that: the freest countries are also richer and per-capita income has long been shown to be correlated with both economic freedom and pollution.

Economic Freedom and Air Quality examines a dataset for over 100 countries from 2000 to 2010 to identify the relationship between economic freedom and two environmental indicators (concentrations of fine particulate matter and carbon dioxide emissions). After controlling for the effects of income, political freedom, and other confounding variables, the authors find that a permanent one-point increase in the *Economic Freedom of the World* index results in a 7.15 percent decrease in concentrations of fine particulate matter in the long-run, holding all else equal. This effect is robust to many different model specifications and is statistically significant. This effect is in addition to a general 36 percent decrease over time in fine particulate matter due to unidentified factors.

The results for carbon dioxide emissions per capita are not as promising. The authors do find evidence of a short-run negative effect in their preferred statistical model specification. However, this effect disappears under other plausible model specifications. Put simply, they cannot find an effect of economic freedom on carbon dioxide emissions. Ultimately, they can only conclude that economic freedom is indeed important for reducing local environmental problems.

A permanent one-point increase in the Economic Freedom of the World index results in a 7.15 percent decrease in concentrations of fine particulate matter.

Nevertheless, the results lend support to the proposition that economic freedom creates the incentive to abate local air pollution, such as particulate matter. It appears that the same may not be true for environmental issues of a global nature, such as carbon dioxide emissions. Nevertheless, it appears that appropriately designed and managed institutions that promote economic freedom and strong property rights are an integral step in the direction of sustainable development. It is especially notable that this effect is distinct from that of political institutions, income, and other country-specific characteristics. [FI](#)



Joel Wood was Associate Director for the Centre for Risk and Regulation. He holds a Ph.D. in Economics from the University of Guelph. Ian Herzog is an Economist at the Fraser Institute. He holds a Master's degree in economics from the University of Toronto.



Students rapping about “time”—the most valuable scarce resource and the reason we make choices.

Our popular spring program for junior and senior high school students came to a successful conclusion in May. These four fully attended programs, held in Vancouver and Victoria, saw over 500 students attending from 18 schools; another 177 students joined the wait list.

By teaching students the fundamental principles of economics at a young age, we aim to help them learn how to think critically about the decisions they make today, the future consequences of those decisions, and how their behavior influences the world around them.

Unfortunately, many students are not exposed to this economic way of thinking in their classrooms. Of those who have been taught economics, many associate it with a dry textbook and find it difficult to understand. Students who come to our junior and senior high school programs enjoy award-winning economic educators teaching in a hands-on, interactive environment that uses short lectures, games, videos, and activities. Once

a concept has been introduced to the larger group, students break into smaller groups to participate in interactive simulations and games that review the concept with a group leader. Students are engaged and begin to understand just how relevant economics is in their lives.

“This seminar helped me learn that I always have more than one choice.”

JUNIOR HIGH SCHOOL STUDENT

Economics is Everywhere! Applying Basics Concepts to Everyday Life is offered to junior high school students (grades 7–9). This exciting new program is similar to our senior student program, but introduces economic concepts at a more basic level suitable for younger students. From a fishing game demonstrating incentives to group karaoke showing supply and demand, students



Students wearing hats they made during an activity that demonstrates different economic systems.

“I learned that opportunity costs are part of every decision I make, so I better think about what they are before I make a decision.”

HIGH SCHOOL STUDENT

participate in a fun-filled day that shows how economic thinking can be applied in their daily lives.

Why Do People Behave the Way They Do? An Introduction to Economic Reasoning is offered to students in grades 10-12. Students are encouraged to apply economic thinking to common situations and scenarios. From pop culture phenomena to hitting the “snooze” button on an alarm clock, from balancing a budget to saving for college, students learn how every decision they make stems from an economic choice.



Students learning about incentives and answering the question, “Who would bring an apple a day to their teacher if it meant they could get an ‘A’ in the class?”

These programs are a great complement to many courses including economics, social studies, career planning, and business education.

TEACHER WORKSHOPS

In April we held one of our teacher workshops, *The Economic Way of Thinking*, for the first time in Edmonton, Alberta. It is part of our ongoing effort to expand and develop our network of teachers interested in learning about exciting new ways to teach students about economics. Participants spent the day with expert economics instructors who brought a series of lessons and activities to life. The teachers left with handouts, lesson plans, and exciting ideas to implement in their own classrooms. As an added bonus, they enjoyed valuable networking opportunities with other teachers of economics.

To ensure optimal attendance at our workshops we keep teachers’ busy schedules and small budgets in mind. We offer a limited number of travel and substitute teacher bursaries; we hold the workshops in major cities that are easy to reach; and we provide quality materials. We aim to ensure each teacher’s time has been well invested.

The 17 teachers in attendance in Edmonton had many positive things to say and asked us to return to offer more workshops, which we intend to do in the fall.



Two teachers assist instructor Charity-Joy Acchiardo in an activity demonstrating price discrimination at our Edmonton workshop.

The power of our workshops to have an impact on large numbers of students is impressive: these 17 workshop participants will each go on to teach a yearly average of 90 students the lessons we provided. That's 1,530 students annually who will be influenced from this

I just wanted to mention that this was probably the most useful teacher workshop that I have attended in a very long time. The content was well presented, activities very useful and even inspiring. I look forward to incorporating many ideas from the workshop in my classes.

Please let me know if you have any further presentations in this series as I would love to attend them.

PARTICIPATING TEACHER

one workshop. Assuming the teachers will continue to teach and use some, if not all, the materials for at least another four years, that's an additional 6,120 students being reached.

2014 INTERNS WELCOMED

It's that time of year again when the summer interns are arriving. With them comes an injection of youthful exuberance to our head office. This year, we will have seven interns in Vancouver working in both research and education programs. We expect a summer full of fresh perspectives, engaging discussions, and great work from these bright minds.

Among the interns are:

Jason Chau has a 2D Animation Diploma from the Vancouver Institute of Media Arts and a BA in Sociology from the University of British Columbia.

Taylor Jackson holds a BA in Political Science from Simon Fraser University and is currently an MA candidate at SFU. This will be his second internship at the Fraser Institute.

Aaron Jacobs completed his MA in Economics at the University of Toronto. He holds a B.A.Sc. from McMaster University.

Matthew Lo completed a BES (Hons.) from the University of Waterloo in Economics, and Environment and Business.

Loreena Percy will complete a Bachelor of Commerce in International Business and International Relations in the fall at McGill University's Desautels Faculty of Management.

Snow Ren holds an MA in Economics from Lakehead University, and is a PhD candidate in Economics at the University of Ottawa. She also has a BA in Statistics from Hunan Normal University.

Alyson Tan recently graduated from the University of Western Ontario, Huron University College, with a BA (Hons.) in Global Development. [FI](#)

Is There Any Wonder Why Ontario Is in the State It's In?

Niels Veldhuis and Sean Speer

ONTARIO DEBT



As Ontario continues to undermine its economic future with growing debt, the province does not receive near the critical scrutiny it should from the media and financial markets. In reading CIBC World Markets' latest *Economic Insight*, it's not hard to understand why.

CIBC takes aim squarely at a recent study published by the Fraser Institute highlighting Ontario's worrying level of indebtedness by comparing it to that of California, which has received widespread attention for its long-standing inability to balance its budget and growing government debt.

The study finds that California's \$144.8 billion (US) debt pales in comparison to Ontario's \$267.5 billion (Cdn)

government debt, despite California having a larger economy and population. When boiled down to a per person basis, Ontario's government debt is more than five times that of California.

CIBC, however, leaps to Ontario's defense, claiming that the Fraser Institute study misses "the fundamental point" that Canadian provinces and US states "aren't peers" and that comparing them "is folly."

In reading the CIBC's *Economic Insight*, one of course must ponder just who exactly is missing the point.

CIBC's *Economic Insight* explains that provinces and states cannot be compared because "provinces are endowed with great fiscal flexibility, including sovereign-like taxing powers, an unchecked ability to run bud-

get shortfalls.” Meanwhile US states, “exhibit less fiscal flexibility; they’re generally prohibited from running operational shortfalls, must clear higher hurdles when it comes to raising taxes, and face more binding constraints on issuing debt.”

It is certainly true that US states have different fiscal rules than Canadian provinces. However, arguing against comparisons of jurisdictions with different fiscal rules is akin to arguing that you can’t compare how many cookies kids eat because one has easier access to the cookie jar.

If the CIBC authors had actually read our studies on Ontario and California, they would have come across a three-page section, “Stating the Obvious—US States are Different from Canadian Provinces,” where we explain that unlike the provinces in Canada, US states have their own constitutions that can restrict the fiscal powers of the respective state governments.

As CIBC notes, California, like most other US states, has a constitutional mandate for a balanced budget. However, that requirement only applies to the annual operating budget, which in California is referred to as the General Fund. In addition to its General Fund, California has two other funds for state-level spending: the Special Fund, and the Bond Fund that in 2012-13 comprised 28 percent of state spending. When all three funds are included, the scope for debt accumulation is much greater and any proper analysis should include all three funds, as ours does.

The CIBC, however, wants people to “forget comparisons of Ontario to California” and instead claims “it’s more relevant to stack up Ontario vs. Alberta” and other provinces.

Again, had the CIBC economists actually read our report, they would have realized that Ontario was compared to other provinces. Ontario has the second highest level of net debt in the country at 37 percent of GDP, second only to Quebec (49 percent). And although Quebec’s debt is higher, Ontario is accumulating debt at a faster pace, and if reforms are not put in place, Ontario will soon be the most indebted province in the country.

But again, CIBC jumps to Ontario’s defense, noting “Quite simply, not all provinces are endowed with equal opportunity. When it comes to economic performance,

Canada’s resource-rich Western provinces have enjoyed a pronounced edge over Central and Eastern Canada.” It seems that the CIBC authors want us to believe that Ontario’s higher debt is because the west has resource riches.

The CIBC report says nothing about Ontario destroying its investment climate through bad policy. Consider that Ontario has raised personal income and business taxes, made labour laws more unbalanced, created uncertainty with imprudent management of its finances, destroyed its energy markets which will result in some of the highest energy costs in North America, and has done little to incentivize the extraction of its own natural resources.

Compare that to Saskatchewan, a historic economic laggard despite its resources, which has improved its investment climate and is now reaping the rewards.

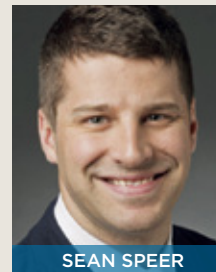
But the CIBC saves the best for last, noting that there is a “silver lining for the more distressed provinces.” As the CIBC puts it, the federal government is set to balance its budget next year which means there is a “potential for a more accommodating federal government in Ottawa.” What exactly does that mean? Well, according to the CIBC, “deploying stimulus dollars at the federal level may help.”

And there you have it: an analysis by one of Canada’s leading banks incorrectly concludes that Ontario can’t be compared to California, should only be compared to other provinces, isn’t necessarily at fault for being the second most indebted province, and argues that the federal government should consider bailing Ontario out.

No wonder Ontario is in the state it’s in. [FI](#)



NIELS VELDHUIS



SEAN SPEER

Niels Veldhuis is president and Sean Speer is associate director of fiscal studies at the Fraser Institute.



Measures of Indebtedness, California vs. Ontario, 2011/12



CALIFORNIA

ONTARIO



\$144.8
billion

Bonded
Debt
(gross)

7.6%
of GDP

\$3,844
per
capita

2.8%
Percent of
revenue spent
on interest



\$267.5
billion

Bonded
Debt
(gross)

40.9%
of GDP

\$20,166
per
capita

9.2%
Percent of
revenue spent
on interest



Nearly twice as much
bonded debt

A \$243,000 Bill, Courtesy of Canada's Governments

Charles Lammam, Hugh MacIntyre, and Milagros Palacios



Imagine receiving a credit card bill that totals \$243,476. This would no doubt be a shock for most Canadians. But if you add up all the liabilities of every Canadian government—federal, provincial, and local—that is in fact how much each taxpayer would owe of the \$4.1 trillion total in direct debt and unfunded liabilities.

This is a very large number and is much bigger than what politicians and pundits usually talk about. So let's deconstruct it to gain a better understanding.

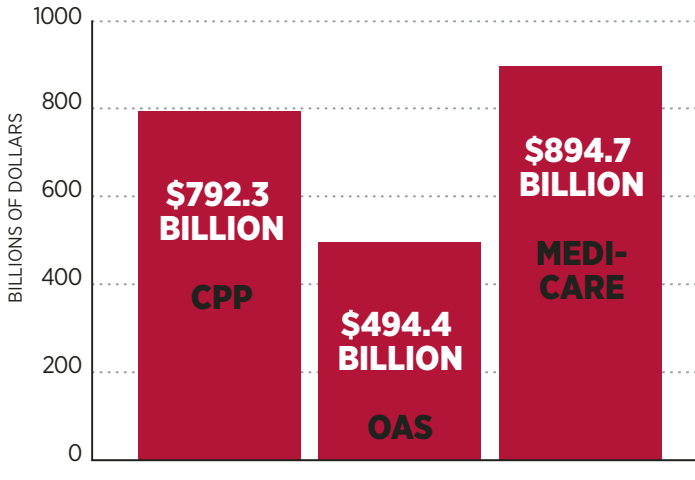
Too often the public discourse about government liabilities focuses solely on money directly borrowed by governments—so-called “direct debt.” With the federal and most provincial governments returning to deficit spending in recent years and borrowing a lot of money,

direct debt has re-emerged as an important issue. But direct debt is just the tip of the liability iceberg, representing less than one-third of all government liabilities.

As of 2011/12, the combined net direct debt of the federal, provincial, and local governments totaled \$1.2 trillion. Direct debt alone translates into a \$71,901 bill for every Canadian taxpayer. Although not the largest component of total government liabilities, direct debt has important consequences.

Governments, like families, have to pay interest on the money they borrow. And these payments aren't insignificant. All levels of government combined paid \$62.3 billion in interest payments in 2011/12. That represents 10 percent of total government revenue in the same year. In other words, for every dollar collected by Canadian

FUNDING SHORTFALL DUE TO UNFUNDED LIABILITIES TOTALS \$2.2 TRILLION IN 2011



governments, 10 cents went to paying interest on direct debt. That’s money not used for programs that Canadians care about, such as health care, education, and social services—or other important priorities like tax relief.

Over time the borrowed money (including principal) must be paid back, so direct debt is basically a deferred tax bill. That means future taxpayers—today’s young Canadians—will partly pay for current deficit spending.

The burden on the next generation of taxpayers is much greater when we account for the unfunded liabilities of government programs. In addition to direct debt, Canadian governments have committed themselves to providing programs that are not fully funded. That is, they have promised to provide a host of programs which current tax rates leave underfunded.

Three such programs with large unfunded liabilities are the Canada Pension Plan (CPP), Old Age Security (OAS), and Canada’s public health care system.

When these programs were designed around a half century ago, the assumption was that demographic and economic trends of the time would continue. The idea was to tax a relatively large cohort of younger workers to pay for the benefits of a relatively small number of elderly.

The demographic assumptions turned out to be incorrect. In 1956, only 7.7 percent of Canadians were over 65 years old. That proportion doubled to 15.3 percent in 2013 and is expected to increase further to 25.4 percent by 2061.

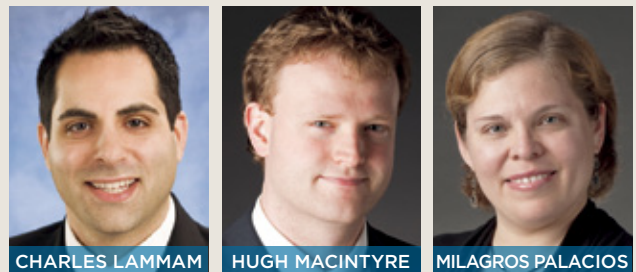
Put simply, the aging of Canada’s population has resulted in large and growing unfunded liabilities. The funding shortfall is estimated at \$792.3 billion for the CPP, \$494.4 billion for OAS, and \$894.7 billion for medicare. Together the unfunded liabilities in Canada’s public pensions and health care programs total \$2.2 trillion, or \$134,841 for each income tax payer.

These unfunded program obligations make up more than half of total government liabilities. And their sheer size calls into question the structure of taxing current workers to provide benefits for retirees. Ultimately, to maintain current levels of spending in the future, taxes will have to increase or benefits for other programs will have to be cut—or both.

To its credit, the federal government recently announced changes to OAS benefits including a phased-in increase to the eligibility age from 65 to 67 starting in 2023. The trouble with this reform, however, is that it is too timid as a large unfunded liability remains. Consider that had the eligibility age increased in lock-step with life expectancy since 1966, the current age for accessing OAS benefits would be 74.

Bolder reforms are needed, not only for OAS but also for CPP and medicare, to restructure programs in a way that accounts for demographic changes in Canada.

Along with restructuring program obligations, governments must make balancing their budgets a more immediate priority. Otherwise, the annual deficits currently planned for the future will simply add to the existing stock of government liabilities. If action is not taken, young Canadians will be stuck carrying the bill. **FI**



Charles Lammam, Hugh MacIntyre, and Milagros Palacios are co-authors of *Canadian Government Debt 2014: A Guide to the Indebtedness of Canada and the Provinces* available at www.fraserinstitute.org.

First Nations, but Second Tier Democracy

Ravina Bains



The concept of “democracy” is important to many Canadians. Prime Minister Stephen Harper has received awards identifying him as a “champion of democracy, freedom, and human rights” and the government has frequently spoken out against democratic violations in other countries.

Here at home, there has been a great deal of discussion in recent weeks around the federal government’s proposed *Fair Elections Act*, which looks to re-

form Canada’s existing election laws. These proposed reforms have resulted in public outcry from some elected officials, leading to town hall meetings, countless media panels, extensive debates in the House of Commons, and even a public letter writing campaign from a group of international scholars. And rightfully so; election laws are the cornerstone of a democracy and any proposed reforms should be the subject of analysis and rigorous debate.

So as international champions of democracy and with so much debate over federal election reforms, how would you expect our elected officials to react when democratic rights are being stifled in First Nations communities in Canada? Unfortunately, in recent weeks, they've responded with neglect and evasion.

Garden Hill First Nation, a community of over 5,000 members in Manitoba, elected a new chief and council on April 3rd. Few Canadians have probably heard about this election or the rules under which it was conducted—rules that do not meet standards that most would expect in Canada.

How can a government that stands up for electoral rights abroad stay silent about exclusionary laws at home?

This election was subject to a new law approved in Garden Hill in early March that imposed significant restrictions on who can stand for election. Among the changes set out are requirements that candidates for chief must be at least 50 years of age, councillors must be at least 40 years of age, and anyone in a common-law relationship is ineligible to run for office. These new provisions have resulted in more than 80 percent of the Garden Hill community being ineligible to run for their local government. Some legal experts have argued that the new laws violate the Charter of Rights and Freedoms.

Young Garden Hill residents, who have been essentially excluded from the democratic process, publically voiced their opposition and concern with the new election laws. However, there was no public outcry from our elected officials on these discriminatory practices, no media panels, no letter writing campaigns—just a simple statement from the federal government that said, “AANDC (Aboriginal Affairs and Northern Development Canada) has no role in the selection of community leadership, or how governance disputes are resolved.” In other words, the government intends to stand idle in the face of this subversion of the electoral process.

In fact, it's worse than that. The government will continue to transfer over \$30 million in taxpayer funds to the new chief and council who were elected under these new discriminatory election laws.

And under what justification? That is, how can a government that stands up for electoral rights abroad stay silent about exclusionary laws at home? Well, the government recognizes community or custom election codes that “provide the rules under which chiefs and councillors are chosen for those First Nations who are not under the Indian Act election rules.” The Department of Aboriginal Affairs and Northern Development Canada states that it “is never involved in the election processes held under community or custom election codes, nor will it interpret [or] decide on the validity of the process.” So even if elections are held under a discriminatory process, the federal government has opted to remain a silent bystander, thereby effectively legitimizing an undemocratic process.

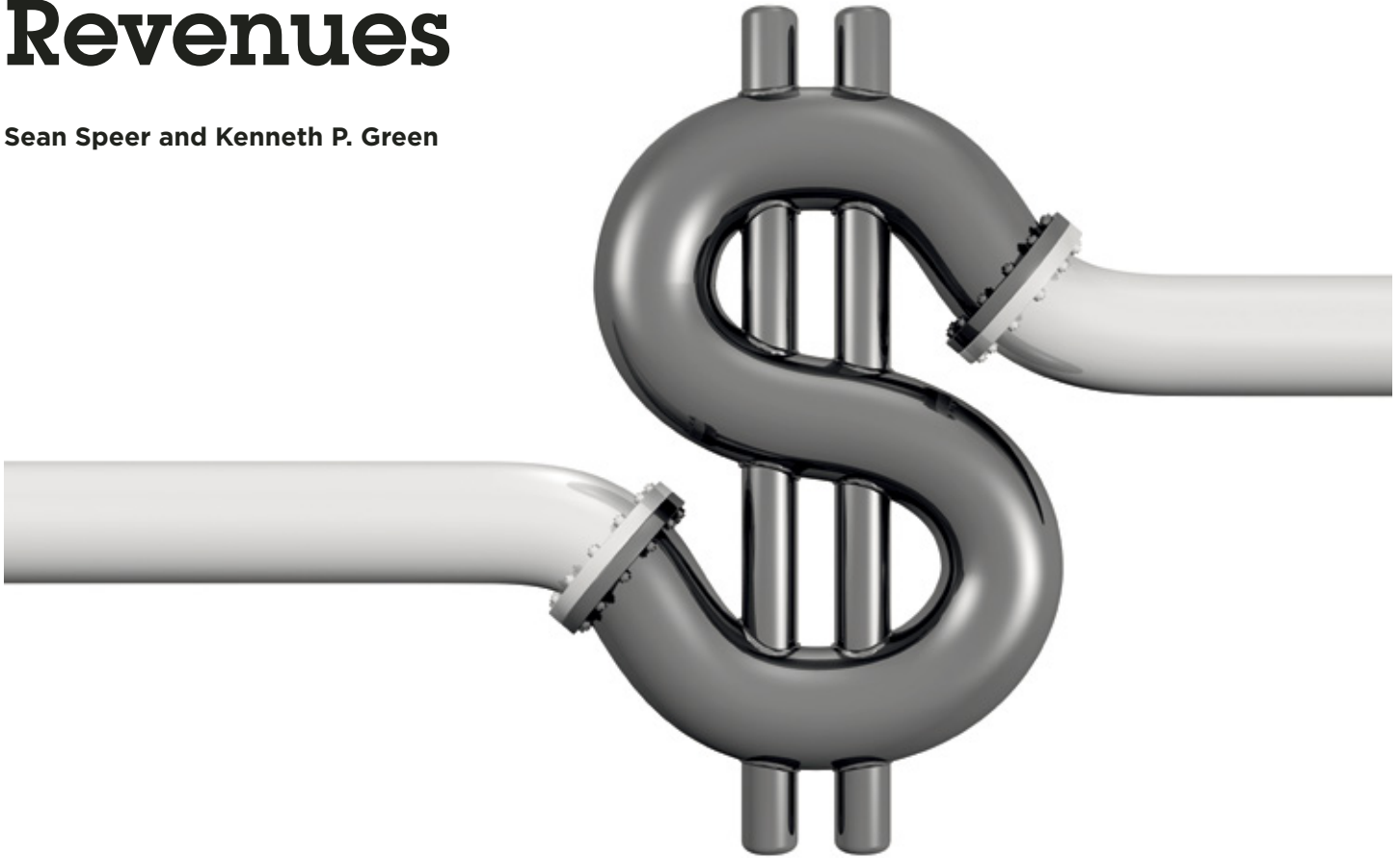
The fact that in 2014 a Canadian could be prohibited from running for local leadership because of their age or marital status is appalling. Even more troubling, our elected officials are standing silently on the sidelines and legitimizing this undemocratic process. We've heard countless political leaders from all parties stress the need for citizens, particularly youth, to be active in Canada's democratic process. It's unfortunate that these same leaders stayed silent while 80 percent of Garden Hill's members were denied the opportunity to run for local government and, in effect, are living under a second-tier democracy. [FI](#)



Ravina Bains is the associate director for the Centre for Aboriginal Policy Studies at the Fraser Institute.

Pipeline Construction would Boost Government Revenues

Sean Speer and Kenneth P. Green



Discussions surrounding the need for new pipelines to transport Canada's oil to market have been a dominant economic, environmental, and political issue for the past several years. Canada's overwhelming reliance on the United States as a customer, the US's growing energy self-sufficiency, and limited pipeline infrastructure have placed a low ceiling on the prices Canadians are able to secure for our energy exports.

New pipeline infrastructure to east and west coast ports is key for Canadian resource companies to diversify their customer base and to raise Canadian export prices relative to global benchmarks. But the

cause of new pipelines—not to mention the reassignment of existing ones—has become politicized and run into opposition.

At present the debate has reached a stalemate of sorts. The economics of greater market access for Canadian resources has run directly into an environmental backlash led by some with concerns about pipelines in particular and some who are just generally opposed to fossil fuel resource development.

One aspect of the debate that seems to have attracted little attention, however, is the impact that the current impasse has had on government finances. Specifically, low energy prices stemming from limited transport op-

tions have come to reflect themselves in less revenue for Canadian governments.

The economic case for new pipelines is well-documented. Canada has the world's third largest proven oil reserves, is the fifth largest exporter of crude oil, and is the fifth largest producer of crude oil. And that is only expected to grow. According to the Canadian Association of Petroleum Producers (CAPP), production of oil from Alberta's oil sands is expected to more than double between now and 2030, rising from 3.2 million barrels of oil per day to 6.7 million barrels per day.

What are the economic benefits of such development? A 2011 study by the Canadian Energy Research Institute projects that investments and revenues from new oil sands projects would be over \$2 trillion between 2010 and 2035. This would result in a \$2.1 trillion increase in the Canadian economy, and job growth in the oil sands industry from 75,000 in 2010 to over 900,000 by 2035. And it is worth noting that this study's estimates are based on considerably lower production forecasts than those published by CAPP.

Oil transport limitations are reducing revenues from Canadian oil sales by at least \$17 billion per year and, depending on market fluctuations, those losses could reach \$25 billion per year according to a 2013 study.

The lack of safe, low-cost transportation capacity to move oil to world markets is the major barrier to this substantial economic development. Oil transport limitations are reducing revenues from Canadian oil sales by at least \$17 billion per year and, depending on market fluctuations, those losses could reach \$25 billion per year according to a 2013 study.

The fact is that Canada's current price discount for its energy exports also means less tax revenue for the federal and provincial governments. The numbers are considerable. Alberta collected \$2.4 billion less in oil sands

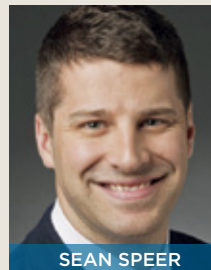
royalties in the most recent fiscal year while Saskatchewan has also lowered its projected royalty revenue by \$287 million in 2012-13.

Governments are further affected by lower personal and corporate income tax revenues resulting from slower employment growth and reduced business profits. The federal Department of Finance, for instance, has estimated that if Canadian prices for crude oil and natural gas were to return to historic norms for crude oil and half the prevailing natural gas prices in Europe, the federal government would collect an additional \$4 billion in revenues.

To put this in perspective: \$4 billion in new revenue would almost wipe out the \$5.5 billion budgetary deficit the government is currently projecting for next year and is more than the size of budgetary surplus it anticipates for 2015-16.

So the potential for additional government revenues is not insignificant, and they could be put to good use increasing Canada's tax and economic competitiveness. For example, this additional revenue could be used to lower personal incomes tax rates in Canada which are high relative to other jurisdictions such as the United States. It could also be used to reduce government debt and in turn lower debt servicing costs freeing up room for other budget priorities.

The current debate about new pipeline construction typically fails to account for the potential impact on government revenues. It is important aspect of the issue and, as we head into government budget season, one that should not be ignored. [FI](#)



SEAN SPEER

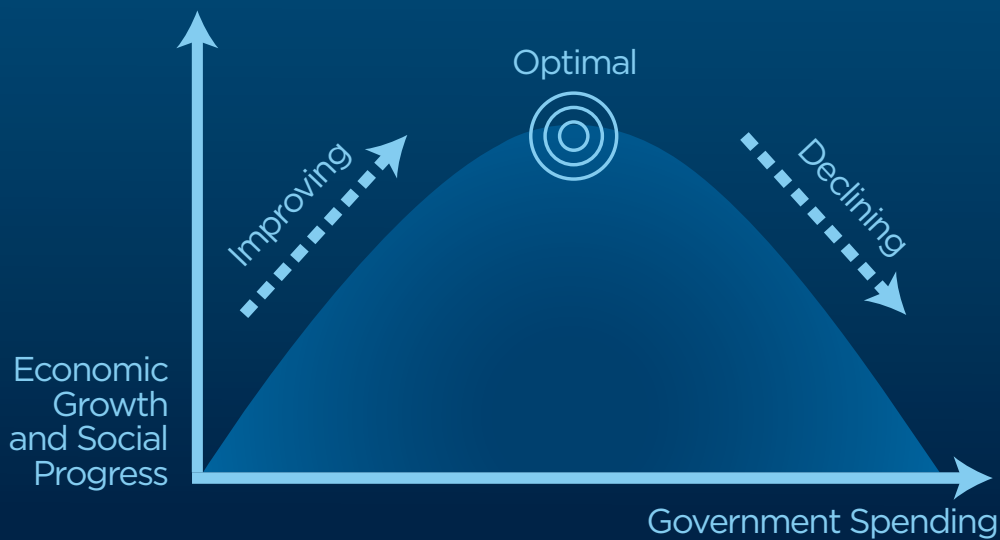


KENNETH P. GREEN

Sean Speer is the associate director of fiscal studies and Kenneth P. Green is senior director of energy and natural resource studies at the Fraser Institute.

More Taxes Buy More Government, Not a More Civilized Society

Mark Milke



Government Spending and Its Effects on Growth and Social Progress

“Income tax has made more liars out of the American people than golf,” said the American humourist Will Rogers. Indeed, but let’s not stop there. In Canada, debates over taxes, government, and civilization lead some journalists and others into the land of make-believe, this by setting up straw men to knock down.

For example, consider a recent CBC story headlined, “Not all business people hate taxes—but just try to get them to admit it.”

To which one can only say: This is news?

The reporter advanced a general assertion with which no thinking person would disagree: “Taxes are necessary,” to help set up the straw man. That some people

are ostensibly anti-tax and how silly is that? was thus easy to knock down; just mention an essential function like courts or cops that only governments can provide.

The general notion that taxes are necessary was followed by an interview with a former civil servant who said taxes are not a four-letter word; a polling question one would expect to elicit a tax-friendly response (your health care or tax relief, as if this was the only choice); and generic clichés about taxes and civilization.

The reporter even managed to sneak in the bizarre assertions that the Fraser Institute and Canadian Taxpayers Federation are anti-government and “anti-tax.”

The charges are silly though I don’t mean to pick on the CBC or one reporter.

Others too have offered up versions of the charge that to question government and particular tax levels undermines civilization. The list includes Naomi Klein, Olivia Chow, and Calgary Mayor Naheed Nenshi. So, too, Linda McQuaig, who set up a straw man of her own once when she asked her readers to imagine the “complete removal of government”—as if anyone serious suggests this.

The healthy preference for moderate government, including moderate taxation, has existed throughout human history. In the English world, it has been a constant since at least the Magna Carta, which put a limit on the King’s ability to overly interfere with one’s property. And one’s money, for the record, is property.

In Canada, pre-and post-Confederation politicians asserted the role of government was to protect the citizen from government and to provide basic services, albeit defined rather narrowly.

For instance, a 1940 Royal Commission described Canadian views after Confederation this way: “Government was thought to have met its purpose when it provided for adequate defence, the enforcement of the general law through the equal administration of justice, and maintenance of a few essential public works. Within this framework of order provided by public authority, individuals were expected to work out their own destiny.”

But here is the more functional argument for limited government and moderate taxation: governments that attempt too much often do little well. (Insert your favourite government waste story here.) Instead of zeroing in on how to make education, health care, and pensions sustainable, political attention is fragmented in a thousand-plus directions.

And there is empirical proof on how bigger government rarely produces better government. My colleagues recently looked at the literature on the optimal size of government. They found after you reach 30 to 35 percent of the economy, government spending has minimal effects on economic and social outcomes—you’re pushing on a string. This is not a surprise for students of politics. Vested interests such as government unions seeking above-market compensation or businesses looking for subsidies, to use two examples, often swallow up extra taxes.

“Taxes are the price we pay for civilization” wrote the American Justice Oliver Wendell Holmes, Jr. in a now-

famous 1927 judgment. About then, direct and indirect taxes in Canada amounted to just 13 percent of the economy. Now, the figure is 38.6 percent. Taxes as a percentage of GDP have been higher, up to 44 percent in the late 1990s. But anyone who thinks Canadians should be taxed more has no historical conception of their still relative highness or their relative ineffectiveness at present levels.

Most Canadians well know that a functioning country requires courts, judges, and police to protect persons and property; social workers to try and rescue children from awful situations; and for governments to carry out other functions. All that requires taxes.

Switzerland is civilized. That alpine country has universal health care, an educated population, and a safety net. The taxes-to-GDP ratio in that country amounts to 33.4 percent, five points below Canada.

But here’s a thought: Switzerland is civilized. That alpine country has universal health care, an educated population, and a safety net. The taxes-to-GDP ratio in that country amounts to 33.4 percent, five points below Canada. Here’s the point: After some basic level of taxation, more taxes do not buy more “civilization,” they simply buy you more government, and the two are not the same thing. **FI**

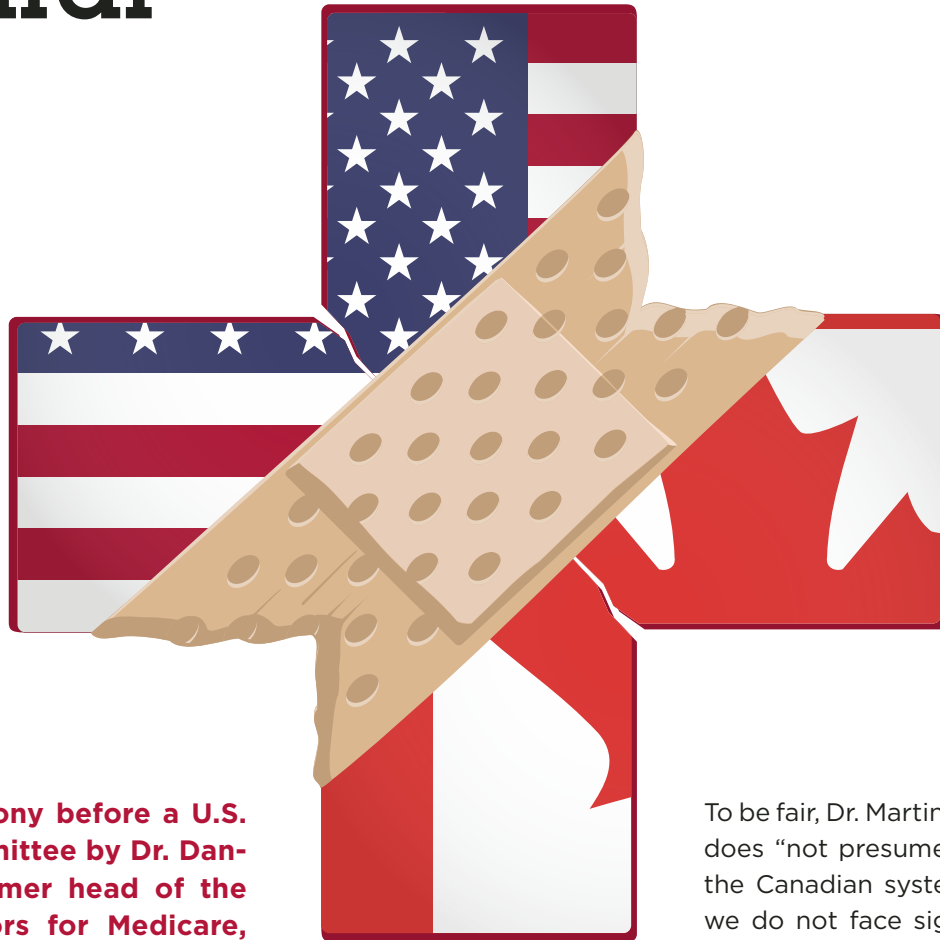


MARK MILKE

Mark Milke is a Senior Fellow at the Fraser Institute and author of *Tax Me I’m Canadian! A Taxpayer’s Guide to Your Money and How Politicians Spend It*.

When Health Care Myths Go Viral

Bacchus Barua



A recent testimony before a U.S. Senate subcommittee by Dr. Danielle Martin, former head of the Canadian Doctors for Medicare, has given Canadians the chance to indulge in what may be a favourite pastime—criticizing the American health care system.

Unfortunately, rather than sparking a discussion about how to improve both the Canadian and US health care systems to better serve their populations—pundits, online commenters, and tweeters have simply resorted to nationalistic chest pounding, accompanied by the usual overly simplistic arguments about why each system should be considered a model for the other.

Easily forgotten is the fact that both the Canadian and American health care systems are widely considered to be expensive and inefficient.

To be fair, Dr. Martin did mention that she does “not presume to claim today that the Canadian system is perfect or that we do not face significant challenges.” However, in the polarized environment following her speech, it is important to

set the record straight on some key figures she chose to cite, as well as some of the important information she conveniently left out.

Let’s start with the big one: her claim “that there are 45,000 in America who die waiting because they don’t have insurance at all.” It’s pretty safe to surmise that she’s referring to a 2009 study by Wilper et al., who piggybacked their research on a previous study by the Institute of Medicine in 2002 (which pegged the number at 18,000).

Of course, promoting health care insurance coverage for the population is not a bad thing. But to propose that a lack of insurance coverage in and of itself leads to

death is absurd. People don't die simply because they lack health insurance.

In fact, the sensationalistic conclusions drawn from these two studies have been criticized by several economists. John Goodman points out that both studies fail to account for changes in insurance status during the periods examined, while Jenny Kim and Jeffery Milyo demonstrate the pitfalls of such observational studies by replicating Wilper et al.'s methodology to conclude that Medicaid (governmental health insurance for lower income Americans) coverage is also associated with higher mortality. Further, June O'Neill (former director of the Congressional Budget office) and Dave O'Neill concluded that health-care insurance itself is not the primary reason for higher mortality rates among populations that are uninsured (who may face multiple disadvantages), while Richard Kronick found no difference in mortality between the uninsured and those with employer-sponsored insurance once demographic factors, health status, and health behavior characteristics were controlled for.

Inordinately long wait times, medical resource shortages, and ballooning health care costs have become defining characteristics of health care in our country—and denigrating the American approach will not fix those problems.

There's even some evidence (again, from June and Dave O'Neill) to suggest that, for some health services (e.g., screening for cancer), uninsured Americans may actually be better off than "insured" Canadians.

Dr. Martin's second major claim, and one that Canadian defenders of the status-quo have latched onto, presumably relies upon a study by Stephen Duckett (former head of Alberta Health Services) which suggests that in Australia "increased private sector activity [in health care] is associated with increased public sector waiting times." First, this statement says nothing about overall wait times, only those in public hospitals. Second, it doesn't inform us about the line of causation, or direc-

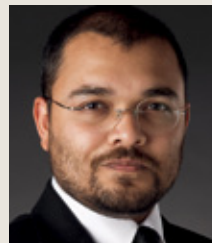
tionality. In fact, Duckett entertains the possibility that increased private sector activity may have actually been a response to inadequate public sector services rather than the cause of longer public wait times. And there's still the complex matter of how governments respond to expansions in private sector activity (including, sometimes, deliberate reductions in public activity), as well as the question of why waits occurred in the first place.

Finally, the entire argument breaks down when one is confronted by data from the Commonwealth Fund, which indicates that fewer Australians than Canadians waited two months or more for specialist appointments and four months or more for elective surgery.

In fact, all of the best performers on the Commonwealth Fund's list (Switzerland, the Netherlands, and Germany) have universal health care systems with private parallel options. Further, their performance is in stark contrast to Canada's, where over-reliance on government planning, lack of competition, and lack of cost-sharing have resulted in some of the longest wait times in the developed world.

These are the countries, and policies, we should be talking about if we are truly interested in delivering timely access to quality health care for our citizens.

While the American health care system has some important shortcomings, the same holds true for Canada's. Inordinately long wait times, medical resource shortages, and ballooning health care costs have become defining characteristics of health care in our country—and denigrating the American approach will not fix those problems. **FI**



BACCHUS BARUA

Bacchus Barua is a senior economist with the Fraser Institute.

BC's Business Tax Regime Needs a Competitive Jump Start: Here's How

Charles Lammam and Milagros Palacios

BRITISH COLUMBIA
BUSINESS
TAX



One item sorely missing from Finance Minister Mike de Jong's provincial budget was a plan to make BC's business taxes more competitive and attractive for investment. When the province shifted back to the PST from the HST last year, the cost of doing business and investing increased dramatically. Disappointingly, de Jong's budget did nothing to address this shackle around BC's economy. Tax reform, however, might be the light at the end of tunnel.

Before getting into the details of our proposed solution, it's important to understand why the PST is so harmful to our economic well-being. Under the PST,

BC's entrepreneurs now pay sales tax on the goods and services they purchase and use to produce what they sell to their customers. This means they pay a seven percent tax on things like machines, equipment, technology, materials, and energy. The taxation of these business costs is unique in the developed world—and increasingly in Canada—where most major provinces have adopted a sales tax that exempts these costs.

According to calculations by tax policy expert and University of Calgary professor Jack Mintz, BC's overall tax rate on new investment is now the highest in the country at 27.5 percent, up from 17.8 percent before the PST's reintroduction. For perspective, the rate in neighbouring Alberta is 17.0 percent.

BC is competing with other provinces (and US states) for investment, so the harsh reality is that BC risks losing investment and jobs that will instead gravitate to jurisdictions with more competitive tax policies.

Despite inaction on this issue, de Jong seems to understand the magnitude of the problem. At recent presentation on his budget, he acknowledged as much but worried about finding the fiscal room necessary to take action.

With the HST a political non-starter, a second-best tax reform option begins with the government's own Expert Panel on Business Taxation recommendation: introduce a refundable investment tax credit equal to the PST paid on machinery and equipment.

Our best estimate is that 40 percent of the government's \$5.6 billion in PST revenue is from sales tax on business inputs (the amount on capital-based inputs would certainly be less). That means de Jong needs to make up at most a \$2.2 billion gap.

BC's overall tax rate on new investment is now the highest in the country at 27.5 percent, up from 17.8 percent before the PST's reintroduction. For perspective, the rate in neighbouring Alberta is 17.0 percent.

One place to look for the money is in the government's nearly \$6 billion in tax expenditures. The province currently provides special tax breaks for certain activities through the personal (\$2.5 billion), corporate (\$558 million), property (\$986 million), fuel (\$57 million), and sales (\$1.9 billion) tax systems. These tax expenditures represent foregone revenue and in many cases are economically ineffective, reward activities that would be undertaken anyway, and disproportionately benefit certain groups and industries at the expense of the broader population.

For instance, in 2012 the BC government announced the introduction of the Children's Fitness Tax Credit, pig-

gy-backing on the federal program. However, a recent study published in the *Canadian Tax Journal* found that the tax credit has done little to actually influence parents' decisions on enrolment in a fitness program and has disproportionately benefited higher income households. Similar inequities have been found with tax credits for tuition and education.

Research on corporate tax expenditures also casts doubt on the effectiveness of special industry privileges. The tax credit for film and TV is a clear example; it is slated to cost the provincial treasury \$167 million this year. Contrary to industry claims, independent research including by the US-based Tax Foundation concludes that film subsidies "cost the treasury more than they recoup from taxes on induced economic activity."

A tax credit for capital inputs is different from other tax expenditures in that it would partially correct a highly distortionary feature of the PST system: the taxation of intermediate inputs. The provincial government tried to fix this problem in 2001, but limited the sales tax exemption by narrowly interpreting the types of machinery, equipment, and companies that qualified. In the end, the exemption was not available to most businesses, which resulted in an administrative disaster and eventually deterred many companies from seeking eligibility.

If de Jong is serious about improving BC's tax competitiveness and the future economic prospects of the province, he should consider tax reform that exempts business inputs from the PST in exchange for eliminating or significantly scaling back ineffective tax expenditures. **FI**



CHARLES LAMMAM



MILAGROS PALACIOS

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Federal Liberals Reject the Party's Successful Pragmatism of the 1990s

Jason Clemens, Niels Veldhuis,
and Milagros Palacios



The policy direction of the Liberal Party of Canada and its leader Justin Trudeau, as evidenced by the speeches, motions, and debate at the recent national party convention, seem to indicate that the party is rejecting the successful pragmatism of the 1990s. Instead, the federal Liberals favour a more interventionist and activist government, much like that of the current Ontario Liberal government. If such policies are enacted, the results would be ruinous for Canada.

One of the central themes repeated consistently at the convention was the need for the federal gov-

ernment to incur more debt in order to finance infrastructure and other long-term spending. Mr. Trudeau and his policy advisers seem to have been influenced greatly by US economist Larry Summers. Mr. Summers, who served in the Clinton and Obama administrations, is a vocal advocate for more expansive government spending using debt as a method by which to stimulate the economy.

One problem of many for this approach is that it belies history, both in the US and Canada. Bill Clinton and Jean Chretien enjoyed enormous economic and political success by doing the opposite. US President Obama and the Ontario Liberals have struggled with a weak econo-

my by doing exactly what Mr. Trudeau now proposes for the entire country.

Beginning in 1995, the Chretien Liberals cut program spending by almost eight percent in just two years and continued to constrain spending even after balanced budgets were achieved for the following three years. Federal program spending as a share of the economy declined from over 17.1 percent in 1992-93 to just under 12 percent by the end of the decade. Federal debt was reduced from 67.1 percent in 1995-96 to roughly 30 percent by the time the Tories took over. And critically, the Liberals enacted a series of tax cuts and reforms aimed at making our economy more efficient and competitive.

The results, contrary to the rhetoric of Mr. Summers, were stunningly positive. Over the decade spanning 1997 when the federal budget was first balanced to roughly 2007, Canada led the G7 in both economic growth and business investment. Our record on job creation was unparalleled, more than doubling the US rate and higher than any G7 country. And poverty rates fell by more than 40 percent.

The assumption that government can simply flick a switch and spend efficiently is both conceptually and historically false.

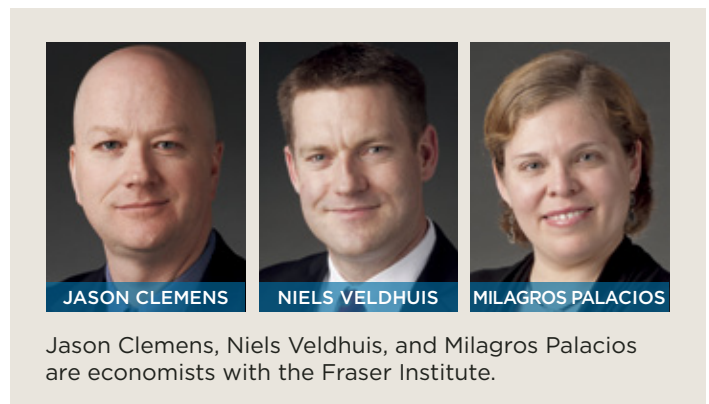
These actual results stand in stark contrast to the predictions of Mr. Summer: “To start, this means ending the disastrous trend towards less and less government spending and employment each year and taking advantage of the current period of slack to renew and build out our infrastructure.”

Of additional concern is the naiveté that Mr. Summers continues to display and has apparently now infected Mr. Trudeau with in terms of the actual ability of governments to do the things he advocates. Mr. Summers was front and centre in advocating for and shepherding through the Obama stimulus, which contained hundreds of billions of dollars for “shovel-ready” projects. Mr. Summers insisted that the mark of success of such

policies were that they were timely, temporary, and targeted. The reality of what happened is that, not surprisingly, politics affected the program. High priority projects were shelved for more politically expedient ones. Projects were delayed and hung up in red tape and bureaucrat infighting. The assumption that government can simply flick a switch and spend efficiently is both conceptually and historically false.

Mr. Summers can be forgiven for not being aware of the experience in Ontario. The same cannot be said of Mr. Trudeau. The large and continuing deficits in Ontario, despite economic growth, coupled with heavy-handed interventionism in a host of sectors have placed Ontario on a path of decay, not prosperity. Economic growth in the province has remained sluggish despite large-scale deficits and debt accumulation. (As a measure of the province’s problems, Ontario is markedly worse on every measure of indebtedness compared to California.)

It’s not at all clear how the country will benefit from Ontario-style policy when such policies have been an abject failure. The country would benefit from a return to the sound policies of the Chretien era in the 1990s—balanced budgets, reducing debt, decentralization of responsibility and authority for services to the provinces, better value-for-money focused spending by the federal government, and incentive-based tax relief and reform. That’s a recipe for success for any government, or government in waiting. The Trudeau Liberals should look back to this period rather than down south for their policy ideas. [FI](#)





Milagros Palacios

What's your role at the Institute?

I'm a senior research economist at the Institute. I contribute directly to studies as an author in addition to providing statistical support to my colleagues. Over my ten years at the Institute, I have co-authored over 40 research studies on a wide range of issues including taxation, government finances, productivity, labour markets, and charitable giving, among others. I am the key point of contact for almost all of the Institute's datasets and statistical analyses, which means I get to work with almost all of my research colleagues.

How did you arrive at the Institute?

Like many other researchers at the Institute, I started as an intern. I interned at the Institute in 2004, working on the State of Urban Air project for the Risk, Regulation, and Environment Centre. When I arrived in Canada from Peru in 2002 I started looking for Canadian work experience. After learning that Hernando de Soto, an accomplished and internationally-recognized Peruvian economist, gave a speech at a Fraser Institute event, I did some research on the Institute and discovered they

offered an intern program.

I applied and secured an internship and after a year of interning I was offered a full-time position in Fiscal Studies.

Something exciting you're working on now for the immediate future.

The nature of my position means that I get to work on a host of projects over the course of a year but one particularly exciting project I'm involved in is the creation of a large dataset for government spending and taxes. The project will allow us to more easily analyze and forecast government spending (and hopefully revenues), which allows us to better understand the consequences of policy decisions being made today.

What you enjoy doing in your spare time that your colleagues might not be aware of?

Some of my colleagues know that in my spare time I dance flamenco and those that don't are probably often asking themselves why I incessantly tap my feet in my office and the lunchroom. I love dancing and I find it a great tool to relieve stress. [FI](#)

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Institute supporter names the Foundation as the beneficiary of his registered investment accounts

Rod, a retired consulting engineer and longtime Fraser Institute supporter, has travelled to many developing countries, which has given him a real appreciation of the Fraser Institute's work on many key issues. As a result, Rod decided to leave a legacy of freedom and prosperity by

naming the Fraser Institute Foundation as the beneficiary of several of his registered investment accounts.

Unfortunately, the financial institutions holding Rod's plans would not allow him to do this, claiming that a charity could not be the beneficiary of an RRSP or a RRIF. The institutions were incorrect. The Income Tax Act has no such restriction on registered retirement plan beneficiary designations. It took some consultation and negotiation, but in the end, Rod was delighted to be able to fulfill his wish of supporting

the Fraser Institute with the legacy gift of his choice.

By designating a charity as the recipient of your retirement savings plan, you provide a future gift while protecting your present financial security. Your estate receives a donation receipt that can be applied against tax on your final income tax return.



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