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The case for privatizing Canada Post

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*Global Petroleum Survey 2011* summary

The welfare state is an illusion

BC pesticide prohibition

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# Fraser Forum

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## From the editor

# Labour in Canada

This issue of *Fraser Forum* arrives shortly after Canadians celebrate the economic and social achievements of workers on the first Monday of September; as such, it seems appropriate to have a labour-themed issue. In the July/August issue of *Fraser Forum* was an article about Tax Freedom day, which discussed the day in the year that marks the point at which Canadians start working for themselves rather than merely to fulfill their tax burdens; however, rather than focus on the financial impacts of Canadian labour, this issue centers around the ways in which certain forms of labour are structured.

Particularly, this issue of *Fraser Forum* addresses the concerns, further emphasized by the Canada Post strike this summer, about the dangers of the monopoly that the Canadian government has on our national mail distribution. In *Recent mail disruption strengthens case to privatize Canada Post* (pg. 12), Charles Lammam and Amela Karabegović raise the important point that while the postal system continues to be a crown corporation, it will not have consumers' best interests at heart. In the future, to protect charities, small businesses, and ordinary individuals from similar labour disagreements and subsequent service disruptions like the one we experienced this summer, the solution is to privatize Canada Post.

Similarly, two other articles in this issue of *Forum* directly address notions of labour and labour markets. In the article *Indecent disclosure* (pg. 16), Niels Veldhuis and Amela Karabegović question why Canadian unions are not held to the same standards of transparency and accountability as are their American counterparts. Moreover, with recent legislation in Canada increasing disclosure requirements for publicly traded companies, charities, and other public organizations, one must ask (as the authors do) isn't it time for the special treatment of Canadians unions to end? Finally, Niels Veldhuis, Peter Cowley, and Milagros Palacios once again express concern over the structure of teacher compensation in British Columbia (pg. 15) and argue that, in order to focus on teaching effectiveness, a future collective agreement with the British Columbia Teachers' Federation should tie teacher pay to performance. Also in this issue is a summary of the *2011 Global Petroleum Survey* (pg. 28), our Quarterly Research Alert (pg. 19), and a commentary by Mark Milke on the false existence of a successful welfare state (pg. 8). Lastly, included also is another new article in our regulation section about the proposed ban on BC pesticides, in which Nachum Gabler and Joel Wood discuss better options (pg. 33).

Cari A. Ferguson (fraserforum@fraserinstitute.org)

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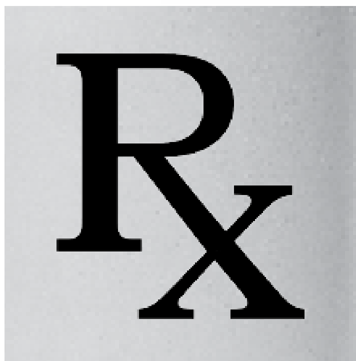

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# *Flaherty's plan on shaky ground*

Niels Veldhuis and Charles Lammam

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On August 9th, 2011, the *National Post*'s editorial page celebrated the continuation of Canada's AAA credit rating, in light of the US downgrade to AA+ (*National Post*, 2011).[1] While there is no doubt that our fiscal health is relatively better than that of the United States and many European countries, recent market volatility combined with declining commodity prices should not make Canadians too complacent.

The *Post* noted that Canada had learned its lesson years ago. However, the way we see it, the federal government is making the same basic mistake: pinning hopes for a balanced budget on a combination of significantly higher future revenues while trying to slow the growth in spending.

In June 2011, the federal government tabled a plan to balance the budget in five years (Department of Finance, Canada, 2011).[2] To get there, the Conservatives forecasted revenues to grow at a robust average rate of 5.6% over the next five years, while planning to hold program spending increases to an average rate of 2.0%.

The problem with this plan is that while the federal government directly controls the amount it decides to spend—though Canadians should exercise healthy scepticism as the Conservatives' track record on spending suggests it will be unable to hold the line at 2.0%—the government is exposed to revenue shocks that are beyond its control.

A balanced budget plan that relies on robust average revenue growth of 5.6% is one with significant risk and little-to-no upside potential. Lower than forecasted revenue growth will mean larger deficits for a much longer period and significantly more government debt.

As we previously pointed out in our analysis of the June budget, "The same approach did not work in the 1980s and early 1990s. Successive

federal governments failed to balance the budget by trying to slow the growth in spending while hoping for higher revenues" (Veldhuis and Lammam, 2011).

Like the incumbent Conservatives, the Progressive Conservative government in the late 1980s and early 1990s was at least notionally predisposed to lower levels of government spending and balanced budgets. However, failure to eliminate the deficit came from the Progressive Conservative's inability to constrain spending growth coupled with lower than expected revenues. That ultimately resulted in ongoing deficits, mounting debt, and a loss of Canada's AAA rating in 1994.

Now, just months after the 2011 budget was tabled, the current government's fiscal plan is facing similar risks with signs of a slowing US economy and the possibility of a double-dip recession increasing. Given that Canada's economy is tied heavily to the US, any material slowdown in the US will likely have a negative impact on the Canadian economy, federal revenues, and the Conservatives' deficit-reduction plan.[3]

To reduce the frailty of the current fiscal plan and to set Canada apart from the rest of the world, the Canadian government must quickly balance its budget. Finance Minister Flaherty can use the government's fall economic and fiscal update to do just that—and balance the books in two years, not five.

First, Flaherty should ensure that program spending is returned to pre-stimulus levels. This can be achieved by greatly expanding the government's *Strategic and Operating Review*, currently a one-year review of program spending —excluding transfers to individuals and governments—which proposes to find a mere 2% in savings from the $352.5 billion in departmental spending planned from 2012–13 to 2014–15.

The expanded *Strategic and Operating Review* ought to prioritize spending so that important areas are spared deep cuts while lower priority areas carry a greater burden of the spending reductions. A good starting point is to significantly reduce, or eliminate, corporate subsidies, which have grown substantially under the Conservative regime.[4]

A two-year, balanced budget plan would substantially reduce the risks associated with a revenue shock like a slowing US economy. Such a plan also provides the Conservatives with upside potential. That is, if revenues rebound strongly, the Conservatives could then implement a much-needed, multi-year plan to reduce personal income taxes.

In the wake of the American credit downgrade, the stock market plunge was an arresting reminder of the risks facing the Canadian economy. The US economy is looking ever more fragile, sovereign debt concerns are growing in Europe, and commodity prices are softening; all reasons why Canadians should feel increasingly uneasy about the government's fiscal plan. The newly minted Conservative government should use its majority to implement the type of balanced budget plan that the Prime Minister and his colleagues once championed while they were members of the opposition.

## Notes

1 A credit rating evaluates the credit worthiness of an issuer of debt, in this case government. AAA is the highest rating meaning the debt issuer is not likely to default.

2 Please note that, unless otherwise indicated, all data referenced in this article are sourced from Department of Finance, Canada (2011).

3 Interestingly, the Conservatives' plan is built on the assumption that the US economy will grow robustly at an inflation-adjusted average rate of 3.2% over the next five years—faster than the Canadian economy at 2.7%.

4 Federal subsidies to the auto sector—just one of many sectors that receive corporate welfare—grew by around $10 billion in 2009-10 (see Department of Finance, Canada, 2010).

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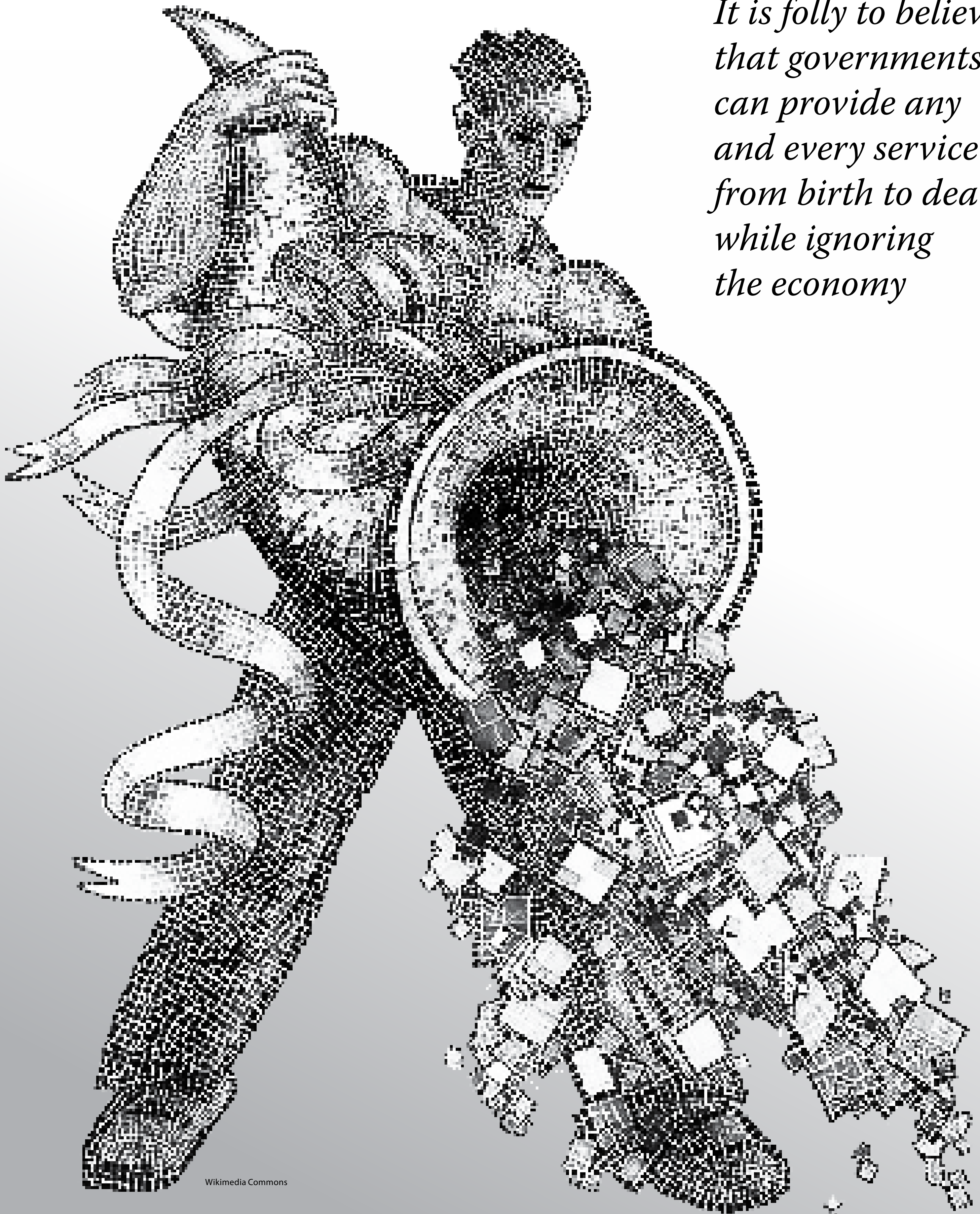
*It is folly to believe that governments can provide any and every service from birth to death while ignoring the economy*



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# The welfare state was always an illusion

**Mark Milke**

The latest European Union (EU) deal for Greece will see yet another infusion of Euros directed towards one of that continent's most profligate member states. The entire package, $109 billion Euros in total, will be split between EU member countries who will contribute $72 billion Euros with the private sector offering up $37 billion Euros (European Union, 2011). That is the equivalent of Canadian $149 billion (Bank of Canada, 2011).

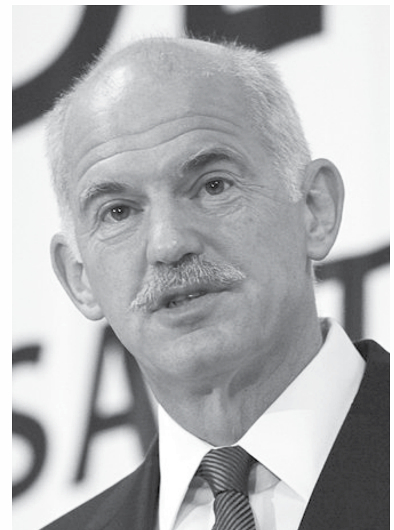
It is proper that Europe's private sector finally participate in the bailout; it's overdue for financial institutions to bear part of the cost for the risk they took on by lending money to Greece in the first place. But the latest Greek bailout, as well as the budget problems in the United States, should cause both citizens and governments around the world to revisit cherished assumptions about the viability of the welfare state.

If the recent high-profile problems in Greece (and the US) demonstrate anything, it is how the notion that governments can provide almost any and every service from birth to death—and yet ignore the economy and demographics—is folly. Much of the welfare state concept was always an illusion, one financed by lavish amounts of debt for which present and future taxpayers will pay in the form of higher taxes and reduced services during their lifetimes.

That this is not yet clear to many is unfortunate. The denial only delays a consideration of policy remedies that would better provide for international shifts and thus better secure people's financial and social needs. For example, it would have been preferable to mandate health care and savings accounts for individuals and families over the decades; that would at least have partially reduced the pressure to borrow from future generations via the public purse.

The denial starts at the highest levels. In a recent closed-door meeting in Washington, D.C., where I was present, several current and former European politicians, including at least two former heads of state, asserted that the European model—by which they meant lavish social services—was a success. Here is the problem with that boast: insofar as European, American, and Canadian social programs have been financed by government borrowing in most years—and they have— it is an exaggeration to argue that such models are a success or sustainable. It is akin to buying an expensive home and several luxury sports cars and handing the payments to the kids once they have become adults.

In the case of governments, the borrowing has been substantial. To understand the scope, consider the debt trajectory of the United States



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Greece's President Papandreou has secured a second bailout for his country from the European Union.

and selected European countries since 1995, about the time (or shortly after) that many Canadian governments began to grapple with our red ink. (All the following figures are from OECD, 2011a and OECD, 2011b unless otherwise noted.)

In 1995, Greece's net liabilities were already 81% of GDP, in a year when Canada's equivalent figure was 71%. Italy stood at 99% of GDP. Back then, France, Germany, and the United Kingdom had net liabilities of 38%, 30%, and 26% respectively. Portugal's was 24% and the US figure was 54%.

Fast forward to 2011, and all the countries are further in debt save Italy

**Figure 1: Net liabilities then and now as a percentage of GDP**

| | 1995 | 2011 |
|---|---|---|
| Canada | 70.7 | 33.7 |
| France | 37.5 | 60.2 |
| Germany | 29.7 | 50.2 |
| Greece | 81 | 124.8 |
| Italy | 99 | 127.8 |
| Portugal | 24.3 | 75.5 |
| UK | 26.3 | 62.4 |
| US | 53.8 | 74.8 |

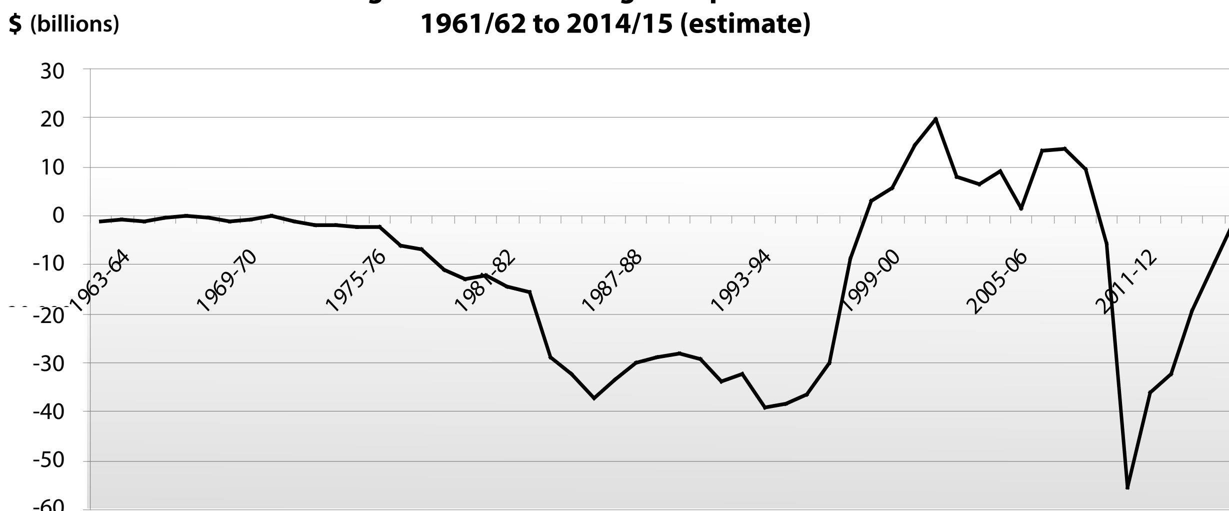
Source: OECD, 2011.

(which is almost the same). Here are the current OECD estimates for net liabilities as a percentage of each country's economy: Greece: 125%; Italy: 101%; France 60%; Germany: 50%; Portugal: 76%; the United Kingdom: 62%; and the United States: 75%. In Canada, our net liabilities are 34% of our economy. That is down substantially from 1995, though up from the low-point in 2008 when the figure was just 22% of GDP.[1]

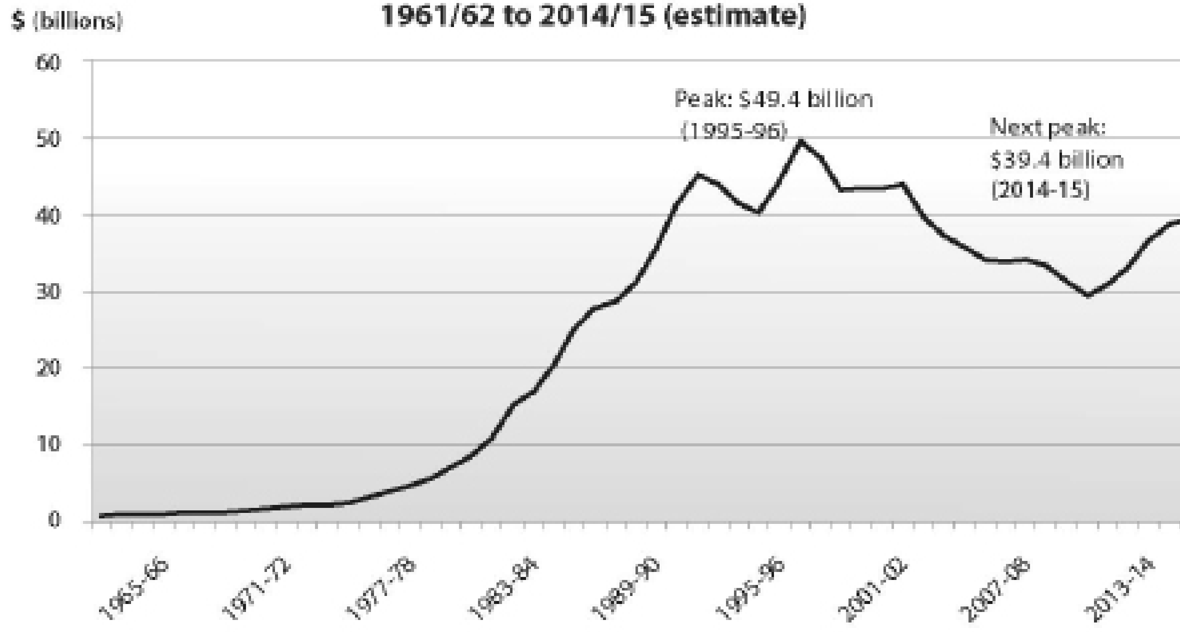
Here is the problem, even in Canada's case. Insofar as the assertion is that the modern welfare state has been a success, it only appears that way if one ignores the debt burden placed on future generations. For the record, the fault for the ramped-up public debt cannot be placed on "too low" taxes. A variety of countries with widely differing tax takes have each put themselves into deeper debt. For example, since 1995, Greece's total tax take as a percentage of GDP has been about one-eighth to one-fifth higher (depending on the year) than the United States; as a share of its economy; however, Greece managed to put itself even deeper into debt than did the US.

Or consider the UK: its tax take has risen steadily since 1995 and so too has its debt. Meanwhile, Canada's taxes as a percentage of GDP have been declining, as has our debt (until recently). However, we should not feel overly confident despite our relatively low net debt-to-GDP ratio. Since 1961 and to this year, the federal government will have run deficits in 37 of 50 years and we are now in the fourth-consecutive, red-ink year once again (all the following figures are Canada, 2011a and Canada, 2011b.) In other words, the 11-year string of surpluses, which ended as of 2008/09 were a rarity in post-1960s Canada.

That comes with a cost. The federal finance department forecasts a deficit until at least 2014/15, at which point the federal debt will stand at




Source: Canada, 2011a and 2011b.




Source: Canada, 2011a and 2011b.

$615 billion. That means taxes will have to remain higher than otherwise would be the case, or program spending cut, this in order to finance the debt payback and the interest payments in the meantime.

By that budget year, interest payments since 1961/62 will have amounted to almost $1.3 trillion (in nominal dollars) on those 40 years' worth of deficits (the extra three added to the 37 just noted are courtesy of the next three deficit years).

So why does it matter and what does it have to do with the welfare state? Insofar as debt has been used to finance a large chunk of what government does, any vaunted social welfare model really has not been tested for affordability. All that's happened is that successive generations have gone to the doctor, availed themselves of various government programs, built roads, and enjoyed other benefits, but handed part of the bill for the same to successive generations. That intergenerational sleight of hand works for a while. But as Europe and the United States are finding out now, borrowing cannot carry on forever without consequences.

## Notes

1 Note the following from the OECD as it concerns net debt measurements between countries: "Net debt measures are not always comparable across countries due to different definitions or treatment of debt (and asset) components. First, the treatment of government liabilities with respect to their employee pension plans may be different…Second, the range of items included as general government assets differs across countries. For example, equity holdings are excluded from government assets in some countries whereas foreign exchange, gold and SDR holdings are considered as assets in the United States and the United Kingdom. For details, see OECD Economic Outlook Sources and Methods (http://www.oecd.org/eco/sources-and-methods)." Despite the foregoing, what is obvious from the OECD data—the best comparison available—is the direction of each country's debt vis-à-vis its own economy.

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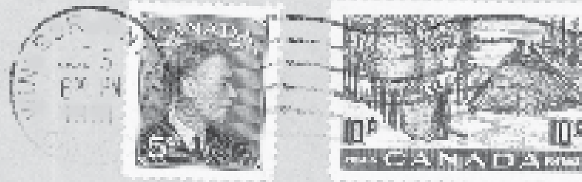
Charles Lammam
and Amela Karabegović



# Recent mail disruption strengthens case to privatize Canada Post

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Staring on June 2nd, 2011, several Canadian cities were subject to rotating strikes by Canada Post mail carriers when negotiations between Canada Post management and the Canadian Union of Postal Workers first stalled. Negotiations ultimately broke down resulting in a full-blown, country-wide lockout on June 14th that ended on June 27th, only after the federal government passed legislation forcing postal workers back to work.[1]

Naturally, Canadians who rely heavily on this crown corporation for mail delivery—including charities, small businesses, and ordinary individuals who receive their bills in the mail—were the ones adversely affected by the disruption. Episodes like these are unnecessary. To protect consumers in the future, the solution is to privatize Canada Post.

Canada Post has the exclusive right to deliver letters by "snail mail," meaning that its services are protected from competition by law. In other words, Canada Post has a monopoly on certain mail services. Private firms like FedEx and UPS, however, are only permitted to deliver goods, newspapers, books, magazines, and "letters of an urgent nature" (with fee stipulations).[2]

Postal services do not need to be delivered by a public monopoly protected from competitive pressures. Canadians would benefit tremendously from privatizing Canada Post and opening up all postal services to competition

Real world evidence indicates that private firms typically outperform their public sector counterparts.[3] Research that has looked specifically at Canada Post suggests privatization would greatly improve services and benefit consumers. For instance, *The Mail Monopoly*, an in-depth analysis of Canada's postal service, found that Canada Post has failed to provide Canadians with expedient and reliable services. As an example of poor service, the author, Professor Douglas Adie of Ohio University, notes that it took about the same amount of time to deliver a letter in 1990 as it did 200 years prior (Adie, 1990).

Adie points to New Zealand's experience with privatizing postal services as one reason for Canada to follow suit. After being privatized, the New Zealand Post Office moved from generating a loss to creating a profit by reducing its staff by 20% and its costs by 30%. It also sped up mail delivery and increased "on time" delivery by 15%. Professor Adie concludes that postal services are not likely to improve in Canada until Canada Post is privatized and subject to competition (Adie, 1990).

Additionally, in a 2007 study, University of Toronto professor Edward Iacobucci and his colleagues concluded that privatizing Canada Post would result in efficiency gains and improvements in service quality (Iacobucci et al., 2007). The study found that labour issues, particularly the presence of the Canadian Union of Postal Workers, make it difficult for Canada Post to improve efficiency and productivity. For instance, in 2005, Canada Post lost 16 days per full-time employee to absenteeism in delivery and mail processing operations. This was 60% higher than the Canadian average for manufacturing employees and 20% higher than the rate for all unionized employees (Iacobucci et al., 2007).

After reviewing the performance impacts of postal deregulation in Sweden, Finland, New Zealand, the Netherlands, Australia, Germany, and the United Kingdom, the Iacobucci study found that postal companies

increased service quality, adapted products and services to demand, introduced several mail-related innovations, reduced employment, and improved labour performance.

Privatizing Canada Post may also result in decreased stamp prices. A recent report from the Montreal Economic Institute summarized the European experience with privatization and competition in postal services and found that Austria, the Netherlands, and Germany experienced an 11% to 17% decline in the price of stamps for letter mail after privatization (Geloso and Chassin, 2011).

Lower prices and other benefits of privatization result from key differences between the behaviour of private sector firms and crown corporations and the incentives each face. Crown corporations typically operate in a state-provided monopoly shielded from competitive discipline. This means they are not required to constantly update technologies and production processes or offer innovative products and services to customers. The lack of competition also translates into less pressure to avoid or minimize work stoppages; in the private sector, the decline in profits and market share would be detrimental to a firm's viability.

In addition, crown corporations use less capital and are more labour-intensive than private sector firms (Megginson and Netter, 2001). As a result, they tend to be less productive.

Another essential difference is that crown corporations are influenced heavily by governments preoccupied with fulfilling political goals rather than pursuing economic or business objectives. Instead of allocating capital where it yields the highest economic return, governments typically allocate capital to areas that maximize their chances for re-election. This leads to a misallocation of resources.

Finally, crown corporations rarely go broke, since governments generally bail them out. If private businesses incur sustained losses, the decline of capital will push them into bankruptcy. To prevent this from occurring, private sector firms must provide customers with the quality of goods and services they demand, in a timely and efficient manner and at affordable prices. Crown corporations simply do not face the same pressures.

Canadians have much to gain from the privatization of postal services and our recent mail disruption only strengthens the case. It is time to privatize Canada Post.

## Notes

1 The dates cited in this paragraph are sourced from Canada Post's website: http://www.canadapost.ca/cpo/mc/aboutus/news/pr/2011/index.jsf.

2 For additional details on the exclusive privileges of Canada Post, see the Canada Post Corporation Act: http://laws-lois.justice.gc.ca/eng/acts/C-10/page-4.html.

3 See Lammam and Veldhuis (2009) for a survey of the academic evidence on the benefits of privatization.

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# New compensation package for BC teachers should tie pay to performance

Niels Veldhuis, Peter Cowley, and Milagros Palacios

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Given the current fiscal climate—the BC government's significant deficit ($1.4 billion over the next two years)[1]— and comparisons with the income of average BC families, now is hardly the time for increased wages and benefits for BC teachers. Rather than give all teachers more, the next collective agreement should tie teacher pay to performance.

Largely as a result of the recent recession, the income of BC families has grown by only 0.8%, on average, over the past four years (The Fraser Institute's 2011 Tax Calculator; calculation by the authors). That is lower than the rate of inflation (Statistics Canada, 2011; calculations by authors). In other words, consumer prices have increased faster than the income of average BC families, meaning that many families are actually worse off today.

But this is not true for BC teachers who signed a generous collective agreement in 2006, which gave them an annual average wage increase of 2.5% over five years (add in benefits and total compensation increase by 16% over the life of the agreement). In addition, each teacher received a $4,000 signing bonus (British Columbia Public School Employers' Association, 2011a; British Columbia Teachers' Federation, 2006a).

While average BC families struggled during the recession, BC teachers prospered. And after all this, the BC Teachers Federation (BCTF) wants even more as it renegotiates its contract.

Based on media reports, the BCTF is currently asking for[2]:

- 26 weeks (half year) paid leave to care for someone (being a family member is not a requirement);
- a year's pay as a "bonus" for retiring veteran teachers;
- two weeks paid leave upon the death of any friend; five paid days per year for professional activities;
- two sick days a month that can be saved up; and
- a substantial pay increase (not yet specified) that

would make BC teacher “the best paid teachers in the country.”

According to the teachers’ “employer”— the BC Public School Employers Association— it would cost BC taxpayers more than $2 billion to meet these demands (British Columbia Public School Employers’ Association, 2011b). And that doesn’t include their full salary demands.

The BC teachers union continues to ask for more, but refuses to consider a “merit pay” system that rewards teachers for effective teaching and encourages less successful teachers to improve their skills.[1] Such systems are common in both the public and the private sectors. Sales commissions, bonuses for established levels of superior performance, piecework, team incentives, and pay raises based on past success are all of common systems merit pay.

BC teachers generally earn a pay increase in two ways: they all get an annual increase upon completion of each of their first ten years of service or they get a boost through additional schooling.[2]

The research here is clear. Except for the first couple of years of teaching, more experience does not make a teacher more effective. Likewise, an advanced degree does not necessarily produce a more effective teacher either (Cowley and Veldhuis, 2011).[3] The current compensation system for BC teachers simply does not recognize effectiveness, and the BCTF is not willing to consider one that does.[4]

Add to this the fact that it is nearly impossible to penalize a failing teacher and you have a compensation system that contributes little to the improvement of our children’s futures. BC families need a reasonable deal to be finalized before kids return to school in September. Unfortunately, the BCTF’s current demands are not reasonable.

*It is nearly impossible to penalize a failing teacher*

## Notes

1 See British Columbia, Ministry of Finance (2011) for deficit estimates for 2011/12 and 2012/13.

2 See http://www.ctvbc.ctv.ca/servlet/an/local/CTVNews/20110104/bc_abbott_carbon_tax_110104?hub=BritishColumbiaHome

3 See the Teacher Qualification Service (TQS) category requirements at www.tqs.bc.ca/requirements.html and Local Collective Agreements 2006-2011 at http://bctf.ca/BargainingAndContracts.aspx?id=23150

4 There is solid evidence that properly designed merit pay systems can have positive affects. Please see Cowley and Veldhuis for a review of the literature.

5 See Local Collective Agreements 2006-2011 http://bctf.ca/BargainingAndContracts.aspx?id=20788&libID=20778

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# Indecent disclosure

## Canadian unions should reveal financials

Niels Veldhuis and Amela Karabegović

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Before Parliament was shut down, the mood in Ottawa was one of increased transparency and accountability. For instance, two private member bills making their way through the House and Senate were aimed at increasing the transparency of First Nations reserves and Canadian charities. Before this mood changes, the federal government should consider greater disclosure for another sector that severely lacks it: Canadian unions.

## The current push for greater transparency

The push for greater transparency on First Nations reserves has gained traction with Canadian politicians over the past year. In the fall of 2010, Kelly Block, a Conservative member of parliament tabled a private member's bill (Bill C-575: *Reserve Politicians' Pay Transparency Bill)* that would require public disclosure (on the Internet) of the salaries and reimbursement of expenses for First Nations chiefs and council members across Canada (Parliament of Canada, 2011a; Craig, 2011). The bill has passed its second reading in the House of Commons with 151 MPs voting for the bill and 128 against (Parliament of Canada, 2011a).

Similar developments have occurred in the charitable sector. Albina Guarnieri, a Liberal member of parliament drafted a bill (Bill C-470: *An Act to Amend the Income Tax Act Disclosure of Compensation — Registered Charities)* into parliament that proposes public disclosure for annual compensation of any executive or employee (at a registered charity) paid over $100,000. The House of Commons passed the bill on March 8th, 2011, and the next day it then passed its first reading in the Senate (Parliament of Canada, 2011b).

Of course, greater transparency and accountability are goals most Canadians would support. Canadian taxpayers, after all, provide billions to First Nations reserves and should therefore receive information on how their money is spent.

Registered charities, on the other hand, are exempt from taxes and

can issue receipts providing their donors with tax credits for their donation. Many charities also receive direct funding from the government. In part for these reasons, registered charities are already required to provide financial information including staff compensation to Canada Revenue Agency, which publishes it for public viewing on its website (see http://www.cra—arc.gc.ca/chrts—gvng/lstngs/menu—eng.html).

## The benefits of transparency and accountability

Public disclosure of financial information allows interested parties to gauge the financial health and performance of organizations. In addition, transparency leads to, and is essential for, accountability. Disclosing financial information publicly allows people to determine the appropriateness and effectiveness of spending (Palacios, et al., 2006). Empirical research has found that the benefits of greater transparency include improved governance and reduced corruption.[1]

## Indecent union disclosure

While public companies, charities—and hopefully soon, First Nations reserves—are subject to significant level of disclosure, little is required of unions in Canada in terms of releasing financial information. Currently, neither the federal government nor provincial governments require public disclosure of union financial information (Palacios, et al., 2006). This special treatment is striking given that unions receive funding from tax-deductible union dues.

In addition, workers in Canada can be legally forced to join a union as a condition of employment and have no choice but to remit union dues. Union leaders are able to use these mandatory and tax-deductible union dues to fight political battles, which their "members" and non-members may or may not support.

Union leaders in most jurisdictions (provincial and federal) would likely highlight that unions are required to make financial statements available to their members; Alberta, Prince Edward Island, and Saskatchewan do not require disclosure of financial statements to union members (Palacios, et al., 2006). However, union members must formally request financial statements, meaning the requests are not anonymous (Palacios, et al., 2006). Lack of anonymity, seriously compromises a worker's confidentiality and ability to make assessments without influence from union representatives.

This also means that the dues paying unionized workers who have not been forced to join the union, or have chosen not to join, have no right to information about how their money is being spent—even though they must pay those dues to keep their jobs. In addition, no Canadian province or the federal government prescribes or mandates a particular amount of detail in the financial statements (Palacios, et al., 2006). For instance, unions are not required to delineate expenses by type of activity. Most importantly, there is no requirement that financial statements indicate a breakdown between money spent on activities directly related to representing workers and activities unrelated to representation such as political activities.

In comparison, the United States requires significantly more disclosure from unions. To counter corruption and mismanagement, and to increase the transparency of union operations, the US government enacted new financial disclosure requirements in 2004. This legislation has required all unions

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to submit detailed financial statements to the Federal Department of Labor (DOL). Large unions—those that spend over $250,000 per year—are required to provide information for 47 financial items and another 21 non-financial items organized into two financial statements and 20 supporting schedules. Less onerous requirements are imposed on smaller unions, which spend less than $250,000 (Palacios, et al., 2006). Critically, all unions in the United States must specify the breakdown between spending on collective representation and spending not related to representation.

Another important aspect of union financial disclosure in the US is that union members and the public have equal access to all this information on the DOL website. This allows anonymous access in which union representatives are less likely to influence a worker's decisions.

Providing publically disclosed information about the financial status of unions enables workers to assess more accurately the financial position, activities, and performance of their representatives. Disclosing financial information publicly allows workers and interested parties to determine the appropriateness and effectiveness of union spending. The increased transparency that comes from public disclosure is also essential for accountability and provides an incentive for union leaders to manage membership dues properly.

Despite its depth and coverage, there is room for improvement when it comes to union disclosure in the United States. For example, the available data lack simplicity, making it difficult for an average person to get a true picture of unions' finances (Palacios, et al., 2006). Unfortunately, many additional disclosure requirements that would have made union disclosure more comprehensive were stalled and/or rescinded by the Obama Administration (Sherk, 2010; Korbe, 2011).

Specific differences in laws regarding union membership and union dues payments magnify the differences in union disclosure laws in Canada and the United States. As noted, workers can be forced to join a union as a condition of employment and are required to pay full union dues; this stands in stark contrast to the United States where workers cannot be forced to join or maintain membership in a union to retain their jobs. In addition, federal laws in the US allow workers a choice when it comes to financially supporting union activities that are not linked directly with worker representation, such as political activities.

Put another way, US workers have a choice regarding union membership and full dues payment, and have anonymous access to detailed information on union finances. Canadian workers have neither.

## Conclusion

Canadian politicians should be applauded for encouraging increased transparency and accountability. Public disclosure of financial information allows interested parties to gauge the financial health and performance of organizations, and the transparency created by disclosure laws serves to improve the governance of those organizations. Given the disclosure requirements already in place for publicly traded companies, charities, and other public organizations, it is time to end the special treatment of unions. At a minimum, Canadian unions should have the same level of financial disclosure as do their counterparts in the US. As the saying goes, "a little information goes a long way."

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## Note

1 For a summary of the literature on the benefits of transparency, see Palacios, et al., 2006.

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# Quarterly Research Alert

## Tax policy

**Kesselman, Jonathan (2011). Consumer Impacts of BC's Harmonized Sales Tax: Tax Grab or Pass-Through? *Canadian Public Policy* 37, 2: 138–162.**

Based on the notion that businesses do not pass on tax savings to consumers, many British Columbians believe that the harmonized sales tax (HST) shifts the tax burden from businesses to consumers and results in significantly higher prices. Using data from Statistics Canada's Consumer Price Index, which helps measure monthly and annual price changes, this study analyzes the actual impact of BC's HST on prices in the six months after its July 1st, 2010 implementation. The study finds that the overall price level in BC increased initially in July relative to three western provinces without a harmonized sales tax (Alberta, Saskatchewan, and Manitoba), but fell in the ensuing months. All told, the HST raised BC's overall price level by only 0.5% to 0.6%. This increase is equivalent to consumers paying an additional $1 for every $165 to $200 spent on all goods and services. The increase in overall prices is negligible and suggests businesses have passed on much of their tax savings to consumers in a very short period.

—Milagros Palacios

**Perotti, Roberto (2011). *The Effects of Tax Shocks on Output: Not So Large, But Not Small Either.* NBER Working Paper No. 16786. National Bureau of Economic Research.**

Despite much evidence showing that tax increases hinder economic growth, a hotly debated public policy issue is the magnitude of the impact. In this paper, the author builds on seminal work by University of California, Berkley professors Christina and David Romer, which found that a 1.0 percentage point increase in government tax revenue as a proportion of gross domestic product (GDP) leads to a decline in GDP of 3.0 percentage points after three years. Using a slightly different methodology than the Romers—one that separates the effects of two types of tax changes (policy-driven and business-cycle induced)—the author finds that the impact of tax increases is still significant but smaller than what the Romers estimated. The period of analysis in this paper is also different. The author examines quarterly data from the United States over the period 1945 to 2009 (vs. 1947 to 2006). In the end, he finds that "a one percentage point of GDP increase in taxes leads to a decline in output by about 1.5 percentage points after 12 quarters [three years]" (p. 38).

—Charles Lammam

## Government performance

**Bergh, Andreas, and Magnus Henrekson (2011). Government Size and Growth: A Survey and Interpretation of the Evidence. *Journal of Economic Surveys* (forthcoming).**

While some level of government activity is necessary for a well-functioning economy, excessively large government sectors can have dulling effects. This study comprehensively surveys the recent literature on the relationship between government size and economic growth with a special focus on studies including: highly developed countries such as Canada; measurements of government size being total taxes or spending relative to gross domestic product (GDP); and the effects of changes in government size over time. The authors conclude the "consensus" is that larger governments and income growth per person have a negative correlation. Typically, an increase in government size of 10 percentage points of GDP (measured by total taxes or spending) is associated with a 0.5 to 1.0 percentage point lower annual growth rate. The negative effects of big government can occur because of increased economic distortions through the tax system or unproductive spending that damages otherwise well-functioning markets. The composition of government also matters for economic growth. For example, a tax system that relies more on personal income taxes is more damaging than one that relies more on sales taxes. On the spending side, government transfers and consumption are negatively related to growth while education spending is positively related. In addition, the study tries to explain why some big government countries (i.e., Sweden) might experience above-average economic growth. First, high levels of social trust in the population may mitigate the harms from big governments on the economy. Second, "market-friendly" policies in other areas may offset growth-damaging policies from big government such as high taxes.

—Charles Lammam

## Underground economy

**Terefe, Berouk, Conrad Barber-Dueck, and Marie-Josée Lamontagne (2011).** ***Estimating the Underground Economy in Canada, 1992–2008*** **(June 2011). Income and Expenditure Accounts Division: Statistics Canada.**

The authors estimate the size of Canada's underground economy—economic activities that are not captured by traditional measures due to their hidden, illegal, or informal nature—over the period 1992 to 2008. Their estimate excludes illegal activities related to drugs and prostitution because reliable data in these areas is unavailable. Between 1992 and 2008, there was a total of almost $444 billion in underground activity in Canada (excluding illegal drugs and prostitution). Although the dollar value of Canada's underground economy nearly doubled from $18.8 billion in 1992 to $35.7 billion in 2008, it declined as a proportion of gross domestic product (GDP) from 2.7% to 2.2% over the same period. The decline occurred because traditionally underground industries (i.e., construction) are a shrinking portion of the overall economy and because non-underground industries (i.e., public administration) are growing quickly. In 2008, the three largest underground economy industries (excluding illegal drugs and prostitution) were construction (30%), retail trade (16%), and accommodation and food services (12%).
—Milagros Palacios

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## Labour market policy

**D'Amuri, Francesco, and Giovanni Peri (2011).** ***Immigration, Jobs, and Employment Protection: Evidence from Europe.*** **NBER Working Paper No. 17139. National Bureau of Economic Research.**

This paper revisits the question: do immigrants "steal" jobs from native workers? The authors examine the impact of immigrant workers on native jobs (i.e., total employment) in 14 Western European nations over the period 1996 to 2007. First, they find that an increased immigrant share of the population does not lead to lower employment levels for natives but rather boosts the proportion of natives working relative to the population. Second, increased immigration leads to a reallocation of jobs among natives. That is, with increased immigration, immigrants begin filling more "manual/routine" jobs while natives tend to transition to more "complex" ones relying more on language and cultural knowledge. Finally, the authors find that countries with more flexible labour markets—those where workers and employers can more easily adapt to changing market conditions—have greater native job reallocation. That suggests native workers in countries with less flexible labour markets have greater difficulty adjusting to immigration inflows.
—Amela Karabegović

**Bartelsman, Eric, Pieter A. Gautier, and Joris de Wind (2011). Employment Protection, Technology Choice, and Worker Allocation. DNB Working Paper No. 295. http://www.dnb.nl/en/binaries/working20paper%20295_tcm47-253008.pdf .**

Since the mid-1990s, overall productivity growth has been much slower in the European Union compared to the United States. This paper explores the role of Employment Protection Legislation (EPL)—laws that dictate the firing process and ultimately the cost to employers of terminating employees—in explaining the difference. In theory, employment protection legislation that increases firing costs for firms discourages business investment, which is a key determinant of productivity growth and higher living standards. The effect is particularly noticeable in high-risk industries such as information and communication because, to survive and prosper, firms must quickly expand or shrink their workforce to respond

to constantly changing market conditions, and also to capitalize on new opportunities in a timely fashion. After examining data on employment protection laws in European countries and in the US, the authors find that "higher firing costs are associated with lower employment shares in high risk industries [like information and communication] and higher shares in low risk industries" (p. 35). They extend the results to explain the European/US productivity gap: the costs of investing in new technology are lower in the US due to lower firing costs so high risk industries are better able to flourish, which increases the country's overall productivity growth.
—Amela Karabegović

## Industrial policy

**Haltiwanger, John C., Ron S. Jarmin, and Javier Miranda (2010).** ***Who Creates Jobs? Small vs. Large vs. Young.*** **NBER Working Paper No. 16300. National Bureau of Economic Research.**

The authors challenge the widespread perception that "most new jobs are created by small businesses." They use a new dataset on US firms spanning 1976 to 2005 and covering all businesses in the private non-farm economy that file payroll taxes with the Internal Revenue Service (IRS). The data is unique because it includes the age of firms. The authors do not find a relationship between net job growth (jobs created less jobs destroyed) and firm size but do find one between net job growth and firm age. That is, young firms—especially firms less than 5 years old—are positively associated with net job growth. This relationship is strongest for business start-ups—firms less than 1 year old—which make up just 3% of total US employment but close to 20% of total US gross job creation.
—Alex Gainer

## Education policy

**Woessmann, Ludger (2011). Cross-Country Evidence on Teacher Performance Pay.** ***Economics of Education Review*** **30, 3: 404–418.**

There has been much discussion recently, particularly in British Columbia, about introducing performance-related pay structures (i.e., "merit pay") for public school teachers. Such structures reward effective teachers for improved student outcomes. This study examines the impact of teacher performance pay on student test scores using data from 28 highly developed countries. Canada is not included in the analysis because data was not provided in the survey of teacher salaries and salary adjustments. The data include standardized test results from the Programme for International Student Assessment (PISA) for students in each country on subject areas covering mathematics, science, and reading. To be classified as using teacher performance pay, a country must award its public school teachers "salary adjustments" for "outstanding performance in teaching." The study finds that student test scores are significantly higher in countries that use teacher performance pay compared to those that do not. This relationship is most pronounced for test scores in mathematics and reading.
—Alex Gainer

## Border policy

**Nguyen, Trien T., and Randall M. Wigle (2011). Border Delays Re-Emerging Priority: Within-Country Dimensions for Canada.** ***Canadian Public Policy*** **37, 1: 49–59.**

Since the unfortunate 9/11 attacks, the Canada-US border has "thickened" due to heightened security causing increased delays. This study estimates the impact of border delays on Canadian trade flows and the Canadian economy more generally. The impact of border delays is quantified for two scenarios. Under the first, border delays are assumed to increase costs for businesses engaged in both merchandise and service trade by 1%. This translates into a shortfall in total Canadian trade of 3.6% and lost economic output valued at 1% of Canada's total gross domestic product (GDP). In the second and less conservative scenario, the assumption is that border delays cause a 2% cost increase for businesses in merchandise trade and a 1% cost increase for those in service trade. Here, the impact is more negative: a shortfall in total Canadian trade of 6.8% and lost economic output equal to 1.8% of total Canadian GDP. The study also finds that Ontario and Quebec are hardest hit by border delays while British Columbia suffers the least. The study concludes that there are large economic benefits from reducing border delays.
—Nachum Gabler

# Using private drug insurance to achieve universal access for new prescription drugs

Mark Rovere

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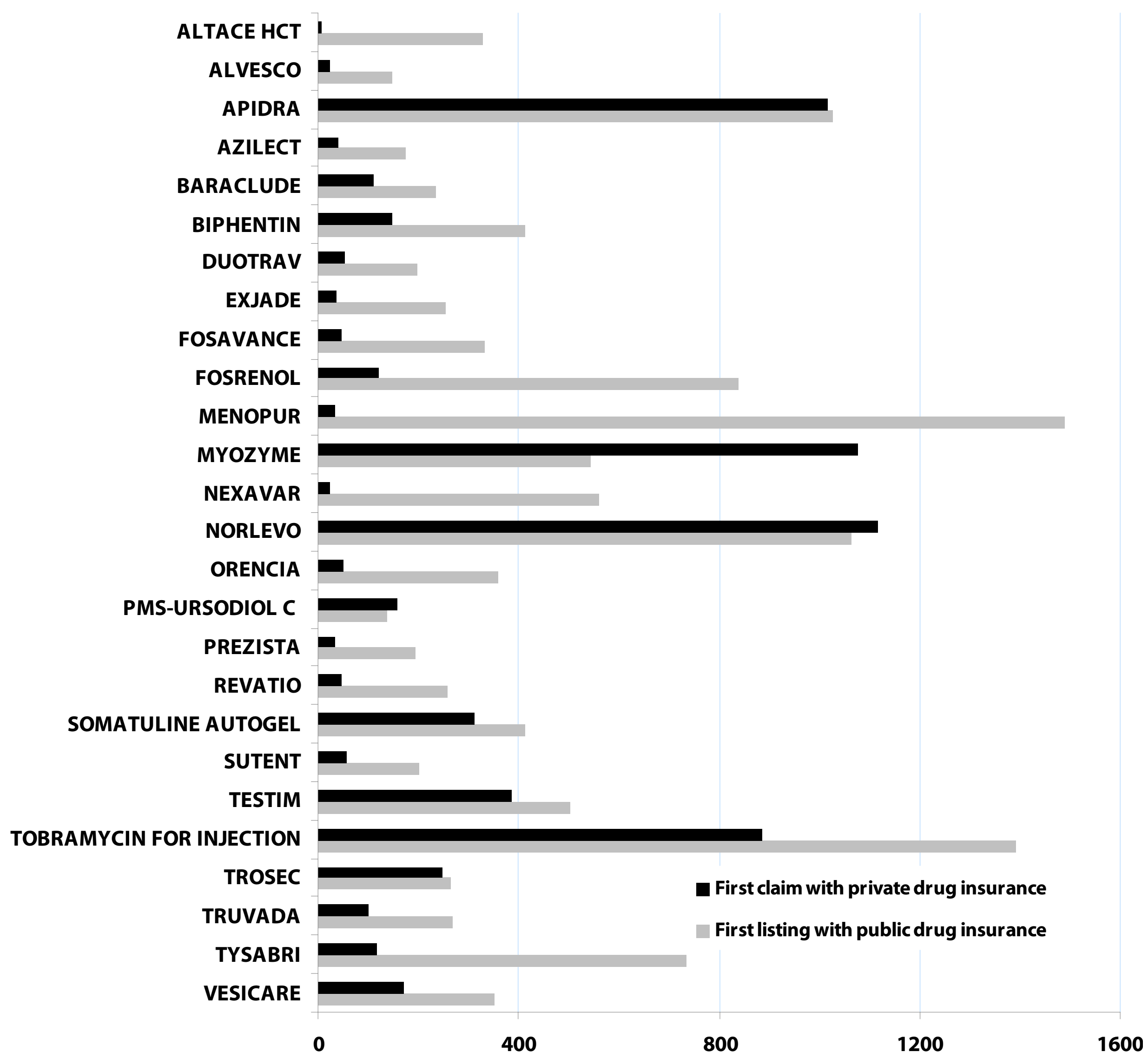
Canadians dependent on provincial public drug plans continue to wait unreasonably long times to access the newest drugs that Health Canada certifies as safe and effective. Moreover, recipients of these programs are often outright denied access to such new drugs. This should come as no surprise, as provinces are faced with political pressures and budget constraints due to unsustainable health care costs (Skinner and Rovere, 2011). While some provincial plans cover more new drugs than others, in general, cost containment policies such as delaying and denying coverage for the newest prescription drugs are common among all provincial drug plans. In contrast, evidence shows that private drug insurance in Canada tends to cover far more new drugs certified by Health Canada and covers new drugs much sooner than public drug programs (Rovere and Skinner, 2011). Under these circumstances, it is clear that private drug insurance in Canada is far more generous in terms of covering new drugs than publicly funded government-run programs. Therefore, if all Canadians want speedy, universal access to the newest prescription drugs approved by Health Canada, the optimal solution is for governments to get out of the drug insurance business altogether and instead facilitate access to private sector insurance through means-tested subsidies for low-income people.

## Waiting for new drugs

Canadians wait longer than their European and American counterparts to access the newest drugs. Our annual update of *Access Delayed, Access Denied: Waiting for New Medicines in Canada* finds that Health Canada's performance was worse than that of the European EMEA (the European Union's drug certification agency) in all four years studied (2006 to 2009). Likewise, the most recently available data indicate that Health Canada's performance was worse than that of the American FDA in five of the last six years studied (2004 to 2009) (Rovere and Skinner, 2011). This means that Canadians are often deprived of many of the new drugs that are available in other countries.

Once Health Canada certifies a new drug—giving the drug manufacturer permission to sell the product in Canada—the wait is not over for many Canadians. This is because insurers, both public and private, must decide whether or not the new drug will be covered under their respective drug plans. Although it is normal for drug insurers to take "some" time when deciding if they will cover a specific drug, the data indicate that public drug insurance plans in Canada take far longer than private drug insurance plans to make a decision. Figure 1 displays the difference in days between the first claim that was made with a private insurance plan and the first listing of the drug with a public insurance plan (aggregated across provinces) for all drugs that received certification from Health Canada in 2006 (pharmaceutical and biological), and that have been approved for reimbursement by at least one public *and* private drug insurance plan as of June 9$^{th}$, 2011. As figure 1 shows, only three drugs (*Myozyme, Norlevo*, and *PMS-Ursodiol C*) were listed for public reimbursement before being covered by at least one private insurer. Put another way, out of the new

**Figure 1: Difference (in days), between the first listing with a public insurance plan and the first claim with a private insurance plan for new drugs that were certified by Health Canada in 2006, aggregated across all provinces and drug plans**




Sources: Rovere and Skinner, 2011.

drugs that were certified by Health Canada in 2006, and were approved for coverage by at least one public *and* private insurer as of June 9th, 2011, 88.5% were covered by a private insurer first. In some extreme cases (figure 1), such as the biological drug *Menopur*, the difference in reimbursement approval between public and private drug insurance was 1,458 days (approximately 4 years). The average difference in delays across all drugs listed in figure 1 is 241 days (nearly 8 months). Notably, this is shorter than in previously years where the difference in approval delays between public and private insurers was 444 days (approximately 15 months) and 539 days (almost 18 months) for drugs certified by Health Canada in 2004 and 2005 respectively (Rovere and Skinner, 2011).

Therefore, the data show that Canadians dependent on public drug programs are waiting longer than those with private drug insurance before they have access to the newest prescription drugs. Critically, this represents nearly 30% of the entire population (approximately 10 million Canadians), which include recipients of various provincial programs covering seniors, people with low incomes, and patients with catastrophic drug costs; in addition to a federal plan that covers members of the armed forces, veterans, federal inmates, and First Nations (ISPOR, 2011).

## Denial of access

While it is clear that Canadians dependent on public drug plans wait longer to access new drugs than those who have private insurance, the data also show that in many cases, Canadians relying on public drug plans are often denied coverage altogether.

## Table 1: Public reimbursement approvals, as a percentage of new drugs approved by Health Canada, by province, 2004–2009, as of June 9th, 2011

| | 2004 | | 2005 | | 2006 | | 2007 | | 2008 | | 2009 | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Number of drugs approved | Drugs approved as a % of NOCs | Number of drugs approved | Drugs approved as a % of NOCs | Number of drugs approved | Drugs approved as a % of NOCs | Number of drugs approved | Drugs approved as a % of NOCs | Number of drugs approved | Drugs approved as a % of NOCs | Number of drugs approved | Drugs approved as a % of NOCs |
| **AB** | 8 | 17.0% | 4 | 9.1% | 12 | 24.0% | 5 | 11.9% | 6 | 18.8% | 6 | 13.3% |
| **BC** | 10 | 21.3% | 2 | 4.5% | 9 | 18.0% | 7 | 16.7% | 8 | 25.0% | 10 | 22.2% |
| **MB** | 9 | 19.1% | 5 | 11.4% | 11 | 22.0% | 8 | 19.0% | 6 | 18.8% | 1 | 2.2% |
| **NB** | 11 | 23.4% | 12 | 27.3% | 23 | 46.0% | 16 | 38.1% | 11 | 34.4% | 4 | 8.9% |
| **NL** | 11 | 23.4% | 9 | 20.5% | 18 | 36.0% | 11 | 26.2% | 10 | 31.3% | 4 | 8.9% |
| **NS** | 9 | 19.1% | 13 | 29.5% | 16 | 32.0% | 9 | 21.4% | 7 | 21.9% | 5 | 11.1% |
| **ON** | 8 | 17.0% | 7 | 15.9% | 11 | 22.0% | 11 | 26.2% | 7 | 21.9% | 4 | 8.9% |
| **PEI** | 9 | 19.1% | 8 | 18.2% | 13 | 26.0% | 7 | 16.7% | 2 | 6.3% | 4 | 8.9% |
| **QC** | 20 | 42.6% | 14 | 31.8% | 24 | 48.0% | 22 | 52.4% | 14 | 43.8% | 16 | 35.6% |
| **SK** | 13 | 27.7% | 11 | 25.0% | 18 | 36.0% | 11 | 26.2% | 10 | 31.3% | 5 | 11.1% |
| **Provincial average** | | 23.0% | | 19.3% | | 31.0% | | 25.5% | | 25.3% | | 13.1% |
| **Total new drugs** | 47 | | 44 | | 50 | | 42 | | 32 | | 45 | |

Source: Rovere and Skinner, 2011.

## Table 2: Drugs covered by at least one private insurer, as a percentage of new drugs approved by Health Canada, averaged across all provinces, as of June 9th, 2011

| | 2004 | | 2005 | | 2006 | | 2007 | | 2008 | | 2009 | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Number of drugs claimed by at least one private insurer (across the provinces) | Drugs claimed as a % of NOCs | Number of drugs claimed by at least one private insurer (across the provinces) | Drugs claimed as a % of NOCs | Number of drugs claimed by at least one private insurer (across the provinces) | Drugs claimed as a % of NOCs | Number of drugs claimed by at least one private insurer (across the provinces) | Drugs claimed as a % of NOCs | Number of drugs claimed by at least one private insurer (across the provinces) | Drugs claimed as a % of NOCs | Number of drugs claimed by at least one private insurer (across the provinces) | Drugs claimed as a % of NOCs |
| | 46 | **97.9%** | 40 | **90.9%** | 41 | **82.0%** | 31 | **73.8%** | 22 | **68.8%** | 37 | **82.2%** |
| Total new drugs | 47 | | 44 | | 50 | | 42 | | 32 | | 45 | |

Source: Rovere and Skinner, 2011.

Averaged across all provincial public drug programs, as of June 9th, 2011, only 23.0% of all drugs that Health Canada approved as safe and effective in 2004 had actually been approved for reimbursement (fully or partially) by the provinces; compared to 19.3% of new drugs certified in 2005, 31.0% of new drugs certified in 2006, 25.5% of new drugs certified in 2007, 25.3% of new drugs certified in 2008, and 13.1% of new drugs certified in 2009 (table 1). The coverage rate (percentage of drugs that were approved for public reimbursement) averaged across all years was less than 23%.

In contrast, a comparison of private insurance coverage over the same period shows that private insurers in Canada (averaged across provinces and insurers) are far more generous in terms of covering the amount of new drugs. As table 2 shows, averaged across all provinces, 97.9% of all new drugs that Health Canada approved as safe and effective in 2004 were covered by at least one private insurer as of June 9th, 2011. Similarly, 90.9% of new drugs certified in 2005, 82.0% of new drugs certified in 2006, 73.8% of new drugs certified in 2007, 68.8% of new drugs certified in 2008, and 82.2% of new drugs certified in 2009 were covered by at least one private insurer (averaged across all provinces) as of June 9th, 2011. The coverage rate (percentage of drugs that were approved for coverage by at least one private insurer) averaged across all years was almost 83%.

## Allow a competitive private drug insurance market to facilitate universal access for all Canadians

The data show that private drug insurance in Canada covers new drugs sooner—and covers far more new drugs than public drug plans. While some Canadians cannot afford to purchase private drug insurance, they should not be penalized by being forced into a centrally planned public program that is bound by political decisions and budget constraints, which ultimately restrict consumer choice. In order to achieve universal access to new drugs, regardless of income, all Canadians should have the ability to purchase a drug insurance plan that meets their individual needs in the private market. This could be achieved by replacing existing government drug plans with a regulated, competitive, private-sector market in which universal access to catastrophic drug insurance is facilitated through means-tested subsidies for people with low incomes.[1] This sensible policy would restrict subsidies to only those requiring financial assistance to pay for their drugs, as oppose to age-based subsidies which are common in a number of provinces.

In recent years there has been growing pressure on the federal government to create a national pharmacare program, ostensibly to improve access to new drugs. But such an approach is the opposite of what we should do. Expanding the role of government in the provision of drug insurance will certainly only increase the politicization of coverage decisions and further stretch the already bursting budgets currently facing governments. Whereas income-based subsidies will provide all Canadians[2] with access to private drug insurance, and therefore offer the benefits of more generous and timely coverage of the newest prescription drugs. It is time for governments to get out of the business of drug insurance; governments only need to target subsidies to those who genuinely need help to pay their drug costs, and allow a competitive private sector to do what it does best: respond to consumer demand.

## Notes

1 Research shows that most people spend a very small share of their income on prescription drugs. Those who have 'catastrophic drug costs' (high drug costs relative to their income) – should receive public subsidies. Critically, tax funded subsidies must solely be allocated based on need (income-based).

2 This is precisely how Switzerland and the Netherlands achieve universal health care coverage. Public subsidies are allocated to those with low-income – which are used to purchase a basic health insurance plan in the competitive private insurance market. .

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# Corporate headquarters in Canada

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Alex Gainer

Which Canadian city is home to the largest number of corporate headquarters for Canada's top 500 corporations?[1] How has this changed over time?

Table 1 contains data from 1990, 2000, and 2010 showing how many corporate headquarters are located in Canada's five main corporate centres: Montreal, Toronto, Winnipeg, Calgary, and Vancouver.[2] Toronto was overwhelmingly the dominant location for corporate headquarters in all three years examined. In 2010, 35.0% of corporate headquarters for Canada's top 500 corporations were located in Toronto. Montreal ranked second, Calgary third, Vancouver fourth, and Winnipeg last.

## Is the absolute number of corporate headquarters an effective measure of corporate headquarter activity?

No. A better way to measure corporate headquarters activity is to adjust for population. Simply counting the number of corporate head offices without adjusting for the size of the city ignores the real effect that the concentration of corporate headquarters can have on an economy. This concentration is important because of the spin-off effects associated with corporate headquarters. Support professionals such as lawyers, consultants, and accountants tend to establish themselves near these headquarters and create a larger professional community, a greater concentration of knowledge, and easier access to high quality services for other companies nearby.

By this measure, Calgary is by far the Canadian leader in the concentration of corporate headquarters, with 6.0 corporate head offices per 100,000 people in 2010. Calgary's concentration is double that of Toronto, which had 3.0 corporate head offices per 100,000 people (table 2; figure 1). Montreal had 2.1 corporate head offices per 100,000 people. Vancouver was fourth among the cities with 2.0 corporate head offices per 100,000 people, and Winnipeg had 1.9 corporate head offices per 100,000 people.

**Table 1: Corporate headquarters overview**

| | 1990 | | 2000 | | 2010 | |
|---|---|---|---|---|---|---|
| | Number of top 500 headquarters | % of top 500 | Number of top 500 headquarters | % of top 500 | Number of top 500 headquarters | % of top 500 |
| Montreal | 96 | 19.2% | 92 | 18.4% | 81 | 16.2% |
| Toronto | 186 | 37.2% | 190 | 38.0% | 175 | 35.0% |
| Winnipeg | 18 | 3.6% | 18 | 3.6% | 14 | 2.8% |
| Calgary | 44 | 8.8% | 50 | 10.0% | 75 | 15.0% |
| Vancouver | 45 | 9.0% | 41 | 8.2% | 49 | 9.8% |

Sources: *FP Magazine*, 1991, 2001, 2011. Calculations by author.

## How does adjusting for Canada's government-held corporations affect the rankings?

There were a total of 51 government corporations3 on the top 500 list in 2010, approximately 10% of the total. Twenty-six of the 51 (51.0%) are among the top 200 Canadian corporations. Put differently, 13.0% of the top 200 Canadian companies in Canada are government holdings.

Table 3 shows the concentration of private corporate head offices, excluding government-held corporations. If government corporations are removed from the mix, Winnipeg's concentration is the most affected, dropping 35.7% (five headquarters). After Winnipeg, the concentration in Vancouver is the next most affected (8.2% or 4 headquarters), followed by Montreal (7.4%, or six headquarters), and Toronto (5.1%, or nine headquarters). Calgary's count is affected the least with a change of only 2.7% (two headquarters).

## Notes

1 Only corporate headquarters for the top 500 Canadian corporations as reported by the Financial Post are included in this analysis.

2 The five centres are defined as "Census Metropolitan Areas" by Statistics Canada for the 2006 census. This means, for example, that Toronto includes not only the City of Toronto, but also Mississauga, the fourth largest city for headquarter activity (headquarter count), as well as the municipalities of Ajax, Aurora, Bradford West Gwillimbury, Brampton, Caledon, East Gwillimbury, Georgina, Halton Hills, King, Markham, Milton, Mono, New Tecumseth, Newmarket, Oakville, Orangeville, Pickering, Richmond Hill, Uxbridge, Vaughan, and Whitchurch-Stouffville.

3 Fifty of these government-held corporations were wholly owned, while 90% of the 50th (Enersource Corp.) was held by the City of Mississauga.

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***The full FP500 for 2010, as well as rankings for 2008 and 2009, can be found on the Financial Post's website: <http://www.financialpost.com/magazine/fp500/index.html>.

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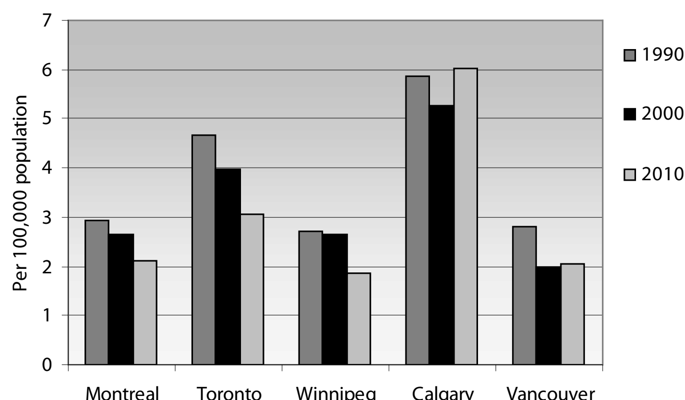
**Table 2: Canadian corporate headquarters per 100,000 population, 1990, 2000, and 2010**

| | 1990 | 2000 | 2010 |
|---|---|---|---|
| Montreal | 2.9 | 2.6 | 2.1 |
| Toronto | 4.7 | 4.0 | 3.0 |
| Winnipeg | 2.7 | 2.6 | 1.9 |
| Calgary | 5.9 | 5.3 | 6.0 |
| Vancouver | 2.8 | 2.0 | 2.0 |

Sources: *FP Magazine*, 1991, 2001, 2011; Statistics Canada's CANSIM database <http://cansim2.statcan.ca/>. Calculations by author.

**Figure 1: Canadian corporate headquarters per 100,000 population, 1990, 2000, and 2010**



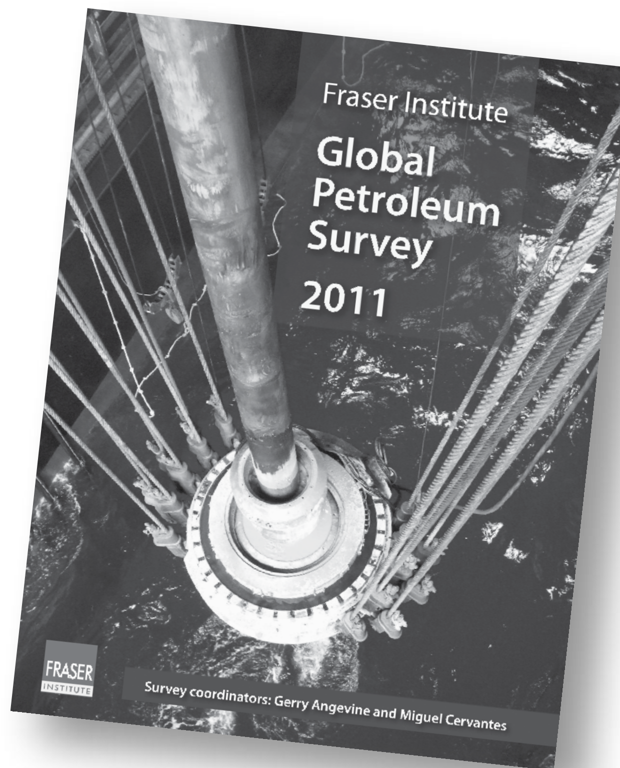

Sources: *FP Magazine*, 1991, 2001, 2011; Statistics Canada's CANSIM database <http://cansim2.statcan.ca/>. Calculations by author.

**Table 3: Private Canadian corporate headquarters per 100,000 population, 2010**

| | 2010 | Percentage change in concentration of corporate headquarters |
|---|---|---|
| Montreal | 1.9% | (7.4) |
| Toronto | 2.9% | (5.1) |
| Winnipeg | 1.2% | (35.7) |
| Calgary | 5.9% | (2.7) |
| Vancouver | 1.9% | (8.2) |

Sources: FP Magazine, 2011; Statistics Canada's CANSIM database: <http://cansim2.statcan.ca/>. Calculations by author.

# Overcoming regulatory obstacles to upstream petroleum investment




**Gerry Angevine and Miguel Cervantes**

The Fraser Institute's annual global survey of petroleum explorers and developers measures the extent to which each of 17 factors poses a barrier to investment in jurisdictions around the world. This year a total of 502 individuals with 478 companies participated in the survey, providing sufficient data to evaluate 135 jurisdictions. This article discusses how the survey data were used to evaluate the regulatory climate in provinces, states, and countries around the world, and which jurisdictions appear to pose the most and least concern for petroleum investors because of regulatory issues. It also examines where and why the most deterioration and most improvement have occurred in the regulatory climate since the first half of 2010.[1]

## The survey process

The survey questionnaire provided a list of 146 jurisdictions that respondents could evaluate.[2] Respondents were requested to evaluate only those jurisdictions with which they were familiar.[3]

For each of 17 factors judged to be important determinants of investment decisions, respondents were asked to select one of the following responses as best describing each jurisdiction that they chose to evaluate:

**1.** Encourages investment
**2.** Is not a deterrent to investment
**3.** Is a mild deterrent to investment
**4.** Is a strong deterrent to investment
**5.** Would not invest due to this criterion

For each jurisdiction, scores were assigned to each factor according to the percentage of responses received that indicated that the factor posed a barrier to investment, i.e., either a mild or strong deterrent, or a problem of such degree that the respondent "would not invest at all." The greater the proportion of negative responses garnered by a jurisdiction for a given factor, the greater the investment barrier that the factor was seen to pose. Jurisdictions with the lowest scores were assumed to pose fewer investment barriers and, therefore, ranked higher in terms of their attractiveness for investment.

The discussion that follows is based on "Regulatory Climate Index" (RCI) values derived from responses pertaining to 6 factors addressed in the survey questionnaire that pertain regulatory conditions.[4] For each jurisdiction, higher index values point to greater barriers to development.

## Where the regulatory climate is of most and least concern

Of the 135 jurisdictions ranked in the survey, 41 had RCI values greater than 60. These jurisdictions were judged to have relatively unattractive regulatory climates (table 1).

The first 14 jurisdictions in this group have RCI values greater than 80, meaning that they have unsavory regulatory environments. In general, the most important reason why jurisdictions such as Venezuela, Kazakhstan, Ecuador, Iran, Russia, and the others in this group (except for the US Offshore-Pacific) have such poor RCI ratings is because of negative responses to the question on legal system fairness and transparency. The second most important reason is uncertainty regarding the interpretation and administration of existing regulations. The cost of regulatory compliance, labour regulations, and agreements and

regulatory duplication and inconsistencies were also high on the list of concerns. Of the most concern about US Offshore-Pacific is uncertainty regarding environmental regulation, judged to be the worst in the world. Similar concern was also expressed for Ecuador, Kazakhstan, Uzbekistan, Russia, Chad, and India.

Among the remaining 27 jurisdictions with RCI values of 60 or higher were Quebec, the Northwest Territories, 6 African countries, 4 of the 5 Argentine provinces included in the survey, a number of former USSR republics, Bangladesh, Indonesia, Yemen, and China. Italy is the sole European jurisdiction to fall within this group.

The North American jurisdictions in the group of 41 for which the regulatory climate poses a significant barrier to investment all scored relatively poorly on 3 of the 6 questions underlying the RCI. Conversely, 14 jurisdictions with RCI values below 20 seem to pose relatively few regulatory obstacles for investors. Of the 7 US states included in this category, the most notable was Ohio, which received no negative responses to any of the 6 questions. Canada's own Saskatchewan, with an RCI value of 21.7, is the 16th most attractive jurisdiction worldwide in terms of regulatory climate. The next-best Canadian jurisdiction is Nova Scotia in 47th place.

## Where the greatest deterioration in regulatory climate has occurred

The greatest regulatory climate deterioration from 2010 to 2011 occurred in the US Offshore-Gulf of Mexico, the Northwest Territories, US Offshore-Alaska, Uganda, Quebec, Wyoming, Equatorial Guinea, Philippines, US Offshore-Pacific, and Cambodia. The most pronounced decline occurred in the case of the US Offshore-Gulf of Mexico, where the BP oil spill occurred. Here, the survey notes an increase in negative responses to uncertainty regarding environmental regulation, uncertainty in the interpretation and administration of regulations in general, and regulatory duplication and inconsistency. As a result, that region's RCI value increased from slightly below 18 to almost 66.

The Northwest Territories experienced the second-largest deterioration in regulatory climate as reflected by an increase in its RCI value from 45 to 78, to rank 16th worst globally. The slippage in performance resulted from worse scores on the same 3 factors that had the greatest impact on the RCI rating of the US Offshore-Gulf of Mexico. In the case of the Northwest Territories, the numerous onerous conditions attached to the National Energy Board's December 2010 decision on the Mackenzie Gas Project are at least partly to blame as they gave rise to considerable regulatory uncertainty and will have a substantial impact on the cost of regulatory compliance faced by investors in natural gas exploration and development.

US Offshore-Alaska and Uganda saw their RCI values increase (deteriorate) by slightly more than 26 points and 22 points, respectively. The US Offshore-Alaska received poorer scores on all 6 of the RCI questions, but especially with regard to regulatory duplication and inconsistency, the cost of regulatory compliance and uncertainty pertaining to the interpretation and administration of regulations.

Uganda performed worse this year on all of the RCI factors except regulatory duplication. The country experienced the most deterioration with regard to uncertainty in relation to environmental regulations, but also slipped considerably in terms of both the cost of regulatory compliance and the labour regulations and agreements factors.

The increased negative perception surrounding Quebec's regulatory climate (almost a 22- point worsening according to the RCI) is mainly a result of poorer scores on questions about environmental regulation uncertainty, regulatory uncertainty in general, and increased concern about the obstacles that labour regulations and agreements pose for upstream investment. Poorer scores on the cost of regulatory compliance and regulatory duplication questions also contributed to Quebec's rating as one of the least favourable (19th worst) regulatory climates worldwide. Although not specifically addressed by the survey respondents, the deterioration in Quebec's RCI value and ranking appears to reflect uncertainty with regard to regulations which face companies seeking approval of shale gas exploration and development projects. For example, companies that had been granted exploration permits by the Quebec government are now prevented from moving ahead pending the outcome of a strategic environmental assessment process.

Wyoming, Equatorial Guinea, the Philippines, US Offshore-Pacific, and Cambodia each experienced deterioration on the RCI scale by 18 to almost 22 points. In Wyoming's case, the increased concern was mainly due to the cost of compliance factor although regulatory duplication and inconsistency and uncertainty with respect to environmental regulation also received greater percentages of negative responses than in 2010.

The US Offshore-Pacific region is noteworthy in that it is seen as the least attractive for investment globally because of uncertainty in environmental regulations and regulatory duplication and inconsistency. Deterioration in the region's score on the latter question, and with regard to the cost of compliance, largely explains why the US Offshore-Pacific's

**Table 1: Regulatory climate index values (for the worst 41 of 135 jurisdictions ranked in the *2011 Global Petroleum Survey*)**

| Jurisdiction | RCI value |
|---|---|
| Venezuela | 100.0 |
| Kazakhstan | 98.9 |
| Ecuador | 94.8 |
| Iran | 93.4 |
| US Offshore-Pacific | 91.3 |
| Bolivia | 91.1 |
| Russia | 89.7 |
| Uzbekistan | 86.2 |
| Iraq | 85.3 |
| Turkmenistan | 82.9 |
| Nigeria | 82.6 |
| India | 81.3 |
| Chad | 80.7 |
| Algeria | 80.3 |
| Libya | 78.2 |
| Northwest Territories | 78.2 |
| Equatorial Guinea | 77.2 |
| Azerbaijan | 77.2 |
| Quebec | 76.9 |
| Ukraine | 76.0 |
| California | 75.3 |
| Bangladesh | 73.6 |
| Indonesia | 73.0 |
| US Offshore-Alaska | 71.9 |
| Uganda | 71.3 |
| Argentina-Neuquen | 71.2 |
| Democratic Republic of the Congo (Kinshasa) | 70.9 |
| Argentina-Chubut | 68.5 |
| Yemen | 67.9 |
| Angola | 67.4 |
| Timor Leste | 67.4 |
| Argentina-Santa Cruz | 67.1 |
| Cambodia | 65.9 |
| US Offshore-Gulf of Mexico | 65.7 |
| Argentina-Mendoza | 65.1 |
| Kyrgyzstan | 64.4 |
| Myanmar | 64.0 |
| China | 63.7 |
| Pakistan | 63.6 |
| Italy | 62.4 |
| Mauritania | 60.8 |

Source: Angevine, 2011.

RCI rating worsened as much as it did during 2011. In the Philippines and Cambodia, the deterioration in the regulatory climate was mainly a result of greater concern about the cost of regulatory compliance. In Equatorial Guinea, increased uncertainty in relation to environmental regulation was the principle contributor to the higher (therefore less desirable) RCI value this year, although other factors, such as the cost of regulatory compliance and legal system fairness and transparency had a role to play.

Among the jurisdictions with the most improved regulatory climates this year are Morocco and Bahrain, each with RCI values about 22 points lower than in 2010, Côte d'Ivoire and Japan with nearly 21-point and 20-point improvements, respectively, and Turkey with a 19-point improvement. Other top achievers were Ohio (-17), Sudan (-16), Kyrgyzstan (-15), Bulgaria (-15), Ukraine (-14), Ghana (-13), and Romania (-13). Eight other jurisdictions scored lower on the RCI by 10 points or more than in 2010, suggesting some significant improvement in the regulatory climate. Included in this group are Norway-North Sea, Norway, the Netherlands-North Sea, and West Virginia

In Bahrain, the improvement in the RCI value resulted mainly from better performance on the labour regulations and agreements and the uncertainty surrounding environmental regulation factors. Morocco's better regulatory climate resulted from improved scores on all 6 questions, particularly regarding the cost of regulatory compliance and uncertainty with regard to the interpretation and administration of applicable regulations.[5]

Côte d'Ivoire scored much better on the regulatory duplication and inconsistency question than a year earlier, but also improved significantly with respect to the labour regulations and agreements, and legal system transparency factors. Japan improved considerably on labour regulations and agreements, and also scored substantially better on legal system fairness and regulatory duplication and inconsistency than in 2010.

Among the jurisdictions with the most improved RCI values this year, the most common reasons for the improvement related to the regulatory duplication, legal fairness, and labour regulations factors. Although reduced concern over uncertainty in environmental regulations, the cost of regulatory compliance, or regulatory uncertainty were not frequent

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Northstar Island, constructed in Alaska's Beaufort Sea to provide stability and address environmental issues.

contributors to better RCI ratings, some of these factors were important in some countries, such as Kyrgyzstan, Morocco, and Bahrain.

## Policy implications

This year's survey questionnaire invited respondents to indicate the extent of the difference that "full and complete transition to best practices" could make to petroleum exploration and development. Not surprisingly, in the case of 36 of the 41 jurisdictions with poor regulatory climates, the results show that adoption of best practices could make a substantial difference. While "best practices" was meant to apply to all of the main determinants of investment, and not just the 6 regulatory factors captured by the RCI measure, this strongly suggests that improvement in the regulatory climate could quite considerably increase activity in the upstream petroleum industry.

In order to encourage investment, governments need to ensure that regulatory concerns do not pose significant barriers to investors. This means that policy makers must strive to reduce uncertainty over how regulations will be interpreted and administered, and how they are likely to be altered (as with carbon emissions controls). Regularly reviewing regulations with an eye to simplification and, wherever possible, streamlining regulatory processes and procedures will help to ensure that compliance costs do not balloon compared with other jurisdictions. Similarly, ensuring that the legal system is fair and transparent, abiding by existing contractual agreements, and striving to remove duplication and inconsistencies in the regulatory framework will help to improve attractiveness for investment.

Without regulatory certainty, viable projects that meet environmental protection and labour standards, and that would generate jobs and prosperity are often unable to proceed. On the other hand, projects that do not meet the requirements of environmental and safety regulations but yet have backers with close ties to government decision makers sometimes get approved. Experience teaches that no matter the ideology—left, right, or green—uncertainty must be reduced. Nobody would accuse Socialist Norway of being lax on environmental or labour requirements, yet Norway ranks higher in the eyes of investors these days than Quebec, California, and the US Offshore-Pacific region.

## Notes

1 The survey is undertaken each year during February, March, and April.

2 The list from which respondents could select included most Canadian provinces, the Northwest Territories, and Yukon, many US states (including the Atlantic, Pacific, Gulf Coast, and Alaska offshore regions), all six Australian states, the Australian offshore and the Timor Gap, and other countries with current petroleum production capacity. Mexico and Saudi Arabia, where investment in upstream petroleum exploration and development is essentially confined to government-owned entities, were both excluded.

3 Although 146 jurisdictions were listed, the minimum number of 5 responses required on each survey question to allow a jurisdiction to be ranked was obtained for only 135 jurisdictions.

4 These are: 1.Uncertainty concerning the basis for and/or anticipated changes to environmental regulations; 2. Uncertainty regarding the administration, interpretation, and enforcement of existing regulations and concern with the frequency of changes to regulations; 3. The cost of regulatory compliance in relation to applications, public hearings, etc.; 4. Labour regulations, employment agreements, and local hiring requirements; 5. Legal system fairness and transparency; and 6. Regulatory duplication and inconsistencies.

5 This year's global petroleum survey was undertaken during the period from the beginning of February 2011 to the third week of April 2011. At that time, much of the Arab world, including Tunisia, Egypt, Yemen, Bahrain, and Syria were in various degrees of political turmoil which, in some cases, is far from settled. It will be interesting to see how the 2011 "Arab spring" impacts the survey scores and rankings achieved by the various Arab countries in the 2012 survey.

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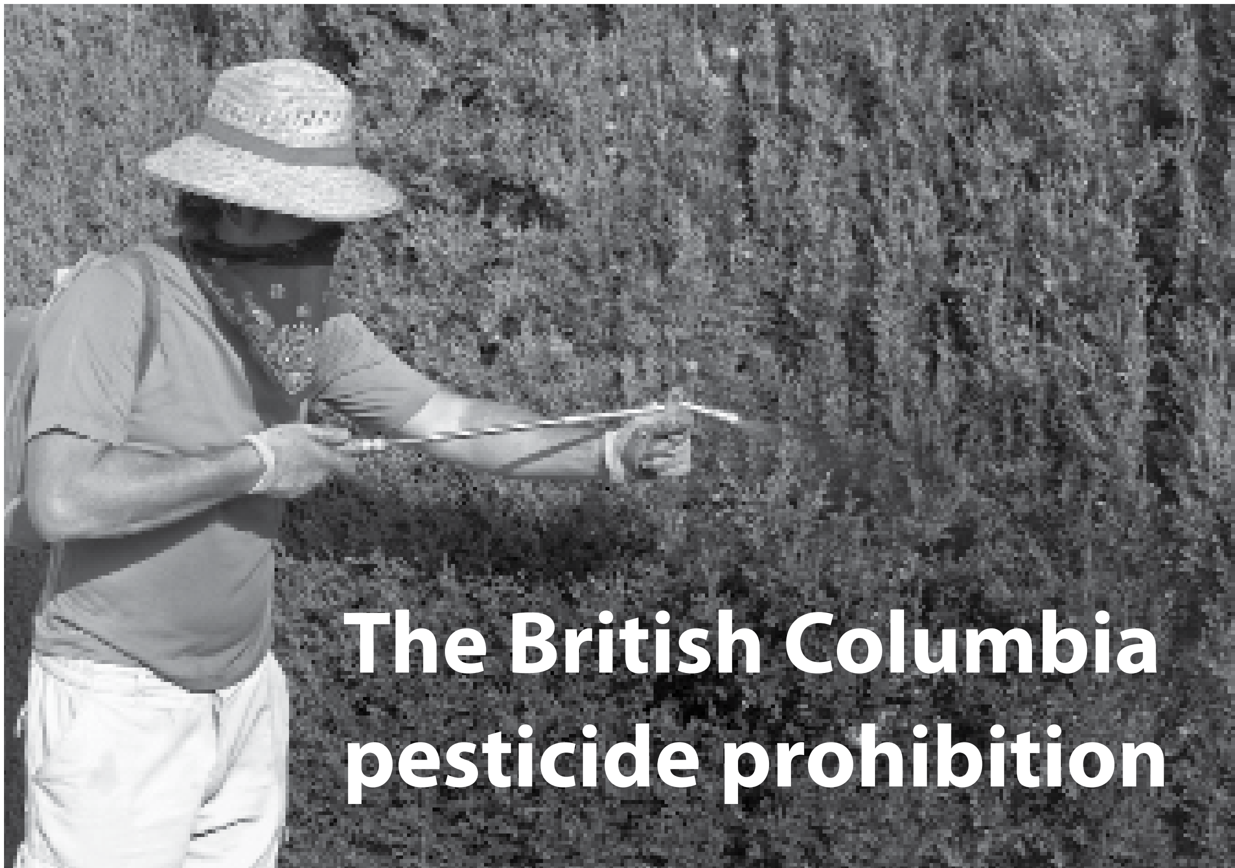

# The British Columbia pesticide prohibition

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**Nachum Gabler and Joel Wood**

The zeal of Canadian politicians in promoting public wellbeing is leading to the regulation of what had hitherto been the quintessential private domain of Canadian green thumbs—green domestic lawns, colourful flower beds, and ripening vegetable gardens. The British Columbia government is currently considering banning the sale and use of synthetic pesticides for cosmetic uses (Shore, 2011).

Similar policies have been adopted in other provinces: Quebec in 2002, Ontario in 2008, Nova Scotia in 2010, and Prince Edward Island in 2010 (MDDEP, 2002; MEO, 2011; NSE, 2010; DEEF, 2010). For example, Ontario has restricted the sale and use of over 250 pesticide products and 80 pesticide ingredients (Government of Ontario, 2009). New Brunswick has taken a less extreme approach and does not have a specific ban on the cosmetic use of synthetic pesticides, but instead has enacted a myriad of laws and regulations that make cosmetic pesticide use burdensome (Government of New Brunswick, 2011). These provincial prohibitions on cosmetic use of synthetic pesticides may apply to lawns, vegetable and ornamental gardens, driveways, cemeteries, public parks, and school grounds. Similarly, controls and bans on cosmetic pesticide use have been implemented municipally in dozens of cities across Canada as well.[1]

The justification for a ban on the cosmetic use of synthetic pesticides is mainly based on a possible link that between synthetic pesticide exposure and the risk of developing cancer. The Canadian Cancer Society alleges that a connection may exist between synthetic pesticides and cancer, and according to the "precautionary principle" any activity that might potentially constitute a "threat of harm" on humans or the ecosystem should be curtailed and abated, irrespective of whether or not a "cause-and-effect" relationship has been definitively established scientifically (Canadian Cancer Society, 2010).

# Banning pesticides imposes costs on Canadians

In fact, many of the synthetic pesticides that would be banned have not yet been proven to be carcinogenic. For example, the World Health Organization only lists the common pesticide 2,4-D in the same cancer risk category as pickled vegetables and cell phones (IARC, 2011).[2] And just recently, the United States Environmental Protection Agency conducted a review of the scientific literature and concluded that there was no evidence of a link between 2,4-D and cancer (EPA, 2007).

From an economics standpoint, banning the use of synthetic pesticides for cosmetic purposes imposes costs on individual Canadians and the wider Canadian public. The existence of a market for pesticides that can be used for aesthetics suggests that Canadians derive value from having these landscape-enhancing products available for purchase. Prohibiting the cosmetic use of synthetic pesticides ignores the benefits enjoyed by Canadians in maintaining aesthetically pleasing green landscapes. The proposed blanket prohibition on cosmetic pesticide use in BC is devoid of the careful contrasting of costs and benefits that should be undertaken before any regulations are adopted. A better approach to evaluating the merits of any and all regulations controlling cosmetic pesticide use would involve a proper cost-benefit analysis and would weigh the trade-offs implied by the regulation(s) in question.

If external health, environmental, or economic damages are present[3] and are imposed on parties not currently participating in the cosmetic use of synthetic pesticides, a more efficient alternative to a blanket prohibition would involve the adoption of an environmental tax to sufficiently reduce, but not ban, the cosmetic use of synthetic pesticides. The purpose of the tax is to negate external damages by placing the entire cost of pesticide use onto the individuals using them. By taxing the sale of a pesticide by an amount equal to the expected external damages resulting from the use of that pesticide, the pesticide user is forced to account for the effects of the pesticide on his/her neighbours and will likely reduce usage.

However, research suggests that the external damages from pesticide use may be exaggerated. The Environmental Impact Quotient[4] (EIQ) for many synthetic pesticides is actually lower than the EIQ for many mundane household items and other "natural" alternatives to synthetic pesticides. For example, Table 1 shows that the

**Environmental impact quotient values (EIQ)**

| Synthetic pesticides | EIQ |
|---|---|
| 2,4-D (Killex) | 16.67 |
| Glyphosate (Round up) | 15.33 |
| **Natural pesticides** | |
| Soap | 19.45 |
| Sulphur | 32.66 |
| Pyrethrin | 37.12 |

Sources: Kovach et al., 1992; Kovach et al., 2010.

EIQ for both soap and sulphur are higher than the EIQ for the common pesticide ingredient 2,4-D.

Either a blanket ban or an environmental tax will encourage individuals to substitute natural alternatives that can be potentially more harmful. Consider the recent case of a Victoria couple who set their own home ablaze while trying to eradicate their weed problem with a specialized blow torch, which they did because artificial pesticide use is banned in Victoria (Clarke, 2011). Though this case is anecdotal, it lends credibility to the assertion that using public policy to subvert market forces and regulate the availability of certain commodities that might potentially pose some kind of a risk is likely to give birth to other risks. These other risks arise from the sometimes clever, sometimes careless, ways that Canadians adapt to altered incentives resulting from regulation.

## Notes

1 At the federal level, Health Canada is the main agency responsible for devising and enforcing regulations and guidelines that govern pesticide availability, distribution, and use in Canada. Those synthetic pesticides being banned for cosmetic use at the municipal and provincial levels are deemed safe to use by Health Canada.

2 2,4-D is included in the classification of Chlorophenoxy Herbicides in IARC (2011).

3 External damages are incurred by individuals from the use of pesticides by other individuals (e.g., effects on neighbours from your own pesticide use).

4 Developed by scientists at Cornell University, the Environmental Impact Quotient measures the relative impact on humans and the environment of commonly used synthetic and natural pesticides. For more information see Kovach et al. (1992) and Kovach et al. (2010).

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