● (2002)

AFTER RECESS

The House resumed at 8 p.m.

GOVERNMENT ORDERS

[*Translation*]

THE BUDGET

FINANCIAL STATEMENT OF THE MINISTER OF FINANCE

Hon. Jean Chrétien (Minister of Finance) moved:

That this House approves the budgetary policy of the government.

He said: Mr. Speaker, the purpose of my budget tonight is to take positive and responsible action to deal with the problems which face the Canadian economy in a very troubled world. These problems are complex and difficult. We are being held back by serious unemployment and inflation, and we must do all we can to deal with them. But we also face longer-term problems and opportunities calling for structural adjustment in many industries, sectors and policies. These were the challenges brought out very clearly by the recent Conference of First Ministers.

In the past days and weeks I have sought the advice of many individual Canadians. I have spoken to all provincial finance ministers. I have benefitted from vigorous public discussion of our economy. My cabinet colleagues and I have considered briefs from groups large and small, national and regional.

Many of the suggestions made to me for this budget would be popular politically but unwise economically. I will not follow such suggestions. I believe this is time for Canada to face our problems critically and realistically. If we do, we can turn the tide against inflation and unemployment. The measures of this budget should secure and reinforce the progress we have already made.

It is now clear that many of our current difficulties have their roots in the period of extraordinary growth Canada experienced between the mid-1960s and the mid-1970s. With the great advantage of hindsight, we can see that we did not always use our good fortune wisely.

Our economy boomed. The world environment was good to us. Canadians enjoyed a very large increase in their standard of living.

But we all came to expect too much of the economy. Governments increased their spending too quickly. The money supply was increased too fast.

Too much was asked and given at the wage bargaining table. Other forms of income also rose too rapidly. Too little attention was paid to the long-run efficiency of the Canadian economy, and its ability to compete.

And so Canadians were not well prepared to deal with the shocks of the early 1970s. Sharp increases in the price of oil, food and other major world commodities speeded up our inflationary spiral.

World recession arrived and compounded our loss of competitiveness. A large deficit opened up in our balance of payments. Our growth slowed down. The loss of sales meant the loss of jobs.

At the same time, we experienced more conflict and confrontation in Canada. Conflict between the provinces and Ottawa. Conflict between separatist and federalist forces. Conflict between employers and employees. All of these things breed uncertainty and weaken the economy.

[*English*]

The Signs of Progress

By the fall of 1975 it was clear that strong economic action had to be taken. The anti-inflation program launched at that time has made a major contribution in turning our situation around.

The expenditures of all levels of government in Canada have since been brought under better control. In our own case we have cut back the growth in our total outlays from 26 per cent in 1974-75 to 18 per cent in 1975-76 to 10 per cent or less since then.

The Bank of Canada has brought down the rate of increase of the money supply in line with its announced targets for continued growth and declining inflation.

Wage increases have returned to more realistic levels. New settlements came down from 17 per cent in 1975 to 10 per cent in 1976 and under 8 per cent in 1977. They are now down to the guideline of 6 per cent.

The underlying rate of inflation has also been reduced. We can see this in the trend of non-food prices which has been improving steadily. Another indication is the fact that the average price of all the goods and services which Canada produces rose only by 6.5 per cent last year, compared with 9.5 per cent in 1976 and 11.2 per cent in 1975.

● (2012)

The controls program has played a key role in these developments. Controls over prices and incomes cannot succeed unless they are supported by the right setting of fiscal and monetary policy. But the underlying rate of inflation would not have been brought down so quickly without the controls. Without their help, we would have had less growth and more unemployment.

Given the erosion that our competitive position suffered over several years, it was inevitable that an adjustment of the exchange rate would be required sooner or later. That adjustment has taken place in several stages. The government has permitted it to occur by allowing the exchange value of the

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Canadian dollar to move in response to changes in the balance of supply and demand in the foreign exchange market. That continues to be our policy.

It also continues to be our policy to intervene directly in the market to moderate short-term fluctuations in the rate of exchange. This intervention dampens the more erratic short-term movements. It also provides resistance to appreciable movements of the rate in either direction. The intervention does not prevent the exchange rate from moving in response to the market situation. It moderates the speed of change.

Such intervention gives rise to changes in Canada's official reserves. In the event of a sustained declining trend in the exchange rate, such as we have been experiencing, the drain on the official reserves can be considerable. In such circumstances it is prudent for the government to replenish the foreign exchange component of reserves by borrowing foreign currency. As hon. members know, we have been following just such a policy.

Changes in the official reserves arising from exchange market interventions reflect the over-all balance in Canada's international payments. When, as at present, we have a deficit in the current account of our balance of international payments, changes in official reserves can be regarded as adjusting the net inflows of capital that finance the current account deficit.

In recent months the net inflow of capital to Canada, particularly that arising from the usual foreign borrowing of Canadian provinces, municipalities and corporations, has been low in relation to the size of the deficit on current transactions in goods and services. For seasonal reasons, this deficit is normally much larger in the first several months of the year than in the other months. In these circumstances the Government of Canada has used exchange reserves to supplement the inflow of capital. The Bank of Canada has raised the bank rate on two recent occasions to encourage Canadian borrowers to raise funds abroad. In summary, it is our policy to undertake such foreign borrowings as are required to replenish our reserves and to provide assurance that the government is in a position to supplement the net inflow of capital to Canada.

With our costs now under better control and a lower exchange rate, we have become more competitive internationally. This has helped us to turn around our trade balance from a deficit of $500 million in 1975 to a surplus of almost $3 billion in 1977.

In other ways, our progress has been no less important, but perhaps harder to measure. Expectations have changed. Hopefully they are more realistic. Some of the divisions in our society have been narrowed or closed.

We have also seen a remarkable improvement in relations between labour and management. In 1976 we lost 11.6 million man-days in strikes. Last year that number fell 70 per cent to only 3.4 million man-days. More important, labour and business are talking to each other about their common problems.

There is also a more effective dialogue among governments and between governments and business, labour and other groups in our society. It is not a matter of choice whether we pursue this dialogue. We must achieve more agreement on economic issues and find more ways to co-operate, or we cannot get the best out of our economy.

[Mr. Chrétien.]

[*Translation*]

The Challenge of Structural Reform

The federal government discussed co-operation and structural change in the paper entitled *Agenda for Co-operation*. The first minister's conference was a milestone in federal-provincial relations both in terms of the range of policy agreement and the commitment to structural reform. A comprehensive work program is now underway as a result of the meeting. For example, studies are proceeding with the private sector in 22 manufacturing industry categories. A major effort is underway to cut down the burden of government regulation. Measures have been taken to help arrest and reverse the tourist deficit. Food and agricultural policies are under review. We are looking forward to developing the potential created for our fisheries by the 200-mile limit.

For my part, I can encourage useful structural adjustment as minister responsible for tariffs and tax policy.

Commercial Policy and the Tariff

The multilateral trade negotiations now taking place in Geneva have longer-range potential for the productive sectors of our economy. We are participating actively in the talks, and seeking reductions in both tariff and non-tariff barriers to give us better access for our exports, especially highly processed resources and manufactured goods. We will also be prepared to reduce Canadian tariffs, but only in return for concessions of real value. Canada's development in the 1980s will depend very largely on the ability of our industries to grasp significant new export opportunities and compete more effectively against imports at home. As First Ministers have urged, we will be ready to support the private sector adjustments that will be needed for our success in the trading environment of the decade ahead.

The Geneva talks are moving ahead quickly and we hope for a successful conclusion in the coming months. In the meantime I am not submitting any major amendments to the Customs Tariff. However, I am proposing tonight that most of the temporary tariff reductions introduced in 1973 on a broad range of consumer products be extended for another year beyond their scheduled expiry date of June 30. The extension will contribute, as it has in the past, to our efforts to minimize inflation.

I am also proposing to withdraw the British Preferential rate from certain goods imported from Britain and Ireland, including certain diesel engines, radio and television apparatus, truck-mounted cranes, knitted goods and confectionery products.

To assist Canadian producers, increases in the MFN rates are being proposed for certain chemicals and industrial tires and tubes.

I have received a number of inquiries about implementation of the Tariff Boards's proposals for changes in the tariffs on fruits and vegetables. We have notified our trading partners that we intend to renegotiate certain GATT commitments which currently prevent us from increasing existing rates of duty on products covered by the Board's report. The government will try to conclude these negotiations as soon as possible and then introduce legislation to provide for a new schedule of rates for fresh and processed fruits and vegetables.

[*English*]

The Tax Structure

Our tax system is another instrument which can support innovation and change. I want to proceed immediately with major structural changes in three areas of industrial policy highlighted by First Ministers. They are research and development, transportation and energy.

Research and Development

We must continue to encourage Canada's research and development efforts. An adequate level of R&D is crucial to achieve gains in productivity and to strengthen Canada's position in an increasingly competitive world. At present, corporations are allowed to write off immediately 100 per cent of all R&D capital and operating expenditures. Last year these outlays also became eligible for the federal investment tax credit of from 5 to 10 per cent. In many cases they also qualify for direct assistance under significant federal grant programs.

● (2022)

I now propose that for 10 years starting tonight, taxpayers be allowed to deduct from their income a further 50 per cent of additional R&D expenditures. The deduction will apply to both current and capital expenditures to the extent that they exceed the average amount over the preceding three years. This means that there will now be a special incentive for companies to *expand* their R&D. I want to emphasize that this special allowance comes on top of the incentives already in place.

The new allowance will make Canada's tax treatment of research and development one of the most generous in the world. The after-tax cost to companies of one dollar's worth of additional expenditure will be reduced to as little as 20 cents. I hope this incentive will lead to significant improvements in R&D performance by the private sector. And I look to companies to ensure that the resulting new technology is used within Canada to create new jobs.

Railway Investments

Discussions at the First Ministers' conference underlined the importance of transportation for industrial and regional development in Canada. Railways continue to be a crucially important mode of transportation, particulary for long hauls and heavy commodities. Recently, the government has announced significant changes in the organization of the CNR to improve the efficiency of its operations. Measures were introduced in the last budget to encourage track and grading investments by railways. Looking to the medium term, major new investments are needed in this sector if efficiency and productivity gains are to be captured.

I am therefore proposing a significant increase in the capital cost allowance for railway investments. This will take the form of an additional depreciation allowance of 6 per cent per year for five years for most capital expenditures of a railway. It will apply to investments undertaken after tonight and before 1983. The measure will help improve the railway system in all regions of Canada and will be of benefit to suppliers of railway equipment.

Energy Development Incentives

We must also continue to place high priority on our national energy policy, and in particular the need to extend self-reliance for oil and gas. We are fortunate in our existing and potential resources, and many tax incentives and other measures have been put in place to encourage their development. But increasing attention is now focussed upon the heavy oil reserves and oil sands deposits of the western provinces which can be tapped only by advanced technology and multi-billion dollar investments. These are projects requiring long lead times for planning, organization, design and construction. It is important to get them moving now, and I have concluded that some modification and clarification of their tax treatment can be helpful in that regard.

First, I want to make clear that the up-grading plants to process the heavy oil produced from wells into a type of oil similar to conventional crude will be treated as a manufacturing facility, eligible for fast write-offs and the reduced tax rate.

Second, it will be important to extract as much oil as technologically possible from all deposits. It has already been established that enhanced recovery systems can greatly increase total production. After today, therefore, special machinery, equipment and other facilities acquired for enhanced recovery systems—specifically, so-called "tertiary" recovery—will be able to earn depletion at a rate of $1 for every $2 of expenditure as compared to the normal earning rate of $1 for $3.

Finally, earned depletion may be applied at present only to reduce taxable resource profits, and only up to a ceiling of 25 per cent. This provision will be significantly improved. Effective immediately, corporations may deduct depletion earned through certain qualifying investment in non-conventional oil projects up to the extent of 50 per cent of total income—both resource and other profits. The qualifying investment will include expenditures on tertiary recovery equipment and certain depreciable property acquired for use in a bituminous sands mining project.

I am confident that these measures, added to the ones already in place, will in future years help reduce our dependence on imported oil, especially in eastern Canada.

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I would like also to say a word about the mining industry. The First Minister's conference directed Finance and Resource Ministers to undertake an early review of the taxation of the mineral industry. The government is proceeding with its review and looks forward to further consultation with the provinces in the near future.

Retirement Income

Almost two million Canadians have Registered Retirement Savings Plans, enabling them to set aside funds to provide income after retirement. The wide range of choice allowed in setting up these plans and the generous tax treatment for contributions have made them very popular.

I have some concern, however, over the limited choice available to RRSP holders when the time comes to turn their savings into retirement income. A taxpayer is now required to invest his RRSP proceeds in a life annuity with an insurance company prior to his 71st birthday. The only alternative he has is to withdraw the funds in a lump sum and pay income tax on this amount in the same year.

I propose to introduce two additional alternatives that will increase flexibility while retaining the basic principle that RRSP funds are intended to be used for retirement income.

The first alternative will allow the purchase of a fixed-term annuity to provide benefits to age 90.

The second alternative will allow the taxpayer to have his RRSP savings placed in a new kind of investment vehicle to be known as a Registered Retirement Income Fund. Each year a set fraction of the total assets in the Fund—capital plus accumulated investment earnings—will be withdrawn and taken into income. This fraction will be determined by a formula designed to provide benefits to age 90. Payments would grow over time at a rate reflecting the investment performance of the Fund and thus provide a degree of protection against future inflation. There will be provisions enabling a taxpayer to manage his investments in much the same way as he can now with a self-administered RRSP.

Institutions with the right to issue RRSPs will be permitted to sell fixed term annuities or retirement income funds. At present this includes mainly life insurance and trust companies.

● (2032)

The transfer of an RRSP into any of the retirement income options must occur between age 60 and age 71.

I am confident that the added alternatives will provide the range of choice that taxpayers desire in planning for retirement. They respond to concerns expressed to me by many Canadians.

Family Law Reform

A number of provinces have introduced fundamental changes in the laws relating to the division of certain properties between marriage partners. These changes in law raise a number of important issues which are far from being resolved. Because they affect several provisions of the Income Tax Act, I am monitoring the developments in this area very closely. In the meantime, I am proposing a change in the provisions so that transfers of property between spouses pursuant to provincial family laws will not give rise to taxable capital gains.

The Ways and Means Motion contains several other important changes. First, the current provisions which permit the transfer of farm land and buildings by a farmer to his children without payment of capital gains tax will be extended to incorporated family farms. Second, single employees will now receive the same tax exemption as married employees on the value of free board and lodging provided at logging camps and other remote work locations. Third, I am proposing certain tax changes to further promote the production of good Canadian films.

Problems of the Past Year

The structural changes in the economy which these measures will encourage will help us achieve the growth we need over the next four or five years. I have also had to consider what measures would be helpful in dealing with the immediate problems which confront us.

[*Translation*]

Although the prices of the things we produce continued to slow down last year, the prices of the things we consume have risen more sharply. There were two major factors—higher prices of imported foods and the decline in the exchange rate. I do not believe the price surge will last. I believe the direct impact of our dollar's decline is now largely behind us. Further, an improving supply situation should help to slow the rise in food prices.

The growth of output was disappointing last year. The rate dropped from about 5 per cent in 1976 to 2.6 per cent in 1977, according to the preliminary estimate. The most unfortunate consequence was the rise in unemployment. Unemployment has reached unacceptable levels despite a substantial increase in the number of Canadians who are working. Employment has increased more than 3 per cent in the past year. Almost 300,000 more Canadians are working today than one year ago. But our labour force has also been growing rapidly, much more rapidly than in other countries. Since 1970, our labour force has increased by about 3½ per cent a year, compared with 2 per cent in the United States and well under 1 per cent in the United Kingdom, France and Japan. In Germany, the labour force has actually dropped over this period.

An important reason for the growth of our labour force has been the growing number of Canadian women who are working. Since 1970 the number of adult women in the labour force has increased from 1.9 million to 2.7 million, a rise of more than 40 per cent. There has also been a surge of young people coming into the labour market. This surge will not last; in many schools, there are now empty desks. But the immediate challenge is to create enough jobs for all our young people. Youth unemployment is one of our most serious problems. It cannot be dealt with only by general economic policies. Our

[Mr. Chrétien.]