1982

Ontario Budget

The Honourable
Frank S. Miller,
Treasurer
of Ontario

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Presented by the Honourable Frank S. Miller,
Treasurer of Ontario
in the Legislative Assembly of Ontario
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Table of Contents

Budget Statement

Towards Economic Recovery 3

Immediate Measures to Create Jobs 5

Assisting New Home Buyers and Reducing Pressures on Rental Markets 8

Revenue Requirements 9

Options for Change in Ontario's Tax Structure 13

Restoring a Climate of Confidence 14

A Major Incentive for Small Business 16

Public Sector Restraint 17

The 1982-83 Fiscal Plan 20

Conclusion 21

Appendix A: Details of Tax Changes 25

Appendix B: The Ontario Health Insurance Plan 32

Appendix C: The Ontario Renter-Buy Program 33

Budget Papers

Policies for Economic Recovery . . . . . A

Fiscal Federalism in Canada: The Record to Date The Challenge Ahead . . . . . B

Public Investment and Responsible Financial Management C

1982 Budget at a Glance

	1981-82	1982-83	Growth Rates
	($ million)		(%)
Gross Provincial Product	123,716	135,500	+ 9.5
Spending	20,415	22,777	+ 11.6
Revenue	18,855	20,545	+ 9.0
Cash Requirements	1,560	2,232	

1982 Budget Statement

Mr. Speaker:

I rise to present the 1982 Budget of the Province of Ontario. This is the fourth Budget which I have had the honour to present and I daresay that it has been the most difficult one to write.

We live in troubled economic times. For nine years now, the industrial economies of the world have tried to cope with massive problems of energy shocks, slow growth and inflation. No country has been able to fully master the challenge. Each time that we seem to be regaining a pattern of reasonable growth we are swamped by yet another wave of inflation. Last year the monetary authorities of the United States launched a hell-bent-for-leather attack on inflation by driving interest rates to unprecedented levels. The U.S. Administration was determined to bring inflation to a halt even if it meant stopping the American economy dead in its tracks and that is what happened.

The Bank of Canada followed suit. But in our country, we had to bear not only the cross of crushing interest rates but also the thorns of the November federal budget. Canadians now stand amid the fallout from these draconian policies. Investors have lost confidence. Business people, farmers and homeowners suffer under high interest charges. Worst of all, people have been laid off, others are taking pay cuts and some live in daily fear of losing their jobs.

It is understandable that many of our citizens are frustrated and concerned. They do not comprehend why a nation such as ours, with its enviable bounty of human and natural resources, can find itself in such circumstances. Quite frankly, I don't blame them.

Mr. Speaker, in no way do I belittle the challenge that faces this great province of Ontario. But I am confident we can meet it. I am confident, not just because I am a natural optimist, but because our track record is strong. In the past decade, Ontario businesses and workers have clearly demonstrated their ability to rebound from setbacks thrust upon us by international economic conditions. I am confident because we have come through the past ten years with one of the best job-creation performances recorded anywhere in the western industrial world. I am confident because this fine province continues to be led by the Government of the Honourable William G. Davis.

With this Budget I cannot solve all the problems that confront us. Nor can I heal all the economic wounds that many of us bear as a result of the international and national economic situation. No one would suggest that any provincial government could do all that. Moreover, when our revenues are reduced because of slow economic growth and substantial federal cutbacks, I cannot conjure up a way of paying for a decent standard of public services that does not involve some increases in tax levels or the deficit.

Mr. Speaker, when I wrote this Budget, I did not bemoan what could not be done. I sought out the positive things that we can do to create jobs and new investment, that we can do to reinforce confidence in our future and that we can do to maintain an affordable standard of services for our people. I believe that the proposals outlined in the Budget which I am placing before the Members tonight will help accomplish these positive objectives.

Towards Economic Recovery

As I have said, Mr. Speaker, these are difficult economic times, and not just in Canada. We can sometimes be so preoccupied with our own problems that we fail to notice those of our neighbours. Yet their problems are vitally important to us because they have a profound impact on our own circumstances and on our abilities to pursue a strong economic recovery.

The world economy is struggling in the grip of a serious recession. The number of people out of work in the member nations of the Organisation for Economic Co-operation and Development rose sharply to 25.8 million in the latter part of 1981. The United States, the world's largest and most vital economy and our major trading partner, has been in deep recession for at least six months. The average unemployment rate for the whole of the United States is currently at a post-war record of nine per cent. The unemployment rate in the neighbouring state of Michigan, an auto-based economy, is over 16 per cent. When such conditions prevail in our export markets, it is difficult for Canada's export-oriented economy to perform well.

The chief reason for this international recession is, of course, abnormally high real interest rates. In Canada, they are more than three times the average of the past 15-year period. While all sectors are adversely affected, the initial victims are industries such as autos, machinery, furniture, appliances, steel, metals, agriculture, housing construction and small business. These industries and their many suppliers are major employers. When their sales fall off, inventories accumulate and they are forced to slash production and lay off workers. This reverberates throughout the whole economy.

Real relief for the international economy awaits the reduction of interest rates to more realistic levels. In this regard, a crucial debate is under way in the United States over the fiscal and monetary policies of President Reagan's Administration. Some reduction in the projected massive federal budgetary deficit must occur before interest rates in the United States will fall to levels more conducive to economic growth. When they do, this will provide for a world-wide economic expansion, just as high rates triggered a precipitous decline. The underlying strength of pent-up demand supported by a high level of savings gives the North American economy a strong recovery potential.

The recent federal budget was formulated in the context of the very strong job-creation performance of the first half of 1981. However, when the federal Minister of Finance brought down his budget in November of 1981, the Canadian economy was already in recession.

Therefore, it did not address the economic conditions of the day. In my response to that budget, I warned my federal counterpart of the weakened state of the economy. High interest rates and sharp increases in domestic oil prices had already undercut the strong expansion of the first half of 1981.

In recognition of the state of the Canadian economy and the need to re-establish a climate of confidence, Premier Davis presented forty-five specific recommendations to the February, 1982 First Ministers' Conference on the Economy. The priorities outlined by Ontario were:

- immediate actions for job creation;
- encouraging small business creation and development;
- increasing investment;
- developing human resources;
- enhancing trade and export opportunities; and,
- restoring a climate of confidence.

Mr. Speaker, we continue to feel that our proposals, which have received widespread support from the private sector, should guide economic policy in Canada. They have played an important role in shaping this Budget.

Economic Outlook

Let me turn to my forecast for the Ontario economy.

While the last few months have been very difficult, there is now a strong potential for the economy to follow a recovery path throughout the rest of the year. Businesses have been meeting demand in large part by running down inventories, a process that I expect will end soon. This means that sales will be increasingly filled from current production, leading to the recall of workers. Also, the combined effect of tax cuts, increases in social security payments, and higher defence spending in the United States should restore some momentum to that economy. This will aid the recovery of Canadian exports.

Later in this Statement, I will outline a major job-creation program, a new initiative for housing construction and an important incentive for small business that will also add significant stimulus to the Ontario economy.

Because of these factors and actions, the Ontario economy should strengthen during the balance of the year. Employment by year end should reach 125,000 over current levels. Real growth in GPP in the second half of 1982 should be four per cent on an annual basis.

Inflation is forecast at 10.7 per cent. While this is an improvement from last year's rate of 12.5 per cent, I am still deeply concerned. The inflation that we are experiencing is becoming embedded in the cost structure of our economy. This bodes ill for our long-term international competitiveness, especially as inflation in the U.S. continues to moderate.

Mr. Speaker, the Ontario economy faces great challenges, both in the long term and in the short term. In the long term, we must adapt to growing international competition and technological complexity. I will be proposing measures to address these issues. However, given the current state of the economy, we have a responsibility to supplement our long-term efforts by taking immediate action to create jobs.

Immediate Measures to Create Jobs

Accordingly, we are moving ahead with a comprehensive short-term employment-creation program which I shall now outline for the Members. This four-point program has been developed to achieve the maximum impact per dollar of expenditure. It is targeted on those sectors of the economy where there is the highest potential for both direct and indirect job creation in our province. In addition, the short-term employment initiatives will:

- focus on regions, industries and groups most affected by unemployment;
- provide useful jobs, not make-work projects; and,
- be implemented quickly.

To ensure these criteria are met, the Board of Industrial Leadership and Development will be co-ordinating the administration of our employment-stimulation program.

Co-operative Projects Employment Fund

For some time now, the Province has been calling for the innovative use of unemployment insurance funds. A breakthrough was achieved earlier this year with the establishment of the Accelerated Forest Improvement Program in co-operation with the federal government. Under this arrangement, laid-off forestry workers are paid $240 per week from Unemployment Insurance benefits plus a $60 per week Provincial supplement to work on forest management projects. We want to see more of this kind of resourceful approach.

Therefore, we are establishing a new $15 million Co-operative Projects Employment Fund to finance participation with the federal government in further projects. To start off, the Ontario share of the recently announced Mining Special Employment Program will be financed out of this Fund. We are developing more temporary programs of this nature. Assuming we continue to receive the same level of co-operation from Ottawa, my colleagues will be announcing more new programs in the next few weeks. I have set a target of 6,000 jobs to be created by this Fund.

Accelerating Capital Projects

Accelerating public investment projects can make an immediate contribution to employment. Therefore, the second component of our employment-creation program will involve a speed-up of capital projects in all parts of the province, with emphasis on those areas where unemployment is highest. To accomplish this, I am providing an additional $133 million to:

- accelerate repairs and additions to public buildings and other capital projects, including construction and maintenance of highways, roads, municipal bridges, and water and sewage treatment projects;
- pay for renovation and repair projects sponsored by municipalities, school boards, universities and colleges; and,
- provide for upgrading of forest and fishery resources.

We estimate that this program will directly create 14,500 temporary jobs. Additional details concerning these initiatives will be announced by my colleagues in the next few days.

Youth

To recognize the fact that unemployment amongst young people has risen sharply in this recession, our youth-employment programs, which are already substantial, will be expanded further. The allocation for youth-employment programs in 1982-83 will be increased to $91 million, a 14.2 per cent increase over last year. In total, Mr. Speaker, some 93,000 young people will get jobs under these programs.

Youth Employment Programs, 1982-83

	Funding	Jobs
	($ million)	
Ontario Youth Employment Program	30.4	57,000
Ontario Career Action Program	16.8	15,300
Experience '82	12.0	8,800
Junior Rangers	4.7	1,800
Summer Replacement and Co-op Students	22.0	7,500
New Winter Program	3.8	2,000
Other Special Programs	1.0	300
Total	90.7	92,700

Agriculture

This Government has demonstrated its commitment to our agricultural sector. We have responded quickly to assist farmers who were in difficulty because of the current econ)mic environment. For example, under the 1981-82 Emergency Beef Payment Programs some $57 million has been paid to 30,000 Ontario beef producers.

Rather than wait until this Budget, we took action last December with a new program to provide direct assistance to farmers experiencing extreme difficulty in coping with high interest rates. The Farm Adjustment Assistance Program has already provided assistance to hundreds of farmers. In total, I anticipate that, including funds already expended in the previous fiscal year, some $60 million worth of assistance will be taken up by as many as 5,000 farmers.

Tonight, I am proposing $11 million in additional measures to create jobs in our farming communities this summer.

First, I am increasing funds available for tile drainage by over 26 per cent. Second, there will be a new $5 million Farmstead Improvement Program, which will provide grants to farmers to improve their farms. These measures will create 2,100 additional rural jobs this year.

My colleague, the Honourable Dennis Timbrell, Minister of Agriculture and Food, will be announcing details of these measures in the near future. He is also finalizing details of our new program for young farmers which was announced in the Throne Speech.

Ontario's 1982 Short-Term Job-Creation Programs

	Funding Level		Number of Temporary Jobs	
	($ million)			
Co-operative Projects Employment Fund		15.0		6,000
Accelerating Capital Projects		133.0		14,500
• Road Projects	60.5		2,475	
• Repairs to University and College Buildings	10.0		2,000	
• Water and Sewerage Projects	5.6		600	
• Renovations and Repairs to Public Buildings	9.9		575	
• Repairs to Schools	5.0		1,000	
• Local Government Projects	35.0		7,500	
• Upgrading of Forest and Fisheries Resources	7.0		350	
Youth Programs Enrichment		12.0		8,400
Farm Improvement		11.0		2,100
Total		171.0		31,000

Mr. Speaker, this Government cares about creating jobs and is doing something about it. The four-point program I have just outlined will create 31,000 temporary jobs at a cost of $171 million in this fiscal year. It will provide a needed bridge over troubled economic waters, particularly for many of our young people.

Let me now turn to another new initiative which will create jobs and help our young families.

Assisting New Home Buyers and Reducing Pressures on Rental Markets

High interest rates have led to high unemployment in the residential construction sector. We must maintain a solid base in this industry to ensure capacity is available to meet future housing demand.

When people buy new homes, they not only create jobs in the construction, household furnishings and appliance sectors but also free up rental accommodation.

Tonight, I am proposing a new program whereby Ontario residents, who have been renting for the previous twelve months or who have never owned a home, will be eligible for an interest-free loan of up to $5,000 upon the acquisition of a new house. This program, called the Ontario Renter-Buy Program, applies to closings after today and will remain in effect for committed purchases made by October 30, 1982. Assistance will be limited to new homes costing up to $115,000 in and around Metro Toronto and $90,000 in the rest of the province.

Mr. Speaker, I estimate that this program will provide $75 million for the purchase of 15,000 new homes which represent 38,000 man-years of employment. The rental units freed up by this program will help reduce the pressures in the rental market.

The Ontario Renter-Buy Program will be administered by the Ontario Mortgage Corporation under the direction of my colleague, the Honourable Claude Bennett, Minister of Municipal Affairs and Housing. He will be providing full details tomorrow.

Additional actions to increase the supply of rental housing are under consideration. The Minister of Municipal Affairs and Housing has been meeting with his federal counterpart to ensure that effective and viable measures for Ontario will be forthcoming.

I would like to deal briefly with the question of mortgage interest for existing homeowners. The federal government has introduced a program to help people who have extreme difficulty renewing their mortgages. Since this program was introduced early last month, hundreds of Ontario families have received assistance. Little would be gained by a Provincial initiative that would only duplicate a program that seems to be working. Nevertheless, the Government is concerned about this situation and we are closely monitoring the progress of the federal program and the state of mortgage markets.

Mr. Speaker, I have proposed important new programs to create employment and to assist new home buyers. I have also reviewed our substantial assistance programs for farmers. Later in the Statement, I will outline an important new measure to assist small business. Now I wish to turn to revenue requirements for the current fiscal year.

Revenue Requirements

In my Budget last year, I documented the relatively slow growth in Ontario's revenue base. Inflation has a much more direct and immediate impact on our expenditures than it does on our revenues. When the deficit is under pressure, many will urge spending cuts before raising taxes. I totally agree with that approach and that is what we have been doing. In fact, I would remind the Members that, in delivering a high level of services, Ontario spends less per capita than any other province in Canada. But we cannot always find all the required savings on the expenditure side of the ledger without cutting too deeply into needed social and economic programs.

Impact of Federal Retrenchment

The Members will be aware of the stance this Province has taken with respect to unilateral federal cuts in our transfer payments. May I draw to your attention that Budget Paper B provides a complete perspective on the record and challenge of fiscal federalism in Canada.

Clearly, the federal action to withdraw some $5.8 billion in support for health and post-secondary education over the next five years will make it harder to maintain national standards and inevitably will make it more difficult to ensure balanced economic growth across the country. Our share of this cut will cost almost $300 million in 1982-83 and some $1.9 billion over the next five years.

At the January federal-provincial meeting of Finance Ministers, I illustrated that the cutback in transfers to this Province was as large as the combined operating budgets of Ottawa, Carleton, Queen's and Western Ontario universities, with an overall enrolment of 59,000 students. In health, all ten hospitals in the Ottawa area, with some 3,400 beds, incur operating costs which account for two-thirds of the federal cut in transfers.

Mr. Speaker, it goes without saying that this Government has no intention of making up these serious fiscal losses by large-scale closures of our hospitals and universities. But the federal cutback will coincide with lower growth in the Province's overall revenue structure. So, if we are to protect our level of essential services and still maintain a stance of fiscal responsibility, we have no choice but to raise additional tax revenues.

Responding to Federal Cutbacks

In searching for a way to offset these federal cutbacks, I had to look at my chief sources of revenue, the personal income tax, the retail sales tax and the corporate income tax.

The need for Ontario to remain internationally competitive, as well as to repair the damaged climate of confidence in this country, precludes any increases in the corporate income tax. Also, the federal budget's changes to personal income tax investment incentives has left taxpayers confused and dismayed. I cannot add to this undesirable impact, nor do I want to snuff out the small flame of hope offered by federal cuts in marginal rates, by increasing Ontario's personal income tax rate. This leaves the retail sales tax as the only alternative.

A one-point increase in the retail sales tax rate would provide adequate replacement for lost federal transfers. Mr. Speaker, I have carefully considered this option and rejected it. Therefore, I have sought another option which keeps Ontario's sales tax rate at seven per cent.

I have concluded that the best way of recovering the lost revenue is to broaden the retail sales tax base. It was not an easy decision but I am convinced that it is better to bring certain items to tax than to raise the general rate.

I now propose to eliminate the exemptions for a number of items. These are discussed in more detail in the Tax Appendix to this Statement and include:

- certain household and personal hygiene products;
- building materials and certain other items purchased by publicly-funded bodies such as municipalities;
- plants and household pets;
- cloth and clothing patterns;
- magazines; and,
- items such as storm doors and windows, thermal insulation, chillers and wind deflectors for trucks.

I would, however, propose to enhance the Province's commitment to promoting alternative transportation fuels. The present retail sales tax exemptions for licensed motor vehicles powered exclusively by non-petroleum based fuels and for kits used to convert vehicles to utilize such fuels will be broadened to include licensed vehicles with dual-fuel capacity and dual-fuel conversion kits.

Another retail sales tax action I am taking in response to federal cutbacks relates to soft drinks, candy and confections. These items currently have a special exemption level of 49¢. I am proposing that this level be reduced to the general exemption level of 20¢ applicable to all sales and that the list of taxable confections be expanded.

These changes will be effective midnight tonight.

I am also proposing that, effective June 14, 1982, the taxation of services be expanded to include the labour content of the repair, maintenance and installation of tangible personal property. This means that the labour charged to carry out repairs to cars, trucks and most appliances will be taxable.

These changes will yield some $230 million this year. The revenue yield will be somewhat less than the projected losses resulting from the removal of the Revenue Guarantee by the Government of Canada.

Mr. Speaker, I should make it clear to people that I am not changing the long-standing exemptions for food, children's clothing, fuel for heating and lighting, prescription drugs and medical appliances.

I should also like to propose a number of other measures to improve our revenues.

Hospitality

One of these measures involves the hospitality industry. In my view, Mr. Speaker, it is no longer appropriate to tax prepared meals differently on the basis of price. Therefore, I am proposing to apply the retail sales tax to all prepared food and meals at the single rate of seven per cent. Prepared meals will include those served by restaurants, cafeterias and caterers and all take-out food.

The Province will realize an additional $110 million from this action this fiscal year.

The Members will recall my re-imposition of the retail sales tax on accommodations in January of this year. I have reviewed this move in light of the needs of the tourist industry. In my view, some modification is necessary to help the hospitality industry remain competitive, particularly with respect to international conventions. Therefore, I propose to reduce the rate on transient accommodation from seven to five per cent. This change will create a $10 million incentive for tourism. The effective date for implementation will be June 14, 1982.

The Minister of Revenue, the Honourable George Ashe, will be bringing forward legislation to implement all these retail sales tax changes.

OHIP Premiums

Mr. Speaker, one message I get loud and clear as I travel this province is that people want us to maintain our quality health care system. This cannot be done without adequate funding. Last year our health expenditures increased by about 18 per cent and the system continues to experience cost pressures. In order to maintain the funding of a reasonable share of costs from OHIP premiums, rates must be adjusted. Effective for the benefit month of October 1982, monthly OHIP premiums will be increased by $4 and $8 for single persons and families respectively. Additional revenues from this rate increase will be in the order of $170 million this fiscal year. I would remind the

Members that, despite this rate adjustment, premium revenues will cover less than 20 per cent of total health costs, compared to 23 per cent in 1979-80.

All residents of this province who now benefit from the system of premium exemptions will continue to do so. This means that all senior citizens, individuals experiencing temporary financial difficulties, social assistance recipients and their families will continue to receive a waiver of premiums. Individuals with low incomes will continue to benefit from premium assistance. I would also point out that 70 per cent of premiums are paid by employers.

While I continue to believe our premium system is a good one, I know that some Members would disagree. In a spirit of open consultation, I am tabling a staff discussion paper which deals with the question of substituting a payroll tax for premiums. I will elaborate on this paper later in my Statement.

Alcohol and Tobacco

I also propose to increase revenues from alcohol and tobacco.

With respect to alcoholic beverages, I am making changes that will increase revenue by an estimated $27 million in 1982-83. The changes are effective May 25, 1982.

- Mark-ups on domestic spirits will be increased by five percentage points, which amounts to an increase of about 30¢ per 25-ounce bottle.
- Mark-ups on imported spirits will be increased by three percentage points, which amounts to an increase of about 25¢ per 25-ounce bottle.
- The licence fee on domestic beer will be increased by 1.2 percentage points, resulting in an increase in the retail price of 15¢ per case of 24.

With respect to tobacco, I am proposing that, effective midnight tonight, the ad valorem rates of tax on cigarettes and cut tobacco be increased to 40 per cent. This will result in a tax increase of about 3.5¢ per package of twenty cigarettes. The extra yield is estimated at $30 million in this fiscal year. Wholesalers will be required to declare their cigarette inventories and to remit the appropriate tax.

Legislation to effect this tobacco tax change will be tabled later this evening by the Minister of Revenue.

Motor Vehicle Registration Fees

The Members will be aware that a new system of motor vehicle registration has been announced by my colleague, the Honourable James Snow, Minister of Transportation and Communications.

For the 1983 registration year, the proposed annual motor vehicle registration fees are as follows:

- $48 for passenger cars and for lightweight commercial vehicles used for personal purposes, registered in Southern Ontario. For such vehicles registered in Northern Ontario, the fee will be $24;
- $72 for commercial motor vehicles weighing 3,000 kilograms and less; and,
- $24 and $6 for motorcycles and mopeds respectively.

The revenue yield of the motor vehicle registration fees under the proposed system will be comparable to that of the old system.

Before turning to other matters, I would like to discuss briefly options for change in Ontario's tax structure.

Options for Change in Ontario's Tax Structure

Mr. Speaker, we live in a world where things are ever-changing. An important and disturbing development is that our federal government is apparently redirecting its economic priorities and indeed may have transmogrified the very way in which it views our Confederation.

Amidst these developments, it is important for me, as Treasurer, to examine our taxation system to see if it is appropriate to this changing environment. If it is not, then we must consider making alterations, even fundamental ones.

I must be concerned about not only what change might be appropriate, but also how major taxation change is made. Since the federal budget last November, all of us in Canada have witnessed with anguish what happens when sweeping tax moves are introduced without prior consultation. When governments try to re-write fundamentally the tax laws, they must work together with citizens and businesses in a co-operative manner. Those directly affected, not just bureaucrats and politicians, must have a real say in these matters. I would hope that the recently tabled federal discussion paper suggests a new awareness of consultation by our national government.

Ontario believes in the consultation process. To that end, I am tabling today a discussion paper on two important areas of taxation in Ontario. I hope that this paper will stimulate discussion so that all of us in Ontario can determine what is best for our province's future. The paper deals with two issues. It discusses how Ontario could replace its existing OHIP premium structure with a health-care payroll tax and shows, from a technical point of view, the impact of one way in which this could be done. In the field of personal income tax, it discusses the potential problem of continuing to be a participant in an income tax system which may not be suitable to the economic needs of Ontario.

I would emphasize that this paper is presented for discussion and does not reflect the Government's policy at this time. In the case of health financing, I have doubts about the wisdom of abandoning our existing premium system. Nevertheless, I am asking those interested in the issues raised in the paper to submit briefs to me before the end of 1982. In the case of a possible Ontario-run personal income tax, I have asked the Ontario Economic Council, chaired by Dr. Thomas Courchene, to review the economic implications of this matter and to report to me by December.

Restoring a Climate of Confidence

I would now like to turn to another matter of utmost concern to this province and this nation — that of restoring a climate of investment confidence. Before I am accused of "fed-bashing", let me say that Ontario has a long and honourable record of supporting the powers required by the Government of Canada to govern our country and to manage its economy. There is no question that occasionally we have differences of opinion. I believe it is important that they be fully aired. There is nothing wrong with that. It is the nature of democracy in a federal state. The fact that we can have such open and honest debates within the Canadian family simply reflects the strength of our country.

I wish to point out that Ontario finds itself in serious disagreement with Ottawa on two fundamental matters of economic policy. One concerns the federal government's apparent preference for a national industrial strategy based primarily on the resource sector. The other relates to its apparently negative attitude towards private investment.

I need hardly point out that Ontario supports the continued development of a strong resource economy in all parts of Canada. We want to see further development of energy resources in the West, off the East Coast and at the frontier. However, we are concerned that such policies not be pursued single-mindedly by the national government. It must continue to recognize the importance of manufacturing to Canada's economic future.

We believe that private investment from both domestic and foreign sources will be required to create the large number of new jobs that our people need. Therefore, our national policy should be carefully tailored to encourage productive investment from all sources. Canadianization should be a long-term goal that does not have features which are seen by international investors as unfair. Also, Canadians themselves must have the appropriate incentives to invest in their economy.

In line with these considerations, I would now like to discuss our own policies for industrial development and the stimulation of investment.

Industrial Leadership

Mr. Speaker, through our BILD program we have made a major commitment to supporting a climate of confidence and to stimulating long-term economic development. Our progress is summarized in Budget Paper C which I am tabling with this Statement. The highlights of our recent initiatives under this program include:

- a new $5 million program that is funding, through our community colleges, a high technology training program for 12,000 workers;
- the stimulation of $60 million worth of investment in 10 new food-processing facilities;
- the development of a new energy park at the Bruce nuclear station;
- the upgrading of six municipal airports;
- financial support for new convention centres in Toronto and Ottawa; and,
- the launching of new technology centres for microelectronics in Ottawa, for computer-aided design and manufacturing in Cambridge and Peterborough respectively, for farm technology in Chatham, for automotive parts in St. Catharines and for resource machinery in Sudbury.

BILD provides us with a way of involving business, communities and government in realizing our long-term economic development potential. Since its inception, BILD has initiated 66 specific programs. These initiatives are creating jobs in Ontario right now and will create many more in the future.

Corporate Income Tax Policy

It is vitally important, Mr. Speaker, that our corporate income tax policy be appropriate to our economic requirements.

Since last November, I have repeatedly asked Ottawa to reconsider some of its proposed changes to the corporate income tax. I am disturbed about the impact of the capital cost allowance changes on investment in the Ontario manufacturing sector in general and the steel and auto industries in particular. Moreover, the proposed change in the definition of resource income will have a further damaging effect on our steel industry which, through the direct employment of 50,000 people and indirectly many more, is one of the great strengths of the Canadian economy. I am also concerned about the inadequacy of proposed reserve provisions for the disposition of property.

I am encouraged by the fact that no federal legislation has been tabled to date. It is not too late for the federal government to introduce measures that will encourage, not discourage, capital investment and will assist, not penalize, Ontario's industry.

Meanwhile, I am proposing that certain federal proposals *not* be paralleled in Ontario's corporate income tax system.

- The tax depreciation in the year of acquisition of capital assets will not be reduced.
- No change will be made to the definition of resource income for the steel industry.
- No change will be made to existing reserve provisions.

With these actions, the Province will forgo an estimated $135 million in revenue this fiscal year.

I regret that these steps will reduce the harmony of our federal and provincial tax structures. Nevertheless, I will not propose that this House parallel, in the Corporations Tax Act, measures that could damage employment and investment prospects in Ontario.

Equity Investment

Mr. Speaker, the availability of sufficient equity capital to the private sector must be a priority of all governments in Canada who are interested in preserving and creating jobs. Current high interest rates and the economic slowdown only reinforce the importance of generating equity capital. Without sufficient equity businesses become too dependent on debt financing. When interest ratès rise dramatically, this results in a cash flow squeeze and sharply curtailed business activity.

Ontario has already taken important steps to improve the flow of equity capital to small business through the Small Business Development Corporations program and the Ontario Mineral Exploration Program.

These programs were introduced to compensate for the lack of an effective national policy to encourage stock ownership. I remain convinced that the federal government has the responsibility and the means to provide such support, not only for small business but Canadian business of all sizes. I strongly recommend to the Minister of Finance that he institute a program that would provide substantial income tax incentives for people to buy common stocks. Ontario is prepared to work with Ottawa in designing an effective mechanism and to bear its share of the cost of such a program.

A Major Incentive for Small Business

I mentioned earlier, Mr. Speaker, that I would be proposing a major new incentive for small business.

In recent years, over 50 per cent of all new jobs in this province have been generated by small business. Small business is the heart of entrepreneurial drive and spirit which has developed our economy in the past and will build it in the future. As I examine the current situation of small business, I find great cause for concern.

In order to improve the confidence of small business people, to give them the incentive, desire and resources to weather the economic storm, to improve productivity through investment and, most important, to continue to preserve and create jobs, I am proposing to remove the corporate income tax on small businesses in Ontario.

This substantial incentive will be in place for the next two taxation years. Instalment payments will be cancelled over the period of the tax holiday. Tax already paid during the current business year will be refunded.

This means that small businesses will not pay any Provincial income taxes on funds reinvested in the business. Of course, funds paid out in the form of dividends and income will be taxed as personal income.

By abolishing their corporate income tax, I am returning more than $250 million in 1982-83 alone to some 60,000 small businesses. In so doing, we are saying to small business people that there is one government that believes in them and in their desire and ability to succeed and to create jobs for our people.

Public Sector Restraint

Mr. Speaker, before concluding, I would like to deal with the issue of public sector restraint. The major theme of this Budget is getting people back to work. Economists do not agree on many issues, but there is one on which they are unanimous. Continuing high inflation is destroying jobs and is preventing the creation of the new jobs that our people need.

To get inflation under control there is a strong need for those who are employed, both in the private and public sector, to exercise restraint in their wage demands. This applies equally to employers with respect to prices.

It is a time when we must appeal to the sense of community of all our people. It is a time when we must ask everyone to demand a little less of the system and to put a little more back into it.

I would like now to address my attention to what this means for the public sector. I am referring here to the public sector in the broadest context, namely all those activities which are financed largely by tax dollars. Employment in the public sector has one advantage that most private sector employment does not have — a considerable degree of job security. It can be argued that those insulated from job insecurity should not be fully protected against inflation, when many taxpayers are facing reduced work hours, lower or no salary increases, or layoffs.

Ontario has led the way in the past with restraint of public sector growth. I now serve notice to all recipients of Provincial funds that they should not count on future funding at or above inflation rates. If we did so, we would doom our economy to continuing high inflation and high unemployment.

In this approach, we feel that we are not asking those in charge of public programs, funded by the taxpayers, to accept any more stringent requirements than we have imposed upon ourselves as a Government. Over the last seven years, the number of our public servants has actually been decreased by six per cent, from 87,000 to 82,000, at a time when the general population has increased by six per cent. The salaries at the most senior level have grown at less than half the rate of inflation, not only in the last few years, but since 1973.

Increasing Efficiency in the Ontario Public Service

	March 1975	March 1982	Change Since 1975
Classified Staff	69,618	66,966	(2,652)
Unclassified Staff	14,632	13,509	(1,123)
Other Crown Employees	2,859	1,351	(1,508)
Total	87,109	81,826	(5,283)
Decrease (%)			(6.1)
Total Population (000)	8,172	8,696	
Population Served per Public Service Position	94	106	

It is a simple and well-known fact that one of the causes of inflation has been the failure of the Government of Canada and certain other areas in the public sector to exercise similar restraint in both numbers and salaries. At the highest level in the Government of Canada and in some of the other provinces, salaries are from $20,000 to $25,000 in excess of those paid in the Ontario Government.

We have talked about the public sector but we must also consider the total economy. Wage and price restraint in all sectors will be essential if we are to avoid pricing our economy out of international markets. In this respect, we are one of the most export-dependent jurisdictions in the world. We depend upon exports for some 30 per cent of our GNP, compared to the United States at 12 per cent.

Currently, we are hearing arguments supporting wage and price controls. It is surely preferable, at this time, to see a serious effort made by all sectors to exercise voluntary restraint in the interest of the common good.

If we are asking people in all walks of life to exercise restraint, we must begin with ourselves. At the more senior levels of government, wage restraint, as I mentioned, has since 1973 kept our people behind many other governments and far behind the private sector. In the normal course of events, therefore, salary adjustments to these groups would have been at least in the range of settlements already negotiated for the unionized bargaining groups. However, because of the severe economic conditions we now face, we will be cutting these increases to six per cent this year. This will apply to the top levels of the public service. Flexibility will be introduced to allow somewhat higher adjustments in the lower ranges of the non-bargaining group.

We recognize that to our senior employees this is a further imposition. As the economy improves, the Province will undertake to review the salary inequities that have been shouldered by this group. However, we believe that during tough times the public sector must be prepared to show tough leadership.

Mr. Speaker, we feel that those of us in this House must demonstrate our recognition of the adverse economic situation as well. Each year the Election Expenses Committee of the Legislature recommends increases for the Members. This year the recommendation is for nine per cent. The Government will propose to the Legislature that the Members also set an example and agree that this award be cut to six per cent.

We expect municipal councils, boards of education, universities, colleges, hospitals and all those agencies funded principally from taxes, to review carefully their compensation plans and to show similar restraint. It is also our view that all agencies of the Crown, corporations whose members are appointed by the Government and bodies receiving the majority of their operating budgets from public funds should follow the example of this Government by publishing all senior salaries above $30,000 in some form of "public accounts". A sunshine law on public agency incomes within Provincial jurisdiction will, therefore, be presented to the Legislature. This will require the filing with the Government of the total compensation package for all individual employees receiving over $30,000, by range. The legislation will require information on senior public sector remuneration in 1981, compared with the results that are achieved in 1982 and in subsequent years.

With respect to direct Provincial programs, we intend to initiate a thorough-going analysis of options for trimming expenditures and introducing more efficiencies. This review will be under the direction of my colleague, the Honourable George McCague, Chairman of the Management Board of Cabinet.

We hope that similar actions and examples can be accomplished by the federal government and other governments in Canada, as well as by the private sector.

The 1982-83 Fiscal Plan

Mr. Speaker, let me summarize the Government's fiscal plan for 1982-83. I am projecting overall expenditures to increase by 11.6 per cent and revenues to go up by nine per cent. I am planning for a deficit of $2.2 billion which is approximately equal to the level of capital investments to be undertaken this year. The $672 million increase in net cash requirements over last year will provide a necessary economic stimulus. I am pleased to note that the Province will finance this level of cash requirements through non-public borrowing and liquid reserves. Our continuing policy of restraint has paid off. Now that we need to increase the deficit temporarily to accommodate difficult economic conditions, we have the flexibility to do so without putting our financial position in jeopardy.

Mr. Speaker, Ontario's record of debt management and capital investment is discussed at some length in Budget Paper C. It shows that we have managed Ontario's finances effectively and have ensured that borrowing over the past decade has been prudently held below the level of public capital investment.

Ontario's Capital Investments
($ million)

	1980-81	Interim 1981-82	Estimated 1982-83
Physical Assets (roads, highways, bridges, water and sewer facilities, drainage and flood control, etc.)	922	944	1,077
Buildings (schools, universities, colleges, hospitals, housing projects)	344	473	523
Land (right-of-way and other)	59	46	52
Transportation Vehicles (buses, subway and street cars, etc.)	27	45	50
Financial Assets (investments, mortgages, commercial loans, etc.)	33	360	94
Employment Development Fund/BILD	124	150	341
Total Capital Investments	1,509	2,018	2,137

Ontario's 1982-83 Fiscal Plan
($ million)

	Interim 1981-82	Estimated 1982-83	Year-to-Year Change
Revenue	18,855	20,545	+1,690
Expenditure	20,415	22,777	+2,362
Net Cash Requirements	1,560	2,232	+ 672
Net Non-Public Borrowing	1,425	1,864	
Net Public Borrowing	− 62	− 47	
Reduction in Liquid Reserves	197	415	
Total Financing	1,560	2,232	

Conclusion

In conclusion, Mr. Speaker, this Budget has been crafted in some of the most difficult economic times facing Ontario and Canada. Nevertheless, the Budget I place before you fashions economic and financial policies to meet the challenges of today and tomorrow.

- It provides investment incentives to create jobs in the future.
- It shows leadership in restraining the public sector.
- It provides for an expansionary deficit to stimulate the economy, while remaining true to our solid tradition of sound financial management.
- It continues and strengthens our commitment to the farming community.
- It avoids major tax increases or reductions in public services despite federal cutbacks.
- It helps to restore confidence in our manufacturing industries.
- It creates 31,000 temporary jobs in Ontario.
- It helps 15,000 families buy new homes and creates thousands of needed jobs in the construction industry.
- And, it totally eliminates Provincial corporate income tax on our small businesses.

The Ontario Economy, 1980 through 1982

	1980	1981	1982	80/79	81/80	82/81
		($ billion)			(per cent)	
Total Output						
Gross Provincial Product	109.6	123.7	135.5	9.4	12.9	9.5
GPP (constant 1971 dollars)	49.2	50.5	50.0	−1.1	2.6	−0.9
Investment						
Machinery and Equipment	9.2	11.0	11.9	17.4	19.5	7.6
Non-Residential Construction	6.7	8.0	8.9	18.6	18.5	12.2
Residential Construction	3.1	3.8	4.2	−11.5	20.2	11.1
Other Components of Demand						
Housing Starts—Units (000)	40.1	50.2	50.0	—	—	—
Retail Sales	29.7	33.8	37.2	7.8	14.0	10.1
Exports	39.2	42.4	44.6	15.1	8.3	5.1
Imports	30.9	35.7	36.5	11.5	15.6	2.0
Income						
Personal Income	91.0	105.6	117.8	11.2	16.0	11.5
Corporate Profits (before taxes)	13.2	12.4	11.6	8.1	−6.0	−7.1
Prices						
Consumer Price Index	—	—	—	10.1	12.5	10.7
Jobs						
Labour Force (000)	4,366	4,481	4,542	1.8	2.6	1.4
Employment (000)	4,066	4,186	4,196	1.4	3.0	0.2
Unemployment Rate (% of labour force)	6.9	6.6	7.6	—	—	—

Source: Ontario Treasury.

Appendix A

Details of Tax Changes

The purpose of this appendix is to provide a more detailed description of the tax changes outlined in the Budget Statement. This is a concise summary only, and the reader is advised to consult the statutes for exact information.

Retail Sales Tax Act

Tax Base Changes

- The following exemptions from the 7 per cent tax under subsection 5(1) will be withdrawn:

Paragraph	*Description*
16	trees, shrubs, bushes, seeds and seedlings, cut flowers, plants and bulbs (except when purchased for use in farming);
24	personal hygiene and household cleaning products;
27	street flushers and street sweepers (fire-fighting vehicles will remain exempt);
29	materials and equipment such as storm doors, storm windows and chillers;
30	consumables, such as soaps and tissues, purchased for use in the provision of transient accommodation;
51	classroom supplies;
52	students' supplies;
67	buses and repair parts purchased by municipalities;
68	materials incorporated into buildings and structures owned by schools, colleges, universities and public hospitals;
69	materials incorporated into buildings or structures owned by municipalities and local boards;
72	household pets;
76	clothing patterns;
77	textiles and trimmings, such as cloth and fabric, sold by the metre or yard for domestic use; and,
78	smoke alarms.

Effective: May 14, 1982.

- Amendments to subsection 5(1) will be made to effect the following changes:

Paragraph	*Description*
1	The exemption for candies, confections and soft drinks priced at 49¢ or less will be withdrawn. These items and snack foods as defined by the Minister, priced at 21¢ or more, will be subject to the 7 per cent tax.
14, 14a	Exemptions for conversion kits and licensed motor vehicles using non-petroleum based fuels will be broadened to include those with dual-fuel capacity.
55	Magazines purchased otherwise than by subscription will be subject to the 7 per cent tax.

Effective: May 14, 1982.

- The 7 per cent tax will be extended to include labour costs for installation, repair and maintenance of tangible personal property such as:
  - automobiles, televisions, radios and appliances; and,
  - all other items that are not, or are not installed as, a part of real property.

Effective: June 14, 1982.

Hospitality Industry

- All prepared food including meals served at restaurants and cafeterias, and take-out food and all other prepared food sold at snack bars, lunch counters, etc., will be taxed at 7 per cent.
- The $6.00 exemption level for prepared meals will be withdrawn.
- Transient accommodation, as defined in the Retail Sales Tax Act, will be taxed at 5 per cent.
- American Plan charges will be taxed at 5 per cent.
- The tax on beverage alcohol will remain at 10 per cent.

Effective: June 14, 1982.

All enquiries regarding retail sales tax changes should be directed to:

Retail Sales Tax Branch
Ministry of Revenue
Parliament Buildings
Queen's Park
Toronto, Ontario
M7A 1X9

or

the nearest Retail Sales Tax District Office. For telephone enquiries in Toronto call 487-1361 or 965-4801.

Revenue from Beverage Alcohol

Domestic Beer

- The licence fee on the production of beer for sale in Ontario, which applies to the laid-down cost of the various package sizes, will be increased from 20 to 21.2 per cent.

Effective: May 25, 1982.

Spirits

- Mark-ups on domestic spirits will be increased by 5 percentage points.
- Mark-ups on imported spirits will be increased by 3 percentage points.

Actual price changes for individual products will be announced by the Liquor Control Board of Ontario.

Effective: May 25, 1982.

All enquiries regarding domestic beer and spirits price changes should be directed to:

Ministry of Consumer and Commercial Relations
Liquor Control Board of Ontario
55 Lakeshore Blvd. East
Toronto, Ontario
M5E 1A4
(416) 963-1926

Fees and Licences

Motor Vehicle Registration Fees

In conjunction with the new system of vehicle registration which will be implemented by the Ministry of Transportation and Communications for the 1983 vehicle registration year, the Province is adopting a flat fee structure for all passenger vehicles and light-weight commercial vehicles. The new fees will be based on a 12-month period and are as follows:

Fees in Southern Ontario

- Passenger cars, and commercial vehicles weighing 2,400 kilograms or less used for personal purposes: $48.
- Commercial motor vehicles weighing 3,000 kilograms or less: $72.
- Motorcycles and mopeds: $24 and $6, respectively.

Fees in Northern Ontario

- Passenger cars, and commercial vehicles weighing 2,400 kilograms or less used for personal purposes: $24.
- Commercial motor vehicles weighing 3,000 kilograms or less: $72.
- Motorcycles and mopeds: $24 and $6, respectively.

Effective: December 1, 1982.

All enquiries regarding motor vehicle registration fee changes and details of the new vehicle registration system should be directed to:

Public and Safety Information Branch
Ministry of Transportation and Communications
1201 Wilson Avenue
Downsview, Ontario
M3M 1J8
(416) 248-3501

Other Fees and Licences

A number of other changes in fees and licences will be introduced by various ministries. Dates of changes and the new levels will be announced by the respective ministries at a later date.

Tobacco Tax Act

Tax Rate Changes

- Cigarettes and cut tobacco will be taxed at the rate of 40 per cent of their retail prices as determined by the Minister of Revenue.
- The tax applicable will be:
  - 1.84¢ per cigarette; and,
  - 1.1¢ for each gram, or part of a gram, of cut tobacco and all other tobacco products except cigars.
- The tax rate on cigars remains at 45 per cent.

Effective: May 14, 1982.

Inventories

- Wholesalers will be required to declare their cigarette inventories as of the close of business May 13, 1982, and to remit tax on such inventories as directed by the Ministry of Revenue.

Compensation to Tobacco Tax Collectors

- The maximum annual compensation allowed to designated tobacco tax collectors will be increased to $2,000 commencing this fiscal year.
- Effective June 1, 1982, an appointed tax collector may claim a *shrinkage* allowance of not more than one-tenth of one per cent of the tobacco tax collected and remitted, provided that remittance obligations are duly met.

All enquiries regarding tobacco tax changes should be directed to:

Motor Fuels and Tobacco Tax Branch
Ministry of Revenue
Parliament Buildings
Queen's Park
Toronto, Ontario
M7A 1Y3
(416) 965-5407 or
(416) 965-3889

Corporations Tax Act

Income Tax Exemption for Small Business

- **The Ontario corporations income tax payable on income eligible for the small business deduction under subsection (1) of section 125 of the Income Tax Act (Canada) will be suspended for two years.**
- The exemption will be based on the higher annual and total business limits of $200,000 and $1,000,000 respectively announced in the federal budget of November 12, 1981.
- This change will apply to any two taxation years of corporations ending after May 13, 1982 and before May 14, 1984.
- Qualifying corporations will be allowed to apply for a refund of any instalments already paid with respect to the exempt period that are in excess of the amount of the revised tax for the year.
- No credit interest will be paid by the Government on any such overpaid instalments to May 14, 1982 that are requested and refunded prior to the filing of the return for that year.
- The normal loss application rules will apply to losses and income in the two-year period, i.e. losses made outside the period must be applied against income arising during the period and losses arising within the period must be applied against income within or outside the period as the case may be.

- The tax that would otherwise have been payable during the exempt period should be taken into account in calculating the tax instalments payable for the first taxation year immediately following the two-year exemption.

Small Business Tax Credit

- The small business tax credit on depreciable property, which was in effect for a two-year period from April 22, 1980 to April 23, 1982, will not be extended.

Federal Budget Changes

The following changes proposed in the federal budget of November 12, 1981 and *Notes on Transitional Arrangements and Adjustments* of December 18, 1981 will not be paralleled:

Capital Cost Allowance

- The capital cost allowance deduction in the year an asset is acquired will remain at the normal rate of write-off currently provided and will not be reduced to one-half the normal rate.

Reserves

- Reserve provisions for all dispositions of property in respect of the profit or capital gain to a taxpayer attributable to unpaid instalments will not be altered.

Iron Ore Mining and Processing

- There will be no change in the definition of resource income beyond the primary pellet stage. This income will continue to be eligible for the determination of Ontario's automatic depletion allowance.

All enquiries regarding corporations tax changes should be directed to:

Corporations Tax Branch
Ministry of Revenue
Parliament Buildings
Queen's Park
Toronto, Ontario
M7A 1Y1
(416) 965-4040

Provincial Land Tax

- Telephone and telegraph companies will pay tax equal to 5 per cent of gross receipts in areas without municipal organization. The definition of gross receipts will parallel that in the Municipal Act.
- Assessment of telephone and telegraph wire mileage will be discontinued.
- The existing schedule of rates for pipeline assessment will be replaced by one schedule for gas pipelines and one for oil pipelines, corresponding to the schedules presently used for municipal taxation, as set out in the Assessment Act.

Effective: January 1, 1983.

All enquiries regarding provincial land tax changes should be directed to:

Motor Fuels and Tobacco Tax Branch
Ministry of Revenue
Parliament Buildings
Queen's Park
Toronto, Ontario
M7A 1Y3
(416) 965-1071

Appendix B

The Ontario Health Insurance Plan

Premium Increase

- Ontario Health Insurance Plan (OHIP) premiums will be increased from the current single and family certificate rates of $23 and $46 per month to $27 and $54 per month, respectively.

Effective: for premiums paid in respect of benefit months from October 1, 1982 onwards.

Premium Assistance

- Premium assistance limits will continue to be as follows:

  (a) *Free Coverage*
  —single persons having taxable incomes of $3,000 or less;
  —families having taxable incomes of $3,500 or less.

  (b) *75 per cent Premium Reduction*
  —single persons having taxable incomes between $3,000 and $3,500;
  —families having taxable incomes between $3,500 and $4,500.

  (c) *50 per cent Premium Reduction*
  —single persons having taxable incomes between $3,500 and $4,000;
  —families having taxable incomes between $4,500 and $5,000.

  (d) *25 per cent Premium Reduction*
  —single persons having taxable incomes between $4,000 and $4,500;
  —families having taxable incomes between $5,000 and $5,500.

- Pensioners and social assistance recipients will continue to be eligible for free OHIP coverage.

All enquiries regarding the Ontario Health Insurance Plan should be directed to the nearest OHIP office or to:

Ontario Health Insurance Plan
7 Overlea Boulevard
Toronto, Ontario
M4H 1A8

Appendix C

The Ontario Renter-Buy Program

- An eligible individual purchasing or building, and moving into, a new eligible housing unit in Ontario, between May 14, 1982 and April 30, 1983 inclusive, may apply for an interest-free loan, provided that a binding contract to purchase is made on or before October 30, 1982, and the home is to be used as a principal and permanent residence.
- The purchaser must have equity of at least 10 per cent in the eligible property.
- As soon as an individual agrees to purchase or begins to build a housing unit, he or she may apply to the Ontario Mortgage Corporation for an interest-free loan of 10 per cent of the purchase price or cost, up to a maximum loan of $5,000.
- The loan will be secured by a mortgage on the property subsequent in priority to all other mortgages registered at the time of purchase or building of the housing unit.
- Repayment is due in 60 equal monthly payments, beginning on the first day of the first month after the 10th anniversary of purchase.
- Any and all outstanding amounts become due and payable if the housing unit is sold or if it ceases to be the principal and permanent residence of the individual receiving the loan.

Eligible Housing Unit

- An eligible housing unit is a unit suitable for permanent year-round habitation for one family and which was not previously occupied for residential purposes and includes:
  - a house containing not more than one housing unit;
  - a condominium unit;
  - a mobile home meeting specified housing standards; and,
  - a unit in a building converted from non-residential use.
- The price of the housing unit must exceed $20,000 but cannot exceed $115,000 in the Toronto area and $90,000 in the rest of the province. The Toronto area includes:
  - all municipalities in Metropolitan Toronto;
  - all municipalities in the Region of Peel;
  - all municipalities in the Region of York except the Township of Georgina;
  - the City of Oakville; and,
  - the Towns of Ajax and Pickering.

Eligible Applicants

- Applicants must be 18 or more years of age, Canadian citizens or landed immigrants, and resident in Ontario for the previous twelve months.
- An applicant is eligible if:

  (i) he or she rented a principal residence for the preceding 12 months, **and** neither the applicant, nor his or her spouse, owned during that period, alone or in conjunction with other owners, any interest in residential property, excluding vacant land or property suitable for seasonal use only;

  OR

  (ii) neither the applicant, nor his or her spouse, ever owned, alone or in conjunction with other owners, any interest in residential property, excluding vacant land or property suitable for seasonal use only.

All enquiries regarding the Ontario Renter-Buy Program should be directed to:

Ontario Mortgage Corporation
60 Bloor Street West, 11th Floor
Toronto, Ontario
M4W 3B8
(416) 963-1560

Outside Toronto Area: 1-800-268-1158 (toll free)

Budget Papers

Presented for the information of
the Legislative Assembly of Ontario
by the Honourable Frank S. Miller,
Treasurer of Ontario and
Minister of Economics, May 13, 1982

Budget Papers

Budget Paper A

Policies for Economic Recovery

Budget Paper B

Fiscal Federalism in Canada: The Record to Date
The Challenge Ahead

Budget Paper C

Public Investment and Responsible
Financial Management

Review of the 1981 Budget

Financial Tables and Charts

Budget Paper A

Policies for Economic Recovery

Table of Contents

Introduction **3**

I International Economic Setting **4**
- Rising Unemployment 4
- Large Budgetary Deficits 6
- High Interest Rates 7

II Canadian Economic Environment **9**
- The November Federal Budget 9
- Impact of High Interest Rates on Regions and Sectors 10

III Ontario Job-Creation Policy **12**
- Job Creation: A Priority for Ontario 12
- Long-Term Approach 13
- Immediate Job Creation 14

IV Restoring the Canadian Economy **19**

Conclusion **20**

Policies for Economic Recovery

Introduction

In recent months, job creation and policies for economic recovery have become the primary focus of international concern. Every large industrial nation, including Canada, is experiencing a sharp decline in employment. The international dimensions of this issue cannot be ignored. Indeed, the monetary and fiscal measures adopted by our trading partners are a major cause of the Canadian recession. Also, the intolerable social and economic costs of world-wide unemployment create an added hazard — the grave potential for increased protectionism and the imposition of foreign exchange controls. Therefore, much is at stake in the current efforts to resolve the problems of world-wide recession.[1]

The international economic environment has become increasingly unsettled. The large industrial countries have been struggling to deal with high inflation, enormous budgetary deficits and weakness in their balance of payments. Led by the United States, they have adopted, in varying degrees, policies that have produced extremely high interest rates. The result has been a synchronized and severe international recession in which unemployment has risen to unacceptably high levels.

In Canada, federal fiscal and interest rate policies are undermining confidence and are compounding the effects of weak export markets on the domestic economy. In particular, abnormally high real interest rates already have imposed large economic and social costs and threaten to prolong the downturn in domestic economic activity. Ontario's production of durable manufactured goods (for example, automobiles, steel and appliances) and its housing construction industry have been especially hard hit. Owners of small businesses, farmers and youth have been among the principal victims of high interest rates and recession.

The Government of Ontario continues to regard the control of inflation as a major priority. However, in its view, policies to contain inflation need not, and should not, lead to higher unemployment.[2] Indeed, the Ontario Government strongly believes that policies for job creation must be an urgent priority. Ontario pressed this view at the recent First Ministers' Conference on the Economy.[3]

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[1]A rethinking of recent policy trends is already occurring in some countries. For example, Germany is in the process of legislating a major job-creation program which will cost $20 billion over the 1982-85 period. Most of this increased spending will be financed by tax increases. In addition, France and Germany are examining ways to break the link between U.S. interest rates and their domestic rates.

[2]In this regard, Ontario has suggested a number of alternative anti-inflation measures. See Hon. William G. Davis, *A Blueprint for Economic Recovery* (Toronto, 1982).

[3]*Ibid.*

Within the constraints imposed by the fiscal and economic environment, Ontario has, therefore, developed a set of job-creation measures to ameliorate the adverse impacts of the recession on the provincial economy. These measures are an immediate response to an immediate problem. They are in addition to the longer range structural adjustment policies initiated in recent Ontario Budgets and developed more extensively in the Board of Industrial Leadership and Development (BILD) program.

I International Economic Setting

Ontario's policies for economic recovery have been formulated in an international economic setting in which all major industrial nations are facing the following challenges:

- rising unemployment;
- large budgetary deficits; and,
- high interest rates.

It is not within the power of a relatively small jurisdiction, such as Ontario, to overcome on its own, problems that are international in origin. However, it is important that these problems be understood in order to design policies that can be effective within the constraints imposed by international conditions.

Rising Unemployment

The nations of the Organisation for Economic Co-operation and Development (OECD) experienced modest growth in the first half of 1981, fuelled by unexpectedly strong exports to the non-OECD area, principally the members of the Organisation of Petroleum Exporting Countries (OPEC).[4] By the summer of 1981, however, economic growth in most OECD nations was stalled, primarily due to high interest rates originating in the United States. Real output in the OECD area is estimated to have shown no growth in the latter part of 1981, as declines in the United States, United Kingdom, Germany and Canada offset growth in Japan, France and most of the smaller countries. It is now evident that recession in the major economies has spilled over into 1982.[5]

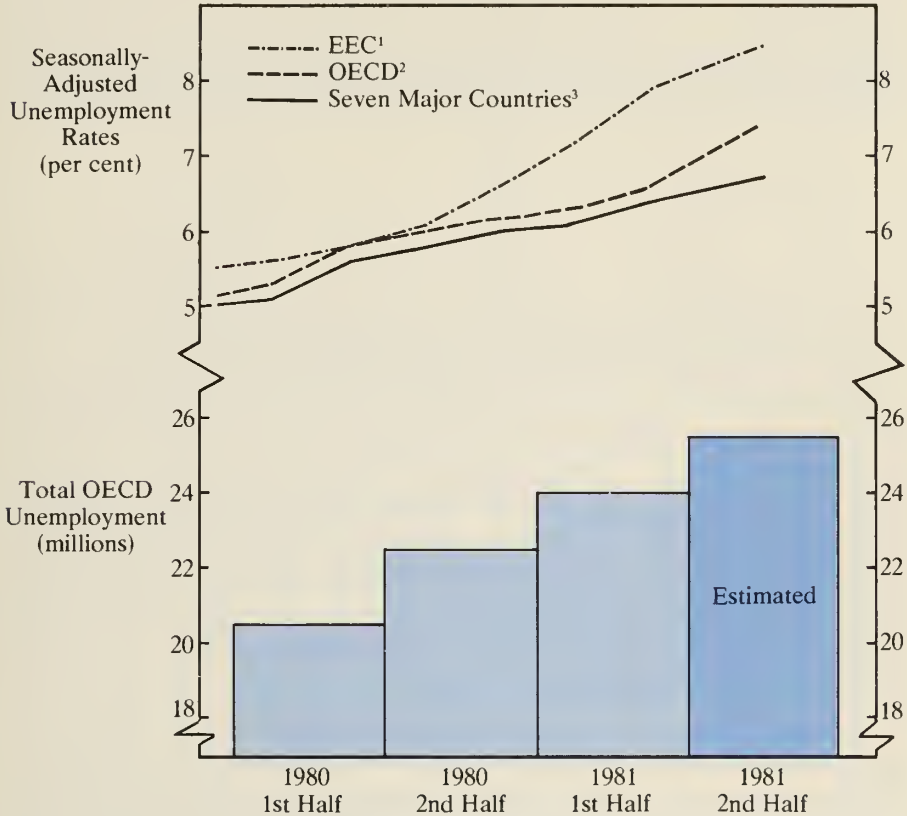
As Chart 1 indicates, the recession which currently grips the OECD area has resulted in a significant increase in unemployment. While some economies were hit later than others, the average unemployment rate for the OECD countries rose to 7.3 per cent in the second half of 1981

[4]By the end of 1980, the member nations of OECD had absorbed much of the impact of the 1979 oil price rise.

[5]On the positive side, the reduction of economic activity has brought about a reduction in the average rate of inflation for the OECD area.

from its 1980 average of 6.2 per cent. Countries, such as Germany, that had managed to hold their unemployment rates well below the OECD average in the 1974-75 recession have not been as successful this time.

Unemployment Levels and Rates, OECD 1980 and 1981 — Chart 1



Source: OECD, *Economic Outlook,* December, 1981 and *Labour Force Statistics,* August, 1981.

[1]Belgium, France, Germany, Italy, the Netherlands and U.K. only.

[2]Covers 15 principal countries, representing 85 per cent of employment in the OECD area.

[3]Canada, U.S., Japan, France, U.K., Germany, Italy.

Table 1 presents unemployment rates in Ontario and seven OECD nations. The rise in unemployment rates over the past year has been substantial in all but Japan. Increases range from zero in Japan to 2.1 percentage points in the United Kingdom. Canada's increase of 1.3 percentage points was just below that of the United States which had a 1.4 percentage point increase.

The number of unemployed persons in the OECD area has risen rapidly to an estimated 25.8 million in the latter part of 1981, up 4.4 million from the 1980 average. Not only has unemployment risen because of a failure to create new jobs, but also there has been a substan-

Unemployment Rates: Ontario and Selected OECD Countries
(per cent)

Table 1

	First Quarter 1981	Most Recent Quarter[1]
Japan	2.2	2.2
Germany	3.7	5.2
Ontario	6.5	7.6
France	7.0	8.0
Canada	7.3	8.6
United States	7.4	8.8
Italy	7.6	8.9
United Kingdom	10.3	12.4

Sources: OECD, *Labour Force Statistics;* Statistics Canada, *The Labour Force Survey*; and U.S. Department of Labour, *Monthly Labour Review.*

[1]1981 fourth quarter data, except for Ontario, Canada and the United States which are 1982 first quarter.

tial number of layoffs. For example, job losses last year were over one million in the United Kingdom, over 250,000 in West Germany and almost 75,000 in Italy. In North America, there was a drop of almost 1.5 million in the United States and over 220,000 in Canada from the 1981 peak levels. Even Japan suffered a loss of 70,000 jobs during the year 1981. Ontario, too, has experienced layoffs as a result of this deteriorating international environment.

These job losses and the current international recession can be explained in the context of the link between projected budgetary deficits in the United States, high interest rates and balance of payments problems in many OECD countries. High real interest rates emanating from the United States have spread the recession internationally and have forced countries to consider the trade-off between the inflationary effects of falling exchange rates and the mounting social costs of higher unemployment.

Large Budgetary Deficits

All major industrial countries have been striving, with varying degrees of success, to reduce their budgetary deficits. In terms of its impact on the world economy, the most important budgetary problem has arisen in the United States where President Reagan has embarked on a program of tax reductions, defence expenditure increases and reductions in other areas of federal government spending.

Despite large cuts in other government programs, the President's tax initiatives and defence program are widening the gap between revenues and outlays. Congress has rejected several reductions in social services sought by the Administration. As a result, the effect of the expenditure cuts that have been approved will be overwhelmed by the combined impact of increased defence spending and reduced taxes. Unless a compromise is reached, federal deficits are likely to be well in excess of $100 billion (U.S.) in each of the next two years.

Fiscal Balances in Selected OECD Countries — Table 2
(per cent of GNP or GDP)

	1980	1981
Germany	−3.4	−4.4
France	0.4	−2.4
United Kingdom	−3.5	−2.3
Italy	−7.8	−9.4
Japan	−4.1	−3.6
United States[1]	−2.3	−2.3
Canada[1]	−4.4	−4.0

Sources: OECD, *Economic Outlook*, December, 1981; *Congressional Quarterly Weekly Report*, February, 1982; and Hon. Allan J. MacEachen, *The Budget in More Detail* (Ottawa: Department of Finance, November, 1981).

[1]This refers to the federal budgetary positions only.

Over the past two years, most European countries also have been attempting to contain deficits in government budgets. Deficits have been attacked mainly with expenditure restraint, although a significant role has also been assigned to tax increases. Nevertheless, in most European countries budget deficits remain large. The continuing recession has trimmed revenue growth, while expenditures have steadily increased as a result of indexed social programs and mounting debt-service costs. In Germany, tax increases have been introduced to contain the budgetary imbalance. The United Kingdom, drawing on its strong petroleum position, imposed huge energy taxes in 1981 as the principal means of reducing its deficit.

High Interest Rates

The United States has led the major industrial nations in generating high interest rates. Initially, a tight control over U.S. money supply growth and substantial increases in energy prices caused a rise in interest rates and a slowdown in the economy. Recently, this has been compounded by U.S. fiscal policies. Tight credit policies together with significant levels of government borrowing to finance deficits have created conditions under which interest rates have risen to record levels.[6]

High interest rates have, in turn, compounded budgetary problems

[6]In an apparent effort to reduce the expected conflict between large deficits and slow monetary growth, Chairman Paul Volcker of the Federal Reserve Board announced, in early 1982, that it would be appropriate for the narrowly-defined money supply to grow in the upper half of this year's target band of 2.5 to 5.5 per cent.

by stalling the economy. A weak economy reduces tax revenues and increases required outlays for social services. The U.S. Administration has estimated that a one per cent increase in the rate of unemployment raises the federal deficit by $25 billion. In addition, high interest rates directly increase expenditures by raising the cost of servicing the public debt. Interest payments are estimated to have accounted for 10.5 per cent of U.S. federal government outlays in 1981 and there is general agreement that they will be an even larger share of total costs over the next few years.

Current Account Balances in Selected OECD Countries — Table 3

($ billion U.S.)

	1980	First 3 Quarters 1981
Germany	−16.4	−11.7
France	−7.4	−3.8
United Kingdom	7.4	8.5
Italy	−9.8	−11.0
Japan	−10.7	2.8
United States	3.7	6.5
Canada	−1.6	−4.8

Sources: OECD, *Economic Outlook,* December, 1981; and U.S. Council of Economic Advisors, *Economic Indicators*, February, 1982.

The high interest rates in the United States have forced other countries to follow suit. As shown in Table 3, many countries have been experiencing large balance of payments deficits which are being financed by net capital inflows. This situation requires that interest rates in these countries remain competitive with the high interest rates in the United States, thereby spreading their recessionary impact. As a partial offset, however, some European countries have allowed the international value of their currencies to slide. For example, during 1981, the Italian lira depreciated by about 30 per cent in relation to the United States dollar while the French franc fell by 26 per cent, the British pound by 21 per cent and the German mark by 13 per cent. The decision to allow currency values to decline reflects the increasing concern over the detrimental effects of high real interest rates on employment and investment.

II Canadian Economic Environment

The November Federal Budget

Like its major trading partners, Canada entered a recession in the past year. However, the November, 1981 federal budget was developed in the context of the vigorous economic performance experienced in the first half of 1981. The federal government considered inflation, rather than unemployment, to be the main problem.

> "The strength of the economy through the middle of 1981 led to a large increase in employment and to a decline in the unemployment rate. As of the second quarter, total employment was up 3.5 per cent or 375,000 from the same period in 1980. The unemployment rate declined one-half of one percentage point over this period to 7.2 per cent. The downward trend in the unemployment rate was fairly widespread, but was especially marked for young people, with the rate down one percentage point . . .
>
> The rapid growth in output has been accompanied by a faster rate of increase in prices. The year-over-year increases in the CPI have averaged 12.7 per cent this year to the end of August, up from 10.2 per cent for 1980 as a whole."[7]

With this view of the economy and in support of the tight credit policy already in place, the federal government focused on restraining inflation. In this regard, it planned to bring down the deficit from $13.3 billion in 1981-82 to $10.5 billion in 1982-83, or, expressed as a percentage of GNP, from 4.0 to 2.8 per cent. In addition, proposals were announced to eliminate or reduce many investment incentives that the federal government regarded as undesirable forms of tax avoidance.[8]

In short, in designing its budget, the federal government was not principally concerned with unemployment. Therefore, the negative impact of its fiscal measures on future business investment and job creation was ignored.

Unfortunately, however, adverse developments abroad and at home had already been underway since early in the year. In the United States, sharply rising interest rates were driving that economy into deep recession. On the domestic scene, the federal government was boosting petroleum prices in accordance with the National Energy Program and

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[7]Hon. Allan J. MacEachen, *The Current Economic Situation and Prospects for the Canadian Economy in the Short and Medium Term* (Ottawa: Department of Finance, November, 1981).

[8]For Ontario's response to these tax changes see Hon. Frank S. Miller, *A Program for Restoring Confidence in the Canadian Economy*, Statement to the Federal-Provincial Conference of Finance Ministers, Toronto, December 14, 1981.

imposing special oil levies in response to the Alberta production cutbacks. At the same time, the Bank of Canada was pushing interest rates to record levels as an offset to a huge outflow of capital from Canada which was weakening the value of the Canadian dollar. By mid-year, the pressures created by domestic policies had undermined the basis for sustained growth. With recession in the U.S. and European economies, the Canadian economy was deprived of its residual strength in exports.

Impact of High Interest Rates on Regions and Sectors

The aggressive use of interest rate policy by the Bank of Canada has been a dominant feature of Canadian economic policy over the past year. The Bank has been concerned primarily with maintaining the value of the currency in the face of high international interest rates and of reduced confidence in the Canadian economy. As a consequence, it has pushed domestic rates of interest to exceedingly high levels in both nominal and real terms. The real prime rate, as measured by the difference between the prime interest rate charged by banks and the rate of inflation in consumer prices, recorded an average of 6.8 per cent in 1981, more than three times the average of the previous 16 years.

Nominal and Real Prime Interest Rates in Canada, 1965 to 1981 — Table 4
(per cent)

	Nominal	Real[1]
1965-1969	6.5	2.8
1970-1974	7.8	1.9
1975-1979	10.1	1.2
1980	14.2	4.0
1981	19.3	6.8

Source: Bank of Canada, *Bank of Canada Review*, selected years.

[1]Nominal chartered bank rate on prime business loans minus the annual rate of change of the CPI. Calculations are based on period averages.

The current recession in Canada has already spanned three full quarters and is being prolonged by continued high real interest rates. Meanwhile, the economic and social costs are mounting. Small businesses, with characteristically high debt-to-equity ratios, face bankruptcies in increasing numbers. The youth unemployment rate has risen sharply and real agricultural and industrial investment has been weakening.

The severity of the current economic downturn is reflected in employment declines in most regions of the country. Seasonally-adjusted employment in Canada peaked at about 11.0 million persons in June, 1981. By March, 1982, the number employed had dropped to 10.8

million. Excluding the effects of seasonal variation, the decline in employment over the nine-month period has already amounted to 221,000 across the country.

The effects of the recession on employment are widespread among goods-producing and service sectors of the economy. Particularly hard hit, however, are the manufacturing industries where a cyclical decline of 120,000 has occurred in the past nine months. At the same time, employment in primary industries is down by 62,000. Even service-sector industries, which traditionally provide a cushion in periods of economic slowdown, have met with reversal and have temporarily shed 39,000 jobs.

Layoffs have varied considerably among regions. For example, Quebec's employment peaked in March, 1981. By March, 1982, the job loss in Quebec had amounted to 130,000—a drop of 4.8 per cent from the peak. In Ontario, the decline from its June, 1981 peak employment was 78,000, or 1.9 per cent. British Columbia maintained its job creation well into the fall, but since that time employment has fallen by 33,000, or 2.6 per cent from its peak. While the prairie region has not suffered an actual decline, the rate of job creation has slowed considerably.

Regional Job Creation Since 1981 Peak[1] — Table 5
(seasonally adjusted)

	(thousands)	(per cent)
Atlantic Provinces	−16	−1.9
Quebec	−130	−4.8
Ontario	−78	−1.9
Prairie Provinces	10	0.5
British Columbia	−33	−2.6

Source: Statistics Canada, *The Labour Force.*
[1]From regional peaks in 1981 to March, 1982.

These differences among regions and sectors are due to the nature of the prevailing recessionary forces. The principal reasons for the current downturn are the drop in U.S. economic activity, escalating energy prices, and abnormally high interest rates. Each of these factors exerts its impact unevenly across the country. For example, declining output in the U.S. hits the export sectors of Ontario, Quebec, New Brunswick and British Columbia relatively harder than those of the prairie provinces. By the same token, rising energy prices have strong adverse effects on the petroleum "importing" regions of central and eastern Canada and positive impacts on the western provinces. Combined, the U.S. recession and higher energy prices are imposing a relatively greater burden on central and eastern regions than on the west. With regard to interest rates, the dampening effects are widely distributed across regions and industries. Nonetheless, there is a tendency for the reduction in output to be slightly above the national average in Ontario, Alberta and British Columbia.[9]

As Table 5 reveals, however, while the Ontario economy has suffered a considerable employment loss relative to its peak employment base, its performance has been favourable compared with most other regions. The impact of the recessionary forces outlined above is blunted in the aggregate because of the overall balance in Ontario's economy between resource, service and manufacturing sectors.

III Ontario Job-Creation Policy

Job Creation: A Priority for Ontario

> "Throughout the 1970s, the social imperative in Canada was to create jobs. It is the Ontario view that sustaining and creating employment should continue to be the nation's highest priority".[10]

Over the past five years, the average annual rate of growth of the labour force was 2.9 per cent in Canada and 2.7 per cent in Ontario. By contrast, in most other industrial jurisdictions, the number of people looking for employment was increasing at a much lower rate. In the case of West Germany, the labour force grew at an average rate of

Labour Markets, 1975 to 1981 — Table 6
(average annual rates)

	Labour Force Growth	Employment Growth
	(per cent)	
Canada	2.9	2.8
Ontario	2.7	2.7
United States	2.5	2.6
United Kingdom	0.2	−1.0
Japan	1.2	1.1
Germany	0.3	0.2

Sources: Statistics Canada, *Historical Labour Force Statistics;* and U.S. Department of Labour, *International Comparisons of Unemployment.*

[9]For example, if real interest rates are sustained at four percentage points above normal levels for a full year (as was generally the case in 1981) it is estimated that real output in Canada would be reduced by approximately 0.86 percentage points over the same period. The drop in provincial Gross Domestic Product (GDP) in Alberta, Ontario and British Columbia could be in the range of 0.88 to 0.96 percentage points while the reduction in the Atlantic provinces, Manitoba and Saskatchewan might be in the order of 0.78 percentage points. The industries most sensitive to credit costs include motor vehicles and parts, machinery and transportation equipment and construction. The impact on service sectors is smaller, although still quite significant. These are simulations of increases in domestic real interest rates and do not take into account the added decline in employment and output that results from similar real interest rate increases in Canada's export markets.

[10]Hon. William G. Davis, *op. cit.*

0.3 per cent in the 1975 to 1980 period — one-ninth the rate of growth of the Ontario labour force.

Faced with the challenge of a rapidly growing labour force, Ontario maintained an impressive job-creation record compared to other major industrial jurisdictions. From 1975 to 1981, Ontario's economy generated 610,000 new jobs, including 167,000 in the manufacturing sector.

The Ontario Government's job-creation strategy has concentrated on creating the confidence and the atmosphere needed to encourage private sector investment in Ontario. Indeed, 97 per cent of the employment growth in Ontario between 1975 and 1981 has been in the private sector.

As a measure of the Province's overall success in creating jobs, Ontario's rate of employment growth matched or exceeded the rates in OECD countries, including Germany and Japan. Despite a higher rate of growth in the number of job seekers, Ontario's unemployment rate averaged below that in the United States.

Long-Term Approach

Ontario is going through a period of transition in both its industrial structure and its labour force. Microelectronic technology and energy price increases have brought about fundamental changes in the goods and services people consume and the technology used to produce them. Demographic and social change will result in slower labour force growth, a decreased number of young workers and a growing number of female workers.

The combined effect of a changing industrial structure and changes in the composition of the labour force places a premium on the capacity of the economy to adapt to new circumstances. It is also important to influence the direction of economic change towards those areas in which Ontario can build or develop a competitive advantage. This is the role of the BILD program as outlined in the document *Building Ontario in the 1980's.*[11] This program was designed to:

- create an environment in which enterprise can flourish and generate opportunities for investment and employment; and,
- equip Ontario citizens with the skills needed to seize the opportunities.

To this end, a significant portion of the BILD program is being directed toward the development of the economic infrastructure needed to maintain and build upon Ontario's comparative advantages

[11]Hon. William G. Davis, *Building Ontario in the 1980's*, Board of Industrial Leadership and Development (Toronto, 1981).

and to overcome the difficulties associated with a high degree of dependence on expensive energy sources.[12]

BILD identified Ontario's strengths in the province's extensive transportation and communication networks, wealth of natural resources, capacity to produce electrical energy and in the social fabric of communities. These areas have been the target of BILD's development strategy along with the promotion of technology and, most importantly, an increased investment in the training and education of Ontario's people.

The BILD program is meant to reinforce Ontario's success in creating jobs in the private sector. The program is a joint private sector-public sector initiative that focuses on areas commonly agreed upon as essential for long-term economic development in the province.

A fundamental principle in the BILD strategy is the recognition that investment in human resources is a key to future economic development. Innovation, entrepreneurship and industry flourish where there is a highly-educated and skilled workforce. The long-term employment strategy is to ensure that investments in human and physical capital are undertaken that will provide Ontarians with enduring and enriching job opportunities.

Immediate Job Creation

The solid job-creation performance in Ontario continued into 1981 despite the international economic downturn. The 120,000 jobs created in 1981 were based on particularly strong growth in the first half of the year. However, job creation slowed in the second half and then turned negative at the end of the year.

In response to the federal budget, Ontario warned of the deteriorating state of the economy.[13] Again, at the February, 1982 Conference of First Ministers on the Economy, Ontario recommended that federal and provincial governments should review options for immediate stimulus to the economy.

Although the Ontario economy has been experiencing a cyclical downturn, the prospects over the next twelve months are more promising. Later this year, a recovery is expected to begin as a result of a modest rebuilding of inventory and an improving trade performance as the U.S. economy recovers. Nonetheless, the Government of Ontario believes that there is a need for measures both to speed this recovery and to address current hardships. Since the federal gov-

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[12]For a progress report on the activities of BILD see Hon. Frank S. Miller, *BILD: This is what was done in the first year,* Board of Industrial Leadership and Development (Toronto, 1982).

[13]Hon. Frank S. Miller, *A Program for Restoring Confidence in the Canadian Economy, op. cit.*

ernment has failed to respond with a decisive and comprehensive set of programs, the Government of Ontario has decided to implement new job-creation initiatives of its own.

In developing these measures, the Province is constrained by the current international and domestic environment. Clearly, a reduction in interest rates would be more effective in creating jobs than any measures within the Province's power. As long as interest rates remain at high levels, fiscal measures, particularly at a provincial level, cannot be totally effective. Therefore, the Government of Ontario will continue to urge the federal government to work toward a reduction of real interest rates in Canada.

High interest rates, however, are not the only constraint. Even for a large province such as Ontario, the openness of the provincial economy reduces the effectiveness of generalized tax cuts to stimulate domestic demand. Furthermore, export industries must await the recovery of foreign markets. The Province is also constrained by its limited fiscal capacity to provide general stimulus. In addition to the fiscal pressures directly induced by recession, the Province faces higher debt-servicing charges, higher prices for petroleum products and, most importantly, a significant reduction in federal transfer payments.[14]

Since 1975, Ontario has been making a determined effort to control expenditures and constrain the deficit. The Province has recognized, however, that its targets for reducing the deficit would need to be modified in the light of changing economic conditions. A 1977 Budget Paper noted that "Future weakness in the economy would automatically increase the deficit as revenues fell below projected yields. As well, stimulation in the form of tax cuts and selective expenditure increases may be required. . .".[15]

Now is such a time. In the current economic circumstances, an unrealistic continuation of the deficit reduction strategy could act as a further drag on the economy and undermine, rather than restore, economic confidence. Therefore, a decision has been taken to allow the Provincial deficit to rise temporarily.

In addition, the Province has chosen to accelerate its investment program in those areas where immediate job-creation opportunities exist, consistent with Ontario's long-term economic development strategy. This job-creation program will be based on the principles outlined below.

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[14]Hon. Frank S. Miller, "Fiscal Federalism in Canada: The Record to Date The Challenge Ahead", Budget Paper B, and "Public Investment and Responsible Financial Management", Budget Paper C, *Ontario Budget 1982* (Toronto: Ministry of Treasury and Economics, 1982).

[15]Hon. W. Darcy McKeough, "Towards a Balanced Budget", Budget Paper C, *Ontario Budget 1977* (Toronto: Ministry of Treasury, Economics and Intergovernmental Affairs, 1977).

Complementing Federal Programs

Provincial job-creation programs have been designed to complement federal employment measures, not only to avoid unnecessary duplication but also to make the activities of both levels of government more effective. The success of job-creation programs, particularly those aimed at the private sector, depends on a high degree of public understanding and cooperation. Uncoordinated or competing programs launched by either the Provincial or the federal government would create confusion in the public mind and undermine the effectiveness of both governments' efforts. The Accelerated Forest Improvement Program agreed to by Ontario and the federal government is an example of successful cooperation between governments.

Targeting Regions, Industries and Demographic Groups

Ontario's employment programs have been designed to take into account that unemployment in the province has hit certain regions, sectors and groups of workers heavily. In some industries and communities there is little immediate prospect for alternative employment. For example, forestry workers in Northern Ontario have been seriously affected by the U.S. recession. In addition, young workers face particular difficulties during an economic downturn.

Providing Economically and Socially Useful Jobs

The response to the unacceptable costs of unemployment must not in itself be wasteful. The job-creation effort of the Province has been directed to projects and activities that have enduring social and economic value. This has been achieved by linking employment projects through BILD to areas identified as development priorities. In addition to the other basic principles in the Ontario job-creation program, emphasis has been given to projects that:

- husband and develop Ontario's natural resources;
- enhance and enrich Ontario's communities;
- strengthen the province's human resources, particularly its youth; and,
- contribute to the development of the province's economic infrastructure.

Timing the Impact of Job-Creation Measures

In recognition of the current unemployment and the likelihood of recovery later this year, job-creation programs must be able to start quickly. The present employment initiatives have, therefore, been designed to yield their maximum impact immediately.

The job-creation package is outlined below.

Cooperative Employment Fund

Since 1978, Ontario has been calling for the innovative use of Unemployment Insurance (UI) funds to create jobs. This was accomplished for the first time, earlier this year, in the Accelerated Forest Improvement Program. Under this arrangement, the Province allocated $4.5 million to permit laid-off forestry workers to be recalled to work on forest management projects. Workers are paid $240 per week in UI benefits plus a $60 Provincial supplement. In addition, the Province pays employee benefits and the cost of necessary equipment and materials.

Ontario has created a new fund to participate with the federal government in further job-creation projects of this kind. For example, the Ontario share of the recently announced Mining Special Employment Program will be financed out of this fund. In addition, the Province has already prepared a proposal to expand the Accelerated Forest Improvement Program. A number of other proposals in various sectors are now being developed.

These projects are designed to achieve a number of objectives: complement federal initiatives; target on regions and industries experiencing high unemployment; and, contribute to Ontario's economic development.

Public Sector Investment

The public infrastructure of the province is an essential underpinning to long-term economic development. Many projects involving the building, renovation and repair of essential provincial facilities have been planned as part of the Province's long-term capital program. In addition, municipalities, school boards, universities and colleges have a backlog of renovation and repair projects which could proceed without delay. In order to create immediate employment, the Government has decided to bring forward labour-intensive projects in all parts of the province, with emphasis on those areas where unemployment is high. To accomplish this, the Province has developed a fund to:

- accelerate repairs and additions to government buildings and accelerate Provincial and Provincially-supported capital projects, including construction and maintenance of highways, roads, municipal bridges, and water and sewage treatment projects; and,
- pay for direct labour costs in renovation and repair projects sponsored by municipalities, school boards, universities and colleges.

Youth

Unemployment amongst youth has risen sharply in this recession. In the first quarter of 1982, the average unemployment rate for 15-to-24 year-olds in Canada was 17.5 per cent, up 2.7 per cent from the same period a year earlier. The comparable rate for Ontario was 16.3 per cent, which, although high, was below the level for Canada.

The young are at a disadvantage in labour markets during a recession. When firms are forced to reduce operations, it is usually young workers who are the first to be laid off and the last to be recalled. In addition, youth looking for work for the first time are at a special disadvantage when competing with experienced, older workers in a weak job market.

Therefore, as indicated in the Speech from the Throne, the Government is increasing total funding for youth employment programs with an added emphasis on out-of-school youth suffering from long-term unemployment.[16]

Natural Resources

In addition to participating in the Accelerated Forest Improvement Program and the Mining Special Employment Program, the Province will expand its natural resource programs in three areas of long-term importance. New projects to expand tree nurseries, construct resource-access roads and improve Ontario's sport and commercial fisheries will create needed short-term jobs and contribute to the strengthening of the Province's resource sector.

Agriculture

The long-term well-being of the agricultural sector is a continuing priority in Ontario. To meet this concern and, at the same time, broaden the scope of the Provincial job-creation program, the Government will increase 1982 funding for tile drainage, and will introduce a Farmstead Improvement Program. The additional funding for tile drainage will enable more of Ontario's farmland to be improved, thereby enhancing the productivity of the agriculture sector. Other initiatives will upgrade farm facilities for long-term benefit.

Housing

Housing starts have fallen significantly, with the result that direct employment in the construction industry has suffered. Unemployment in the industry is at a disproportionately high level. As well, employment in related industries ranging from forest products to appliances and furniture has fallen. Stimulus to residential construction will provide a very substantial direct and indirect employment effect in the province. Moreover, leakages from this sector into foreign demand are smaller than is the case with other industries. Therefore, the Province will

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[16]Ontario youth employment programs are: Experience '82, Junior Rangers, Ontario Career Action Program (OCAP), Ontario Youth Employment Program (OYEP), Youth Counselling, Regular Summer Replacement, Co-op Student Hiring, Student Training in Industrial Relations (STIR) and Involvement in Municipal Administration (IMA). For more detail on these programs see Ontario Youth Secretariat and Canada Employment and Immigration Commission, *Employment Programs and Services for Ontario's Youth, 1982.*

undertake a program to support the housing sector. This program will create jobs, encourage new construction and free up rental accommodation.

Small Business

A healthy small business sector is a prerequisite for a balanced economic recovery. These businesses rely heavily on Canadian suppliers of materials, components and business services and they are a key outlet for entrepreneurship and innovation. Most important of all, labour-intensive small businesses are a principal source of employment growth. A number of recent studies point to the crucial importance of this sector in economic development. At the recent First Ministers' Conference on the Economy, the Premier of Ontario asserted the high priority of small business development.[17]

Therefore, the Province has chosen to focus a major tax incentive on this sector. By eliminating the corporate income tax on small business income for two years, Ontario is making a fundamental move to set the stage for province-wide job creation and to strengthen the small business sector in the province. This is in recognition of not only the serious adverse impact that the current recession is having on small business, but also the crucial role that small business plays in the process of economic development and Canadianization of the economy.

IV Restoring the Canadian Economy

Full recovery from the international and domestic downturn requires a number of government initiatives beyond the control of the Province. One of the first issues that must be addressed by the international community is the reduction of real interest rates. In this regard, the United States must arrive at a resolution of its budgetary difficulties. A strong recovery of the U.S. economy will go a long way in alleviating the economic problems currently besetting Canada.

Meanwhile, it is imperative tha. the federal government undertake interest rate policies that do not inflict undue hardship or long-term structural damage on the Canadian economy. There are alternative measures for combating inflation and, in this regard, Ontario has recommended specific initiatives.[18]

Canadian economic policy must also enable Canadians both to participate fully in a U.S. recovery and to make the most of Canada's own domestic market opportunities. This requires a framework of economic development policies such as that set out by Premier Davis at the

[17] Hon. William G. Davis, *A Blueprint for Economic Recovery, op. cit.*
[18] *Ibid.*

February, 1982 First Ministers' Conference on the Economy.[19] The Premier identified five priority areas:

- Restoring a Climate of Confidence;
- Encouraging Small Business Creation and Development;
- Increasing Investment;
- Developing Human Resources; and,
- Enhancing Trade and Export Opportunities.

Investor confidence is the key to economic recovery. Canada's fiscal policies and its regulatory policies must reflect the sensitivity of international capital flows to changes in the rules of the game. As Canadians have learned in the past year, large outflows of capital can have immediate and powerful effects on economic prosperity and the ability to pursue national goals.

The small business sector and the development of human resources should be central components of Canada's economic strategy. Moreover, these priorities are consistent with the objectives of increasing investment and enhancing trade and export opportunities, especially in fully-manufactured and high-technology goods.

Conclusion

The new policies outlined in this Budget Paper are not a replacement of, nor a departure from, Ontario's long-run strategy of economic adjustment and innovative development. Nor are they meant to be a total solution, either alone or as a package, to current economic difficulties. They are an immediate response to an immediate problem — a response that will help restore the climate of confidence that is vital to an economic recovery.

[19] *Ibid.*

Budget Paper B

Fiscal Federalism in Canada:
The Record to Date
The Challenge Ahead

Table of Contents

Introduction 3

I The Record of Federal Retrenchment 4
- Health Care Funding 4
- Post-Secondary Education Funding 5
- The Revenue Guarantee 5
- Indexation 6
- Established Programs Financing 7
- The Social Services Financing Act 7
- The Community Services Contribution Program 8
- Other Reductions 8
- Equalization 8
- The 1982 Fiscal Arrangements 9
- Federal "Generosity" 10
- The "Provincial Appetite" 11

II The Facts on Fiscal Imbalance 13
- Federal-Provincial Balance 13
- Interprovincial Imbalance 17

III The 1981-82 Fiscal Negotiations 24
- The Shares Question 24
- Provincial Underfunding 27
- Program Quality 31
- Equalization and Fiscal Disparities 33
- The Negotiating Process 36

IV An Agenda for the 1980s 39

Conclusion 43

Appendix 46

Fiscal Federalism in Canada: The Record to Date The Challenge Ahead

Introduction

In 1980, the Government of Canada began to adopt a more aggressive approach to the conduct of federal-provincial relations. Breaking tradition, it indicated its determination to proceed unilaterally on both the constitutional and energy issues if it could not secure early agreement with the provinces. This new aggressiveness is now being felt in the field of intergovernmental finance. Recent events and policy statements suggest that the federal government is embarking on a deliberate and continuing program of reductions in transfer payments to provinces. They also suggest that the federal government is preparing for new thrusts into provincial spending areas, with savings from the intergovernmental transfer system being used to finance these new initiatives.

The Prime Minister's reflections on "the new federalism" reveal the foundations of the emerging federal strategy.[1] In his view, the Government of Canada has been very generous toward the provinces, but provinces have responded with a lack of gratitude, a lack of co-operation in meeting federal goals and a continually growing appetite for more federal support. He also maintained that, as a result of federal generosity, the "pendulum" has swung too far in the direction of fiscal decentralization, with the result that the national government's ability to manage the economy and fund its own programs is now in jeopardy.

This paper challenges the federal interpretation of what has happened in Canada over the last decade. The first two sections look in detail at the fiscal record. It is argued that, far from trying to win ever larger federal transfers, provinces have sought merely to protect long-standing agreements. It is also shown that the post-war process of fiscal decentralization came to an end over fifteen years ago; there is a problem of fiscal imbalance in the federation, but it is among the provinces and regions of the country, not between the two orders of government. Section III examines the recent discussions on revised fiscal arrangements, setting Ontario's concerns about the process and outcome within the broader context of the issues that are emerging for the 1980s. The paper concludes with a number of suggestions for improving federal-provincial fiscal relations in the future.

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[1]See Rt. Hon. Pierre Elliot Trudeau, transcript of press conference, February 25, 1982. The relevant parts of the Prime Minister's remarks are reproduced in the Appendix.

I The Record of Federal Retrenchment

During the 1950s and 1960s, provinces were in an expansionary phase. Their expenditures grew rapidly in response to the new demands for highways, education and health care. The federal government recognized the fiscal pressure on provinces and took major initiatives to enlarge provincial revenues through the transfer of unconditional income tax points, enlarged equalization payments and the introduction of major shared-cost programs in the field of social policy. These arrangements represented a partnership between the two levels of government in Canada. The federal government had the necessary financial resources and the provinces had the responsibility for expanding programs which were recognized by all as being national priorities. In agreeing to participate in these major national programs, generally at the urging of the federal government, the provinces took a considerable risk. They left themselves exposed to major cost increases while relying on the assurance of the federal government that it would continue to be a partner in these undertakings.

During the 1970s, the federal-provincial partnership became increasingly strained as the federal government began to cut back on its earlier commitments. The provinces were increasingly put on the fiscal defensive and were forced to argue, not for more, but merely for a continuation of existing federal support. This section documents the history of federal retrenchment during the last decade.

Health Care Funding

With the federal imposition of Medicare on the provinces, significant expenditures were shifted from the private into the public sector. Ontario expressed concern about this development because it already had a very good system of private-public health insurance, and because it was well known that the federal plan had an inherent tendency toward cost escalation. Ontario was nevertheless levered into joining by the Social Development Tax that the federal government levied on all taxpayers, regardless of whether or not their province participated in the plan.

No sooner had provinces joined than the federal government began to worry about rising costs and its promise to share fifty per cent of provincial expenditures. In fact, as early as May 1970, the President of the federal Treasury Board was suggesting "short run national targets should be set for the purpose of limiting the rate of growth of expenditures on hospital and medicare programs and higher education".[2] Throughout the decade, the federal government's attempt to constrain

[2]Letter, Hon. C. M. Drury to Hon. Charles S. MacNaughton, May 15, 1970.

the growth of its contributions was the central feature of all health care discussions.[3]

The provinces shared the federal concern over rising health expenditures and tried to co-operate with the federal government in working out mutually satisfactory solutions. In September 1974, provinces took a major initiative by indicating their willingness "to negotiate changes in cost sharing of high-cost services in exchange for federal sharing in programs not now supported". In response to this offer, a federal-provincial task force was established to examine more flexible ways of funding health care within the context of the existing legislative authority. This exercise in co-operation was brought to an abrupt end in the spring of 1975 when the federal government unilaterally capped its Medicare contributions.[4] At the same time, the federal government served notice of its intent to terminate its cost-sharing commitments under the Hospital Insurance and Diagnostic Services Act in 1980, the earliest date possible, thereby signalling its resolve to make program changes without provincial consent if agreement could not be achieved through negotiation.

Post-Secondary Education Funding

In 1972, the federal government legislated a 15 per cent growth cap on the post-secondary education support program introduced only five years earlier. Moreover, it renewed the program for only two years, indicating its desire to introduce new financing mechanisms. In May 1973, the Secretary of State proposed to convert the existing program to a system of per capita entitlements based on the size of the 18-24 age group in each province, with an escalator of only seven per cent per annum. Had provinces accepted this proposal, their post-secondary transfers over the 1974 to 1976 period would have been $396 million less than they turned out to be. It was only when provinces resisted this federal plan that the capped 15 per cent program was extended to the end of 1976. The cap is estimated to have cost provinces $248 million.

The Revenue Guarantee

The year 1972 also saw the introduction of the Revenue Guarantee. This program was designed to encourage provinces to parallel the 1972 federal income tax reforms by guaranteeing that their revenues during the ensuing five years would be no less for having done so. The Guarantee gave rise to two distinct episodes of federal retrenchment during the 1970s.

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[3]In 1971, the federal government first proposed constraining the growth of its health care contributions to the rate of growth of the national economy (GNE). This objective was realized in 1977 with the use of a GNE escalator under Established Programs Financing.

[4]The ceilings on the growth of federal Medicare contributions became progressively more stringent through time. The 1975 federal budget announced a per capita Medicare ceiling of 13 per cent for 1976-77, 10.5 per cent for 1977-78 and 8.5 per cent for subsequent years.

The first occurred in April 1976 when, without prior consultation, the federal Minister of Finance announced a major change in the method of calculating Guarantee payments in respect of the 1974, 1975 and 1976 personal income tax. The formula change is estimated to have saved the federal government nearly a billion dollars for the three years in question. Provinces took great exception to both the magnitude of this cut and the fact that the change was made in respect of years that had already passed.

A second disagreement concerned termination. The federal government argued in 1976 (as it has again recently) that the Guarantee offered a "breathing space" during which provinces were to have adjusted to the reformed income tax regime by raising their rates.[5] This argument overlooks the fact that original federal estimates had promised no long-term provincial revenue losses from the tax reforms, while annual losses reached almost $1 billion by 1976, even under the adjusted methodology. It also ignores a clear commitment by the Minister of Finance in 1973 to consult with the provinces on concrete proposals to replace the Guarantee when it reached its 1976 termination date. Near the end of the 1976 fiscal negotiations, the federal government finally offered provinces one point of personal income tax plus the national average cash equivalent, to be subsumed into Established Programs Financing (EPF). This offer equalled about 40 per cent of what the Revenue Guarantee was worth in 1976, and was made conditional on provinces agreeing to forgo the generous Hospital Insurance cost sharing to which they otherwise would have been entitled through to mid-1980. The *quid pro quo* was reluctantly accepted, but left provinces to absorb significant losses associated with the 1972 federal tax reform at the same time they were assuming large fiscal risks under EPF.[6]

Indexation

In 1973, the federal government introduced provisions for the inflation-indexing of the income tax system. The provinces were not

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[5]Provinces were required in the first year of the Guarantee to set their taxes at specified "conversion" rates; in 1973 and 1974, the federal government urged provinces not to increase their taxes because this would counteract the stimulative policies being pursued by the national government. The federal argument that provinces had five years in which to adjust is therefore overstated.

[6]An historical comparison of increases in GNP and increases in health and post-secondary education spending demonstrates the extent of the risk assumed by provincial governments.

	GNP Growth	Health and PSE Spending Growth
	(%)	(%)
1972-73	11.4	12.4
1973-74	17.4	11.9
1974-75	19.4	22.7
1975-76	12.1	23.6
1976-77	15.5	14.6
Compound average	15.1	16.9

consulted in advance and Ottawa refused to extend the Revenue Guarantee to this important change in the tax structure. As a result, the measures imposed a very significant cost in terms of forgone provincial revenues. Indexation is estimated to have cost Ontario over $1.6 billion in 1980 alone. The Ontario Government supports the principle of indexation, but notes that the common income tax form leaves Ontarians largely unaware of the significant benefits they receive as Provincial taxpayers under indexation and other federal reductions in the shared tax base.

Established Programs Financing

The federal government and the provinces negotiated a new financing arrangement for health care and post-secondary education, effective April 1, 1977. The essence of this arrangement was that provinces were given greater program flexibility through blockfunding, while the federal government relieved itself of all financial risks by tying its contributions to the rate of growth of the national economy rather than to provincial expenditures. The federal government fully acknowledged that it was encouraging provincial spending restraint in these programs. For example, Prime Minister Trudeau stated clearly that the EPF program

> ". . . suits the current and future imperative, namely fiscal restraint, in that Provinces will have a greater incentive to implement what are admittedly difficult measures to restrain spending in these fields to reasonable levels".[7]

He also made it clear that, from his point of view, EPF was "an important step forward in federal-provincial co-operation to the advantage of the people of Canada".

The Social Services Financing Act

In 1978, the federal government moved to undo the EPF arrangement that had been legislated less than eighteen months earlier. As part of the well-publicized federal restraint exercise in the fall of that year, the Minister of Finance proposed to shave two percentage points off the GNE escalator used under the program. Provinces refused to give the required consent for this change. Consequently, the federal government cancelled the so-called "enrichment factor" under the proposed Social Services Financing Act (SSFA), important legislation that would have led to the blockfunding of a portion of the Canada Assistance Plan. This restraint measure effectively scuttled the SSFA and nullified many years of co-operative effort to reach a federal-provincial agreement.

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[7]Rt. Hon. Pierre Elliot Trudeau, *Statement to the Federal-Provincial Conference of First Ministers*, December 13, 1976.

The Community Services Contribution Program

In early 1978, the federal government announced a new Community Services Contribution Program (CSCP) to replace three existing federal support programs for water and sewerage projects and neighbourhood improvement. On a national basis, the program was to be worth $150 million in the first year and $250 million in each year thereafter. In the midst of ongoing discussions, the federal government announced that the program would be delayed for one year as part of its restraint exercise. This resulted in immediate financing problems for provinces and municipalities. Then, in the fall of 1980, the federal government abruptly and unilaterally cancelled the program entirely, despite an unambiguous commitment to negotiate a long-term funding arrangement with the provinces.[8] This drastic step was difficult for provinces to understand because the CSCP had been carefully designed to give the federal government a great deal of visibility for its financial contribution.

Other Reductions

The year 1978 also saw a major reduction in the Public Utilities Income Tax Transfer, under which the federal government rebated to provinces 95 per cent of the federal corporate income tax paid by privately-owned utilities. Although this transfer was reinstated at the 95 per cent level in 1980, the restraint measure nevertheless presented cash flow difficulties. A number of other transfer programs have been capped or reduced since 1977. The Official Languages program is just one significant example. The so-called "formula payments" under this arrangement have been capped at $140 million per annum, nationally, since 1979.

Equalization

Canada has had a formal equalization program since 1957.[9] The transfers under this program enable the fiscally deficient provinces to provide public services comparable to those elsewhere in the country, without having to resort to unduly high taxation. The program has often been described as the hallmark of fiscal federalism in this country.

The equalization program nevertheless affords further proof of federal retrenchment. The formula was significantly enriched in 1973 by the inclusion of school property tax revenues, but this improvement in revenue coverage was negated almost immediately by the

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[8]Clause 5 of the Canada-Ontario Agreement read as follows:
"Canada and the Province agree that prior to December 31, 1980 they will endeavour to replace this Agreement with a new Agreement that provides long-term certainty to the Community Services Contribution Program . . .".

[9]For a description of equalization and Ontario's views on the program, see Hon. Frank S. Miller, "Equalization and Fiscal Disparities in Canada", Budget Paper A, *Ontario Budget 1980* (Toronto: Ministry of Treasury and Economics, 1980).

changed treatment of oil and gas revenues, however necessary that change may have been from a strictly financial point of view. In 1978, the federal government announced that the revenue from Crown lease sales would be phased out of the formula over a two-year period; the cumulative cost of this decision to the equalization recipients is estimated at $460 million. In 1981, a per capita income "override" was legislated retroactively to preclude Ontario from over $1.6 billion in equalization to which it otherwise would have been entitled during the 1977-78 to 1981-82 period.[10] Ontario accepted that its "entitlements" had arisen as a result of an inappropriate treatment of resource revenues in the formula, and agreed not to contest its arbitrary exclusion provided that steps were taken toward fundamental reform of the program in 1982. This stands as a clear example of co-operative and responsible policy; it is a far cry from the irresponsible attitude of which Ontario and other provinces have been accused.

The 1982 Fiscal Arrangements

The recent amendments to the Federal-Provincial Fiscal Arrangements and Established Programs Financing Act continue the long-standing pattern of federal reductions in transfers to provinces. The Revenue Guarantee compensation built into EPF as part of the 1977 agreement was arbitrarily removed, at a five-year cost to provinces of $5.3 billion. In addition, the so-called "fiscal dividend"[11] to certain provinces was eliminated, for a five-year federal saving of over $500 million. Table 1 displays the distribution of the EPF reductions by province. The EPF cutbacks will cost Ontario $287 million in 1982-83 and $1.9 billion over the next five years. The growth in this Province's total EPF entitlements going into 1982-83 will be only 5.3 per cent, far below the rate of inflation and completely out of tune with the fiscal realities of health and post-secondary education financing.[12]

[10]Federal legislation to exclude Ontario was initially introduced in February 1978, but died on the Order Paper. A change in the equalization Regulations was then made on a temporary basis to avoid paying Ontario. When the formula "override" was finally passed, the equalization Regulations were changed back. The override said that, regardless of the formula results, a province was not entitled to equalization if its per capita personal income was regularly above the national average.

[11]Under EPF, provinces received a formula-determined amount of "basic" cash, plus 13.5 equalized personal income tax points and 1 equalized corporate income tax point, plus a "transitional" cash payment to ensure that the value of the vacated tax room equalled the value of the basic cash. For certain provinces, a "fiscal dividend" (or negative transitional payment) arose because the value of their tax room came to exceed the value of their basic cash. This meant that they received larger federal contributions per capita than other provinces. Starting in 1982-83, cash payments will be determined by simply subtracting the value of the equalized tax room from twice the "basic" cash (appropriately adjusted to remove the Revenue Guarantee compensation).

[12]See Chart 3 on page 20 for the transfer growth of all provinces.

The Province's EPF cash entitlement from the federal government in 1982-83 will actually drop in absolute terms by $70 million.

In addition, the Act provides for a new equalization formula. The old system based on a national average standard of revenue-raising capacity has been replaced by a new system based on a "representative average standard" of five provinces. The new formula is discussed in a subsequent section of the paper. Ontario agrees that the old formula had to be replaced, for both conceptual and financial reasons. It is nevertheless worth observing that the change saves the federal government about $290 million in 1982-83 compared to what it otherwise would have been required to pay. Following the budget, it became clear that the federal government was locked-in to addressing the problems of the old equalization formula through a change in the national average standard, and little interest was shown in the alternative approaches suggested by provinces or the Economic Council of Canada.

Estimated Impact of EPF Amendments on Provincial Revenues — Table 1
($ million)

	1982-83	1983-84	1984-85	1985-86	1986-87	5-Year Total
Nfld.	−19	−21	−24	−27	−31	−122
P.E.I.	−4	−5	−5	−6	−7	−27
N.S.	−28	−32	−36	−41	−46	−183
N.B.	−23	−26	−30	−34	−38	−151
Que.	−213	−240	−272	−307	−343	−1,375
Ont.	−287	−323	−367	−415	−465	−1,857
Man.	−34	−38	−43	−48	−54	−217
Sask.	−32	−37	−42	−47	−53	−211
Alta.[1]	−178	−195	−205	−216	−230	−1,024
B.C.[1]	−117	−131	−131	−140	−158	−677
All Provinces	−935	−1,048	−1,155	−1,281	−1,425	−5,844

Sources: Ontario Treasury; Department of Finance.

[1]Amounts include losses of $563 million in respect of the 'fiscal dividend':

Alta.	102	107	103	98	94	504
B.C.	25	25	9	—	—	59

Federal "Generosity"

The many transfer reductions listed above have not been offset by new federal contributions elsewhere in the intergovernmental fiscal system. There have been no unconditional income tax transfers to provinces since 1966. The 1970s saw not one dramatic funding initiative comparable to the introduction of the Canada Assistance Plan, the Post-Secondary Education financing program or Medicare, all of which occurred in the mid-1960s. In fact, there has been a significant reduction in the average rate of growth of federal transfers to the provinces. Data prepared for the Parliamentary Task Force by the Department of Finance shows that, in the 1967-72 fiscal arrangements period, tax and cash transfers rose on average by 21.7 per cent per year; in the 1972-76 period they averaged 16.8 per cent; and in the recently concluded 1977-82 period they increased by just over 11 per cent.[13] As documented in the 1981 Ontario Budget, federal transfers as a whole grew at a substantially lower rate than total federal spending during the 1972 to 1976 period, and continued to grow more slowly, on average, during the 1977 to 1982 period.[14] The evidence for the 1970s simply does not support the claim of increased federal generosity in the area of intergovernmental transfers.

The past decade did see frequent promises of federal funding that never materialized. For example, during the 1974 federal election campaign, Prime Minister Trudeau committed his government to generous grants and cost sharing for the development of new urban transportation systems. Ottawa offered to pay 25 per cent of the capital cost incurred by Ontario or its municipalities for the purchase of buses, streetcars and subway cars; 50 per cent of the cost of commuter train stations, platforms and related facilities; and 100 per cent of the cost of rolling stock required for commuter train services. Virtually none of this assistance has ever materialized. Since the offer was made, the Province and its municipalities have spent over $1 billion on these activities without any federal support.

Another example was Prime Minister Trudeau's statement at the February 1982 First Ministers' Conference that he had "enriched" the federal government's fiscal arrangements offer by $1 billion over five years. Documentation subsequently released by the Department of Finance confirmed the provinces' interpretation that all but $77 million of this increase would have occurred anyway, simply as a result of the impact of new population estimates on the original budget proposals. In short, a misleading comparison was used to create the impression that the federal government had made major financial concessions to the provinces.

The "Provincial Appetite"

The record of federal-provincial conferences in the 1970s does not reveal a pattern of "exorbitant" provincial claims on the federal treasury. The most recent provincial request for an unconditional transfer of income tax room was Ontario's proposition linking phased

[13]See Hon. Allan J. MacEachen, *Federal-Provincial Fiscal Arrangements in the Eighties* (A Submission to the Parliamentary Task Force on the Federal-Provincial Fiscal Arrangements) April 23, 1981, page 31.

[14]See Hon. Frank S. Miller, "Renegotiation of Federal-Provincial Fiscal Arrangements", Budget Paper B, *Ontario Budget 1981* (Toronto: Ministry of Treasury and Economics, 1981).

tax transfers to a program of economic recovery, put forward in 1973, fully nine years ago.[15] All subsequent tax point proposals were put forward in the context of equal-cost alternatives to traditional cost sharing for the mature social programs.

In the 1976 federal-provincial negotiations on EPF, the provincial consensus proposal included a transfer of four personal income tax points to replace the expiring Revenue Guarantee. This opening position already conceded about 20 per cent of what the Guarantee was estimated to be worth.

In the 1981-82 discussions, the provinces asked not for more, but for a one-year extension of the existing programs. They subsequently revised their position downward, indicating a willingness to accept a fiscal arrangements transfer ceiling of 12 per cent going into 1982-83.[16] The federal government rejected this concession and refused to change the EPF transfer reductions it had set out in its November 12, 1981 budget, despite the fact that changing circumstances were making the net position of provinces even worse than originally intended. It is simply incorrect to suggest that the provincial appetite for ever more funding was the crux of the 1982 discussions and the reason for the failure of First Ministers to reach a mutually satisfactory outcome.

To conclude, *the record does not support the federal interpretation of fiscal developments in Canada. It suggests not a history of federal generosity in the 1970s but rather a history of federal retrenchment from commitments entered into with the provinces.* The provinces have not been on the fiscal offensive, they have been on the defensive. Far from demanding more, they have sought merely to minimize their losses. Generally, all provincial claims since 1973 were put forward either in the context of equal-cost alternatives or in response to prior federal initiatives aimed at reducing intergovernmental transfers. Nor is it true that provinces as a group have been unco-operative or obstructionist. They have generally continued to work alongside the federal government, despite the latter's disconcerting tendency to sudden policy changes, financial threats and unilateral measures.

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[15]See Hon. John White, *Fiscal Policy Management and Tax Sharing Reform,* Statement to the Meeting of Ministers of Finance, January 18, 1973.

[16]The 12 per cent increase that provinces requested in 1982-83 was the same increase that the federal government said it was prepared to give, on average, over the next five years. The provincial request was therefore not unreasonable.

II The Facts on Fiscal Imbalance

Fiscal imbalance in a federation exists when one order of government or one group of provinces is chronically underfinanced relative to another owing to a constitutional mismatch between expenditure responsibilities and revenue means.

It is generally accepted that an imbalance between the two orders of government existed in Canada during the 1950s and early 1960s. The unconditional transfer of tax room to the provinces and the introduction of large shared-cost programs were among the measures adopted to rectify the situation. Between 1964 and 1966, the Tax Structure Committee of First Ministers and Ministers of Finance undertook a detailed examination of "the nature and extent of federal and provincial taxes in relation to the financial responsibilities which nowadays have to be carried by federal and provincial governments". The Committee Report, updated on several later occasions, was widely interpreted to indicate that the provincial-local sector was structurally underfunded relative to the national government.[17] The federal government chose to ignore the voluminous evidence. The provincial case for further unconditional tax transfers was rejected, and provinces were told to raise their taxes if they felt they needed more money.[18] By 1972, the issue of fiscal imbalance had become entangled with the issue of the long-term impact of tax reform on federal and provincial revenues. By the mid-1970s, the issue had pretty much passed from the federal-provincial scene, with provincial efforts being directed increasingly to the defence of existing agreements.

Recently, however, federal spokesmen have claimed that a new imbalance has emerged in the Canadian federation, with the federal government standing on the verge of losing the fiscal capacity to manage the national economy and finance its own programs. This section examines the issue of fiscal imbalance and shows that the real problem is not between the two orders of government but, rather, between the governments of the provinces which export oil and gas and those which import it.

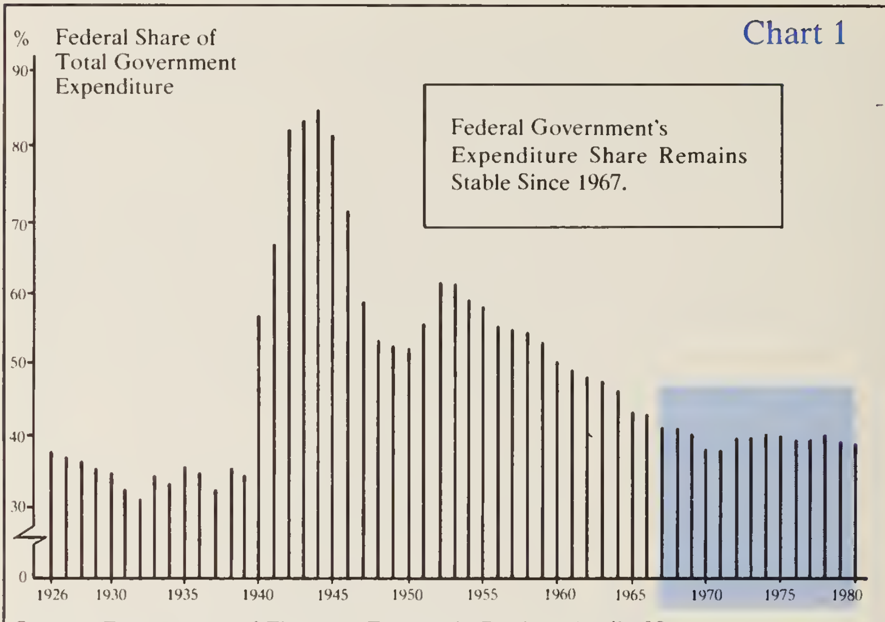
Federal-Provincial Balance

Chart 1 displays the federal government's share of total government expenditure on a national accounts basis, after adjustment for

[17]It was estimated that over the five-year forecast period, federal revenue growth would average 8 per cent and federal expenditure growth 6.5 per cent, while the provincial-local sector's revenues would grow at 7.8 per cent and its expenditures at 8.5 per cent.

[18]See Hon. Mitchell Sharp, *Statement to the Federal-Provincial Tax Structure Committee,* Ottawa, September 14, 1966.

intergovernmental transfers.[19] The federal share fell significantly through the 1950s and into the early 1960s. In 1952, it attained a post-war high of 62 per cent and then fell off continuously to reach 43 per cent in 1965. Since the mid-1960s, the federal share has remained essentially steady at about 40 per cent. The federal share in 1980 is in fact slightly larger than it was in 1970. The pendulum, to use a common analogy, is not on a swing toward decentralization; it is at rest.



Source: Department of Finance, *Economic Review*, April 1981.

It is instructive to note as well that the current federal share is by no means at an historical low. The federal share averaged about 33 per cent over the entire decade of the 1930s and, in the more prosperous 1920s, was several percentage points less than it is today.

Comparisons between different federal countries can also be made. On a post-transfer basis, the national government in Canada spends only a slightly smaller percentage of GNP than the United States national government; the significant difference in the total government shares of GNP is accounted for primarily by the greater expenditures of Canadian provinces and local governments compared to American states and municipalities. In Canada, of course, the provinces operate the national health system, a program which does not exist in the United States. The Canadian federal government spends a much greater share of GNP than the Federal Republic of Germany, even though the total government share here is actually smaller than in that country.

[19]The data on expenditure and revenue shares are reproduced in Appendix Table 1.

Comparisons with Australia suggest that our federal government's share in GNP is about the same as theirs.[20]

In short, whatever the expenditure shares may or may not mean for the structure of political power in Canada, *there is no basis in the time series data or international comparisons for concluding that the process of fiscal decentralization is continuing or that Canada is an overly decentralized federation.*

The revenue statistics reveal a similar story. The federal share of total government revenues, after transfers, reached a post-war peak of 65 per cent in 1952 and thereafter fell to 44 per cent by 1966. The large, discrete drops in the federal share during this period are explained by the previously-mentioned unconditional income tax transfers to the provinces. As noted, these transfers helped provinces finance major new national programs and returned the provincial revenue share toward what it had been in the pre-war years. Over the decade 1967 to 1976, the federal share remained essentially constant, on both a pre- and post-transfer basis. In 1977, the federal share notched down from 38 per cent to 34 per cent. It reached a low of 32 per cent in 1978, but has been trending upward in the last three years. According to the Minister of Finance, it returned to the 38 per cent level in 1981.

There are a number of technical points that need to be made about the revenue shares. For example, they are obviously affected by tax policy decisions. Over the 1970s, the federal government continuously reduced its taxes. According to the Department of Finance, the discretionary tax measures introduced since 1972 are estimated to have reduced 1979 federal revenues by 14 billion dollars.[21] In contrast, provincial tax rates in general rose during the 1970s.

A more important observation is that regional differences within the provincial sector are critical to the issue. The substantial resource levies of provinces such as Alberta impart an upward bias to the provincial revenue share (and indirectly to the expenditure share), making it a somewhat exaggerated measure of the true extent of decentralization. The Minister of Finance has defined federal-provincial imbalance in terms of "the fact that one order of government has a large and persistent deficit or surplus in its accounts in relation to that of another order of government".[22] This is a questionable definition of the problem because it overlooks the foregoing points about tax policy and the concentration of provincial surpluses in a small number of energy-wealthy provinces. Given his definition, however, it should be noted that if the federal government were to raise taxes to eliminate its deficit, and the provincial-local sector as a whole (ignoring the regional

[20]See Department of Finance, *Economic Review*, April 1980 (Ottawa: Supply and Services Canada, 1980).

[21]*Economic Review, ibid*, page 113.

[22]Hon. Allan J. MacEachen, *op. cit.*, page 8.

differences) were to lower its taxes to eliminate its surplus, the federal share of revenues would be significantly higher.

Moreover, federal revenues have been more sensitive than provincial-local revenues to the relatively slow economic growth of recent years, implying a need to distinguish between a cyclical dip in the federal share and its long-run tendency. The substantial drop in the federal share in 1977, for example, is largely attributable to the poor growth of incomes in that year. An unusual "bunching" of cash flow to the provinces also contributed to the notch in 1977.

These interpretive problems aside, the real issue is what can be expected to happen over the next few years. In early 1980 it may have been reasonable to anticipate some weakening in the overall federal share of revenues, depending on what was then assumed about oil and gas pricing and the split of energy revenues. However, the taxation regime and revenue-sharing arrangement now in place redresses that imbalance. The November 12 budget indicates that, over the 1981-82 to 1985-86 period, the federal government will receive some $51.3 billion in oil and gas production revenues, $7.5 billion more than it would have received under the 1980 National Energy Program, and enormously more than it would have had under the pre-NEP arrangements. If federal budgetary revenues as projected on November 12 are compared to the total provincial-local revenues forecast at about the same time, it is observed that the federal share remains essentially constant out to the late 1980s, despite the healthy growth in revenues expected in the oil and gas producing provinces. This conclusion is not materially affected by the recent downward adjustment in the projections of oil and gas revenue.

In short, *there has been no clear trend in the distribution of total government revenues in the past fifteen years. Nor are there grounds for expecting changes in the foreseeable future.*

Over the past year, a number of independent studies have been done on the question of fiscal balance and they all support the conclusion that there is no demonstrable imbalance between the two orders of government. The Parliamentary Task Force on Federal-Provincial Fiscal Arrangements wrote:

> ". . . there does not exist a long-term structural mismatch between the revenue capacities and expenditure responsibilities of the federal government. It cannot be claimed that the capacity of the federal government to raise revenues has reached a structural (as opposed to a political or discretionary) ceiling".[23]

The Economic Council of Canada, in its recent report entitled *Financing Confederation: Today and Tomorrow,* came to a similar conclusion, adding the important point that federal-provincial transfers

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[23]*Fiscal Federalism in Canada,* Report of the Parliamentary Task Force on Federal-Provincial Fiscal Arrangements (Ottawa: Supply and Services Canada, 1981) page 33.

have not been a contributory cause of the federal deficit and, accordingly, that there is "no compelling argument in support of the federal government's proposed reduction in net transfers to the provinces". The Council found

> ". . . no evidence that . . . a structural imbalance exists in our federal system. The mere existence of deficits at one level of government does not indicate the existence of such a structural imbalance nor does it mean that such deficits have to be rectified at the expense of another level of government".[24]

Despite the recent change in its projections of the federal deficit, the Council continues to defend its general conclusions on fiscal balance and intergovernmental transfers.

It is clear, in the view of independent advisors, that the federal government has the fiscal capacity to carry out the functions for which it is responsible under the constitution. This view is shared by the Government of Ontario. Ontario has consistently recognized the need for a fiscally strong national government, but remains unconvinced by federal arguments that the country is excessively decentralized and that the fiscal "pendulum" needs to be set in reverse.

Interprovincial Imbalance

Although there is no demonstrable problem of federal-provincial fiscal imbalance in Canada, there is unquestionably a serious and worsening problem of imbalance among the provinces. Ontario drew attention to this issue in its 1980 Budget Paper entitled *Equalization and Fiscal Disparities in Canada.* The follow-up 1981 paper, *Renegotiation of Federal-Provincial Fiscal Arrangements,* presented data on comprehensive tax base shares and indices of tax base per capita illustrating, for the 1970s, the graphic shift in fiscal capacity in favour of the oil and gas exporting provinces.[25] With the conclusion of the energy agreements between the Government of Canada and the governments of the producing provinces, it became possible to project these indices forward to 1987. Chart 2 illustrates the situation for the fifteen-year period from 1972-73 to 1986-87.[26]

The development of oil and gas resources and the associated growth and diversification of the Western provincial economies are of unquestionable benefit to Canada as a whole. The fiscal consequences, however, cannot be overlooked. Counting all resource revenues, Alberta will enjoy almost one-quarter of the total provincial-local tax base by 1987,

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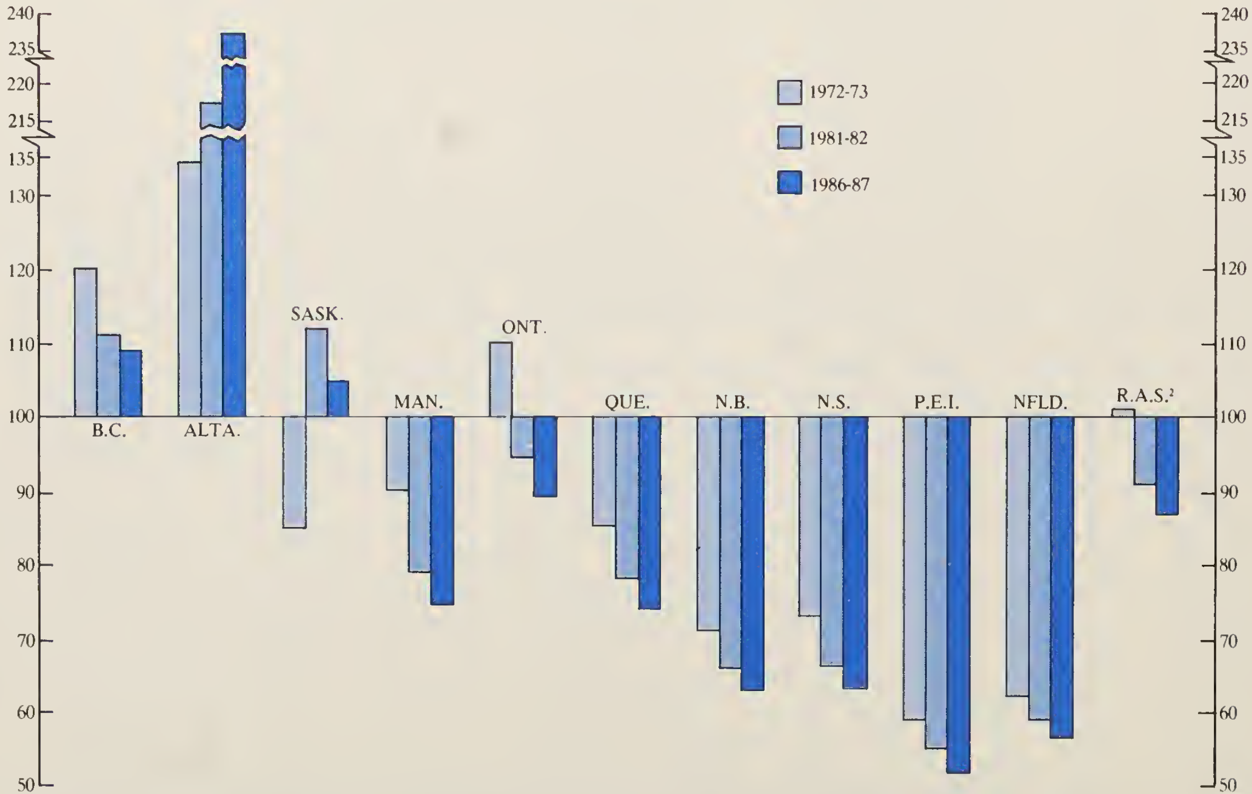
[24]Economic Council of Canada, *Financing Confederation: Today and Tomorrow,* (Ottawa: Supply and Services Canada, 1982) page 118.

[25]The fiscal capacity measures used in this paper are based on the Department of Finance data for equalization, and assume national average tax rates. For the methodology involved in constructing the indices, see the Appendix to the 1981 Ontario Budget Paper *Renegotiation of Federal-Provincial Fiscal Arrangements, op. cit.*

[26]See also Appendix Tables 2 and 3.

Indices of Tax Base Per Capita (Own Source Revenues[1]) **Chart 2**
(National Average = 100)



Source: Appendix Table 3.
[1]All provincial-local revenues included in the 1982-1986 equalization program.
[2]Representative Average Standard provinces: Que., Ont., Man., Sask. and B.C.

up from one-tenth in 1972. Its fiscal capacity in that year will be an unprecedented 137 per cent above the national average. Even ignoring resource revenues, Alberta's share would continue to rise dramatically. It is conservatively estimated that, by 1987, Alberta will enjoy well over 14 per cent of the conventional tax base, up from 8.5 per cent before the first energy price explosion in 1973. Its fiscal capacity on conventional sources alone will be at least 41 per cent above the national average. Over all the years for which data is available, Ontario's fiscal capacity never exceeded the national average by more than 20 per cent.

The implications of these massive disparities for the social and economic structure of the country are only beginning to be understood. The disparities have major consequences for the location of economic activity, the migration of population, the extent of tax competition among provinces and the provision of comparable public services across the nation. At issue are all the traditional notions of interprovincial equity. At a time when federal cuts in EPF transfers are forcing most provinces to face the choice of curtailing services, increasing taxes or expanding their deficits, Alberta, with a tax effort on conventional revenue sources 37 per cent below the national average,[27] is able to budget a 30 per cent increase in total spending, with virtually no tax increases. In the long run, interprovincial fiscal imbalance is a far greater threat to the "national standards" in the social programs than any of the provincial measures the federal government has so far singled out for criticism. Without new transfers to the energy-importing provinces, including Ontario, services will fall behind the pace and expectations being set in the wealthier provinces, at the same time that the interprovincial disparities in tax burden widen.

Very little attention was accorded this problem during the 1981-82 fiscal arrangements negotiations. Early in the process, the federal government initiated general discussions on a "code of tax conduct" to reduce the growing threat of interprovincial tax competition. Federal leadership on this important national issue soon evaporated however, and the impression was left that tax competition was a problem to be solved by provinces themselves. With regard to equalization, important structural changes were made but, as explained in Section III, the reforms were not situated within a comprehensive strategy for dealing with the new fiscal disparities created by oil and gas.

The lack of attention to the interprovincial imbalance is striking, given earlier federal statements. In his submission to the Parliamentary Task Force, the Minister of Finance said

> "... one of the issues of most concern to me when I look at the state of government finance in Canada is the high and growing spread of fiscal capacity disparities among provinces".[28]

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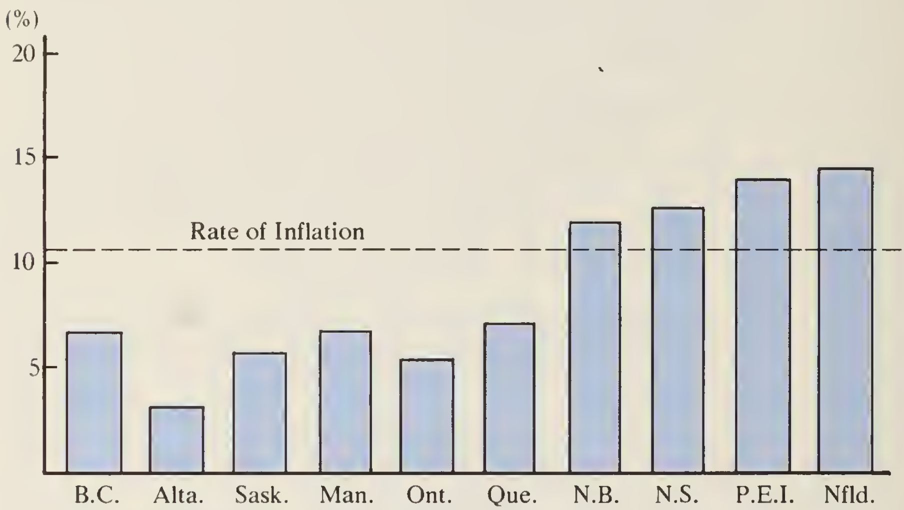
[27]See Appendix Table 4.

[28]Hon. Allan J. MacEachen, *op. cit.*, page 16.

He went on to invite the Task Force "to consider whether we can afford to allow disparities of these kinds to persist and to widen even more in the future".

In fact, it appears that the fiscal arrangements package legislated in April will actually worsen the interprovincial imbalance in the country. Chart 3 shows the 1982-83 growth that provinces will receive in their fiscal arrangements transfers. Central Canada, especially Ontario, fares substantially worse under the new legislation than either the West or the East. The westernmost provinces have the fiscal capacity to sustain the removal of the Revenue Guarantee compensation and the termination of the EPF "fiscal dividend". On the other hand, the Atlantic provinces will receive a fairly healthy increase in their transfers. While equalization has been cut back from what it otherwise would have delivered, these provinces have been cushioned by floor provisions and the effective federal write-off of sizeable 1980-81 and 1981-82 equalization overpayments attributable to high population estimates.

Rate of Growth in Provincial Entitlements for EPF plus Equalization, 1981-82 to 1982-83[1] Chart 3



Source: Appendix Table 5.

[1]Does not include the write-off of past equalization overpayments arising from census population adjustments in the Atlantic provinces and Manitoba.

The relatively harsh treatment accorded Ontario ignores the fiscal realities facing this Province. The long-term trends in provincial fiscal capacity were noted above. Ontario's relative fiscal capacity, measured in terms of provincial-local own source revenues, and excluding natural resources, will fall from 15 per cent above the national average in 1972 to 4 per cent by 1987.

It is interesting to further refine the fiscal capacity measure by taking intergovernmental transfers into account. Chart 4 graphs the effect of federal transfer payments on the relative fiscal capacity of

Indices of Tax Base Per Capita (Own Source[1] and Post-Transfer[2] Revenues, 1981-82) — Chart 4
(National Average = 100)

Source: Appendix Table 3.

[1]All provincial-local revenues included in the 1982-1986 equalization program.
[2]Total federal transfers to provincial and local governments.
[3]Representative Average Standard provinces: Que., Ont., Man., Sask. and B.C.

provinces. It shows that, as a result of the total federal transfer system, the relative fiscal capacity of the equalization-receiving provinces is greatly enhanced while Ontario's fiscal capacity drops below that of all other provinces. The Minister of Finance reported the same finding in his submission to the Parliamentary Task Force.[29] The Economic Council comes to a similar conclusion in its work on post-transfer fiscal capacity. It writes,

> "After taking account of the impact of all federal-provincial transfers, Ontario's revenue capacity was lower than, or equal to, the majority of provinces receiving equalization. Furthermore, when the effects of federal financing are taken into consideration, according to our estimates, Ontario's revenue capacity is reduced considerably more than that of provinces with "above-average" revenue capacity. This result reinforces our concern about the impact of the Equalization Program on the revenue capacity of this province".[30]

Appendix Table 4 presents associated information on relative provincial tax effort. In 1981-82, the provincial-local tax effort in Ontario was higher than in four of the six equalization-receiving provinces. Ontario's relative tax effort has risen modestly since the mid-1970s and is currently at the national average. When surpluses and deficits are taken into account, Ontario's imputed tax effort is above the national average. Ontario's findings are once again consistent with those reported by the Minister of Finance.

Table 2 provides an alternative perspective on the fiscal situation of provinces. It shows total provincial-local spending on a per capita basis, indicating the source of revenues employed. The high per capita spending of Alberta and Saskatchewan is clearly influenced by the availability of resource revenues which, to an important extent, substitute for more conventional types of provincial and local taxation. The per capita spending of Quebec significantly exceeds that of Ontario, while the Atlantic provinces spend about the same per capita. The spending of the five eastern provinces is significantly raised by the availability of payments from the federal government. Ontario, which has no meaningful oil and gas revenue, receives about the same per capita federal support as Alberta, despite the enormous difference in their respective fiscal capacities.

As noted below, spending data has to be interpreted carefully because it ignores the structure of "needs" and the differential availability of economies of scale in program delivery. The facts nevertheless suggest that more attention should have been given to interregional differences in need and fiscal capacity when designing the revised fiscal arrangements for the 1982 to 1987 period.

The Government of Ontario has long supported the many programs

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[29] *Ibid*, page 48.

[30] Economic Council of Canada, *op. cit.*, page 23.

Table 2

Provincial Finances, National Accounts Basis, 1980
($ per capita)

	Provincial-Local Taxes	Resource Revenues	Federal Transfers	All Other Provincial-Local Revenue	Total Provincial-Local Revenues	Surplus or Deficit[1]	Total Spending[1]
Nfld.	1,271	55	1,202	144	2,672	+9	2,663
P.E.I.	1,081	0	1,423	122	2,626	−423	3,049
N.S.	1,272	2	983	124	2,381	−234	2,615
N.B.	1,224	13	1,021	113	2,371	−178	2,550
Que.[2]	2,024	8	693	83	2,808	−452	3,260
Ont.	1,924	8	351	171	2,454	−194	2,648
Man.	1,559	30	823	218	2,630	+1	2,629
Sask.	1,604	599	508	312	3,023	+1	3,022
Alta.	1,559	2,083	343	560	4,545	+1,125	3,420
B.C.	2,035	243	393	211	2,882	+149	2,733
All Provinces	1,839	245	540	190	2,814	−88	2,902

Source: Based on Statistics Canada, *Provincial Economic Accounts*, Catalogue 13-213.

[1]Total spending is total current spending plus gross capital formation, excluding the deduction of capital consumption allowances. The surplus or deficit differs from the national accounts definition by the amount of the capital consumption allowances.

[2]Quebec's contracting out tax points are deducted from Provincial-Local Taxes and added to Federal Transfers.

Canada has in place for redistributing incomes among the regions and provinces. Taxpayers in Ontario continue to provide over 40 per cent of federal revenues, and in that sense, contribute significantly to the financing of equalization, the Canada Assistance Plan, DREE grants and other redistributive instruments. Given this observation, there should be greater concern that the overall transfer system leaves the Ontario public sector in a position where its ability to provide provincial-local services is lower than that of any other province. It is clear that Ontario is unable to match the large spending increases on social services in the energy-wealthy provinces without future tax increases and a further widening of interprovincial tax burdens.

To conclude, *the real fiscal imbalance in Canada is between the energy-exporting and energy-importing provinces. In the absence of new measures to deal with this problem, the fiscal situation facing non-energy provinces such as Ontario will become increasingly more difficult through the 1980s.*

III The 1981-82 Fiscal Negotiations

The 1981-82 federal-provincial discussions on new fiscal arrangements represent a turning point in intergovernmental relations and a worrisome indication of the federal government's emerging strategy for dealing with the provinces. Chart 7 provides a brief chronology of recent developments. The purpose of this section is not to record comprehensively what transpired but rather to clarify certain issues that arose in connection with the 1982 EPF cuts. These are issues that will materially affect future discussions on program standards and conditions. The section also includes an evaluation of the new equalization program.

The Shares Question

In 1979, the Minister of National Health and Welfare launched a campaign against the provinces, accusing them of "diverting" federal EPF transfers to purposes other than those mandated by the block-funding arrangement. *The claim effectively repudiated the whole intent and spirit of EPF by denying that restraint had been a joint objective and by implicitly resurrecting the notion of matched funding on individual programs.* The Health Services Review subsequently established under Justice Emmett Hall looked into the federal charge and exonerated provinces of any dollar diversion.[31] The federal government nevertheless persisted in its attacks. A document prepared in the Ministry of State for Social Development (MSSD) during the winter of 1980-81 argued, for example, that the federal share of post-secondary education operating expenditures in Ontario had risen from 45.5 per cent in 1976-77 to 61.0

[31]See Hon. Emmett M. Hall, CC., Q.C., *Canada's National-Provincial Health Program for the 1980s,* August 1980.

per cent in 1979-80 and that, in the period 1975-76 to 1980-81, the federal share of health care funding in Ontario increased from 50.6 per cent to 63.6 per cent. Over the balance of 1981 and into 1982, a variety of conflicting and confusing numbers appeared, all of them implicitly critical of provincial policy in the two program areas. To properly evaluate the EPF experience, it is necessary to briefly examine the construction and meaning of these share calculations.

A key point to note is that a short-term increase in the federal share was planned and fully anticipated in 1977 when the EPF was adopted. As previously noted, the federal government was encouraging provincial restraint under EPF by giving the provinces greater flexibility through blockfunding to introduce cost-reducing alternatives to high-cost programs. Moreover, federal contributions were destined to rise because of transitional financial arrangements and the lag in the EPF escalator.[32] The federal share peaked in 1979 and has been declining ever since. There are, however, a number of technical features that affect the absolute levels of the federal and provincial shares.

For example, it is necessary to decide what to do about the Revenue Guarantee compensation built into EPF. When the compensation is considered to be a federal contribution to health and post-secondary education, there will obviously be a large jump in the federal share between the pre- and post-EPF years. The MSSD document quoted earlier included the compensation as a federal contribution in arriving at those dramatic increases in the federal shares during the last few years. Since the November 12 budget, however, federal spokesmen have defended the termination of the Revenue Guarantee compensation by arguing that this transfer was never a contribution to provincial health and post-secondary education programs. The provinces have consistently maintained that the compensation is indeed part of the federal contribution, but that it needs to be subtracted in making inter-period comparisons. The interpretive problems with the Revenue Guarantee compensation arose only because the federal government used the "artificial" increase in its share as a basis for arguing that provinces had begun to underfund the EPF programs.

Second, it is necessary to define the appropriate expenditure base. If the spending base is defined narrowly for conformity with the pre-1977 cost-sharing definitions, the federal share will be higher than if

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[32]Under EPF, federal contributions to provinces were brought to per capita equality by raising the payments to certain provinces over the initial three years of the program and scaling back payments to others over five years. For certain provinces, this imparted a significant rise to the federal share in the early years. The EPF escalator is a three-year average of GNE. The escalator used between 1977 and 1980 picked up the high growth years of the early 1970s, and was used at a time when provinces were restraining spending. The current escalator picks up the low growth of recent years, at a time when health and post-secondary education spending are rising more rapidly. In short, the escalator results in cyclical changes in the federal and provincial shares.

the base is defined broadly to include the formerly non-shareable expenditures to which federal funds have been allocated under a flexible system of blockfunding.

Third, it is necessary to consider both health and post-secondary education together. This is how they were intended to be treated under the 1977 arrangement introducing the blockfunding principle. For its own internal purposes, however, the federal government decided that it would split its EPF cash contributions between health and education on a 67.9:32.1 per cent basis, the national average split of federal contributions under cost-sharing in 1975-76. For most provinces, this national average ratio was quite different from the program mix actually in place. Moreover, since that time, provincial priorities across Canada have shifted, with health care expenditures increasing relatively faster than post-secondary education expenditures.[33] The broadening of the expenditure base under blockfunding since 1977 further invalidates the use of the 1975-76 ratios. The federal government has ignored these problems and, in fact, continues to use the 1975-76 ratios in the amended EPF legislation. The point is that, if the 1975-76 ratios are arbitrarily used to split current federal contributions, the federal "share" of expenditures will be understated on health care and significantly overstated in respect of post-secondary education. A statement about the federal contribution to post-secondary education, taken in isolation, can therefore be highly misleading. Federal spokesmen overlook this fact and continue to claim remarkably high federal rates of support to post-secondary education in most provinces.

A decision is also required on the treatment of the tax room that forms part of EPF. The tax room was originally transferred to provinces in lieu of federal cash payments. The change had no political cost for provinces since the tax burden on individual taxpayers remained the same. However, over time, provinces have assumed the tax "visibility" for raising these funds. Most provinces agree that the tax room should be considered part of the federal EPF contributions, but a few object to this procedure and acknowledge only the federal cash. The Parliamentary Task Force presented the numbers both ways.[34]

A final point concerns fees and premiums. On many occasions, federal spokesmen have drawn attention to provincial spending shares that they calculate to be extremely low. They have arrived at their numbers by treating fees and premiums as a "direct" contribution from

[33]To illustrate, the actual health and post-secondary spending ratios for all provinces have been as follows:

	Health	Post-Secondary Education
	(%)	(%)
1972	71.2	28.8
1975	72.3	27.7
1978	74.0	26.0
1981	75.7	24.3

[34]*Fiscal Federalism in Canada, op. cit.*, page 133.

people. In the provincial view, premiums are just another universally-applied tax for which provinces bear full political responsibility and, therefore, have to be included in calculating the provincial share. The separate people's "share" is merely an artifice to understate the true provincial contribution. It should be emphasized that governments do not have any funds of their own. All expenditures must be financed ultimately by the people, either through taxes or premiums.

Table 3 presents Ontario's view of the "shares" issue. The information shows that the federal share has never exceeded 50 per cent in this province.

Provincial Underfunding

Closely related to the shares argument is the general impression created by the federal government that provinces have "underfunded" the health and post-secondary education programs covered by the EPF arrangement.

Interjurisdictional comparisons are often made by those wishing to assess provincial spending priorities. Such comparisons have to be interpreted with great caution. Aside from the inevitable problems of data consistency, there are logical explanations for the observation that spending might be higher or lower in a given province. A primary consideration is obviously the fiscal capacity of provinces. As noted in Section II, on a post-transfer basis, Ontario's spending capacity is lower than that of any other province. In view of its revenue position, it is natural that this Province should not head the list in terms of spending. It is to be noted, as well, that national spending levels are levered up by the high spending of the resource-wealthy provinces in the West. They also reflect the ideological preferences of certain provincial governments for larger public sectors and, in some cases, a lesser concern with budgetary deficits.

Most important, the spending data ignores the existence of economies of scale in program delivery — that is, the ability of certain provinces to provide a given standard of service at lower per unit cost. In a province like Ontario, with a diversified economy and a highly urbanized population, economies of scale in program delivery are generally quite significant. A final comment is that spending totals obscure what might simply be called "management efficiency". Ontario's spending has been held down by good management and administration, a fact recognized by the President of the Quebec Treasury Board who has publicly acknowledged Ontario's record in this regard.[35]

[35]During the Quebec Government's economic summit meeting on April 6, 1982, Mr. Yves Bérubé, President of the Quebec Treasury Board, referred to the "widespread opinion in the business community that Quebec's problem with public finances would be solved if the Quebec public sector had the same productivity as Ontario's public sector". He went on to say that this could not be achieved easily or quickly. "To achieve a productivity equal to that of Ontario would require laying off 16,000 people."

Federal Share of Health and Post-Secondary Education Financing[1]

Table 3

($ million)

	1976-77	1977-78	1978-79	1979-80	1980-81	Estimated 1981-82
Federal Contributions to Health and Post-Secondary Education (Tax plus Cash)						
Ontario	2,057	2,477	2,782	3,100	3,433	3,811
All Provinces	5,820	6,811	7,691	8,662	9,618	10,770
Provincial—Local Government Health and Institutional Post-Secondary Education Expenditures (Operating)						
Ontario	4,975	5,386	5,778	6,274	7,126	8,175
All Provinces	13,481	14,340	15,861	17,724	20,409	23,638
Federal Share of Health and Post-Secondary Education Expenditures (per cent)						
Ontario	41.3	46.0	48.1	49.4	48.2	46.6
All Provinces	43.2	47.5	48.5	48.9	47.1	45.6

Sources: Federal-Provincial Subcommittee of Officials on EPF Data; Department of Finance; Ontario Treasury.

[1]The revenue guarantee component of EPF is excluded for comparability with the pre-EPF period.

With these caveats in mind, it is possible to proceed to the evidence on provincial funding. Table 4 presents per capita data for health, post-secondary education and total provincial-local spending. Only Ontario is shown individually as the information for other provinces, gathered by a special data subcommittee, is considered confidential. The table shows that in 1976 Ontario's total spending per capita was in excess of that in Atlantic Canada and only 14 per cent lower than that in Western Canada; by 1981, however, the per capita spending of the Atlantic provinces had overtaken that of Ontario, and Western Canada was spending over 38 per cent more. Despite these trends in aggregate spending, per capita spending on health and post-secondary education in Ontario remained relatively close to the national average. As noted earlier, the averages are significantly levered by the high spending of some Western provinces, particularly in the health area.

Spending Comparisons for Health and Post-Secondary Education
($ per capita)

Table 4

	Health[1]		Post-Secondary Education[2]		Total Provincial-Local Spending[3]	
	1976	1981	1976	1981	1976	1981
Atlantic Canada	348	610	126	189	1,720	2,841
Ontario	439	715	163	233	1,857	2,767
Western Canada	412	792	154	250	2,164	3,839
All Provinces	422	737	166	237	1,968	3,281

Sources: Ontario Treasury; Federal-Provincial Subcommittee of Officials on EPF Data; Statistics Canada, Catalogues 68-202, 68-203, 68-205.

[1]Provincial-local government operating expenditures.

[2]Institutional operating expenditures.

[3]Total provincial-local government expenditures (excluding public debt interest).

Table 5 presents an alternative view, comparing broadly defined health care operating expenditures and post-secondary institutional operating expenditures to Gross Provincial Product (GPP). There is no convincing evidence that the sectors have contracted. In 1976-77, Ontario devoted about 4.8 per cent of GPP to health and this actually increased to 5.0 per cent in 1981-82. In 1976-77, post-secondary institutions in Ontario spent 1.8 per cent of GPP; this dropped very slightly by 1981-82. Ontario's total spending as a proportion of GPP is significantly below that in most provinces, a fact that needs to be recognized when making interprovincial comparisons by program.

A third measurement is how particular expenditures fare as a percentage of the provincial-local sector. Charts 5 and 6 trace this relationship for health and post-secondary education in Ontario and all provinces. Ontario has consistently devoted a higher proportion of total

Comparisons for Health and Post-Secondary Education

Table 5

(Spending as a Percentage of GPP)

	Health[1]		Post-Secondary Education[2]		Total Provincial-Local Spending[3]	
	1976	1981	1976	1981	1976	1981
Atlantic Canada	6.7	7.6	2.4	2.4	33.1	35.5
Ontario	4.8	5.0	1.8	1.6	20.2	19.2
Western Canada	4.3	4.9	1.6	1.5	22.6	23.7
All Provinces	5.0	5.4	2.0	1.7	23.3	24.1

Sources: Ontario Treasury; Federal-Provincial Subcommittee of Officials on EPF Data; Statistics Canada, Catalogues 13-213, 68-202, 68-203, 68-205.

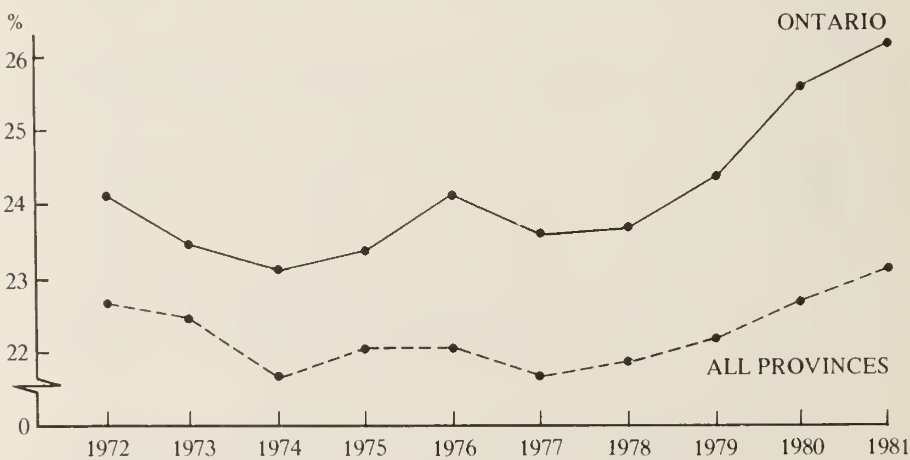
[1]Provincial-local government operating expenditures.
[2]Institutional operating expenditures.
[3]Total Provincial-local government spending (excluding public debt interest).

public sector spending to health than the rest of the country. In 1981-82, this proportion was considerably higher than in 1976-77. Chart 6 shows there has been a modest reduction in the share of total spending accounted for by post-secondary education in all provinces. It also shows that, during the past five years, Ontario's share shifted slightly ahead of that for all provinces.

None of the foregoing approaches establish that there has been provincial "underfunding" of health and post-secondary education since 1977, or that Ontario has been — in the Secretary of State's words — "the worst offender".

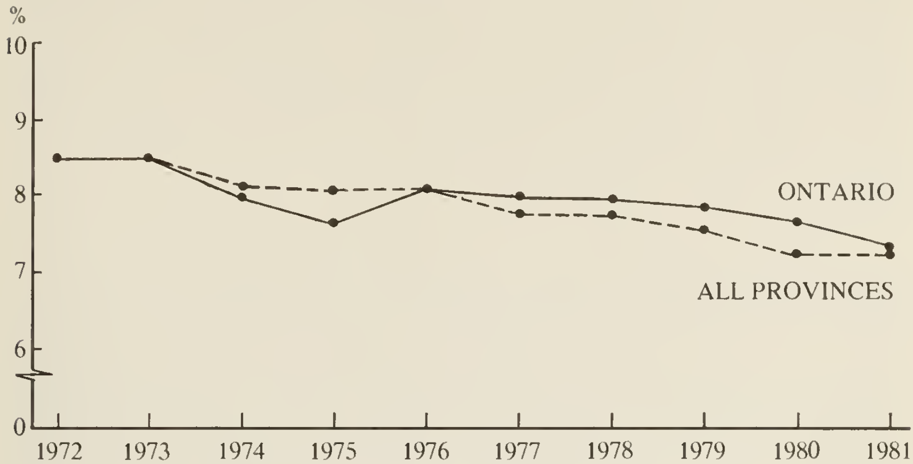
Health as a Per Cent of Total Expenditures[1]

Chart 5



Source: Appendix Table 7.
[1]Provincial-local government operating and capital (excluding public debt interest).

Post-Secondary Education Expenditures[1] as a Proportion of Total Expenditures[1] — Chart 6



Source: Appendix Table 7.

[1]Provincial-local government operating and capital (excluding public debt interest).

The federal conclusion about provincial underfunding derives, not from objective data about the sectors, but from an initial and erroneous view of what has happened to the federal "share". Ottawa's exhortations for provinces to spend more, in addition to being jurisdictionally intrusive, and in total contradiction to federal urgings throughout the 1970s, do not rest on a valid understanding of what provinces are doing, need or can afford.

Program Quality

Implicit in the federal charge of provincial underfunding is the view that provinces have allowed a deterioration of the national standards under health care and have failed to show adequate concern for the national objectives in regard to post-secondary education and human resources development. In recent months federal ministers have made very strident comments about provincial programs. For example, the Secretary of State recently criticized Ontario's post-secondary education funding, accusing this Province of "breaking the spirit, if not the letter, of the agreement of 1977". The headline of the February 11 *Toronto Star* article reporting his speech read "Students 'cheated' by Ontario: Regan". To most provinces, it is evident that the federal government seeks to recapture, under the guise of "deteriorating national standards", some of the direct program control it surrendered to them in 1977.

Canada's health care legislation sets out clearly the national standards that apply in this important area. Provincial health insurance plans must provide comprehensive coverage of services, provide for universal coverage of the population, be portable among provinces, be publicly administered, and provide for the unimpeded access to insured services by all entitled persons. Ontario strongly supports these principles, and is prepared to work with the federal government to ensure that Canadians continue to have the best possible system of national health care. Even during the 1970s, when this Province called for provincial opting out of the established programs, it was still recognized that there is an important federal role in ensuring that national standards are maintained.

With regard to health care, the major federal concern at present is accessibility to medical services, especially as this is affected by doctors "opting out" of the provincial health care plans. Approximately 15 per cent of Ontario doctors are currently opted out, virtually the same percentage as in the early years of Medicare. More important, these opted-out doctors represent only seven per cent of all claims for medical services submitted to OHIP. It is also to be stressed that not all opted-out practitioners extra-bill their patients. Finally, the doctor to population ratio has increased in Ontario from 1 in 637 in 1971 to 1 in 540 in 1981, and the number of opted-in doctors per capita has actually increased significantly. In this sense, competition and availability have improved.

The federal government has also criticized health care premiums. It is not clear that premiums affect the national standards in any way. To the extent that federal spokesmen concern themselves with the *incidence* of health premiums, they overstep their responsibilities and intrude upon the provinces' constitutional right and responsibility to determine their own revenue structures and the *overall incidence* of their fiscal systems. Some provinces avoid premiums by having higher income or sales taxes, the latter as high as 11 per cent. The present mix of taxes and premiums in Ontario is regarded as fair by most people.

In post-secondary education, unlike health, there are no legislated national standards. The federal government, from time to time, has indicated a number of national "objectives" in this area, many of which Ontario and most other provinces can accept as being legitimate goals for the national government to pursue.

The federal government has recently expressed its concern about such things as the economic relevance of programs, access to higher education and interprovincial mobility. There is no substantial proof that, given university autonomy, provinces have underfunded high demand professions such as science, engineering and business administration. According to the Federal-Provincial Task Force on Student Assistance, there are no grounds for suggesting that provincial policies obstruct access by the children of the less well-to-do.[36] Tuition fees as a

[36]*Report of the Federal-Provincial Task Force on Student Assistance* (Ottawa: Supply and Services Canada, 1981).

proportion of total education costs have declined over the last fifteen years, and are now significantly below what they were in the 1950s and 1960s. In 1981, university students in Ontario paid on average 15.4 per cent of their education cost through tuition fees; in 1971 they paid 16.9 per cent. It is difficult to argue, therefore, that tuition fees have become a serious economic barrier. In addition, statistics in the Task Force Report confirm that Ontario has one of the best student aid programs in Canada. There are minor problems of portability in student aid programs, but it is doubtful that these impede the interprovincial mobility of students.

To sum up, *there is little evidence to warrant the serious federal charges that national standards under the established programs are in jeopardy, that services are deteriorating and that clients of the system are being "cheated" by provincial policy. Ontario believes that continuing federal criticisms of provincial health and post-secondary education programs could have the unfortunate consequence of undermining public confidence in services that are in fact of very high quality by international standards.*

Most provinces have indicated their willingness to negotiate program improvements and to make provision for enhanced federal "visibility" and "accountability". For its part, the federal government must document its concerns more thoroughly and come forward with concrete proposals. It should, at the same time, assure provinces that it recognizes their fiscal limitations and their pre-eminent jurisdiction in the health and education fields.

Equalization and Fiscal Disparities

The substantial EPF cuts starting in 1982-83 shift part of the federal deficit problem onto the provinces, exacerbate regional inequalities in services and tax burdens and make future discussions on health and post-secondary education programs more difficult.

These points are important. Equally disturbing are the problems raised by the new equalization formula. As noted, the new formula substitutes a five-province standard of provincial revenue-raising capacity for the previously used national average. Alberta and the Atlantic provinces are excluded from the standard on the grounds that their fiscal capacities are atypical. All resource revenues are included in the formula at 100 per cent, and the formula's revenue coverage is broadened to include municipal tax revenues and local government revenues from the sale of goods and services. A GNP cap has been applied as a safeguard against excessive escalation in program entitlements.

The new formula presents three major difficulties, all of them related to the fact that the program was not reformed "within the context of a comprehensive strategy for dealing with the new fiscal disparities created by oil and gas" — the criterion for the 1982 reform laid down by Ontario in its 1980 Budget, and the condition under which this Province agreed not to contest its arbitrary exclusion during the 1977 to 1982 period.

First, the formula locks-in, as a "base", the 1981-82 entitlements of the recipient provinces. As Ontario explained in its 1980 paper, *Equalization and Fiscal Disparities in Canada,* these entitlements incorporate an equalization "windfall" that flowed to recipients as a result of the rapidly increasing oil and gas revenues in some of the western provinces. Ontario's exclusion from equalization became an implicit measure of the extent to which recipients were being "over-equalized" in the aftermath of the energy crisis. The recipient provinces were, in effect, given the fiscal capacity to provide more than a "basic" level of services. Ontario argued that the rapid growth of resource revenues available to oil and gas producing provinces does not in and of itself bring about a corresponding increase in the fiscal need of other provinces. With the 1982 change in the equalization standard, the definition and measurement of "over-equalization" become exceedingly difficult. It is nevertheless clear that, for an equitable treatment of provinces, either the new formula should have started from a base level of entitlements that excluded the energy-related windfall, or Ontario should have been paid retroactively the $1.6 billion windfall entitlement which it, exclusively, was denied.

Second, the new formula fails to address the fact that one "unrepresentative" province can provide superior public services at tax rates very significantly lower than those prevailing elsewhere in the country. The equalization program that has existed in Canada since 1957 focused on the less-wealthy provinces, and sought to enable them to provide comparable public services at tax rates that are not unduly high. By most standards, the program has been successful in meeting its objectives. However, as stressed in Section II, there is a new fiscal disparity problem in Canada — a rapidly widening gap between Alberta and all the other provinces. This has enormous implications for the very meaning of comparable services and comparable rates of taxation, goals to which the nation is now formally committed under its new Constitution.[37] In Ontario's view, it was inappropriate to set aside, through a change in the equalization standard, the complex questions raised by Alberta's high per capita spending, enormous fiscal capacity and low tax effort. The new fiscal disparities associated with oil and gas urgently need to be addressed, but the new equalization formula overlooks them almost completely.

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[37]The pertinent section of the new Constitution reads as follows:

> "Parliament and the Government of Canada are committed to the principle of making equalization payments to ensure that provincial governments have sufficient revenues to provide reasonably comparable levels of public services at reasonably comparable levels of taxation."

The last phrase is noteworthy because it replaces the old program wording "without resorting to unduly burdensome levels of taxation".

A third observation, therefore, is that the federal government failed to integrate its thinking about equalization with broader ideas about the redistribution and reinvestment of energy revenues, particularly the oil and gas revenues of the producing provinces. With equalization regarded as a separate, self-contained problem, the search for a logical procedure to equalize resource revenues became secondary to the search for a technique which would ensure an acceptable level of payments to the recipient provinces. Changing the fiscal capacity standard was grasped as a convenient way to keep Ontario out of equalization, and to suppress all the important questions that arise in connection with the program's past and future treatment of natural resource revenues.

Its approach has led the federal government into a number of inconsistencies. Crown lease revenues have been put back in the formula in contradiction to the argument that was used in 1978 when it was announced they would be taken out. Other resource revenues have been included at 100 per cent, rather than 50 per cent, removing a previously introduced distinction between renewable and non-renewable resources. The 1977 argument that less than 100 per cent of resource revenues should be used in the formula, thereby reflecting the costs of developing and maintaining the resource base, has been abandoned in 1982. The fact that only a portion of resource revenues are used to finance current public services has been glossed over entirely. The expansion of revenue coverage was undertaken, not out of a conviction that municipal services should be on a par across the country, but because this step was necessary to ensure a target payment level, given that resource-generated equalization is greatly reduced by changing the equalization standard. Finally, the new equalization system continues to use a national average tax rate in the calculation of relative fiscal capacity even though the benchmark tax base is defined by only five provinces. This results in considerable ambiguity with regard to the target level of public services provinces are enabled to supply and leads to dubious procedures for the determination of resource-related equalization.[38]

In Ontario's view, the federal government too hastily jettisoned the underlying and historic philosophy of national averages. Comparability in services and tax rates should not have been defined by ignoring the province that in the next few years will exert the greatest amount of leverage on all the others. A more thorough attempt should have been made to define the basic level of public services that provinces can reasonably be expected to supply, and to address directly the problems posed by the uneven distribution of resource revenues among the provinces. New mechanisms *with different objectives* could then have

[38]Alberta has about 85 per cent of the oil and gas base, but is excluded under the representative average system. As a result, petroleum-related equalization is generated by applying what is essentially an Alberta resource tax rate to the resource bases of Saskatchewan and B.C., a questionable procedure.

been instituted to ensure that all provinces were treated fairly. This was the type of approach that Ontario had recommended as early as 1980.

To sum up, the equalization developments are an unhappy indication of the direction federalism is taking in Canada. The federal government has clearly shown its unwillingness or inability to come meaningfully to grips with the ten-year old problem of energy-related fiscal imbalance among the provinces — a problem that is slowly but surely undermining the structure of fiscal federalism built up in this country during the 1960s. The new equalization program will ignore the issue for another five years; it will inhibit a comprehensive debate about resource revenues; and it will introduce new financial and conceptual constraints to further confound the search for a rational solution.

The Negotiating Process

Provinces have remarked that the 1981-82 fiscal arrangements discussions were not "genuine negotiations" in the traditional sense. The continuous but unsubstantiated federal criticisms of provincial health and post-secondary programs clearly established a difficult environment in which to carry on a constructive dialogue, but the provincial concerns over "process" go far beyond this point.

The compression of the negotiating time frame quickly emerged as a major problem. A full year elapsed between the Minister of Finance's announcement that he was seeking "significant savings" in provincial transfers and the presentation of actual proposals in the November 12 federal budget; but only three and a half months intervened between the presentation of those proposals and the introduction of the fiscal arrangements bill (C-97) in the House of Commons. While it is true that the proposed EPF cuts had been anticipated for quite some time, the "Ontario standard" approach to equalization was a novel proposition. No reference had been made to such an alternative in the federal government's presentation to the Parliamentary Task Force, and no discussion papers on the topic had previously been circulated to provinces. Difficulties with the plan surfaced almost immediately, and the federal government soon found itself offering a variety of adjustments and modifications to its original proposal. The complex interaction between the equalization standard and EPF cash payments created additional problems,[39] and by the time the new population estimates were factored into the formula, the Ontario standard was in serious trouble. The federal government tentatively put forward the five-province, representative average standard in late January, but found it necessary to ignore population-related equalization overpay-

[39]Moving from the national average to the Ontario standard for equalization increased the equalization associated with the EPF tax points and depressed recipients' EPF cash. Moving from the Ontario standard to the five province standard reduced the associated equalization and increased the EPF cash. Changing data on tax bases and population further complicated these interactions.

A Chronology of the 1981-82 Fiscal Arrangements Discussions

Chart 7

October	28, 1980 —	Federal budget announces Ottawa's intention to achieve "significant savings" in social transfer payments to the provinces, starting in 1982.
December	17, 1980 —	At a federal-provincial meeting of Finance Ministers, provinces urge the federal government to put forward concrete proposals, and Mr. MacEachen responds by promising early discussions of a substantive nature.
February	5, 1981 —	The federal government appoints a Parliamentary Task Force on Federal-Provincial Fiscal Arrangements to examine transfer payments "within the context of the (federal) government's expenditure plan as set out in the October 28, 1980 budget".
February	25, 1981 —	Mr. MacEachen states that he is seeking $1.5 billion from provinces over the years 1982-83 and 1983-84.
August	15, 1981 —	The 22nd annual Premiers' Conference concludes with provinces criticizing the lack of concrete federal proposals and urging the commencement of negotiations.
August	28, 1981 —	Report of the Parliamentary Task Force. It rejects its restrictive mandate, recommending that funding levels be maintained.
November	12, 1981 —	Federal budget proposes elimination of Revenue Guarantee compensation from EPF and an Ontario standard for equalization.
November	23, 1981 —	Federal-provincial Finance Ministers meet to discuss budget proposals. Ottawa admits budget error resulting in significant new losses to provinces.
December	14, 1981 —	Second meeting of Finance Ministers. Modest federal concessions on equalization. Provincial consensus papers urge a one-year extension of equalization and EPF.
December	18, 1981 —	Major changes to the November budget tax proposals further increase net losses to provinces.
January	15, 1982 —	Release of new population estimates again causes major revision of provincial entitlements.
January	22, 1982 —	Finance Ministers fail to make any progress. First hints of a five-province equalization standard.
February	4, 1982 —	Conclusion of First Ministers' Conference on Economy. Prime Minister holds to proposed EPF cuts, but claims to have added $1 billion over five years by introducing five-province standard. Provinces propose one-year extension with 12 per cent cap. No agreement is reached.
March	19, 1982 —	Fiscal Arrangements legislation receives first reading in House of Commons.
April	7, 1982 —	New arrangements become law.

ments in 1980-81 and 1981-82 as a means of securing the Atlantic provinces' acceptance of this alternative. In short, just over one month elapsed between presentation of the five-province standard and its introduction to Parliament; there was not a single plenary meeting of Finance Ministers to discuss this formula for transferring $4.7 billion to the fiscally deficient provinces in 1982-83.

A second observation is that the federal government refused to modify its EPF position. As noted, hasty concessions and changes were made to the original equalization proposal, but the proposed level of EPF cuts was defended even as the total package became progressively less attractive. Shortly after the November 12 budget, the federal government had to concede that, due to an error, provinces would be worse off by another $650 million compared to the five-year budget projections. The tax policy changes announced on December 18 reduced the so-called tax "offsets" and further eroded the financial outlook of provinces by at least $400 million.[40] Normal negotiations see the differences between the parties narrowing; the 1981-82 discussions saw the federal offer get progressively worse.

The splitting of the EPF financing and EPF "programming" issues was another major source of difficulty. Provinces were asked by the Minister of Finance to accept a reduction in transfers at the same time that other federal ministers were accusing provinces of severely underfunding health and post-secondary education, threatening the unilateral introduction of stringent new standards and conditions that could markedly inflate provincial costs starting in 1983, and suggesting a post-1983 reallocation of EPF cash to fund new federal initiatives. This left provinces in an untenable position. *The 1977 EPF agreement was predicated on the idea of long-term certainty for both orders of government. In 1982, the only certainty provinces face is a $940 million cut in EPF transfers; there is total* un*certainty regarding the federal government's real commitment to the program.*

Finally, the federal budget included an ultimatum — EPF cash funding could be reduced starting in 1983 if new standards and conditions satisfactory to the federal government are not in place by that time. In the best of circumstances, threats are unacceptable. In the present case, where federal concerns and objectives remain unclear, and where such federal proposals as exist are vague and inequitable among provinces, they are seriously destructive of intergovernmental co-operation. The federal government has argued that EPF transfers to provinces will

[40]As a result of the federal budget tax changes, provincial income tax revenues will increase. The federal government claims these tax "offsets" have to be considered in evaluating the "net" impact of the federal budget on provincial finances. Provinces do not accept the implicit argument that revenues raised under provincial tax legislation are a federal "contribution" to provinces. In any case, the tax offsets have proven highly uncertain, being reduced with every change in the November budget measures. Moreover, they fall off sharply in value over time, while the EPF losses escalate.

grow by nearly 12 per cent on average over the next five years. This ignores the large cutback in transfers during 1982-83 and the even more important point that, given its threats for the period starting in 1983, there is virtually no assurance that the EPF program will even continue for another five years.

Perhaps the greatest irony of the 1981-82 process is the fact that it was supposed to have been a more informed and researched negotiation than those of the past. The Parliamentary Task Force was set up to hear evidence and conduct investigations, and the Economic Council of Canada simultaneously undertook a major review of past fiscal arrangements. The reports of both groups were ignored by the federal government, at least insofar as the EPF cuts are concerned. In the final analysis, federal-provincial discussions were carried on with unprecedented uncertainty, with great unwillingness on the part of the federal government to discuss alternatives put forward in good faith by the provinces, and with serious inattention to underlying problems of a fundamental, long-term nature.

IV An Agenda for the 1980s

During the 1960s, the term "co-operative federalism" was coined to characterize federal-provincial relations. While it is impossible to give a precise definition of what this means, healthy federal-provincial relations clearly require that governments respect each other's basic responsibilities; that they tread carefully, if at all, into each other's jurisdiction; that they negotiate with an open mind to alternatives and a willingness to move off initial bargaining positions; that they avoid levering the other side into expensive programs only to pull out support at a later date; that they eschew policy reversals and not promise long-term certainty one day and major changes the next; and that they try to reach accommodation through honest negotiation, not the use of ultimatums and threats.

By these standards, Canada has a considerable distance to go in establishing a new period of "co-operative federalism". The negotiations of the 1960s were often difficult, but it seems fair to conclude that during the 1970s intergovernmental relations became significantly more strained, largely as the result of differences over energy policy and the constitution. As noted in the introduction to this paper, the federal government is adopting a more aggressive approach to federal-provincial relations, and has on several occasions indicated a general disposition to proceed against and without the provinces, even in matters where provincial rights and interests are of paramount importance. The path of deliberate confrontation and explicit unilateralism is fraught with dangers for any federal state. In Canada, where confidence and unity are key issues, it is vitally important that political leaders continue to make a public display of goodwill, honourable intentions and a resolve to work together, no matter how testy the issues become.

There are, in Ontario's view, certain steps that can be taken immediately to improve the federal-provincial climate.

First, the federal government must affirm its commitment to genuine negotiation. As shown in Section III above, the 1981-82 fiscal arrangements discussions left much to be desired from the point of view of process. The single most important step that could be taken to restore an atmosphere of trust would be for the federal government to withdraw unconditionally its threat of imminent financial sanctions relating to EPF standards and conditions. It is a charade to expect meaningful negotiations when a constraining federal ultimatum has been delivered before talks even begin. The Government of Ontario remains committed to the co-operative resolution of intergovernmental problems, but believes that the onus for re-establishing an appropriate climate rests primarily upon the federal government.

Second, it would be helpful for the federal government to join provinces in emphasizing the achievements that have been made in the fields of health care and post-secondary education. In Ontario's view, very high levels of service are being maintained under the EPF programs and the legislated national standards are being met. It is of course the federal government's responsibility to exercise leadership in identifying improvements that need to be made on a national basis, but its concerns and ideas should be communicated in such a way that public confidence in the programs is not eroded. Federal-provincial discussions on health and post-secondary education "standards and conditions" would be assured greater success if the federal government were to adopt a more positive and constructive approach to the issues.

Third, the federal government should rescind the 1975-76 ratios used in allocating its EPF contributions among the health and post-secondary education programs. As suggested in Section III, these ratios deny the principle of blockfunding and are, in any case, seriously out of date. Their continued use could lead to serious policy errors. For example, the Secretary of State's apparent view that post-secondary transfers could be cut back to free up money for new initiatives is predicated on an artificial and inflated view of the extent of federal support in this sector.

Fourth, it is necessary that there be a reassessment of what constitutes a federal transfer under Established Programs Financing. EPF provides for both a tax transfer and cash payments to the provinces. Traditionally, Ontario has acknowledged that the tax room transfer is a form of federal contribution to provincial health and post-secondary education financing. Unlike certain other provinces, Ontario has regarded this as an implication of the agreements that were made in 1967 and, more importantly, 1977. It was one of the oddities of the past that Parliament was thereby left in the position of seeking accountability and credit for funds actually raised by the independent tax actions of provincial legislatures.

Now that the federal government has unilaterally "undone" the 1977 arrangement by eliminating the Revenue Guarantee compensation, Ontario no longer feels bound by its historic position. Accordingly, the Province will henceforth consider the federal contribution to consist of the cash transfer only. The tax transfer will, in effect, be deconditionalized. The federal government is urged to accept this new interpretation. After twenty years of tax sharing, it would be appropriate for Ottawa to concede that revenues raised under a provincial taxation instrument are indeed provincial funds, not a federal transfer.

This proposed change to EPF is a logical implication of the 1977 agreement. It would lead to a needed clarification of the roles of the two orders of government. Provinces would be seen to have most of the responsibility for the funding of health and post-secondary education, while federal accountability and credit, being defined solely in terms of the cash transfer, would relate more closely to the national government's specific responsibility for the maintenance of national standards.

Ontario recognizes that the federal cash payments would differ on a per capita basis among the provinces. Provinces with high fiscal capacity would receive less. Per capita payments to equalization recipients would be equal and would remain significant. This approach would highlight the legitimate federal role of providing greater support to those provinces who require it if they are to provide comparable levels of service.

Hopefully, progress can be made along the above lines. This would enhance the environment for negotiating certain program-related improvements to the satisfaction of both orders of government.

For the longer term, it is clearly necessary for governments to engage in a new and fundamental dialogue concerning the roles and responsibilities that each order of government should have in the federal structure of the 1980s and 1990s. Ontario therefore proposes a meeting of First Ministers and Ministers of Finance to explore these questions and to commission a report to Parliament and the provincial legislatures by early 1984. This review would follow in the tradition of the Rowell-Sirois Commission of the late 1930s and the Tax Structure Committee of the mid-1960s, and would be a necessary prelude to Round II of the constitutional discussions on the division of powers.

Ontario suggests that the exercise could begin with a detailed analysis of the fiscal situation confronting the federal government and each of the provinces. Until this research is complete, the federal government should refrain from further transfer cuts and major new changes in existing programs. With the fiscal situation well documented, the entire range of social programs could then be examined to set out the logic for continued federal involvement, and to relate that logic to the actual extent of federal funding and program control. For example, an assessment could be made of the efficiency and equity arguments in favour of such alternatives as complete federal assumption of the responsibility for health care and complete devolution of this function to the provinces. In similar fashion, the responsibility for social assistance would be a key item for discussion.

The revenue structure would also have to be examined, with attention directed not only to the appropriateness of the level of revenues to the allocation of expenditures assumed under various scenarios, but also to the effectiveness of different tax mixes in meeting broad objectives such as control over the national economy and the interpersonal and interregional distribution of incomes. It would be appropriate, in this connection, to seriously investigate the problem of interprovincial fiscal imbalance discussed in this paper, its consequences for the division of powers between the federal and provincial governments, and the alternatives for solving this problem in a way that is fair to all regions of the country.

Ontario does not expect that early and definitive conclusions could be reached on any of these complex issues. The merit of its proposal lies simply in the need to establish a base for future discussions and a sketch of the fundamental alternatives that are before the nation. The 1981-82 fiscal negotiations did not serve the country well because they were not properly situated within a debate about the state of fiscal federalism in Canada. For the same reason, it would be inappropriate, in Ontario's view, for the federal government to proceed unilaterally to restructure its own involvement in the joint programs, as it now seems resolved to do. The imperative is to reach a measure of understanding and consensus, so that new departures, if necessary, can be made in an environment of intergovernmental co-operation and growing public confidence in Canadian federalism.

Conclusion

This paper began by noting an apparently new federal strategy for the conduct of intergovernmental relations. Federal spokesmen have repeatedly suggested that provinces are greedy and unco-operative, and that the country is now too decentralized in its fiscal structure. This, in the federal view, seems to mandate increased retrenchment in intergovernmental transfers and a move to a unilateral approach in the design of programs previously undertaken jointly with the provinces.

Ontario believes that the emerging federal strategy is based on a flawed view of fiscal developments in Canada during the past decade and a half. Moreover, it is a strategy that may lead to new and increasing strains in the federal-provincial partnership.

There is a new problem in Canada—a problem of regional fiscal imbalance deriving from the uneven distribution of natural resources. The federal budget proposals and the ensuing fiscal arrangements discussions avoided this critical issue almost completely, despite its centrality to the programs being renegotiated. Official federal thinking continues to turn on the traditional distinction between the federal and provincial orders of government, but this is no longer the axis upon which fiscal federalism is evolving in Canada.

The rebuilding of Canadian federalism will require new ideas, greater federal leadership and a rejuvenation of intergovernmental co-operation. This is the challenge ahead. Ontario has put forward some modest suggestions for consideration by the federal government and other provinces.

Co-operation within the Canadian federation is not ordained to failure. Canadians and their governments can and must make it work.

. . . I made a speech in British Columbia where I went on at great length indicating what I thought the new federalism would be.

. . . the old type of federalism where we give money to the provinces, where they kick us in the teeth because they didn't get enough and they go around and spend it and say, of course, it is all from us, that type of federalism is finished, and I think I indicated why. . . . The provinces are occupying immensely more fiscal room and expenditure room than they did 20 years ago. In other words, the pendulum has swung very strongly towards decentralization of spending, of finances, of taxing powers, tax room, and so on. I was announcing that that would come to an end; there was not much point transferring literally hundreds of billions of dollars over the years to the provinces and weakening the federal government's ability to manage the macro-economy, and to spend money in areas of federal jurisdiction when the only result of that was that the provinces' appetite kept growing and they kept asking for more . . . and they still said, "Not enough." So, I said, "Well, there is no point trying to please them, so let us at least try and please ourselves and hopefully those Canadian people who think that there must be a Government of Canada which will have some powers left and some tax room left," and that is the new federalism, if you want to call it that.

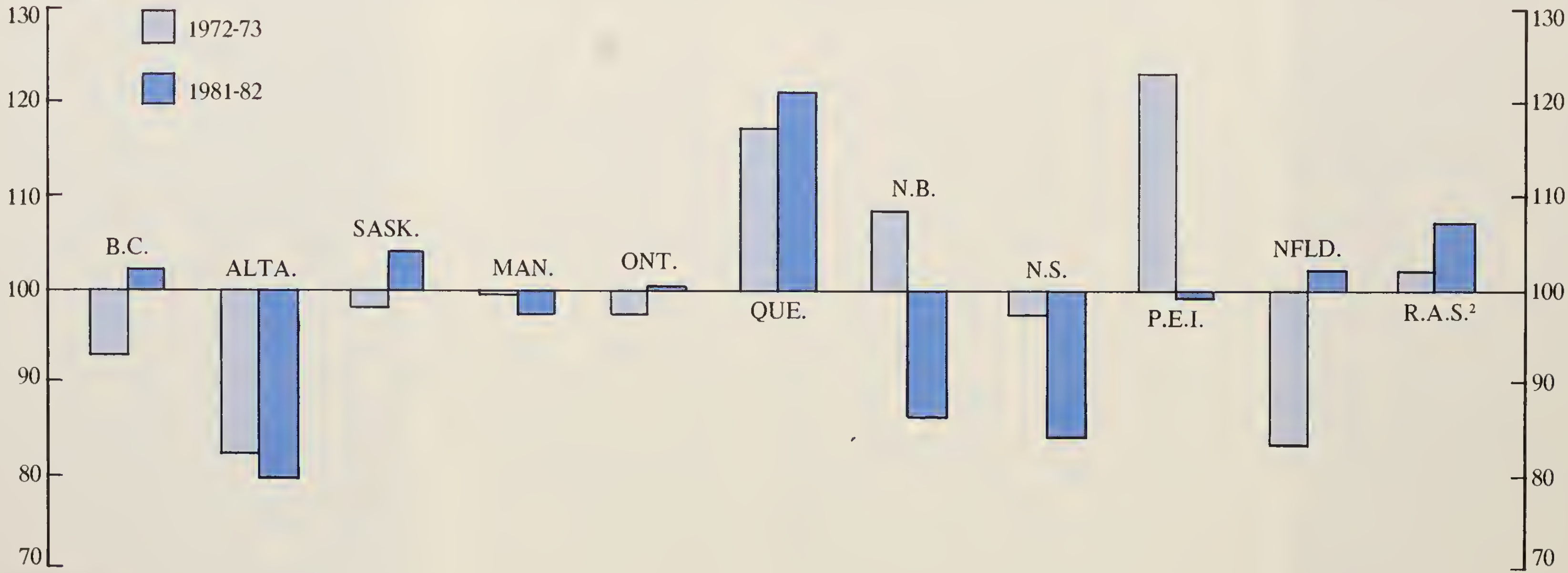
. . . we have tried governing through consensus; we have tried governing by being generous to the provinces, even in the constitutional area; and we have tried governing in 1979 by offering a rather massive transfer of powers to the provinces, and that was never enough. So, we have changed that and we have said on the Constitution, as we are doing on the economy, there is not much point shifting powers and resources to the provinces because there is no stop. The pendulum will keep swinging until we end up with a community of communities or a federation of — a confederation of shopping centres, or whatever it is, and that is not my view of Canada. I thought that we could build a strong Canada through co-operation. I have been disillusioned.

Prime Minister Trudeau
February 25, 1982

Appendix Chart 1

Indices of Relative Tax Effort, 1972-73 and 1981-82 (Own Source Revenues[1])

(National Average = 100)



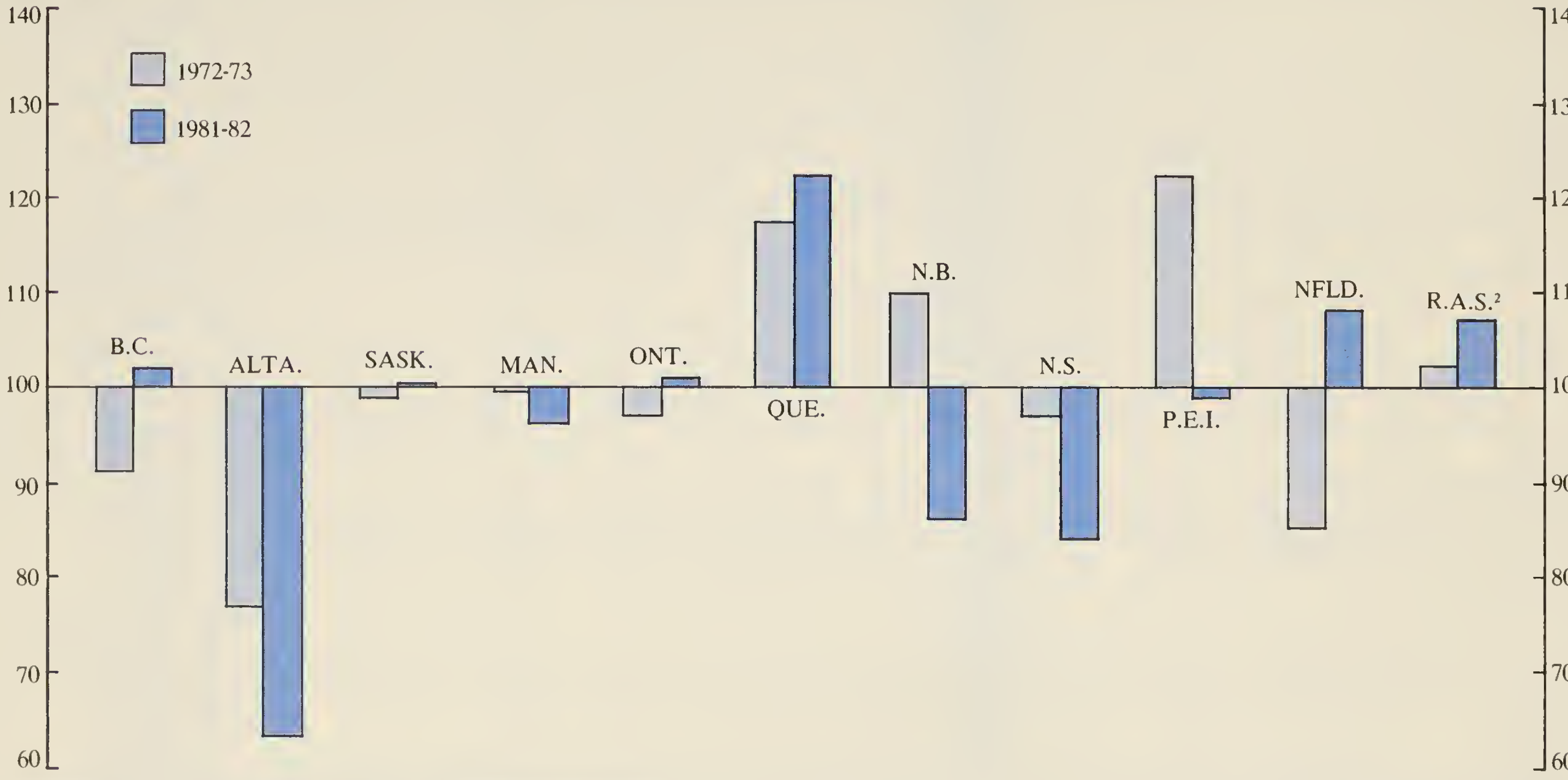
Source: Appendix Table 4.

[1]All provincial-local revenues included in the 1982-1986 equalization program.

[2]Representative Average Standard provinces: Que., Ont., Man., Sask. and B.C.

Appendix Chart 2

Indices of Relative Tax Effort, 1972-73 and 1981-82
(Own Source Less Natural Resource Revenues[1])
(National Average = 100)



Source: Appendix Table 4.

[1]All provincial-local revenues included in the 1982-1986 equalization program.
[2]Representative Average Standard provinces: Que., Ont., Man., Sask. and B.C.

Expenditure and Revenue Shares by Level of Government (after transfers)

Appendix Table 1

	Expenditures[1]			Revenues[1]		
	Federal Share	Provincial Share	Local Share	Federal Share	Provincial Share	Local Share
1945	82.3	9.3	8.4	69.2	16.7	14.1
1946	72.1	14.7	13.2	68.0	17.8	14.2
1947	59.3	22.0	18.7	65.2	20.1	14.6
1948	53.3	25.4	21.3	62.6	21.3	16.1
1949	53.0	25.7	21.3	60.3	22.2	17.5
1950	51.9	26.0	22.1	59.8	22.8	17.5
1951	56.2	23.2	20.7	64.5	20.1	15.4
1952	62.4	18.6	19.0	64.8	19.3	15.8
1953	62.3	18.2	19.5	63.8	19.5	16.7
1954	59.6	19.0	21.4	61.3	20.5	18.2
1955	58.1	19.8	22.1	61.1	20.3	18.6
1956	56.1	21.3	22.6	61.4	20.1	18.5
1957	55.0	21.6	23.4	58.0	21.8	20.2
1958	55.4	21.4	23.1	53.5	23.5	23.0
1959	52.6	23.4	24.0	52.3	24.7	23.0
1960	50.5	24.8	24.7	51.6	24.3	24.1
1961	50.0	25.6	24.5	49.9	24.9	25.1
1962	48.4	26.0	25.6	47.0	27.0	26.0
1963	46.6	26.9	26.5	46.5	27.4	26.2
1964	45.6	28.3	26.1	47.5	27.6	24.9
1965	43.1	29.6	27.3	45.9	29.3	24.8
1966	42.6	30.5	26.9	44.4	30.0	25.6
1967	41.4	32.4	26.2	42.5	32.0	25.6
1968	40.5	33.2	26.3	41.3	33.7	25.0
1969	39.7	33.8	26.5	42.2	34.0	23.8
1970	38.3	35.6	26.0	39.8	35.4	24.9
1971	37.5	37.3	25.2	38.3	37.1	24.6
1972	39.5	36.7	23.8	39.5	36.3	24.3
1973	39.6	36.7	23.7	40.6	36.7	22.7
1974	40.1	37.3	22.7	40.6	38.3	21.1
1975	39.8	38.1	22.1	38.1	38.7	23.2
1976	39.0	38.5	22.5	37.7	39.2	23.1
1977	39.1	38.7	22.3	33.7	41.5	24.8
1978	40.1	38.0	21.9	32.0	43.7	24.3
1979	39.2	38.5	22.3	33.0	42.3	24.7
1980	39.1	38.9	22.0	34.1	42.5	23.4

Source: Department of Finance, *Economic Review*, April 1981.

[1]Starting in 1974, expenditures exclude the federal oil import subsidy and Petroleum Compensation Revolving Fund. From 1973 on, revenues exclude the federal oil export charge.

Shares of Comprehensive Tax Base, Selected Fiscal Years

Appendix Table 2

(per cent)

Measure of Tax Base	Nfld.	P.E.I.	N.S.	N.B.	Que.	Ont.	Man.	Sask.	Alta.	B.C.	R.A.S.[1]
1982-86 Representative Tax System											
Own Source Revenues											
1972-73	1.50	0.31	2.63	2.08	23.53	39.68	4.10	3.58	10.18	12.42	83.30
1976-77	1.46	0.29	2.38	1.98	22.21	35.55	3.78	4.26	16.08	12.01	77.81
1981-82	1.38	0.28	2.29	1.89	20.60	33.23	3.33	4.47	20.01	12.52	74.15
1986-87	1.31	0.26	2.18	1.79	19.00	31.08	3.04	4.19	24.14	13.00	70.32
Own Source Revenues Plus Equalization											
1972-73	2.06	0.43	3.19	2.55	25.12	37.25	4.24	3.95	9.56	11.66	82.21
1976-77	2.06	0.44	3.12	2.55	24.03	33.38	4.01	4.03	15.10	11.28	76.73
1981-82	1.95	0.42	2.93	2.41	22.86	31.10	3.71	4.18	18.73	11.72	73.57
1986-87	1.88	0.40	2.82	2.32	21.15	29.23	3.32	3.94	22.70	12.23	69.88
Own Source Revenues Plus All Transfer Payments											
1972-73	2.31	0.53	3.31	2.72	26.57	36.16	4.32	3.92	9.21	10.95	81.93
1976-77	2.24	0.54	3.28	2.75	25.27	32.98	4.14	4.04	13.70	11.07	77.49
1981-82	2.11	0.49	3.11	2.64	23.90	31.03	3.80	4.23	17.14	11.55	74.52
1986-87	2.00	0.44	2.99	2.49	22.41	29.45	3.40	4.01	20.78	12.03	71.31
Own Source Revenues Less Natural Resources											
1972-73	1.48	0.32	2.74	2.13	24.20	41.18	4.23	3.49	8.45	11.78	84.88
1976-77	1.51	0.32	2.61	2.15	24.19	38.82	4.10	4.07	10.23	12.00	83.18
1981-82	1.45	0.31	2.57	2.09	22.98	37.12	3.67	4.10	12.85	12.86	80.74
1986-87	1.44	0.30	2.55	2.06	22.12	36.24	3.50	4.03	14.35	13.41	79.30

Sources: Department of Finance; Ontario Treasury.

[1]Representative Average Standard provinces: Que., Ont., Man., Sask. and B.C.

Appendix Table 3

Indices of Tax Base Per Capita, Selected Fiscal Years
(National Average=100)

Measure of Tax Base	Nfld.	P.E.I.	N.S.	N.B.	Que.	Ont.	Man.	Sask.	Alta.	B.C.	R.A.S.[1]
1982-86 Representative Tax System											
Own Source Revenues											
1972-73	62	59	72	71	85	110	90	85	134	120	101
1976-77	60	57	66	67	82	99	85	106	201	112	94
1981-82	59	55	66	66	78	94	79	112	217	111	91
1986-87	57	52	63	63	74	89	75	105	237	109	87
Own Source Revenues Plus Equalization											
1972-73	85	84	87	87	90	104	93	94	125	113	99
1976-77	85	85	86	86	88	93	90	100	188	105	93
1981-82	83	83	84	84	86	88	88	105	203	104	90
1986-87	82	82	82	82	82	84	82	99	223	103	87
Own Source Revenues Plus All Transfer Payments											
1972-73	95	102	91	92	95	101	95	93	121	106	99
1976-77	92	104	91	93	93	91	93	100	171	103	94
1981-82	90	96	89	92	90	87	90	106	186	102	91
1986-87	87	91	87	88	87	84	84	101	204	101	88
Own Source Revenues Less Natural Resources											
1972-73	61	62	75	72	87	115	93	82	111	114	103
1976-77	62	62	72	73	89	108	92	101	128	112	101
1981-82	62	62	73	73	87	104	87	103	139	114	99
1986-87	63	62	74	73	86	104	86	101	141	113	98

Sources: Department of Finance; Ontario Treasury.

[1]Representative Average Standard provinces: Que., Ont., Man., Sask. and B.C.

Indices of Relative Tax Effort, Selected Fiscal Years

(National Average=100)

Appendix Table 4

Measure of Tax Base	Nfld.	P.E.I.	N.S.	N.B.	Que.	Ont.	Man.	Sask.	Alta.	B.C.	R.A.S.[1]
1982-86 Representative Tax System											
Own Source Revenues											
1972-73	83	123	97	108	117	97	100	98	82	93	102
1976-77	99	100	93	93	120	96	103	99	78	105	105
1981-82	102	99	84	86	121	100	97	104	79	102	107
Own Source Revenues Plus Equalization											
1972-73	88	115	97	106	115	97	100	99	82	93	102
1976-77	99	100	95	95	117	96	103	99	78	105	105
1981-82	101	99	89	90	118	100	97	104	79	102	106
Own Source Revenues Plus All Transfer Payments											
1972-73	91	110	98	105	111	98	100	99	85	94	102
1976-77	100	100	96	96	113	97	102	99	81	104	104
1981-82	101	99	91	92	115	100	98	104	80	101	105
Own Source Revenues Less Natural Resources											
1972-73	85	122	97	110	117	97	100	99	77	91	102
1976-77	103	100	93	93	121	96	103	97	63	104	105
1981-82	108	99	84	86	122	101	96	100	63	102	107
Own Source Revenues Less Natural Resources Adjusted for Surplus (Deficit)											
1972-73	107	115	96	113	120	99	92	90	76	82	102
1976-77	130	97	93	103	129	102	104	90	30	96	108
1981-82[2]	112	96	96	93	141	108	104	90	5	100	115

Sources: Department of Finance; Ontario Treasury; Statistics Canada, Catalogue 13-213.

[1]Representative Average Standard provinces: Que., Ont., Man., Sask. and B. C.

[2]Surplus and deficit data used pertain to 1980-81 except for Ontario. Ontario's deficit for 1981-82 is estimated to be $1,500 million.

Appendix Table 5

Increase in Fiscal Arrangements Entitlements (Provincial tax plus federal cash) 1981-82 to 1982-83
($ million)

	1981-82			New Fiscal Arrangements for 1982-83[1]			Per Cent Increase		
	EPF[2]	Equalization	Total	EPF[2]	Equalization	Total	EPF[2]	Equalization	Total
Nfld.	220	427	647	224	516	740	1.8	20.8	14.4
P.E.I.	47	103	150	48	123	171	2.1	19.4	14.0
N.S.	349	509	858	361	601	962	3.4	18.1	12.1
N.B.	280	414	694	287	489	776	2.5	18.1	11.8
Que.	2,893	2,322	5,215	3,008	2,572	5,580	4.0	10.8	7.0
Ont.	4,066	—	4,066	4,282	—	4,282	5.3	—	5.3
Man.	446	387	833	463	425	888	3.8	9.8	6.6
Sask.	456	—	456	482	—	482	5.7	—	5.7
Alta.	1,102	—	1,102	1,136	—	1,136	3.1	—	3.1
B.C.	1,294	—	1,294	1,380	—	1,380	6.6	—	6.6
All Provinces	11,153	4,162	15,315	11,671	4,726	16,397	4.6	13.6	7.1

Sources: Ontario Treasury; Department of Finance.

[1]Figures do *not* include special payments introduced to compensate some provinces for recovery of past equalization overpayments arising from census population adjustments. These payments are expected to flow to provinces in 1982-83 in the following estimated amounts:

Nfld.	P.E.I.	N.S.	N.B.	Man.	Total
68	8	44	58	29	207

[2]To avoid double counting, the EPF figures exclude the equalization associated with the EPF income tax points. As this equalization component of EPF increased markedly with the switch to a five-province standard, its exclusion suppresses the EPF growth rates shown for equalization recipient provinces.

Increase in Federal Cash Transfers 1981-82 to 1982-83
($ million)

Appendix Table 6

	1981-82			New Fiscal Arrangements for 1982-83[1]			Per Cent Change		
	E.P.F.	Equalization	Total	E.P.F.	Equalization	Total	E.P.F.	Equalization	Total
Nfld.	164	427	591	159	516	675	−3.0	20.8	14.2
P.E.I.	35	103	138	34	123	157	−2.9	19.4	13.8
N.S.	245	509	754	238	601	839	−2.9	18.1	11.3
N.B.	201	414	615	195	489	684	−3.0	18.1	11.2
Que.	1,309[2]	2,322	3,631	1,164[2]	2,572	3,736	−11.1[2]	10.8	2.9[2]
Ont.	2,362	—	2,362	2,293	—	2,293	−2.9	—	−2.9
Man.	296	387	683	286	425	711	−3.4	9.8	4.1
Sask.	306	—	306	299	—	299	−2.3	—	−2.3
Alta.	561	—	561	466	—	466	−16.9	—	−16.9
B.C.	697	—	697	665	—	665	−4.6	—	−4.6
All Provinces	6,176	4,162	10,338	5,799	4,726	10,525	−6.1	13.6	1.8

Sources: Ontario Treasury; Department of Finance.

[1]Figures do *not* include special payments introduced to compensate some provinces for recovery of past equalization overpayments arising from census population adjustments. These payments are expected to flow to provinces in 1982-83 in the following estimated amounts:

Nfld.	P.E.I.	N.S.	N.B.	Man.	Total
68	8	44	58	29	207

[2]Under "contracting out" arrangements with the federal government, Quebec receives a special abatement of 8.5 personal income tax points in lieu of a portion of EPF cash. If this abatement, valued at $555 million in 1981-82 and $646 million in 1982-83, were added to Quebec's cash for comparison with other provinces, the change in EPF cash for Quebec would be −2.9% and the change in fiscal arrangements cash would be 4.7%.

Spending Comparisons for Health and Post-Secondary Education

Appendix Table 7

(Per Cent of Total Provincial-local Government Expenditures[1])

	1972-73	1973-74	1974-75	1975-76	1976-77	1977-78	1978-79	1979-80	1980-81	Estimated 1981-82
Provincial-Local Health Expenditures[2]										
Ontario	24.1	23.5	23.1	23.4	24.1	23.6	23.7	24.4	25.6	26.2
All Provinces	22.7	22.5	21.7	22.1	22.1	21.7	21.9	22.2	22.7	23.2
Provincial-Local Post-Secondary Education Expenditures[2]										
Ontario	8.5	8.5	8.0	7.7	8.1	8.0	8.0	7.9	7.7	7.4
All Provinces	8.5	8.5	8.1	8.1	8.1	7.8	7.8	7.6	7.3	7.3

Sources: Federal-Provincial Subcommittee of Officials on EPF Data; Statistics Canada, Catalogues 68-202, 68-203, 68-205; Ontario Treasury.

[1]Operating and capital expenditures (excluding public debt interest).

[2]Operating and capital expenditures.

Budget Paper C

Public Investment and Responsible Financial Management

Table of Contents

Introduction 3

I Capital Investment and Borrowing 4
- Accounting for Public Sector Capital Investment 4
- Composition of Provincial Capital Investment 5
- Financing Capital Investment 8
- Ontario Hydro 11

II Debt Structure and Servicing Capacity 12
- **Debt Structure** 12
  - Public Sector Debt 12
  - Provincial Funded Debt 14
- **Capacity to Service Debt** 15
  - Public Sector Debt 16
  - Provincial Funded Debt 16

III Future Investment Directions 18
- Industrial Development 18
- Financing Considerations 20

Conclusion 21

Review of the 1981 Budget and Financial Tables

Review of the 1981 Budget 23

Tables
- C1 Statement of Provincial Net Cash Requirements and Related Financing 27
- C2 Revenue 28
- C3 Expenditure 29

C4 Payments from the Federal Government. 33
C5 Payments into Trust Accounts. 33
C6 Repayments of Loans and Advances. 33
C7 Expenditure by Category. 34
C8 Payments to Local Governments and Agencies. 35
C9 Public Service Strength in Ontario, March 31, 1982. 37
C10 Ten-Year Review of Selected Financial and Economic Statistics. 38

Charts

C1 Revenue Sources, 1978-79 to 1982-83. 30
C2 Expenditure Functions, 1978-79 to 1982-83. 31
C3 Months of Revenue Required to Repay Provincial Funded Debt. 32
C4 Provincial Funded Debt and Publicly-Held Debt. 32
C5 Increasing Efficiency in the Ontario Public Service. 36
C6 Expenditure and Net Cash Requirements as a Per Cent of Gross Provincial Product. 36
C7 The Budget Dollar, 1982-83. 40

Public Investment and Responsible Financial Management

Introduction

Perhaps more than any other aspect of public finance, the level of government borrowing and debt is a matter of public concern and criticism. While the financial community may objectively evaluate the capacity of various governments to undertake deficit financing, the general public more often than not views government borrowing as symptomatic of an inability of the public sector to live within its means. Often such concern is heightened by the other commonly-held belief that government debt is growing too fast and that this will place an unjust financial burden on future generations of taxpayers.

This paper examines in detail these concerns in relation to Ontario. It is suggested that debt financing is a legitimate and, in some cases, even preferable means of paying for capital investments that provide economic and social benefits over a period of years. Therefore, one important criterion in determining whether government is spending appropriately is not the existence of debt *per se*, but the longer term relationship between borrowing and public capital investment.

Another element that needs to be considered in assessing the appropriate levels of deficits is their utilization by governments as a tool of fiscal policy; that is, deficits may be expanded temporarily to stimulate economic growth, or reduced in order to cool down inflationary pressures.[1]

A further aspect is, of course, the capacity of government to carry its debt. Even if it is theoretically legitimate to finance capital spending through long-term debt, this should not be done if tax revenues are only sufficient to service the debt by drawing funds away from needed operating expenditures. Using a number of yardsticks, this paper shows that the relative level of public debt in Ontario has remained fairly constant over the past decade. Finally, the paper discusses new directions and priorities for public investment in Ontario, while also recognizing certain financing limitations.

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[1]For a discussion of the utilization of fiscal policy in Ontario, see Ontario Tax Studies 15, *Reassessing the Scope for Fiscal Policy in Canada* (Toronto: Ministry of Treasury, Economics and Intergovernmental Affairs, 1978).

I Capital Investment and Borrowing

Capital investment is an important aspect of the role and responsibilities of government in our society, be it in the provincial government and its own agencies, or the local government sector. In its responsibility for many social services, government is a major investor in physical assets—hospitals, schools, colleges, universities, and housing. In co-ordinating the development of the basic infrastructure of our society and economy, government invests heavily in roads, rail and air transit facilities, water and sewerage plants, and buildings for administration of government and justice. Governments are the custodians of enormous resources—forests, mineral reserves, water, parks, and the environment generally—and must invest in these resources to ensure their quality and effectiveness in the future. Finally, governments have an investment role as catalysts to economic growth, ensuring the capacity of the private sector to remain competitive, to take advantage of new opportunities, and to provide jobs and incomes to an expanding workforce.

Accounting for Public Sector Capital Investment

While there is no rigorous definition of public sector capital investment, it may generally be defined as the creation or acquisition of assets that have a life span of more than one year and provide public benefits beyond the initial year.

In the private sector, the cost of capital investments is normally spread in the form of depreciation over the period of time in which the investment is expected to produce income for the business. This is based upon the well-accepted commercial principle that to charge the cost of assets against one year's income would grossly distort the true financial picture, understating income in the year of acquisition and overstating it in subsequent years.

At the federal and provincial levels of government, the theory of accounting for capital assets is different from that of the private sector.[2] A business invests in capital to produce revenue for itself. A government usually does not undertake a capital investment to produce directly tax or some other kind of revenue. The benefits of public investments are normally meant to apply to the community at large, or some part of it, with the return to government flowing indirectly via a better society and a stronger economy.

Public sector capital investments are acquired to create specific benefits for society. Before any such capital investment is approved, Ontario, like all provincial governments, applies certain criteria of need before a decision is undertaken to construct, for instance, a

[2]See *Financial Reporting by Governments*, A Research Study of The Canadian Institute of Chartered Accountants, Chapter 2 (Toronto, 1980).

hospital, a school, or a new highway. It is also possible to set priorities to determine whether it is more important to provide, for example, a hospital in one community rather than another.[3]

The need for capital investment can be established on the basis of reasonably objective criteria. However, the contribution of such capital to social services, economic growth and provincial revenue is much more difficult to measure with precision. The Province and its agencies are today involved in the creation of so many different kinds of public capital that a myriad of categories and measures would be needed. While some of these assets are totally Provincial, many are owned by municipalities, school boards, universities, hospital boards and other agencies which receive substantial Provincial grants, subsidies or loans. The Legislature, of course, exercises final authority through Estimates review on an annual basis.

Because of these principles and complexities, it is common practice for senior orders of government to treat the creation and acquisition of physical assets, by themselves or their agencies, as current expenditure. This is the case in Ontario. Capital investments which are capitalized and not treated as current expenditures are those which normally result in direct financial claims on third parties (i.e. loans to corporations, agencies, municipalities, etc.). This treatment of investments has the advantage of simplicity and also imposes a discipline on the use of public revenues.

This accounting method clearly focuses on cash requirements, financing, debt, and financial assets. However, it tends to mask the value of future social and economic benefits associated with capital investment. While government may undertake debt financing to pay for public sector capital investment, such financing may be perceived by the public to be borrowing to pay substantially for current expenditures. In fact, as demonstrated in this paper, borrowing issued by the Province in the past decade has been less than the public sector investment made over the same period.

The rest of this section demonstrates this point by reviewing briefly the composition of Ontario's capital investment during the past decade and relates the magnitude of this investment to borrowing.

Composition of Provincial Capital Investment

Since World War II, Ontario has undertaken marked shifts in the level and type of its capital investments to underpin the growth of a maturing industrial economy and adjust to changing social priorities.

[3]To outline in detail the criteria used by the Province of Ontario to determine the need for, and timing of, the creation of public assets is beyond the scope of this paper. Each ministry involved in the creation of physical assets employs a detailed set of criteria to govern the queuing process which sets priorities on funds available for investment.

Here, the paper focuses on the composition of capital investment over the last ten years, which has been related primarily to three major factors—the size and composition of the population, urbanization, and economic conditions.

Table 1 indicates the size and composition of Ontario's population since 1965. While the number of people in the province is still increasing, the growth rate has declined considerably. From 1965 to 1970, the population grew by over 11 per cent, while from 1975 to 1980 the growth rate was a little below five per cent. The age composition of the population has also changed markedly. In 1970, the post-war baby boom was still fueling rapid growth in the number of young people, but by 1980 the number of people aged 5 to 19 was actually declining. On the other hand, the growth in the number of elderly people exceeded the rate of overall population growth throughout the last decade. Today, there are actually fewer young people (up to age 19) in Ontario than there were 10 years ago. On the other hand, the province has almost 300,000 more elderly people than it did in 1965. Another significant trend during the 1970s was the extremely rapid growth in young families (age 20-34). From 1965 to 1980, the number of people in this category grew by over 70 per cent.

Population Change in Ontario, 1965 to 1985 — Table 1
(thousands)

Age Group	1965	1970	1975	1980	1985[1]
4 and under	760	655	624	604	617
(% change)		(13.8)	(4.7)	(3.2)	2.2
5–19	1,985	2,253	2,279	2,145	1,952
(% change)		13.5	1.2	(5.9)	(9.0)
20–34	1,314	1,637	1,991	2,235	2,451
(% change)		24.6	21.6	12.3	9.7
35–64	2,174	2,380	2,563	2,749	3,114
(% change)		9.5	7.7	7.3	13.3
65 and over	555	626	715	841	955
(% change)		12.8	14.2	17.6	13.6
Total Ontario	6,788	7,551	8,172	8,574	9,089
(% change)		11.2	8.2	4.9	6.0

[1]Ontario Treasury estimate.

Dealing with these variations in the population has been a challenge for the management of public capital investment in Ontario. A complete description of the Province's investment policy throughout the 1970s is beyond the scope of this paper but has been described elsewhere.[4] Table 2 provides a summary of the capital investment

[4]Hon. W. Darcy McKeough, "Ontario's Borrowing and Public Capital Creation", Budget Paper A, *Ontario Budget 1978* (Toronto: Ministry of Treasury, Economics and Intergovernmental Affairs, 1978); and Hon. Frank S. Miller, "A Solid Fiscal Foundation for the 1980s", Budget Paper C, *Ontario Budget 1980* (Toronto: Ministry of Treasury and Economics, 1980).

Ontario's Capital Investment Record,[1] 1972-73 to 1981-82

Table 2

($ million)

	1972-73	1973-74	1974-75	1975-76	1976-77	1977-78	1978-79	1979-80	1980-81	Interim 1981-82
Social Investments										
Educational	264	161	128	144	113	111	91	90	58	72
Health and Social Services	163	149	155	185	155	175	153	111	187	222
Recreational and Cultural	9	18	17	46	36	66	85	78	50	99
	436	328	300	375	304	352	329	279	295	393
Economic Investments										
Transportation	339	432	468	544	499	641	591	688	680	722
Environmental	115	130	211	290	280	263	271	261	276	271
Commercial Loans	43	28	45	52	30	42	40	39	33	35
Employment Development/BILD[2]	—	—	—	—	—	—	—	128	124	150
Other	2	2	5	11	13	15	15	21	39	50
	499	592	729	897	822	961	917	1,137	1,152	1,228
Other										
Financial Assets	64	103	133	206	238	119	35	—	—	325
Land	82	173	195	103	62	62	64	106	27	12
Miscellaneous	22	30	42	46	54	42	16	39	35	60
	168	306	370	355	354	223	115	145	62	397
Total	1,103	1,226	1,399	1,627	1,480	1,536	1,361	1,561	1,509	2,018

[1]Excludes Ontario Hydro.

[2]The Employment Development Fund was established in 1979 and was succeeded by the Board of Industrial Leadership and Development in 1981.

record from 1972-73 to 1981-82. Overall, it shows that the annual level of capital investment rose from about $1.1 billion in 1972-73 to $1.6 billion in 1975-76 and then stayed roughly constant at a point slightly below that level until the fiscal year just completed, when it rose to over $2 billion.

The composition of capital investment during this period was closely related to demographic and urbanization trends. The table shows that new educational investments have largely been scaled down throughout the decade, reflecting the flattening of growth in the number of Ontario students. On the other hand, the rapid increase in the household-formation age group, combined with fast-paced urbanization, required a large increase in public investments for roads, transit, and water and sewerage, as well as recreational and cultural facilities. Investments related to health care and social services were relatively high in the early part of the decade to establish the needed capital for new programs, and then were constrained in the latter part of the 1970s in order to promote more efficiency in the delivery of health and social services.

The Province entered the decade financing a relatively high level of capital investment. In 1972-73, total capital spending represented about one-seventh of Provincial expenditure. In the latter part of the 1970s, the rate of capital spending was deliberately decelerated, partly as a result of the Provincial restraint program, and partly to reflect a reduced growth rate in the Ontario population. By 1981-82, capital investments represented about one-tenth of Provincial spending.

Financing Capital Investment

Financing capital investment through borrowing provides a means of spreading the cost of public assets over a period roughly equivalent to the stream of benefits derived from those assets. Accordingly, one important measure of the appropriate level of debt undertaken by the public sector is the relationship of borrowing to investment.

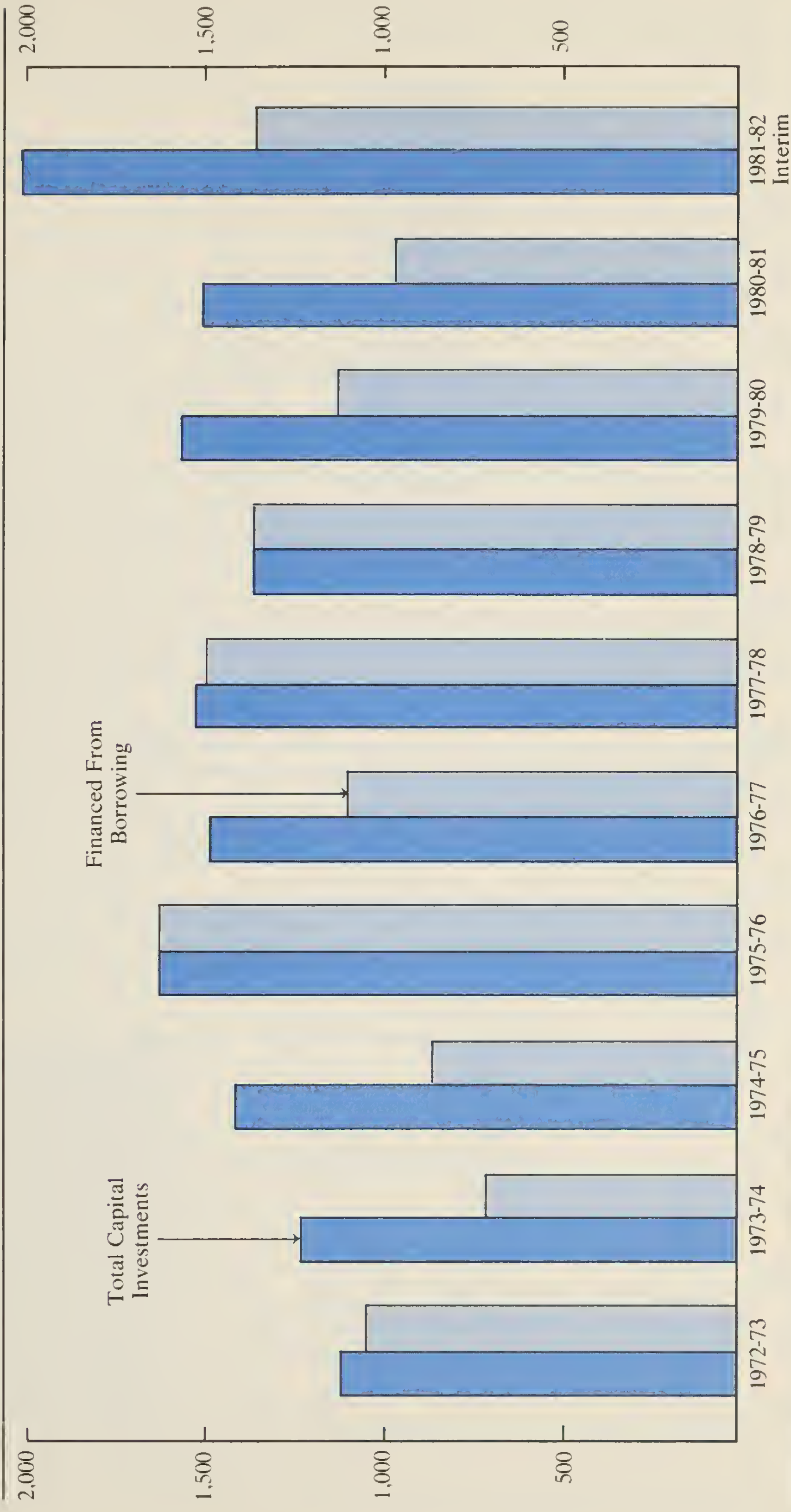
Chart 1 and Table 3 display net Provincial borrowing and total capital investment in Ontario since 1972. They show that, in total, some $14.8 billion of investment was financed by borrowing totalling $12.3 billion and tax revenues of $2.5 billion. This indicates that the overall level of borrowing has been prudent and has virtually all been dedicated to Ontario's capital investment.

As indicated in the table, there were only two years when borrowing exceeded capital spending. In 1975, the Province allowed the deficit to increase significantly in order to stimulate the economy. In 1978, capital investment was unusually low as a result of the Government's expenditure restraint program, and some $300 million of borrowed funds were used to augment cash reserves.

Chart 1

The Financing of Ontario's Capital Investments,[1] 1972-73 to 1981-82

($ million)



[1]Excludes Ontario Hydro.

Financing Capital Investment,[1] 1972-73 to 1981-82 — Table 3

($ million)

	Ontario's Capital Investment	Sources of Financing	
		Net Borrowing	Revenues
1972-73	1,103	1,032	71
1973-74	1,226	710	516
1974-75	1,399	851	548
1975-76	1,627	1,974	(347)
1976-77	1,480	1,092	388
1977-78	1,536	1,506	30
1978-79	1,361	1,652	(291)
1979-80	1,561	1,132	429
1980-81	1,509	968	541
1981-82 Interim	2,018	1,363	655
10-Year Total	14,820	12,280	2,540

[1]Excludes Ontario Hydro.

Table 4 compares the level of borrowing, investment, and total spending during the same period. It documents a point noted earlier in the paper, namely that the Province reduced the annual level of investment in relative terms, since the lower rate of population growth lessened the need for such investment. Further, as a matter of anti-inflationary fiscal policy, the Province decided to reduce its borrowing, and therefore constrained capital expenditures. The table shows that net borrowing has been well below 10 per cent of total spending for the last three years, while capital investment now repre-

Capital Investment and Net Borrowing,[1] 1972-73 to 1981-82 — Table 4

($ million)

	Capital Investment	Net Borrowing	Total Spending	As a Per Cent of Total Spending	
				Capital Investment	Net Borrowing
1972-73	1,103	1,032	7,038	15.7	14.7
1973-74	1,226	710	7,885	15.5	9.0
1974-75	1,399	851	9,832	14.2	8.7
1975-76	1,627	1,974	11,319	14.4	17.4
1976-77	1,480	1,092	12,467	11.9	8.8
1977-78	1,536	1,506	13,544	11.3	11.1
1978-79	1,361	1,652	14,413	9.4	11.5
1979-80	1,561	1,132	15,830	9.9	7.2
1980-81	1,509	968	17,273	8.7	5.6
1981-82 Interim	2,018	1,363	20,415	9.9	6.7

[1]Excludes Ontario Hydro.

sents about 10 per cent of expenditures compared to over 15 per cent at the beginning of the period.

Ontario Hydro

A discussion of public investment in Ontario is not complete without special attention to the activities of Ontario Hydro. Hydro funds its capital construction program from revenue derived from the sale of electric power and from debt financing. Due to the important contribution Hydro makes in overall economic development, and the special relationship between the Province and Ontario Hydro, government financial management is coordinated with Hydro's financing plans and requirements. As a matter of policy, debt financing undertaken by Hydro is guaranteed by the Province. Further, borrowing in the United States capital market is done by the Province on Hydro's behalf. A recent development has been the flow-through of Canada Pension Plan funds from the Province to Hydro when Provincial cash requirement levels have permitted this flexibility.

To ensure long-run security in the supply of electricity, primarily through the development and application of the CANDU nuclear generation technology, Hydro is continuing to invest in upgrading and expanding its facilities. These are financed through borrowing and internal funds. Table 5 shows how the capital construction program of Hydro has been financed since 1972. In total, some $14 billion of new assets have been financed through long-term debt of $11 billion and internal funds of $3 billion.

Ontario Hydro's Capital Formation and Net Long-Term Borrowing, 1972 to 1981 — Table 5
($ million)

	Gross Capital Formation	Net Increase in Long-Term Debt	Funded Internally
1972	562	444	118
1973	997	660	337
1974	890	506	384
1975	1,442	1,463	(21)
1976	1,326	1,287	39
1977	1,425	1,130	295
1978	1,694	1,490	204
1979	1,659	1,117	542
1980	1,529	860	669
1981[1]	2,200	1,725	475
Total	13,724	10,682	3,042

Source: Ontario Hydro Statistical Yearbook, 1979.
Ontario Hydro Annual Reports, 1972-80.

[1]Ontario Treasury estimate.

In addition to ensuring an ample supply of low-cost electricity, Ontario Hydro makes a significant contribution to the Provincial economy. For example, many supply industries benefit directly through the construction program, as do individuals employed in the construction process. In the future, sound capital formation financed by long-term borrowing will continue to provide lasting economic benefits for Ontario.

II Debt Structure and Servicing Capacity

This section deals with the composition of Ontario's debt and examines the various forms of debt and debt instruments that the Province has utilized to finance its capital investment. In addition, it analyzes the capacity of the Province to service its debt.

Debt Structure

Ontario's debt obligations can be divided into two general categories—funded and unfunded debt. Most debt in the Ontario public sector falls into the funded category, which refers to obligations secured by notes or debentures. Unfunded debt, on the other hand, refers to obligations that have no specified term to maturity and are not secured by a debt instrument—such as deposits with the Province of Ontario Savings Office and the obligations of the Public Service Superannuation Fund.

Analysis of provincial debt levels and the ability to service debt usually focuses upon funded debt measures. In part, this is due to the fact that unfunded debt accounts for a relatively small portion of total liabilities. In Ontario's case, unfunded debt accounts for about 14 per cent of total liabilities.[5] Further, funded debt measures assure a standard of conceptual uniformity and comparability across jurisdictions and over time which make it particularly suitable for analytical purposes. The following discussion of Ontario's debt focuses upon funded debt.

Public Sector Debt

The broadest measure of funded debt in the Ontario public sector is Consolidated Public Sector Debt. This consistently measures debt incurred at all levels of provincial jurisdictions, including crown corporations and local levels of government. The consolidated debt approach highlights the effects of Ontario's policy of centralizing public sector financing. This policy, by retaining the major taxing and borrowing powers at the provincial level and by offering support

[5]Total liabilities include borrowing on behalf of Ontario Hydro.

through direct grants, has permitted smaller agencies and local jurisdictions to borrow at a preferred provincial borrowing rate. It has also reduced the number of Ontario public sector borrowers in the capital market.

Table 6 displays the funded debt of the Ontario public sector. Debt issued or guaranteed by the Province itself accounts for over 85 per cent of all public sector debt in Ontario, reflecting the policy of centralized financing. The debt of provincial agencies and corporations accounts for about five per cent of total public sector debt and is accounted for primarily by the Ontario Energy Corporation; and by the Ontario Land Corporation and the Ontario Housing Corporation and their obligations to Canada Mortgage and Housing Corporation.

Consolidated Funded Debt of the Ontario Public Sector
(as at March 31st, 1982)

Table 6

	Amount	Distribution
	($ billion)	(%)
Provincial Direct and Guaranteed		
Provincial Purposes — Direct Debt	17.6	47.4
Provincial Hydro Debt and Guarantees	14.0	37.7
Sub-Total	31.6	85.1
Other Public Sector		
Provincial Agencies	1.8	5.0
Local Government Sector	3.5	9.5
University and Hospital Sector	0.2	0.4
Sub-Total	5.5	14.9
Total	37.1	100.0

Source: Ontario Treasury, interim figures.

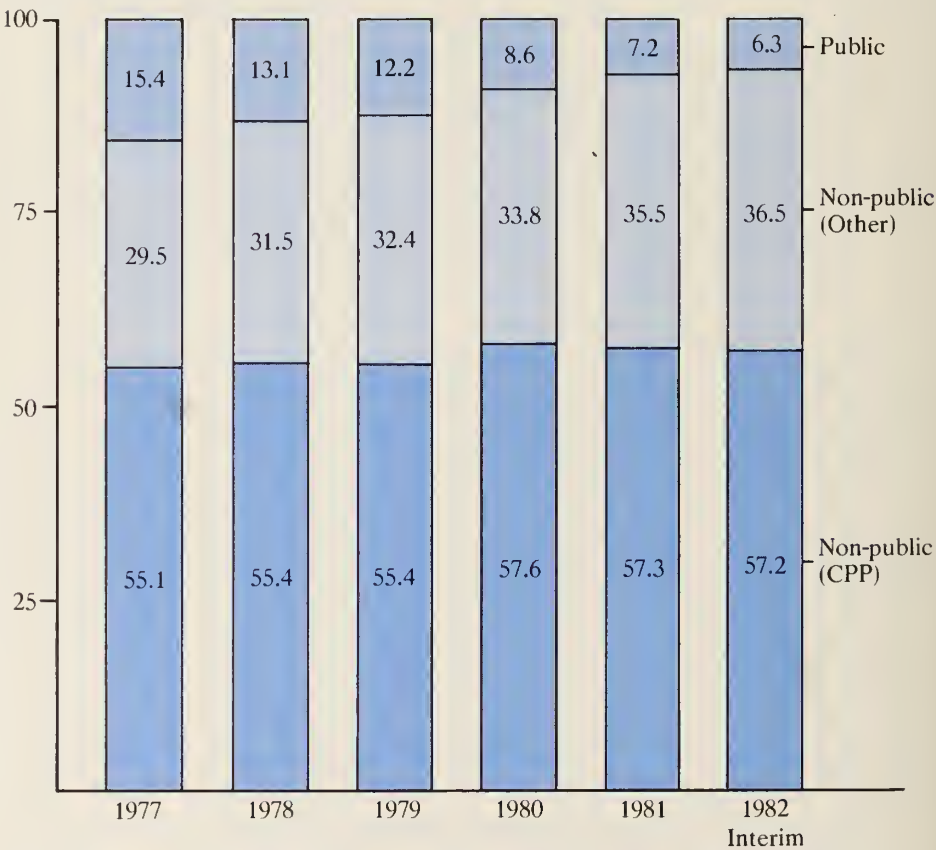
Due to Ontario's policy of centralized financing, there is a limited requirement for public borrowing by local bodies. Internal funds and Provincial capital grants finance about half of local capital expenditures, with the remainder financed by borrowing. The role of the Province is reinforced by the Provincially-appointed Ontario Municipal Board which regulates municipal financing. Public borrowing is concentrated in a few large municipalities and accounts for less than 10 per cent of the total Ontario public sector debt. Less than one-half of one per cent consists of the obligations of universities, colleges, and hospitals.

Ontario direct and guaranteed debt consists almost exclusively of obligations for the Province's own purposes and debt incurred either on behalf of Ontario Hydro or Hydro debt guaranteed by the Province. More than 40 per cent of Ontario's direct and guaranteed funded debt is accounted for by Ontario Hydro, which is effectively the sole user of the Ontario guarantee in capital markets.

Provincial Funded Debt

Ontario's direct own-purpose funded debt, excluding Ontario Hydro, is made up of borrowing from public and non-public sources. The structure of Ontario's own-purpose debt is displayed in Chart 2. Non-public debt, which accounts for about 94 per cent of Ontario's own-purpose debt, consists primarily of funds borrowed from the Canada Pension Plan, the Teachers' Superannuation Fund and the Ontario Municipal Employees Retirement Fund.[6] These funds are invested in long-term, non-marketable securities at market-related rates of interest. These pension plans are thereby provided a safe and competitive investment vehicle, while the Province is provided with a stable source of funds which reduces demands on public capital

Composition of Ontario's Own-Purpose Funded Debt,[1] 1977 to 1982 Chart 2
(per cent of total)



[1]As at March 31.

[6]Ontario has not borrowed from the Ontario Municipal Employees Retirement Fund since 1978-79. See Hon. W. Darcy McKeough, "Ontario's Borrowing and Public Capital Creation", Budget Paper A, *Ontario Budget 1978* (Toronto: Ministry of Treasury, Economics and Intergovernmental Affairs, 1978).

markets. Publicly-held debt accounts for the remaining six per cent of Ontario's own-purpose debt.

The record of Ontario's public and non-public borrowing is shown in Table 7. In most years since 1972, the Province has been retiring, on a net basis, publicly-held debt. In only three of the last ten years has Ontario entered the public market for funds, with 1975-76 representing the only significant year for public borrowing. In that year, as noted earlier in this paper, the Government financed a major expansionary fiscal policy to support a recovery in business activity. Over the last 10 years, Ontario's publicly-held debt has been reduced by $345 million to a level of $1,102 million.

Public and Non-Public Borrowing Levels, 1972-73 to 1981-82 — Table 7
($ million)

	Net Public Borrowing	Net Non-Public Borrowing
1972-73	252	780
1973-74	(228)	938
1974-75	(305)	1,156
1975-76	743	1,231
1976-77	(230)	1,322
1977-78	(66)	1,572
1978-79	105	1,547
1979-80	(411)	1,543
1980-81	(143)	1,111
1981-82 Interim	(62)	1,425

Because Ontario's non-public borrowing is normally carried out in debentures with a term to maturity of 20 years, maturing debt does not constitute a short-run financing problem for the Province. Only five per cent of Ontario's own-purpose debt matures in the next five years. Debt refinancing associated with social capital investments of the past decade occurs mainly in the mid- to late 1990s. Under current and prospective arrangements with those pension plans from which the Province borrows non-public funds, and relative to a growing revenue base, repayment or refinancing of maturing debt can be managed without significant financial strain.

Ontario's debt is almost entirely denominated in Canadian dollars. Only about $44 million, or 0.2 per cent of total own-purpose debt, is in foreign currencies. As a result, Ontario's debt structure and debt-servicing costs are well protected against the effects of volatile exchange rates.

Capacity to Service Debt

The capacity of any government to carry public debt is related to the underlying strength of its economy and its tax revenues. Further, growth of the public debt and its impact on the economy should be considered relative to the capacity, diversity, and potential of the economy. Only then can some accurate assessment of the importance of the relative indebtedness be drawn.

A common measure of the relative indebtedness of a government is debt per capita. The fundamental problem with this ratio is that it requires the comparison of debt measured in current dollars to a real measure of the population base or the human productive capacity of the economy. As a result, inflation will distort this measure dramatically. In order to remove the effect of inflation, debt can be measured in real terms and then divided by the population. This adjustment, however, does not account for the growing ability of the economy to generate wealth. Therefore, debt is usually compared with a general measure of income or wealth, such as Gross Provincial Product (GPP) or Personal Income.[7] Government revenue is also used as a measure of income.

Public Sector Debt

These measures are applied to Ontario's Consolidated Public Sector Debt in Table 8. The series begins in 1973-74, the earliest date from which these comprehensive measures can be constructed in a consistent manner. The table shows that, since 1973-74, Ontario's debt level has been stable. While funded debt per capita has increased, this occurred in a period when inflation grew at an average annual rate of about 10 per cent. The other measures of relative indebtedness have declined slightly since 1978-79. During the entire period, prudent debt management has kept Ontario's public sector debt in check.

Provincial Funded Debt

The above section examined the debt of the entire Provincial public sector. This part looks at the direct debt of the Provincial government, excluding Ontario Hydro. Table 9 displays the relative level of Provincial debt since 1952-53.

As a proportion of GPP, funded debt has remained reasonably stable since 1972, and has even dropped slightly in recent years. This is in contrast to the situation during the 1960s, when a major increase in borrowing took place to finance an expansion of the public sector related mainly to health and education programs. The number of months of budgetary revenue required to retire the funded debt has been quite stable in relation to the size of the debt. In these terms, Ontario is as capable of repaying its debt today as it was a decade ago, and yet some $14 billion has been added to the stock of social capital.

[7]Most studies of the ability to service government debt employ such measures. For example, see McLeod, Young, Weir Ltd., *Consolidated Public Sector Debt of the Canadian Provinces* (Toronto: McLeod, Young, Weir Ltd., 1978); and Dominion Securities Ames Ltd., *Canadian Provincial Government Finance* (Toronto: Dominion Securities Ames Ltd., 1981).

Funded Debt of the Ontario Public Sector[1]

Table 8

	1973-74	1974-75	1975-76	1976-77	1977-78	1978-79	1979-80	1980-81	Interim 1981-82
Funded Debt ($ million)	15,463	17,272	21,197	23,544	26,214	29,369	31,405	33,596	37,108
Funded Debt Per Capita ($)	1,926	2,119	2,569	2,823	3,109	3,458	3,669	3,900	4,283
Funded Debt/Personal Income (%)	38.8	36.7	39.3	38.6	39.0	39.6	38.4	36.9	35.1
Funded Debt/GPP (%)	30.7	29.2	32.7	31.9	32.2	33.0	31.4	30.7	30.0

Source: Ontario Treasury.

[1]Provincial Public Sector includes the Provincial Government, its crown corporations and agencies, and local government activities but excludes the federal government.

Ontario's Debt-Servicing Capacity,[1] 1952-53 to 1981-82 — Table 9
($ million)

	Funded Debt	GPP	Budgetary Revenue	Debt to GPP (%)	Debt to Revenue (Months)
1952-53	675	9,189	383	7.3	21.1
1957-58	903	13,318	646	6.8	16.8
1962-63	1,463	16,335	1,423	9.0	12.3
1967-68	2,694	26,336	2,867	10.2	11.3
1972-73	6,300	43,616	6,046	14.4	12.5
1973-74	7,008	50,422	6,844	13.9	12.3
1974-75	7,844	59,230	8,177	13.2	11.5
1975-76	9,818	64,802	9,010	15.2	13.1
1976-77	10,895	73,721	10,514	14.8	12.4
1977-78	12,364	81,492	11,099	15.2	13.4
1978-79	14,037	89,112	12,322	15.8	13.7
1979-80	15,196	100,168	14,214	15.2	12.8
1980-81	16,214	109,574	15,549	14.8	12.5
1981-82 Interim	17,592	123,716	17,858	14.2	11.8

[1]Excludes Ontario Hydro.

III Future Investment Directions

As the social and economic environment in which Ontario participates changes, government must adopt new policies that will accommodate these developments. The nature and purpose of public investment has, in the past, focused primarily on providing the basic infrastructure for development and the institutions necessary to deliver public services. While Ontario will continue to expand and maintain these facilities, the challenges of the 1980s require that Government turn its attention also to the promotion of industrial development and economic growth. At the same time, the Province will accord a high priority to maintaining a prudent financial management policy sensitive to the discipline of capital markets.

Industrial Development

The main economic thrust of the Government of Ontario will continue to be the maintenance of a stable, reliable, and hospitable climate for private sector investment and job creation. The vast majority of the jobs needed by our people can only be maintained and created in this way. Direct government investment in economic development and job creation will be supported by the Government. It will be targeted to those areas in which there is general agreement that government-industry cooperation is required to permit development with high economic, social, and job-creation returns.

To coordinate and consolidate this investment strategy, the Government has created a committee of Cabinet—the Board of Industrial Leadership and Development (BILD).[8] Six major sectors have been identified as having priority for government action. Each sector represents an area where government investment can be influential in its support for private initiative.

Human Resources: Investment in a broad base of educational institutions, in the past two decades, has been a major focus of Ontario's capital program. As a result, Ontario's workforce is among the most talented and highly educated in the world. Changing economic challenges, however, will force new directions on our educational institutions if they are to ensure that our people are able to enjoy their full potential in the 1980s. Through BILD, the Government will ensure that new investments in the technological capacity of our training and the innovative skills of our people take place.

Natural Resources: Ontario's natural resources will continue to contribute in a major way to the economic prosperity of the province in the 1980s. The Government has a major role to play in ensuring the supply, diversification, and competitiveness of these resources in the future. The capital investment strategy of BILD will aim at the development, in partnership with private interests, of the full potential of Ontario's forestry, mineral, and agricultural resources.

Electricity: Investment in Ontario's electrical generating system has important economic implications, in terms of both the supply of abundant and competitively-priced power, and support to internationally-competitive technological, industrial, and service expertise that has been stimulated by Ontario Hydro. BILD is committed to promoting Ontario's energy security and to reaping the industrial benefits of our electric power technology.

Transportation: Investment in the transportation and communications networks of Ontario has always been a major priority of the Government. Increased fuel costs, international competition, and new technology have dramatically changed the economics of transportation, giving rise to an urgent need to focus attention on the fuel and cost efficiency of our people- and goods-moving systems. BILD's strategy will ensure new investment in the critical areas of our transportation network and in the technologies which will ensure an efficient system in the future.

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[8]Hon. William G. Davis, *Building Ontario in the 1980s,* Board of Industrial Leadership and Development (Toronto, 1981).

Communities: The social and economic structure of Ontario communities is critical to attracting new industry and to expanding the existing base. In the past, Government capital investment has provided an attractive and competitive infrastructure of community services including water, sewerage, and public institutions. Through BILD, the Government will focus increased attention on those investments in Ontario communities which will support their economic growth potential.

Technology: The capacity of Ontario industry to develop and capitalize on new technology will determine its ability to compete in an increasingly tough international marketplace. Government investment in research and development, the educational system, and manpower programs will be an important catalyst in ensuring that Ontario industry has access to, and is able to capitalize on, new technology. The BILD strategy will invest to ensure that the private sector has access to the assistance and expertise it will require to keep pace with the technological revolution of the 1980s.

Since its inception, BILD has furnished some $157 million in new money to promote specific initiatives that will enhance Ontario's future well-being. Commitments totalling $775 million have been undertaken, with the funds to flow over a five-year period, as shown in Table 10.

BILD Commitments
($ million)

Table 10

	Five-year commitments
Human Resources	56
Natural Resources	154
Electricity	22
Transportation	274
Communities	92
Technology	177
Total	775

Equally as important, BILD is working closely with all ministries in Ontario, the federal government, municipalities, and the private sector to ensure that resources are broadly marshalled in support of those investment opportunities which will enhance economic development opportunities, promote growth, jobs and incomes, and keep Ontario competitive in the world.

Financing Considerations

Credit Status: The Province of Ontario has always been recognized in international capital markets as a borrower of the highest quality. This stature was confirmed in 1974 with the awarding of the highest possible credit rating—triple A. This prime credit rating was awarded in recognition of Ontario's strong economic base and sound financial management by the Government. Prime credits enjoy the most favourable rates in capital markets and more ready access to large pools of capital. Since triple A borrowers can generally satisfy their capital requirements with conventional instruments at acceptable maturities in traditional, secure markets, they are not forced to resort to unusual, risky instruments or undesirable markets. Ontario has utilized the flexibility of its prime status to obtain long-term capital, primarily for Ontario Hydro, at favourable rates even in difficult periods in the capital markets. Ontario places the highest priority on the maintenance of its prime credit status.

Borrowing Limits: At times, the requirement for financing both public capital investment and counter-cyclical stimulatory measures, in conjunction with Hydro's capital needs, has placed pressure on the market's capacity to absorb new Ontario and Hydro bonds. Ontario reaffirmed in the mid-1970s that it could not preserve the advantages of its credit status, or the credit rating itself, unless it recognized the existence of limits to the availability of capital, even to a prime government credit, and operated within those limits in forming financing plans. While the measurement of borrowing limitations is, at best, imprecise, the recognition that they exist, and the willingness to plan within them has been an important part of Ontario finance policy. As noted earlier, one result of this recognition of practical financing limits was the introduction of a major expenditure restraint program in 1976. Continued vigilance in this area enabled Ontario to stabilize its net cash requirements and to develop a degree of fiscal flexibility, independent of the capital markets. This policy was successful and has left Ontario in a better condition than many other non-oil producing jurisdictions to deal with the current economic situation and the challenges that lie ahead.

Debt-Servicing Costs: Another restriction on financing, particularly in the recent past, has been the high level of interest rates. These high rates have been increasing the overall cost of debt servicing. Nevertheless, the Province, by maintaining a prime international borrowing status and by judicious choice of debt instruments, has kept debt-servicing costs from rising excessively. However, if current high interest rates continue, the cost of maintaining debt would increase considerably if borrowing were permitted to be excessive.

Conclusion

In the last decade, Ontario significantly augmented the stock of social capital without increasing the relative burden of debt on taxpayers. The Province was also able to scale down its investment program in the latter part of the 1970s to meet financial limitations related to inflationary pressures and slow economic growth being experienced by all industrial jurisdictions. Accordingly, the Province has maintained its sound financial position while still benefiting from a high level of investment in social capital. This prudent fiscal management has given Ontario the flexibility to maintain a solid environment for private investment and job creation in the future.

Review of the 1981 Budget

This section details the in-year adjustments to the 1981 Budget Plan and updates previous quarterly reports published in *Ontario finances.*[1] Table 1 presents the interim results for the 1981-82 fiscal year. The results show that net cash requirements were $563 million above the original Budget estimate, reflecting an increase of $452 million in revenue and $1,015 million in expenditure. The increase in net cash requirements of $563 million was financed entirely from internal non-public sources of borrowing and reserves.

1981 Budget Performance — Table 1
($ million)

		Budget Plan	Interim Results	Change
A.	**Cash Requirements**			
	Revenue	18,403	18,855	+452
	Expenditure	19,400	20,415	+1,015
	Requirements	997	1,560	+563
B.	**Financing**			
	Non-public borrowing (net)	1,248	1,425	+177
	Public borrowing (net)	(61)	(62)	−1
	Reduction in liquid reserve	(190)	197	+387
	Total Financing	997	1,560	+563

On the revenue side, adjustments during the 1981-82 fiscal year brought the total revenue figure to $18,855 million. The major changes are summarized in Table 2.

The most significant increase occurred in personal income tax, where federal adjustments brought revenue $548 million above the original Budget estimate. Of this gain, $336 million reflects a correction for prior year underpayments. The remainder is due to in-year revisions to the 1981 tax year estimate and an increase in the March installment related to the federal November, 1981 budget proposals. High interest rates, which prevailed throughout the 1981-82 fiscal year increased the Province's return on investments by $129 million. Transfers under the Canada Assistance Plan were $48 million over the original forecast, reflecting the Province's increased social assistance expenditures.

[1] Every year, the Ontario Treasury publishes quarterly reports, called *Ontario finances,* which update the Province's budget projections as of June 30, September 30, and December 31.

Payments received from the federal government for Established Programs Financing were $103 million below the original Budget figure. Through the year, the 1981-82 cash entitlement was reduced on

Summary of In-Year Revenue Changes 1981-82 — Table 2
($ million)

Revenue Increases		
• Personal Income Tax	548	
• Interest on Investments	129	
• Canada Assistance Plan	48	
• Investment in Environmental Protection	33	
• LLBO Fees, Licences and Permits	32	
• Retail Sales Tax	21	
• All Other	150	+961
Revenue Decreases		
• Corporation Taxes	192	
• Established Programs Financing	103	
• Mining Profits Tax	84	
• Vehicle Registration Fees	43	
• All Other	87	−509
TOTAL		+452

the basis of higher personal income tax revenue. In addition, cash recoveries were made for prior years. Revenue from corporation taxes and mining profits tax were seriously affected by the high interest rate environment and reduced economic activity in the last half of the 1981-82 fiscal year. In total, these revenue sources were $276 million below the original estimate. Vehicle Registration Fees were $43 million lower than anticipated, reflecting sluggish economic conditions.

Planned expenditures for the 1981-82 fiscal year were $19,400 million. During the year, $1,015 million in net expenditure increases were approved, the most significant change being Ontario's purchase of a 25 per cent interest in Suncor, a subsidiary of the U.S.-owned Sun Oil Company. This investment had the immediate effect of increasing expenditures by $325 million, one half of the purchase price of $650 million. As outlined in Table 3, other major increases include additional funding for the operation of hospitals, increased capital expenditures and further support to the farming community, school boards and municipalities.

In 1981-82, additional funds amounting to $207 million were flowed to hospitals. This amount included $118 million for hospital salary settlements negotiated in 1981. A further $87 million was provided to meet revenue shortfalls of hospitals.

Summary of In-Year Expenditure Changes 1981-82 — Table 3
($ million)

Major In-Year Increases	
• Loan to Ontario Energy Corporation	325
• Operation of Hospitals	207
• Capital Expenditures	98
• Assistance to Farmers	81
• Welfare Assistance	64
• Grants to School Boards	58
• Salary Revision and Benefits	50
• Unconditional Grants to Local Governments	47
• Rental Construction Loans	16
• Public Debt Interest	14
• All Other (Net)	55
TOTAL	1,015

The 1981-82 budget estimate for the Ministry of Agriculture and Food stood at $217 million. In-year increases in expenditure resulted in actual expenditures of $298 million.

This $81 million increase in spending resulted from special in-year stabilization initiatives, as well as greater than expected expenditures in existing programs. The major in-year initiatives were the Emergency Beef Payment Programs. These programs provided immediate cash to assist beef producers being squeezed between low commodity prices and high costs and interest charges. They paid $40 per head of slaughter cattle and $20 per head of stocker cattle sold in 1980, and $40 per cow held for breeding purposes as of September 1981. By the end of the 1981-82 fiscal year, these programs had delivered $57 million to almost 30,000 beef farmers. At the same time, low pork prices resulted in an additional $5 million requirement for the Sow-Weaner Stabilization Program.

Demand for tile drainage debentures far exceeded supply. To relieve some of this pressure, an additional $4 million was provided for the program. In addition, improved administrative efficiency resulted in an additional $15 million in claims being processed under the Farm Tax Reduction Program.

Financial Tables

Statement of Provincial Net Cash Requirements and Related Financing — Table C1

($ million)

	Actual 1980-81	Interim 1981-82	Estimated 1982-83
Revenue (Table C2)	16,470	18,855	20,545
Expenditure (Table C3)	17,273	20,415	22,777
NET CASH REQUIREMENTS	**803**	**1,560**	**2,232**
Financing			
Non-Public Borrowing			
Canada Pension Plan[1]	538	769	1,200
Teachers' Superannuation Fund	569	670	748
CMHC Pollution Control Loans	30	(1)	—
Retirements	(26)	(13)	(84)
Net Non-Public Borrowing	1,111	1,425	1,864
Public Borrowing			
Debenture Issues	—	—	—
Debenture Retirements	(143)	(62)	(47)
Net Public Borrowing	(143)	(62)	(47)
Reduction in Liquid Reserves	(165)	197	415
TOTAL FINANCING	**803**	**1,560**	**2,232**

[1]In 1980-81 and 1981-82 the Province transferred $500 million of CPP funds to Ontario Hydro.

Revenue
($ million)

Table C2

	Actual 1980-81	Interim 1981-82	Estimated 1982-83
Taxation Revenue			
Personal Income Tax[1]	3,578	4,928	5,584
Corporation Taxes			
Income Tax	1,397	1,323	995
Capital Tax	291	329	363
Insurance Premiums Tax	104	118	133
Mining Profits Tax	161	56	40
Retail Sales Tax	2,562	2,852	3,677
Gasoline Tax	618	759	931
Motor Vehicle Fuel Tax	133	172	215
Reciprocal Taxation	52	47	52
Tobacco Tax	284	345	428
Land Transfer Tax	101	125	125
Race Tracks Tax	55	59	65
Other Taxation	113	19	5
	9,449	11,132	12,613
Other Revenue			
OHIP Premiums	1,061	1,179	1,402
LCBO Profits	433	502	530
Interest on Investments	540	613	460
Vehicle Registration Fees	312	297	293
LLBO Fees, Licences and Permits	126	170	185
Other Fees and Licences	159	185	214
Ontario Lottery Profits	116	137	137
Fines and Penalties	73	76	78
Sales and Rentals	63	60	73
Royalties	74	67	70
Utility Service Charges	62	62	66
Miscellaneous	108	119	107
	3,127	3,467	3,615
Payments from the Federal Government (Table C4)	2,973	3,259	3,243
Payments into Trust Accounts (Table C5)	611	661	763
Repayments of Loans and Advances (Table C6)	310	336	311
TOTAL REVENUE	**16,470**	**18,855**	**20,545**

[1]Net of Tax Credits of $455 million, $260 million and $286 million for the 1980-81, 1981-82 and 1982-83 fiscal years.

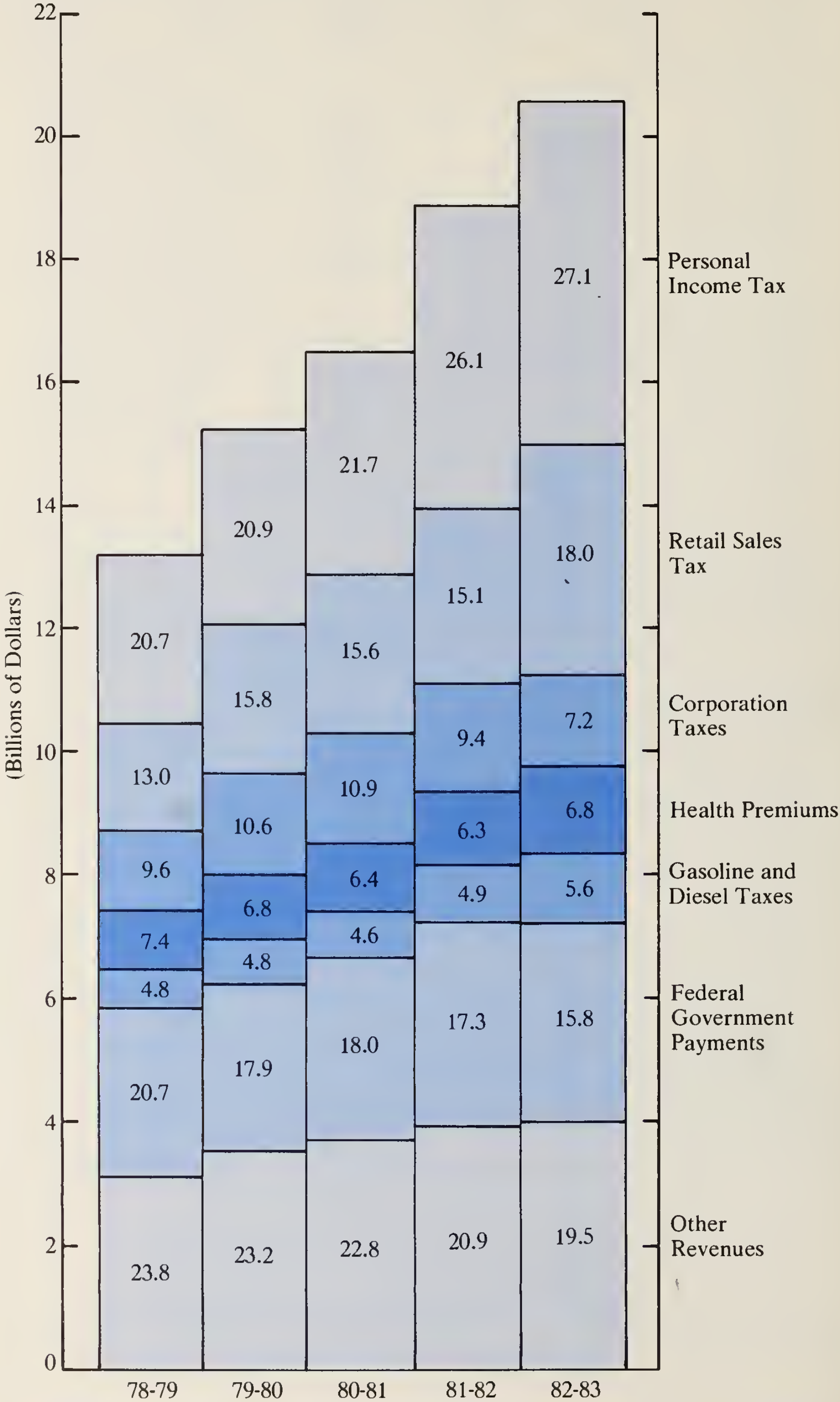
Expenditure
($ million)

Table C3

	Actual 1980-81	Interim 1981-82	Estimated 1982-83
Social Development Policy			
Health	4,897	5,817	6,579
Education	2,604	3,048	3,291
Community and Social Services	1,528	1,779	1,972
Colleges and Universities	1,542	1,677	1,860
Citizenship and Culture	162	181	222
Social Secretariat	3	5	5
	10,736	12,507	13,929
Resources Development Policy			
Transportation and Communications	1,213	1,316	1,414
Municipal Affairs and Housing	739	986	1,018
Natural Resources	342	358	361
Environment	308	361	346
Agriculture and Food	210	298	284
Energy	26	36	67
Ontario Energy Corporation	—	325	62
Industry and Trade	91	105	102
Tourism and Recreation	74	79	89
Labour	53	61	66
Resources Secretariat	2	3	4
	3,058	3,928	3,813
Justice Policy			
Solicitor General	211	257	285
Attorney General	183	206	219
Correctional Services	156	174	185
Consumer and Commercial Relations	91	103	104
Justice Secretariat	1	1	1
	642	741	794
General Government			
Revenue	488	534	605
Government Services	286	313	366
Northern Affairs	157	170	179
Treasury and Economics	127	168	193
EDF/BILD	124	150	170
Board of Internal Economy	43	43	37
Management Board	10	13	16
Intergovernmental Affairs	4	6	7
Legislative and Executive Offices	3	4	4
	1,242	1,401	1,577
Public Debt Interest	1,595	1,838	2,172
Contingency Fund	—	—	246
Short-Term Job Creation	—	—	171
Ontario Renter Buy Program	—	—	75
TOTAL EXPENDITURE	**17,273**	**20,415**	**22,777**

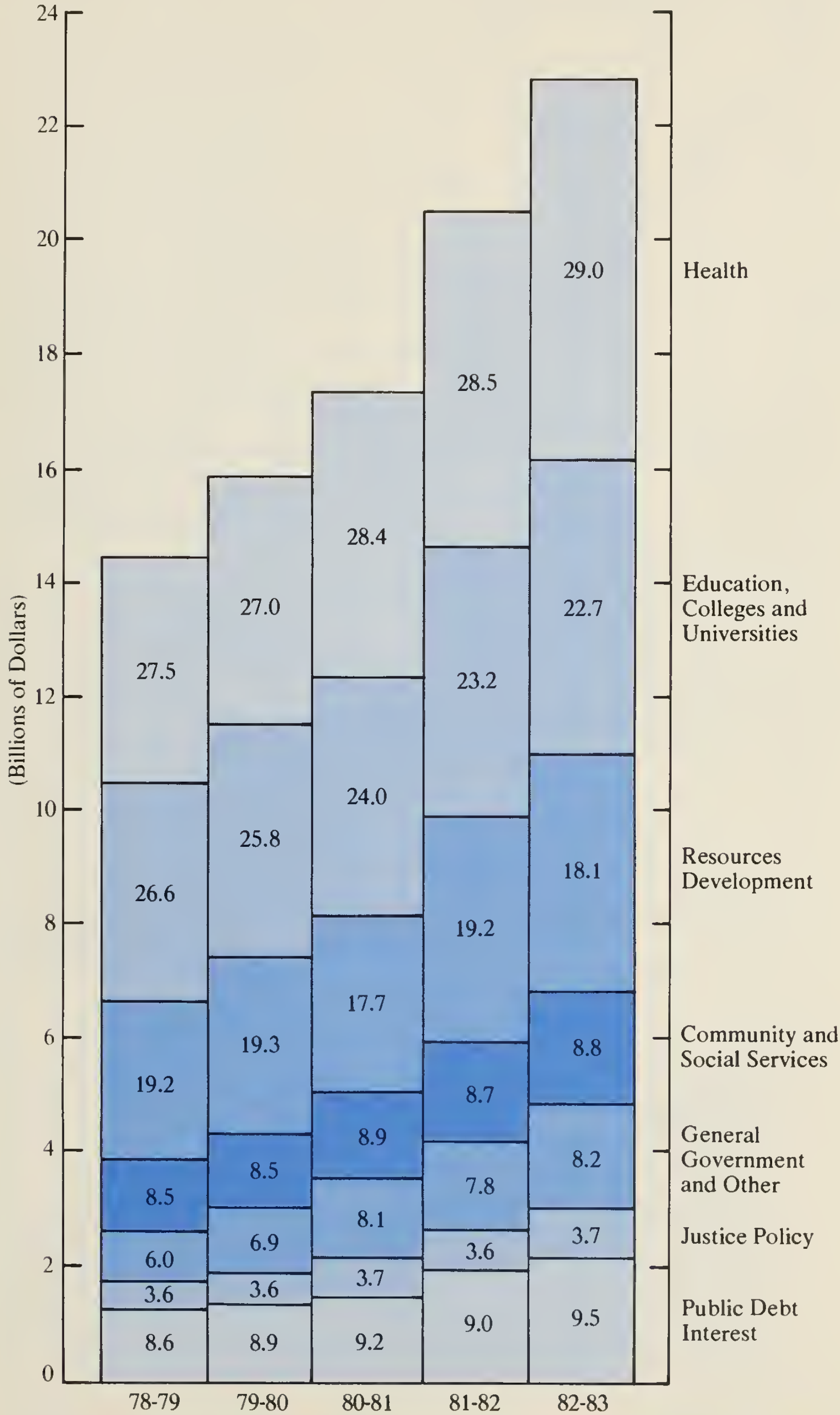
Revenue Sources,
1978-79 to 1982-83
(per cent of total)

Chart C1



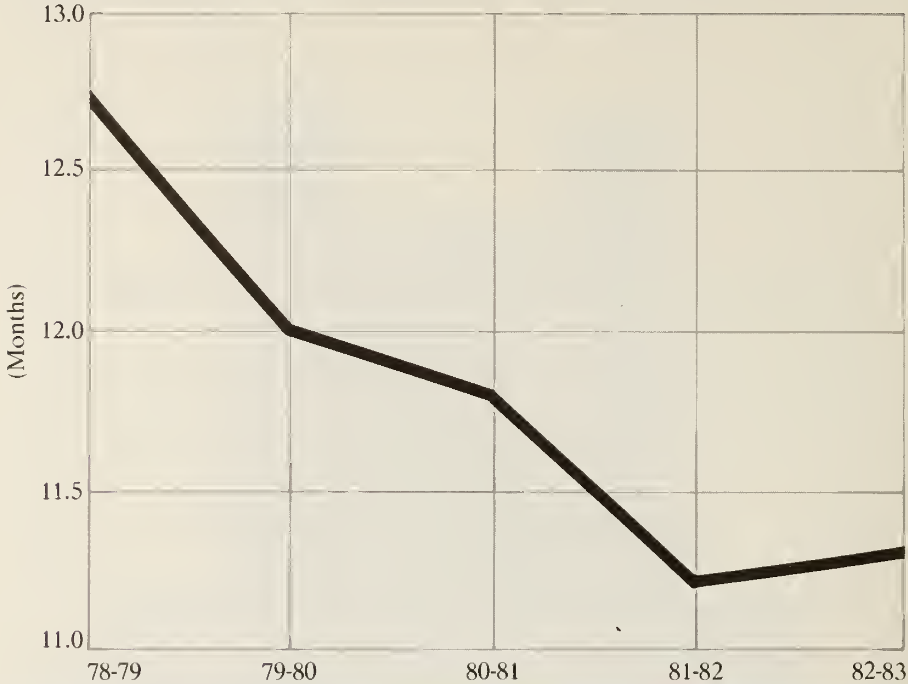
Expenditure Functions,
1978-79 to 1982-83
(per cent of total)

Chart C2



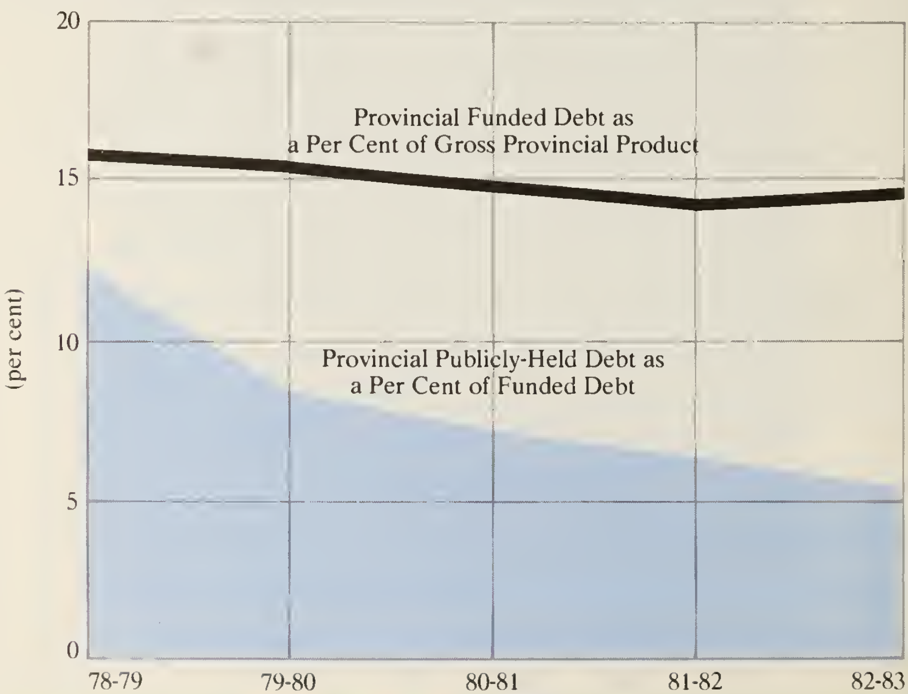
Months of Revenue Required to Repay Provincial Funded Debt, 1978-79 to 1982-83

Chart C3



Provincial Funded Debt and Publicly-Held Debt, 1978-79 to 1982-83

Chart C4



Payments from the Federal Government — Table C4
($ million)

	Actual 1980-81	Interim 1981-82	Estimated 1982-83
Established Programs Financing	1,934	2,044	1,979
Extended Health Care Services	230	257	288
Canada Assistance Plan	548	630	681
Adult Occupational Training	114	124	124
Bilingualism Development	34	37	37
Economic Development	9	19	22
Vocational Rehabilitation	15	17	22
Sewerage Construction Program	—	—	20
Community Services Contribution Program	35	58	2
Crop Insurance	9	21	16
Indian Welfare Services	13	15	15
Other Federal Payments	32	37	37
TOTAL	**2,973**	**3,259**	**3,243**

Payments into Trust Accounts — Table C5
($ million)

	Actual 1980-81	Interim 1981-82	Estimated 1982-83
Public Service Superannuation Fund	361	413	494
Superannuation Adjustment Fund	128	153	189
Province of Ontario Savings Office— Net Deposits	63	40	28
Provincial Lottery Trust Fund	26	20	20
Super Loto Trust Fund	10	10	10
Other	23	25	22
TOTAL	**611**	**661**	**763**

Repayments of Loans and Advances — Table C6
($ million)

	Actual 1980-81	Interim 1981-82	Estimated 1982-83
Education Capital Aid Corporation	78	82	87
Investment in Environmental Protection	70	98	70
Universities Capital Aid Corporation	30	31	32
Ontario Development Corporations	20	30	22
Ontario Mortgage Corporation	17	20	19
Loans to Public Hospitals	19	17	15
Tile Drainage Debentures	12	14	15
Ontario Land Corporation	19	12	15
Crop Insurance Commission	11	7	10
Other	34	25	26
TOTAL	**310**	**336**	**311**

Expenditure by Category — Table C7

($ million)

	Actual 1980-81	Interim 1981-82	Estimated 1982-83
Transfer Payments			
Local Governments			
School Boards	2,141	2,504	2,715
Transportation	553	627	676
Unconditional Payments	452	697	699
Social Assistance	493	571	614
Short-Term Job Creation	—	—	53
Other	436	555	525
	4,075	4,954	5,282
Individuals and Institutions			
Operation of Hospitals	2,535	3,056	3,440
Payments to Doctors	1,334	1,547	1,796
Extended Care Benefits	163	193	219
Other Health	286	358	418
Teachers' Superannuation	315	368	393
Operating Grants to CAATS and Universities	1,151	1,273	1,431
Apprentice and Manpower Training	125	131	139
Student Assistance	97	98	119
Other Education	153	159	151
Income Support	1,088	1,222	1,373
Assistance to Farmers	91	173	143
Short-Term Job Creation	—	—	118
Ontario Renter Buy Program	—	—	75
	7,338	8,578	9,815
Other Transfers			
Loans and Trust Accounts	395	710	466
GO Transit	66	84	99
EDF/BILD	124	150	170
Miscellaneous Transfers	495	553	774
	1,080	1,497	1,509
Total Transfers	12,493	15,029	16,606
Own Account			
General Government			
Salaries and Benefits	1,873	2,115	2,383
Direct Operating Expenditures and Other	1,312	1,433	1,616
Public Debt Interest	1,595	1,838	2,172
TOTAL EXPENDITURE	**17,273**	**20,415**	**22,777**

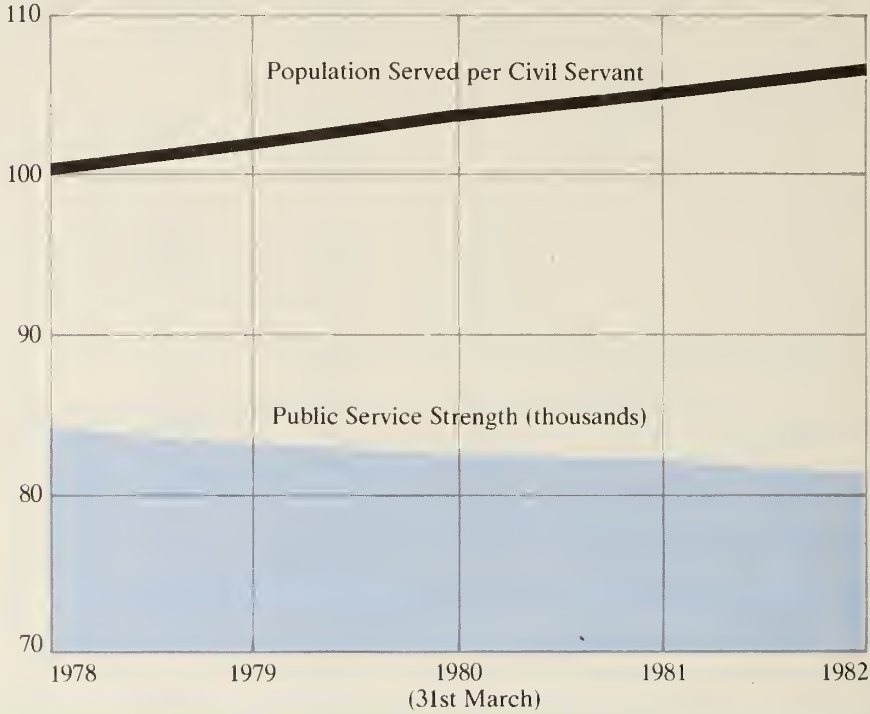
Payments to Local Governments and Agencies — Table C8

($ million)

	Actual 1980-81	Interim 1981-82	Estimated 1982-83
Conditional Payments			
Grants to School Boards			
General Legislative Grants	2,141	2,504	2,715
School Capital Grants	46	61	67
Transportation			
Roads	418	450	475
Transit	133	175	198
Other	2	2	3
Social Assistance			
General Welfare Assistance	224	253	257
Children's Aid Societies	115	131	146
Homes for the Aged	107	130	145
Day Nurseries	40	50	58
Other	7	7	8
Health			
Local Health Units	60	69	83
Other	21	22	25
Environment	69	115	93
Municipal Affairs and Housing	83	107	84
Agriculture	55	76	65
Conservation Authorities	39	36	37
Library Boards	23	25	26
Recreation	15	14	18
Northern Affairs	19	14	15
Short-Term Job Creation	—	—	53
Other Conditional Payments	6	16	12
	3,623	4,257	4,583
Unconditional Payments			
General Support	87	178	201
Resource Equalization	143	164	178
Per Capita—Policing	87	110	113
Per Capita—General	39	113	62
Northern Ontario Support	24	49	55
Payments-in-lieu of Taxes	54	60	70
Other	18	23	20
	452	697	699
TOTAL TRANSFER PAYMENTS	**4,075**	**4,954**	**5,282**

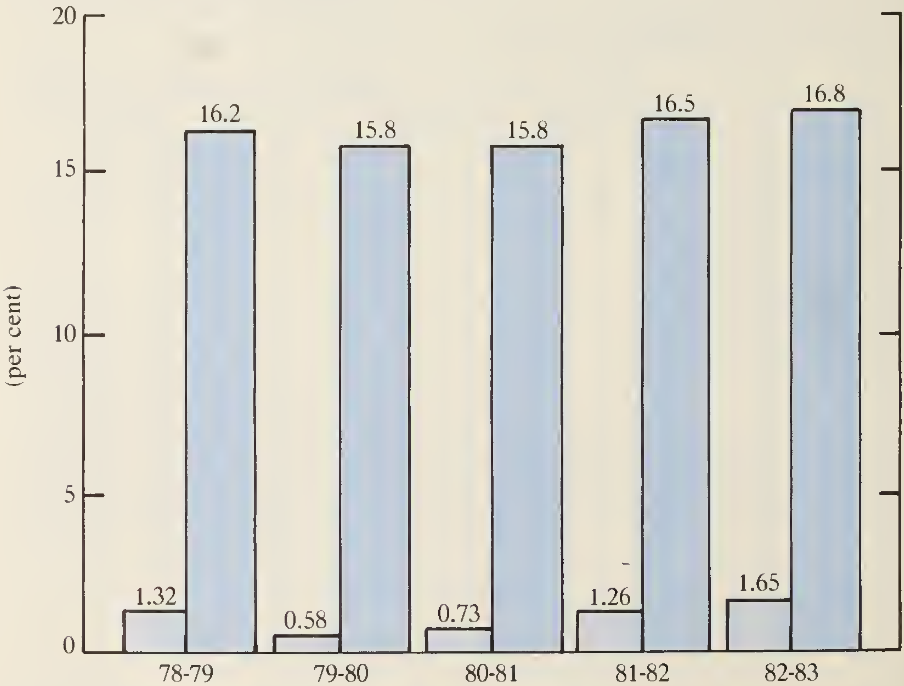
Increasing Efficiency in the Ontario Public Service, 1978 to 1982

Chart C5



Expenditure and Net Cash Requirements as a Per Cent of Gross Provincial Product, 1978-79 to 1982-83

Chart C6



Public Service Strength in Ontario — Table C9

March 31, 1982[1]

Ministry	Classified Staff	Unclassified Staff	Other Crown Employees	Total
General Government				
Office of the Premier	47	13	—	60
Cabinet Office	31	11	—	42
Management Board	58	26	—	84
Civil Service Commission	183	64	—	247
Government Services	2,783	292	—	3,075
Intergovernmental Affairs	50	15	—	65
Northern Affairs	165	57	—	222
Revenue	3,618	423	—	4,041
Treasury and Economics	388	51	1	440
	7,323	952	1	8,276
Justice				
Justice Secretariat	13	5	—	18
Attorney General	3,117	1,909	435	5,461
Consumer and Commercial Relations	1,724	187	284	2,195
Correctional Services	4,670	855	46	5,571
Solicitor General	1,583	712	3	2,298
	11,107	3,668	768	15,543
Resources				
Resources Secretariat	13	47	1	61
Agriculture and Food	1,493	475	—	1,968
Energy	158	46	—	204
Environment	1,452	142	—	1,594
Industry and Tourism	530	151	2	683
Ontario Development Corporations	152	11	—	163
Labour	1,384	85	21	1,490
Municipal Affairs and Housing	1,167	207	—	1,374
Natural Resources	4,301	1,668	—	5,969
Transportation and Communications	9,742	1,669	—	11,411
	20,392	4,501	24	24,917
Social				
Social Secretariat	35	36	—	71
Colleges and Universities	570	74	2	646
Community and Social Services	9,841	1,788	—	11,629
Culture and Recreation	811	342	—	1,153
Education	1,491	547	556	2,594
Health	10,640	1,485	—	12,125
	23,388	4,272	558	28,218
Sub-Total	62,210	13,393	1,351	76,954
O.P.P. Uniformed Staff and Security Guards	4,204	—	—	4,204
Environment Plant Operators	552	116	—	668
TOTAL STAFFING	**66,966**	**13,509**	**1,351**	**81,826**

[1]Excludes staff of the Lieutenant Governor, Office of the Assembly, Ombudsman and Provincial Auditor.

Ten-Year Review of Selected Financial and Economic Statistics
($ million)

	1973-74	1974-75	1975-76
Financial Transactions			
Revenue	7,177	8,855	9,520
Expenditure	7,885	9,832	11,319
Net Cash Requirements	708	977	1,799
Financial Position			
Funded Debt[1] (excluding Ontario Hydro)	7,008	7,844	9,818
Provincial Debt Transactions (net)	710	851	1,974
Publicly-Held Debt	1,471	1,166	1,909
Gross Provincial Product (GPP) at Market Prices	50,422	59,230	64,802
Personal Income	39,884	47,060	53,902
Population — June — (000's)	7,909	8,054	8,172
Funded Debt per Capita (dollars)	886	974	1,201
Personal Income per Capita (dollars)	5,043	5,843	6,596
Net Cash Requirements as a per cent of GPP	1.4	1.7	2.8
Funded Debt as a per cent of GPP	13.9	13.2	15.2
Total Expenditure as a per cent of GPP	15.6	16.6	17.5
Publicly-Held Debt as a per cent of GPP	2.9	1.9	2.9
Cumulative Net Borrowing for Ontario Hydro			
U.S	1,382	1,710	2,240
C.P.P.	—	—	—
Contingent Liabilities (mainly Ontario Hydro)	3,382	3,933	5,147

[1]Funded debt includes bonds, debentures, notes and Treasury Bills.

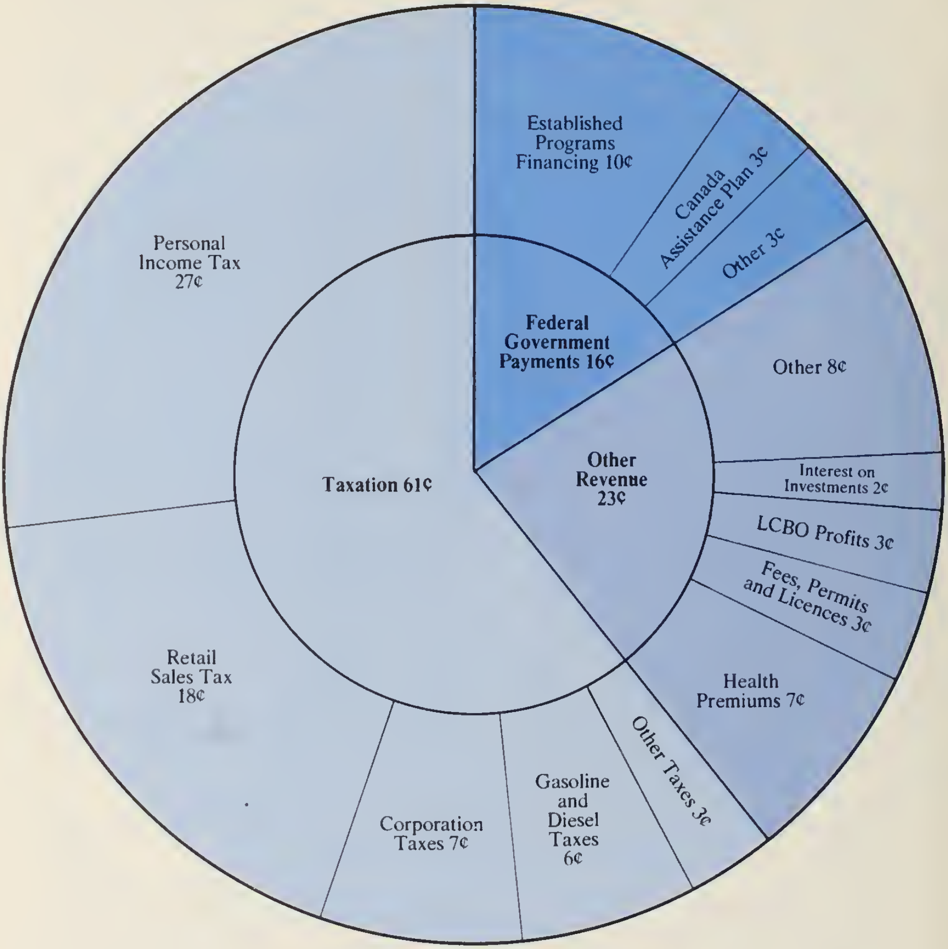
Table C10

1976-77	1977-78	1978-79	1979-80	1980-81	Interim 1981-82	Estimated 1982-83
11,148	11,782	13,233	15,246	16,470	18,855	20,545
12,467	13,544	14,413	15,830	17,273	20,415	22,777
1,319	1,762	1,180	584	803	1,560	2,232
10,895	12,364	14,037	15,196	16,214	17,592	19,409
1,092	1,506	1,652	1,132	968	1,363	1,817
1,679	1,613	1,718	1,307	1,164	1,102	1,055
73,721	81,492	89,112	100,168	109,574	123,716	135,500
60,959	67,164	74,178	81,840	91,002	105,606	117,500
8,265	8,355	8,444	8,505	8,574	8,625	8,696
1,318	1,480	1,662	1,787	1,891	2,040	2,232
7,376	8,039	8,785	9,623	10,614	12,244	13,512
1.8	2.2	1.3	0.6	0.7	1.3	1.6
14.8	15.2	15.8	15.2	14.8	14.2	14.3
16.9	16.6	16.2	15.8	15.8	16.5	16.8
2.3	2.0	1.9	1.3	1.1	0.9	0.8
2,510	2,901	3,568	3,782	4,190	4,530	N/A
—	—	—	—	500	1,000	1,000
5,806	6,212	6,734	7,593	8,289	N/A	N/A

THE BUDGET DOLLAR
Fiscal Year 1982-83 Estimates

Chart C7

REVENUES



THE BUDGET DOLLAR
Fiscal Year 1982-83 Estimates

Chart C7

EXPENDITURES