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Fraser Institute Annual Survey of Mining Companies 2008/2009 by Fred McMahon and Miguel Cervantes: \$40.00

Hospital Report Card: Ontario 2009 by Nadeem Esmail and Maureen Hazel. Download free at www.fraserinstitute.org.

Report Card on Alberta's Elementary Schools 2009 by Peter Cowley and Stephen Easton. Download free at www.fraserinstitute.org.

Canada's Economic Relations with China by Raaj Tiagi with Lu Zhou. *Studies in Chinese Economic Policy*: \$15.00.

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From the Editor



Working together

THERE'S nothing quite like a recession to encourage protectionism. For the last few months, the protectionist impulse has been growing steadily, particularly in the United States. While campaigning to be president, Barack Obama criticized NAFTA on a number of occasions, calling it an "enormous problem" and pledging to "fix NAFTA so that it works for American workers" ("The rising tide of protectionism in the United States," pg. 31). Just recently, the US Congress sparked outcry around the world by including a "Buy American" clause in its omnibus stimulus package.

American protectionism should be especially worrying for Canadians, considering that the United States is our largest trading partner. A quick look at the numbers demonstrates how devastating protectionist measures would be to our economy. In 2008, Canada sold \$375 billion in exports to the United States; its exports to all other countries were worth just \$107 billion ("The benefits of trade," pg. 13).

In light of these facts, it is troubling, if understandable, that Canada has its own "buy domestic" advocates. But enacting such a policy would only encourage similar policies in the United States, which would ultimately harm Canada.

Though the protectionists would have us believe otherwise, trade offers significant benefits to both Canada and the US. The trade balance between the two countries does favour Canada, but Canada's energy exports, for example, are particularly important to the United States. In fact, Canada is the largest supplier of crude oil to the US market, representing about 20% of total American oil imports.

Cooperation on defence and security initiatives is also valuable to both countries, particularly because of our close geographic proximity. Domestic initiatives such as the North American Aerospace Defense Command (NORAD) are an essential part of this cooperation, but more could be done to increase homeland security and protect the interests of the two countries. As Alexander Moens and Alan W. Dowd argue in this issue of *Fraser Forum*, the Arctic is one area where Canada and the US need to direct their attention ("Taking action in the Arctic," pg. 33). With both security and sovereignty at stake, the two countries would be wise to settle their dispute over the Northwest Passage and work together to keep threats at bay.

In this time of recession, it will be difficult for Canada and the United States to resist the urge to turn inward, but resist they must. Instead of giving in to the protectionist impulse, they must continue to cooperate, recognizing that working together is beneficial to both countries.

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

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Gangs, drugs, and the economy

What are the true costs of crime?

ON March 16, Dr. Stephen Easton, professor of economics at Simon Fraser University and Senior Fellow of the Fraser Institute, spoke in Calgary as part of the Institute's *Behind the Spin* series. Dr. Easton discussed the costs of crime and illicit drugs, as well as the problems encountered by those who try to determine the true costs of crime.

In 1998, Easton and Paul Brantingham published a paper titled *The Costs of Crime: Who Pays and How Much?* which concluded that “the Canadian justice system does not encourage scrutiny and systematic data on how efficiently this system catches, convicts, incarcerates, and rehabilitates criminals are not easy to obtain.” Since then, little has changed, he said.

Easton provided the *Behind the Spin* audience with a wide range of information on gangs and the drug business. Gang criminal activities, Easton said, are “entirely motivated by profit” and “grow-ops finance all other activities.” Systematic information is limited, but it is a “significant issue that is not going away,” he said.

Easton noted that the criminal activity of the gangs is extremely well organized by a large number of small groups who have changeable allegiances, great flexibility, and who are not deterred by police actions. The organization of the drug trade has moved beyond groups like the Hell's Angels who are being displaced by more violent gangs in British Columbia and Manitoba. These new groups are not structured; rather, they are “anarchists out for a bank account,” he said. For this reason, while overall crime is in decline, violent crimes are increasing because of the huge profits to be made in the drug trade and the ongoing competition for supply.

Many of the costs associated with the changes in the organizational structure of the drug trade can be calculated. For example, we can calculate the cost of increased insurance and security measures for homes and businesses, as well as the cost of prosecuting criminals and keeping them in prisons. But the social costs associated with crime are less easily determined. The true cost of crime, Easton noted, can only be fully understood only if reliable data is available.

Easton argued that judges and legislators need to be educated about the cost of crime, so that they can weigh costs and



Top: Nigel Hannaford, Editorial Board Editor of the Calgary Herald, poses a question to Dr. Easton.

Bottom: Dr. Easton speaks with Nadeem Esmail, Director of Health System Performance Studies at the Fraser Institute, following his presentation.

benefits when they are making decisions. At the same time, Easton added, the general public also needs to be educated in the debate, as they were in the past when the costs and benefits of alcohol and gambling were being weighed. ■

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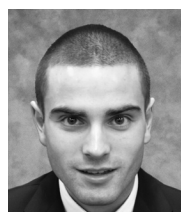
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A blueprint for continued prosperity

*Charles Lamnam &
Niels Veldhuis*

DESPITE the global economic downturn, Saskatchewan is expected to experience positive economic growth this year (TD Bank Financial Group, 2008; Scotiabank Group, 2009). Recent improvements in Saskatchewan's investment climate are paying dividends (Godin et al., 2008); investment is now flowing into the province and Saskatchewan's best and brightest are finally staying in or returning to the "land of living skies." However, the province must not rest on its economic laurels. Instead, the provincial government should use this unique opportunity to solidify Saskatchewan's place as a beacon of investment in Canada. Here's how.

Tax policy

FIRST, the government should improve incentives to work, invest, and take entrepreneurial risks in the province by reducing taxes on personal income and business investment.

More specifically, it should implement a three- to five-year plan to replace its three personal income tax (PIT) rates with a single rate of 9.0%. The single rate would be lower than the 10% rate in Alberta (the only province with a single rate) and would help retain and encourage the return of Saskatchewan's professional, skilled, and educated workers.

Saskatchewan should also reduce taxes on business investment by decreasing the general corporate income tax (CIT) rate from 12.0% to 9.0%. This would give Sas-

katchewan the lowest general CIT rate among the provinces, making it a magnet for investment. In addition, the province should end the taxation of business inputs by harmonizing the provincial sales tax (PST) with the federal goods and services tax (GST). This would improve incentives for businesses to invest in capital and would reduce tax compliance costs. Lastly, Saskatchewan should build on its prosperity-enhancing elimination of the general corporate capital tax by doing away with the capital tax on the financial services sector.

Government spending

To create the fiscal room needed to implement these important tax reductions, the government must rein in spending.

From 1994/1995 to 2007/2008, the government spent \$14.9 billion in addition to what would have been needed to compensate for population growth and inflation (Veldhuis et al., 2009). As of 2007/2008, Saskatchewan's rate of per-person spending was more than 5% higher than the national average and was one of the highest in the country (Veldhuis et al., 2009). At minimum, the government should freeze per-person spending for the next few years to bring the province's spending closer to the national average.

Much of the burden of spending restraint or reductions could be mitigated by reforming the way government services are delivered. For example, money could actually be saved on health care, without negatively impacting quality, if Saskatchewan implemented policies similar to those in Europe and elsewhere

(Ramsay and Esmail, 2003; Esmail and Walker, 2008).

Crown corporations

To improve its investment climate, Saskatchewan will need a plan to deal with the extensive role of Crown corporations in the province's economy. As a percentage of its economy, Saskatchewan has more Crown corporation activity than any other province (Veldhuis et al., 2009).

This figure is significant because a large body of academic research from around the world has found that state-owned enterprises (Crown corporations) invest less in capital¹ than privately-owned enterprises do (Megginson et al., 1994; Bortolotti et al., 2002; Boubakri et al., 2009).² Indeed, Saskatchewan's Crown corporations are no different.

Table 1 displays the capital investment performance of three major Saskatchewan Crown corporations in three different industries, along with the performance of a few Canadian private sector firms in the same industries. The capital investment performance of each firm is assessed using two indicators: capital expenditures per worker and long-term assets per worker.³ The value of each indicator is a five-year average over the period 2003-2007 and is adjusted for inflation.

The results in table 1 demonstrate overwhelmingly that Saskatchewan's Crown corporations under-invest in capital compared to similar private sector firms. In fact, Crown corporations under-invested in 17 of 20 possible comparisons with private sector firms (table 1).

Table 1: Capital expenditures and long-term assets per worker at Saskatchewan’s Crown corporations and at private sector firms in the same industry, 2003-2007 average, in 2007 dollars

Telecommunications firms					
	SaskTel	MTS	Telus	Bell Canada	
Capital expenditures per worker	36,746	53,188	53,390	104,816	
Long-term assets per worker	247,141	427,130	567,504	1,062,262	
Energy firms					
	SaskEnergy	Union Gas	Terasen Gas	Enbridge Gas	
Capital expenditures per worker	83,376	113,858	138,103	198,160	
Long-term assets per worker	1,141,677	1,623,174	3,504,776	2,455,938	
Power generation firms					
	SaskPower	Emera	NF Power	ATCO	TransAlta
Capital expenditures per worker	122,930	88,392	97,829	125,823	163,968
Long-term assets per worker	1,420,570	1,771,294	1,290,385	3,338,524	2,934,059

Source: Veldhuis et al., 2009.

For example, consider how the Crown corporations stacked up on the first indicator for each industry in table 1: capital expenditures per worker.⁴ At SaskTel, Saskatchewan’s telecommunications Crown corporation, average capital expenditures per worker amounted to \$36,746 between 2003 and 2007. Capital expenditures per worker in private companies were significantly higher: \$53,188 at MTS, a Winnipeg-based communications provider; \$53,390 at Telus, a national telecommunications company based in BC; and \$104,816 at Bell Canada, a Quebec-based communications company. On average, SaskTel’s capital expenditures per worker amounted to 57.7% of what the three private telecommunications firms spent.

At SaskEnergy—the Crown corporation responsible for energy transmission, distribution, and storage—average capital expenditures per worker amounted to \$83,376 between 2003 and 2007. In contrast, Union Gas—a private, integrated natural gas storage, transmission, and distribution company serving Ontario, Quebec, and the United States—spent \$113,858 per worker; Terasen Gas,

a BC-based gas and energy company, spent \$138,103 per worker; and Enbridge, a natural gas distribution company serving Ontario, spent \$198,160 per worker. SaskEnergy’s capital expenditures per worker, on average, amounted to only 58.6% of the expenditures by the three private energy firms.

Finally, SaskPower—the Crown corporation that provides power to the province—had average capital expenditures per worker of \$122,930 between 2003 and 2007, while ATCO Electric (a private Edmonton-based company servicing Alberta) spent \$125,823 per worker, and TransAlta (a power generation and wholesale company operating primarily in Alberta) spent \$163,968 per worker. Only Newfoundland Power (a private integrated generation and distribution company) and Emera (a Halifax-based company) spent less on capital expenditures (per worker) than SaskPower.

The solution for the under-investment of Crown corporations is privatization. Transferring ownership of the Crown corporations to private interests would unleash and promote investment in these industries. The increased invest-

ment would ensure that Saskatchewan workers have access to productivity-enhancing tools and technologies. This is of particular importance because productivity gains are ultimately what drive wages up and improve living standards.

Labour market regulation

REFORMS to labour market regulation are also critical. While progress has been made on Saskatchewan’s biased labour laws, further improvements are needed to bring them in line with other provinces, US states, and most other countries.

In general, economic evidence indicates that flexible labour markets—marked by the ease with which workers and employers are able to adjust to changing economic conditions—attract more investment than inflexible labour markets (Javorcik and Spatareanu, 2004; Kleiner and Ham, 2002; Besley and Burgess, 2004). Unfortunately, labour laws in Saskatchewan remain biased towards unions and impose rigidity rather than flexibility.⁵

To increase labour market flexibility, Saskatchewan should prohibit mandatory union membership and dues payment clauses in collective bargaining agreements. Doing so would provide workers with more freedom of choice, bring balance to the labour relations environment, and send a powerful signal to investors that the province has dramatically improved its labour market regulation.

In addition, Saskatchewan should eliminate successor rights, which ensure that collective agreements survive the transfer of ownership from one employer to another. These laws deter potential investors from purchasing businesses if collective agreements prevent them from restructuring the business to improve performance. Technological change laws, which require employers to notify unions of technological investments, as well as legislation that forces

arbitration, should also be reconsidered (Godin et al., 2006).

Interprovincial barriers

FINALLY, Saskatchewan should join the Trade, Investment, and Labour Mobility Agreement (TILMA) forged between BC and Alberta to reduce barriers to worker mobility, trade, and investment between the provinces. By joining TILMA, Saskatchewan would allow for goods and services to flow more freely across provincial borders, thus creating long-lasting benefits for individuals and businesses alike (Knox and Karabegović, 2009).

Conclusion

THE blueprint for prosperity outlined above requires tough decisions, but Saskatchewan is well positioned to make them. Once implemented, the reforms will create an environment of prosperity and opportunity unparalleled in the province's history.

Notes

1 In this context, capital refers to investments in property, land, production plants, technology, machines, and other production equipment.

2 A 2001 study by Professor William Megginson and Jeffrey Netter provides the most comprehensive review of the academic research on the effects of state vs. private ownership on firm performance. A central finding of their broad review was that state-owned enterprises generally invest less in capital than private sector firms do. Megginson and Netter concluded their appraisal of the privatization literature by stressing that "privatization 'works,' in the sense that divested firms almost always become more efficient, more profitable, and financially healthier, and increase their capital investment spending" (Megginson and Netter, 2001: 281).

3 The first indicator divides a firm's capital expenditures by the number of full-time equivalent (FTE) workers employed by the

firm. This ratio measures the amount of capital spending done by a firm while adjusting for the number of employees. Capital expenditures include monies used to acquire or upgrade physical assets such as plant, property, and equipment. The second indicator measures capital investment using a ratio that divides a firm's long-term assets by the firm's number of FTE workers. Long-term assets include land, buildings, plants, equipment, and other long-term investments. These assets are usually referred to as being "fixed" because they last for an extended period of time. These two indicators combine to present a comprehensive view of investment by examining annual spending (i.e., capital expenditures) and accumulated investment (i.e., long-term assets). For further details on the calculations and data sources used to construct the indicators, please see Veldhuis et al. (2009: 54–63).

4 The results for the second indicator, long-term assets per worker, were almost identical and thus are not discussed here for brevity's sake. For a thorough analysis of this indicator, please refer to Veldhuis et al. (2009).

5 Please see Veldhuis et al. (2009: 37–47) for a detailed discussion of Saskatchewan's biased and rigid labour laws.

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Missed opportunities

BC's budget provides few incentives for business development

Niels Veldhuis &
Milagros Palacios

WITH British Columbia facing a recession, the provincial government had good reason to make the economy the focus of its 2009 budget. Unfortunately, it did not make the decisions necessary to make British Columbia more competitive and attractive for investment and business development.

First, little was done to improve incentives to work, invest, and take entrepreneurial risks. Reduced personal income taxes and business taxes would have improved these incentives and provided a stronger foundation for prosperity now and in the future.¹

There were no new reductions in personal income tax rates contained in the budget. As a result, BC's top three personal income tax rates (10.5%, 12.3%, and 14.7%) remain higher than Alberta's single rate of 10%. Eliminating the top two personal income tax rates would have resulted in a top rate of 10.5%, closer to that in Alberta. Doing so would have improved incentives for productive economic behaviour and aided in attracting and retaining professional and skilled workers.

There was also little movement on business taxes, save for the gradual reduction in the corporate income tax to 10% from 11% starting in 2010.² This reduction was implemented to partially offset the scheduled increase in the carbon tax (see British Columbia, Ministry of Finance, 2008). The move

will improve incentives for business investment but it is too little, too late. The government should have immediately reduced its rate to 8%, giving British Columbia the country's lowest corporate income tax rate and thus creating a stronger incentive for businesses to invest in BC.

The government also chose not to match the federal increase in the small business tax threshold to \$500,000 from \$400,000,³ which would have benefited

three years (2009/2010 to 2011/2012), a 16% hike (table 1).

The BC government is again refusing to acknowledge that money is not the answer to our health care woes. Money could actually be saved without negatively affecting the quality of health care if BC implemented policies similar to those in Europe and elsewhere.⁵

At least the government plans to keep a tight lid on total spending. Planned increases in total spending over the next

Despite its conservative plans for spending increases, the government is projecting a deficit of \$740 million over the next two years.

small businesses in British Columbia by mitigating the impact of the higher corporate income tax rate they face as they grow.

Finally, the government again failed to address the sales tax businesses pay on inputs, which reduces incentives to invest in capital.⁴ A lower rate of capital investment will ultimately have a negative impact on productivity and wage growth in the province.

The fiscal room needed to implement these important tax reductions was unfortunately taken up by billions of additional dollars in health spending. All told, health care spending will increase by \$2.4 billion over the next

three years (averaging 2.4% per year) are lower than average expected inflation plus population growth (3.0%) (British Columbia, Ministry of Finance, 2009: 142). Whether the government will actually adhere to its spending plan remains to be seen.

Despite its conservative plans for spending increases, the government is projecting a deficit of \$740 million over the next two years (\$495 million in 2009/2010 and \$245 million in 2010/2011). Deficits coupled with significant capital spending financed through borrowing will increase the government's debt by a worrisome \$6.4 billion over the next three years, an increase of 23% (table 1).

Table 1: British Columbia's budget projections, 2008/2009 to 2011/2012, (in millions of \$)

	2008/09	2009/10	2010/11	2011/12
Revenue	38,455	38,812	39,795	41,182
Expenditures				
Health	15,071	15,722	16,574	17,513
Education	10,238	10,794	10,920	11,036
Social services	3,347	3,410	3,430	3,393
Other expenses	7,590	7,179	6,707	6,666
Debt charges (interest)	2,159	2,202	2,409	2,574
Total spending	38,405	39,307	40,040	41,182
Surplus (Deficit)	50	-495	-245	0
Provincial debt				
Taxpayer-supported debt	27,692	30,213	32,392	34,078

Source: British Columbia, Ministry of Finance, 2009.

Consequently, a larger portion of provincial revenues will be devoted to interest payments in each of the next three years.

Finally, while the finance minister claims that the budget is “prudent,” there is much less prudence than meets the eye. For example, the government eliminated the forecast allowance that protects the budget against unforeseen developments (typically \$750 million per year). It also reduced the contingencies that help ensure fiscal targets are met, and is optimistic with some of its forecasts (i.e., personal income growth). As a result, British Columbians have reason to be concerned about the government's ability to hit its budget target, especially with respect to the deficit.

British Columbia's 2009 budget is not the right budget for the province at this time. This budget should have set the course for a brighter future for

the province. Rather than spending billions on health care without regard for reform, the government should have implemented tax relief aimed at improving the incentives for investment and business development, creating true stimulus for wealth creation now and in the future.

Notes

1 For a comprehensive literature review of the impact of taxes on economic behaviour, see Palacios and Harischandra (2008).

2 The general corporate income tax rate will be reduced from 11% to 10.5% effective January 1, 2010, and to 10% effective January 1, 2011 (British Columbia, Ministry of Finance, 2009: 66).

3 In its 2009 budget, the federal government increased the amount of small business income eligible for the reduced federal tax rate of 11% from \$400,000 to \$500,000 (as of

January 1, 2009). For more details, see Canada, Department of Finance (2009: 319).

4 Five provinces—British Columbia, Saskatchewan, Manitoba, Ontario, and Prince Edward Island—impose sales taxes on business inputs. For a discussion of the benefits of tax harmonization, see Smart (2007) and Clemens and Veldhuis (2008).

5 A thorough analysis of the Canadian health system is presented in Esmail and Walker (2008).

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Centralizing America's health care

The future of US health policy under Obama

Mark Rovere

So far, President Barack Obama has expressed his preference for increased government involvement in the way health care is financed and administered in the United States.

"We have done more in 30 days to advance the cause of health care reform than this country has done in an entire decade," proclaimed Obama after signing a \$787 billion "stimulus" package in mid-February (Biden and Obama, 2009). In its final form, the law that was passed included \$150 billion in new annual public spending allocated to health care reform: \$87 billion for Medicaid, \$24.7 billion for COBRA¹ health insurance, \$19.2 billion for health information technology (IT), \$10 billion for the National Institutes of Health, and \$1.1 billion for comparative effectiveness research (Turner, 2009).

In addition to the controversial stimulus package, one of the first pieces of legislation signed by President Obama was the Children's Health Insurance Program Reauthorization Act of 2009 (CHIPRA),² which expands federal funding for children's health insurance coverage (SCHIP) by \$33 billion over the next four years (Henry J. Kaiser Family Foundation, 2009).

Obama also recently asked Congress for an additional \$634 billion to be included in his budget for a "health care reform fund" (Pear, 2009, Feb. 26).

A new national health plan

ALTHOUGH the administration has not yet put forth all the details of its plan to

reduce the number of people without health insurance in the United States, it has given some indications as to the eventual structure of what it calls a "new national health plan" (White House, 2009).

The new public scheme would be modeled after the health plan already available to federal employees, and would be administered through a National Health Insurance Exchange (Obama, 2008). The public plan, which would be available to all Americans, would operate in competition with private insurance. The exchange would regulate the prices of insurance products for all participating insurers (public and private), and would offer subsidies to low income individuals to purchase a private plan or the new public plan.

There are many concerns being raised throughout America's health policy community regarding this proposal. Among these concerns is the worry that the new public plan could "crowd out" private plans. It has been suggested that, as with Medicare and Medicaid, the government may use its political power, economies of scale, and regulatory authority to obtain prices for medical goods and services that are lower than those paid by the rest of the market. This would create an unfair competitive advantage for the new public plan in terms of cost (Moffit, 2008). Furthermore, under these proposals, private insurers would not be able to deny coverage because of pre-existing medical conditions, and would be forced to charge all customers the same price, regardless of age or medical history (White House, 2009). This restric-

tion on risk-adjusted premium pricing would make it even more difficult for private insurance companies to compete. Consequently, more people would choose the public option, crowding out the availability of private insurance.

In addition, many worry that the new public plan would eventually be funded at the taxpayers' expense. The political influence over price and benefits in the public plan would create incentives for elected officials to subsidize the costs of the public plan through taxes. The history of previous government interventions in health insurance markets in the United States is not encouraging. Research indicates that the current Medicare and Medicaid programs are financially unsustainable (Sisko et al., 2009).

Furthermore, National Center for Policy Analysis (NCPA) President John Goodman contends that if a large number of people purchased the public plan and the plan resembled Medicare (likely offering lower fees than those charged by the private insurers), there would be unavoidable pressure "to evolve into a two-tier payment system with two-tier quality of care" (Goodman, 2008). However, considering that Obama's goal is to ensure that all Americans have an equal opportunity to access the same quality of health care, such a two-tiered health care system would not be what Obama wants.

A tightly controlled market led by a much cheaper government health insurance plan would also increase the possibility of moving towards a single-payer system if individuals began to drop their private coverage for the public alternative (Moffit, 2008). The idea that

Obama's new public plan will lead to a single-payer system has not only been expressed by single-payer opponents (Turner, 2009, Feb. 27), but has also been put forth by universal health care advocates as a means of strategically achieving a single-payer health care system in the long run. In early 2008, Paul Krugman, professor of economics and international relations at Princeton University, suggested that the Obama administration should introduce more "regulation, subsidies, mandates, plus public-private competition that could eventually lead to single-payer." Krugman argued that a single-payer system is politically impossible in the short-term, but contended that if the above-mentioned policies were introduced, a single-payer system could be achieved over time (Krugman, 2008).

Centralized comparative effectiveness review

ONE of the most controversial proposals introduced by President Obama is the use of comparative effectiveness research as a means of controlling health care costs. The proposed Federal Coordinating Council for Comparative Effectiveness Research would conduct research and compare drugs, medical devices, and other methods of treating specific conditions. Supporters of the research council hope that by deciding which procedures and medical devices should be used, the council would be successful at reducing costs associated with expensive and ineffective medical treatments (Pear, 2009, Feb. 15).

However, some American health policy experts wonder if the government would be best suited to perform this task. As Michael Cannon of the Cato Institute notes, "experience suggests the benefits of taxpayer-funded research may be zero" (Cannon, 2009a). Cannon argues that when federal agencies produce research that questions

the value of a particular medical treatment, political pressure from industry is usually successful in persuading the government to disregard the significance of their findings. Economic theory suggests that the government is not in the best position to provide objective comparative effectiveness research as it often suppresses the private production of goods and services. In contrast, Cannon contends that a free market approach to comparative effectiveness research would increase the probability that providers and patients would use it (Cannon, 2009a). Under such an approach, independent third party organizations or industry representatives could conduct comparative effectiveness research, instead of the government. Grace-Marie Turner, president of the Galen Institute, argues that increasing government involvement in cost-effectiveness research would significantly distort incentives and "stifle medical innovation" (Turner, 2009, Feb. 27).

It has also been suggested that comparative effectiveness research would simply be used by the federal government as a means of controlling costs. For example, Peter Pitts, president of the Center for Medicine in the Public Interest, argues that "as currently organized, comparative effectiveness will be used to increase government control over the practice of medicine and introduce price controls" (Pitts, 2009). This is precisely what Dr. Scott Gottlieb, physician and resident fellow with the American Enterprise Institute, found when he studied the British health care system under the National Institute for Clinical Excellence (NICE)—that NICE's real mission is to shelter Britain's health care budget. Gottlieb found that since 2000, NICE has denied patients access to over 200 of the newest cancer drugs that have shown to offer clinical benefits, which are currently being paid for in the United States by American insurers and Medicare (Gottlieb, 2008, Oct. 18).³

Finally, should the government become more involved, comparative effectiveness research would likely be comprised of broad population averages (a one-size fits all approach) and would overlook the unique medical needs of individual patients (Pear, 2009, Feb. 15).

Centralized and subsidized information technology

HEALTH information technology (IT) is another area where Washington is planning to expand its reach. Under Obama's proposal, hospitals would have a mandate to collect and report data on health care expenditures and outcomes with the goal of reducing administrative costs while improving clinical outcomes (White House, 2009). A recent study has shown that an increased use of information technology leads to lower mortality rates, fewer complications, and lower overall costs (Amarasingham et al., 2009). However, skeptics in the health policy community are concerned that the significant funding for health IT does not pass the cost-benefit test (Cannon, 2009b), and past experience suggests that these apprehensions are warranted.

A recent *New York Times* article looked at the Marshfield Clinic, a health clinic in Wisconsin that has been one of the country's leaders in innovative health IT. The author points out that the clinic can show quantifiable savings in certain areas, "but has scant proof they outweigh the millions spent in the past and the \$50 million-a-year technology budget" (Lohr, 2008, Dec. 26).

Similarly, a 2008 study on the costs and benefits of health information technology published by the Congressional Budget Office (CBO) found that savings were observed in certain settings, but that health IT alone would not produce significant savings. The study affirmed that IT could reduce costs if broader system-wide incentives were in place to

encourage savings (Congressional Budget Office, 2008).

While some people in the health care community believe that health information technology is critical, many find the task better suited to the private sector where the appropriate economic incentives are in place. Greg Scandlen, president of Consumers for Health Care Choices, notes that the British government has gone way over budget in its attempts to implement more information technology for its National Health Service (NHS). According to Scandlen, the market is in a better position to test and refine new ideas, and thus health IT should be examined from a market-oriented perspective instead of a government one (Scandlen, 2009). As Turner argues, a great deal must be done to improve American health care, but "more government is not the answer" (Turner, 2009, Feb. 27).

Conclusion

THE significant funding allocated to health reform in February's stimulus package and Obama's almost immediate extension of COBRA demonstrate that the new president has made health care reform one of his top priorities. A number of other controversial proposals, such as giving the federal government the ability to negotiate drug prices for Medicare recipients and allowing the importation of medicines from other developed countries, are also being debated among health experts.

On the political side, Tom Daschle's withdrawal as Obama's nominee for Secretary of Health and Human Services temporarily took some of the steam out of Obama's proposals. However, on March 2, Obama formally nominated Kansas Governor Kathleen Sebelius as Secretary of Health and Human Services. While governor of Kansas, Sebelius tried to implement policies similar to those now proposed by the Obama administration.

As with many policy developments south of the border, any changes to American health policy will likely affect Canadians. Undoubtedly, the health policy debate here in Canada will be influenced by the policy decisions made in the United States. As Obama and his new health secretary attempt to reorganize America's health care, the potential for Canadians to misinterpret the lessons from these events will be very high. This could potentially set back reform efforts in Canada.

Notes

1 COBRA (Consolidated Omnibus Budget Reconciliation Act) is a program that allows people who have lost their jobs to keep their employment-based health insurance coverage for approximately 18 months (Centers for Medicare and Medicaid Services, 2008).

2 Formerly known as SCHIP (State Children's Health Insurance Program), CHIPRA expands federal funding for low-income uninsured children (over the next four years) who are not eligible for Medicaid. The program, which was supposed to expire in 2007, was reintroduced to Congress on two separate occasions in 2007; however, then-President George W. Bush vetoed the bill both times (Henry J. Kaiser Family Foundation, 2009).

3 Although not necessarily correlated, Gottlieb points out that cancer survival rates are significantly higher in the United States than they are in the United Kingdom.

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The benefits of trade

Canadians and Americans should reject “buy domestic” policies

Fred McMahon

WHILE the Canadian media jumps at any chance to highlight a trade dispute between Canada and the United States—no matter how small—few Canadians realize how much Canada benefits from our continental trade and how grave a threat protectionism is to our way of life.

It is also why it is so worrisome that some Canadian public figures are doing the best they can to fan the flames of protectionism, despite the great harm it would do to the people they claim to represent.

Both the magnitude of our trade and the size of our trade surplus¹ with the United States are huge. Many economists argue that it is the magnitude of the trade, and not the size of the surplus, that is important. Nonetheless, our immense US surplus is one indication of how free and open the border is and how little the United States interferes with the flow of goods from Canada, the media’s obsession with small disputes notwithstanding.

In 2008, Canada sold \$375 billion dollars in exports to the United States and had a \$148 billion surplus. The surplus alone is equal to over 9% of the Canadian economy. With the rest of the world, we ran a trade deficit (figures 1a and 1b).

Some complain that our trade with the United States simply strips us of our natural resources and devastates our manufacturing sector. This is false. The

United States is the engine that keeps our manufacturing sector going, while we run a big trade deficit with the rest of the world (figures 2a and 2b).

Protectionism on both sides of the border

THE threat of protectionism was recently highlighted when the US Congress tried to insert a “Buy American” clause into the “stimulus” package. Canada, the European Union, and other world traders loudly announced their opposition. So too did President Barack Obama and the clause was modified to be consistent with US trade treaties.

Yet a powerful group of Canadian politicians and labour officials wanted to turn this protectionist tempest into a global tsunami—and they are still at it. Jack Layton, leader of the federal New Democratic Party, Ken Neumann, Canadian national director of the United Steelworkers, and Ken Lewenza, president of the Canadian Auto Workers (CAW) union, among others, are doing everything they can to exacerbate the threat (*CBC News*, 2009, Feb. 3; Lewenza and Neumann, 2009.) They continue to demand the enactment of a “Buy Canadian” policy.

As of March 20, 2009, the home page of the CAW’s website (<http://www.caw.ca/en/index.htm>) featured this blaring headline: “Made in Canada! Buy Canadian & Build Communities: CAW activists are demanding all levels of govern-

Figure 1a: Overall trade with the United States, 2004-2008 (in billions of CA\$)

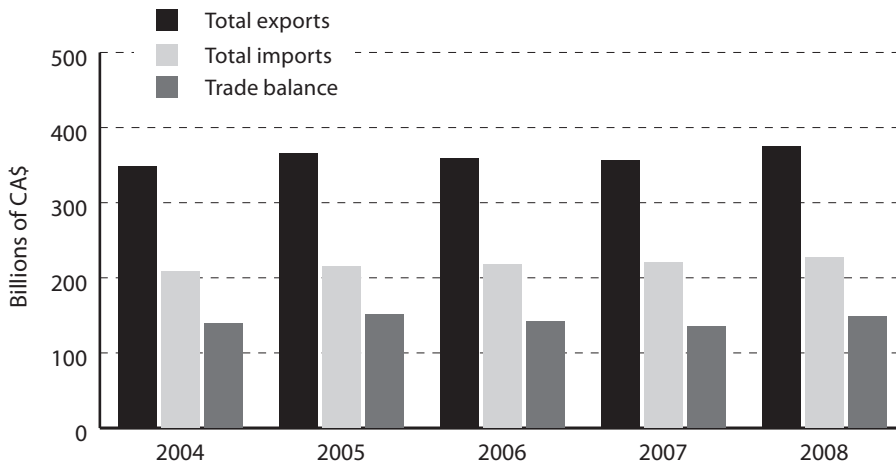
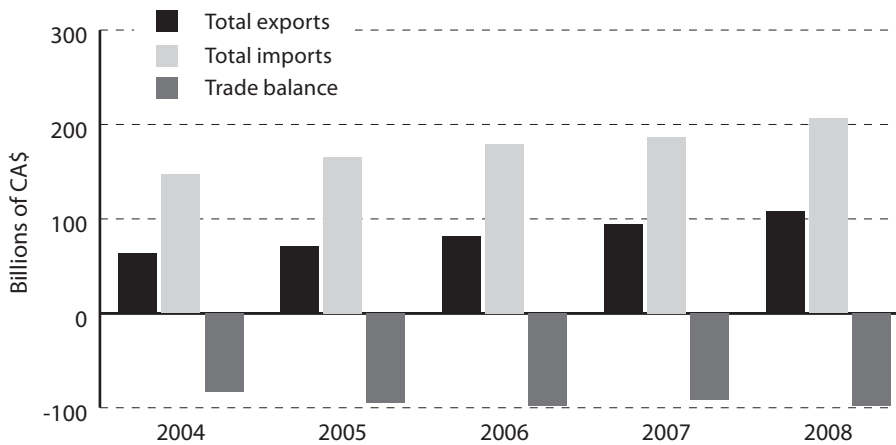


Figure 1b: Overall trade with all countries (excluding the United States), 2004-2008 (in billions of CA\$)



Source (for figures 1a and 1b): Industry Canada, 2009.

ment adopt strong Buy Canadian rules for publicly funded purchases to protect Canadian jobs.”

The daydream of these Buy Canadian advocates seems to be that they can simply bully the government into adopting a Buy Canadian policy and that the rest of the world won’t mind. The CAW has produced a legal opinion saying that buy domestic policies do not violate trade laws. In fact, many of these Buy

Canadian advocates seem fine with a Buy American policy as well, so long as Canada is exempt.

But considering the magnitude of our trade with the United States and our trade surplus, such protectionist policies would not serve the interests of Canadians and, very specifically, the interests of Canadian workers—the people many of these politicians and labour officials claim to represent.

These Buy Canadian advocates should also consider that if the Buy American policy comes back to the table, those US politicians who think that Canada is “stealing” US auto jobs may decide that it is payback time.

That’s the way trade wars work—and they escalate. That is why world leaders reacted so strongly to what, in the grand scheme of things, is a small restriction: a Buy American clause limited to one product group (steel products) and one spending stream. Yet sensible leaders recognized—and feared—that this would be enough to compel other nations—egged on by the sort of protectionist sentiment we face in Canada—to respond with their own protectionism. And that would spark further responses from the United States.

However, this reality seems to be lost on Canadian protectionists. Erin Weir, an economist with the United Steelworkers Canada, argues for a “Buy North America” policy because trade in steel products is well balanced between Canada and the United States (Weir, 2009, Feb. 5). But how long would it take before protectionists in the United States realize that most Canada-US trade is heavily unbalanced in Canada’s favour? Canada’s huge trade surplus could quickly become a bull’s-eye for “saving” American jobs.

Many in Michigan already believe that Canada’s trade surplus, more than the presence of Asian and European car-makers, is responsible for the deserted plants littered across desolate landscapes across Michigan and much of the rust belt. Figure 3 shows that motor vehicle trade between Canada and the United States largely favours Canada. Yet the CAW, which claims to represent Canadian auto workers, is blowing the protectionist horn the loudest. Let’s hope that the racket does not wake up the protectionists in the United States.

The United States has a continent-sized economy and could do fairly easily

Figure 2a: Trade with the United States in manufactured goods, 2004-2008 (in billions of CA\$)

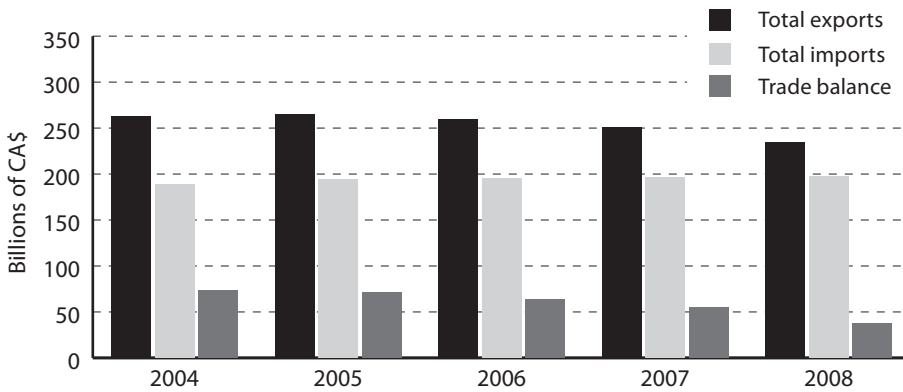


Figure 2b: Trade with all countries (excluding the United States) in manufactured goods, 2004-2008 (in billions of CA\$)

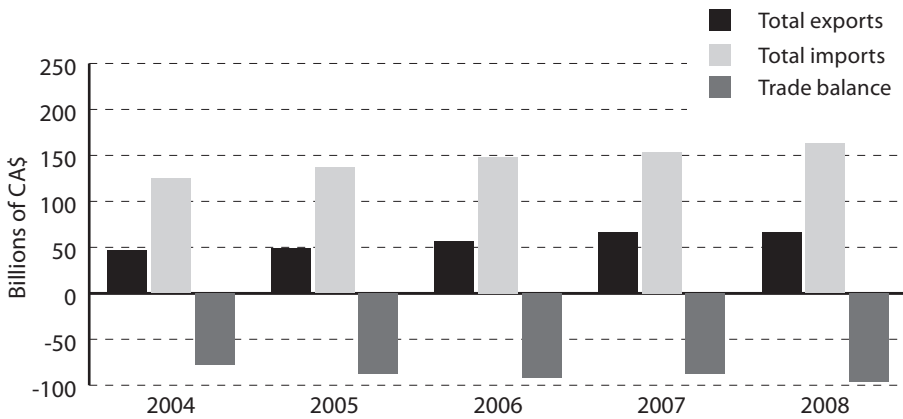
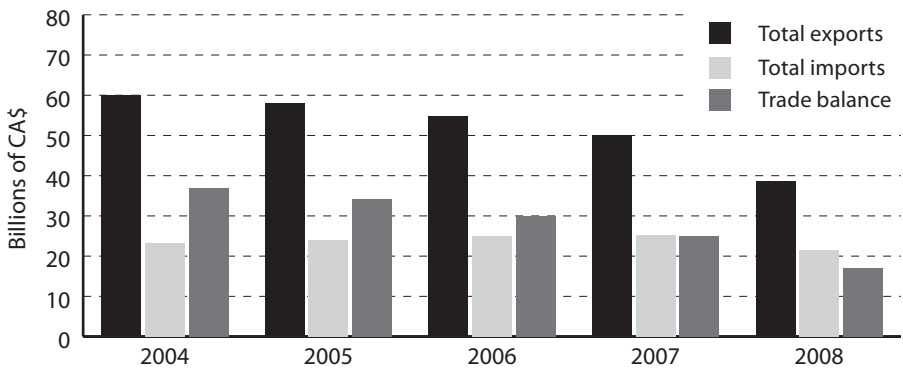


Figure 3: Trade with the United States in motor vehicles, 2004-2008 (in billions of CA\$)



Source (for figures 2a, 2b, and 3): Industry Canada, 2009.

without exports to Canada, but Canada could not do without the US market. A US trade war would devastate Canada's economy and throw tens of thousands of Canadians out of work.

The extent and profile of our trade with the United States will change during the economic downturn, but we will desperately need that trade to cope with the recession and to power our recovery afterward.

The immediate protectionist danger from the United States seems to have passed, but Canadian protectionists are still advocating Buy Canadian measures. In doing so, they seem to be putting their anti-trade ideology ahead of the interests of the people they claim to represent.

Note

1 A trade surplus or deficit is equal to the difference between a country's exports to and imports from another nation.

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MONEY

How it works and why

by Steven Horwitz



Money is one human institution that is so ubiquitous that we do not often step back and try to understand exactly how it works and why. After all, when one thinks about it, it is somewhat strange that a customer can walk into a store, hand over a piece of paper with ink on it, or just transfer some bytes of information over a computer, and walk out with merchandise worth much more than the ink and paper or the bytes. How has it come to be that we engage in this massive network of trust that we call monetary exchange? What exactly makes something money, and what role does money play in the economy and in generating economic growth and preserving economic freedom?

Money, like many other economic institutions, is not the product of human design. No one invented money. Rather, money is a classic example of a spontaneous, or unplanned, order.

Prior to the system of monetary exchange, people had to barter their goods and services for the goods and services of others. But the problem with a barter economy is that it can be very difficult to find someone who both has what you want and wants what you have. Frustrated in their ability to make exchanges, people began to hold stocks of goods that they thought other people really wanted as a way

to make it easier to exchange with them. This so-called “indirect exchange” (e.g., exchanging eggs for corn and then corn for meat) involved two steps rather than one, but it was still easier than direct exchange. Eventually, people discovered that certain goods fulfilled that intermediary role particularly well, and these indirect exchanges converged upon one or two such goods, giving us money. Consequently, money is often defined as a generally accepted medium of exchange. Which goods worked best was often culturally specific—some societies adopted things like shells, stones, or even cattle—but precious metals became standard because they had a commodity value of their own and had physical properties that enabled them to be stored and divided easily.

The use of money means that we no longer have to worry about finding someone who both wants what we have and has what we want. We only need to find someone who has what we want because we know people will accept money for their goods or services. Thus, money makes it much easier for people to engage in exchange, and this, in turn, improves economic well-being by getting goods into the hands of the people who value them most.

The spontaneous order view of money also implies that governments cannot declare as money anything they wish. Money is what money does; it is whatever market traders converge on as a generally accepted medium of exchange. Even when governments create “fiat money”—money that they declare to be money using the law—they will have to somehow link the new money to the one the market has already decided upon. Money must always have a contemporary or historical relationship to an actual commodity that the public has chosen to use as a medium of exchange.

The most important consequence of the use of money is that it makes it possible for each good or service to have a unique price assigned to it in terms of that money. When

all prices in a country are stated in terms of the national currency it is very easy to compare the values of the goods and services in

that economy. The act of exchanging money for goods is a form of communication that enables the prices that emerge from those exchanges to be signals to producers and consumers about value. When prices are stated in terms of money, consumers can formulate budgets and determine the wisdom of their various expenditure choices. Perhaps more importantly, producers can determine which goods will be the most cost-efficient to produce, and they can know, based on profits and losses, whether the choices they have made in the past were good ones. They can also use current prices to inform any changes in behaviour that they think may be necessary in the future. Money prices make it possible for producers and consumers to engage in the crucial task of



KEY CONCEPTS



***Key Concepts** is a series of essays on the fundamentals of economics and markets. In addition to appearing in *Fraser Forum*, these essays will form the basis of a live Ask the Professor discussion, held at www.fraserinstitute.org each month.

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economic calculation, without which economies would not progress. The more extensive an economy's use of money, the easier it is to improve the well-being of all who take part in it.

Initially, money was produced by private actors. Money first came in the form of gold coins, which were originally produced by private minters and stored by goldsmiths. But governments quickly realized that they could profit by monopolizing coin production, particularly if they spent them into circulation by purchasing goods and services for the king or queen to use. Paper money was also pioneered by the private sector, as banks discovered that they could give customers paper "receipts" for gold held in vaults and that those receipts could then be traded in the marketplace instead of the gold itself. As long as banks were required to keep their promise to redeem the paper notes in gold, this system worked quite well. However, here, too, governments realized that by intervening in this process, or by claiming a monopoly over the production of currency, they could use this money to acquire resources. The central banking systems that we have around the world today exist not because the private production of money failed, but because governments saw control over money production as a way to fund their activities, especially the military, without having to raise taxes.

In a modern economy, a variety of financial instruments are used as money or money substitutes. We still use paper bills and coins, but we also use cheques and, more recently, debit cards to make payments. Both cheques and debit cards are ways of conveniently accessing the funds that people keep in banks. Rather than withdrawing money every time we need it, cheques and debit cards offer us a way to order our bank to transfer funds to the bank account of the person from whom we wish to purchase. Credit cards, by contrast, are not technically a form of money but are unsecured lines of credit. Credit cards eventually have to be paid off using money in one form or another.

Other financial instruments can work like money by enabling people to write cheques from them. One good example is money market mutual funds, where small savers' funds are pooled by a bank to purchase interest-bearing financial instruments, with the bank paying a slightly lower interest rate to their customers than they earn on the instruments. Most of these funds allow their owners to write cheques, usually with a high minimum amount, from their accounts, and those cheques are, in essence,

orders to the bank to sell off some of their funds to pay the recipient's bank.

The challenge facing central banks today is knowing how much money to supply and then which actions of theirs will supply that exact amount at the correct time so as to avoid the artificial inflation of the prices of goods and services. If the central bank issues too much money, the public will spend those extra funds on more goods and services, causing their prices to rise ("inflate") above the levels justified by the real factors in the economy. Inflation not only reduces the value of money (and the value of people's financial assets, such as savings accounts, that are denominated in terms of that money), but it also undermines the ability of prices to provide reliable information for economic calculation. Persistent inflation reduces economic growth and can even trigger a depression by making it harder for producers and consumers to disentangle the influence of inflation on prices from that of changes in the real economy.

Severe or "hyper" inflation can ultimately destroy an entire economy by making its money worthless. Such a scenario demonstrates one of money's most important roles: it makes possible a society based on voluntary consent, contract, and exchange. When money is destroyed, our ability to interact on the basis of exchange is also destroyed, leaving force and coercion as the only option for human interaction. In this way, money is not just a symbol of economic freedom, but is also one of its most fundamental institutions. Not only does money allow us as individuals to turn our labour or assets into whatever purchases we desire, but it also enables us as a society to live by consent and exchange, rather than by brute force. Money makes us better off and it civilizes and humanizes us.

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EDUCATION AND OPPORTUNITY

In celebration of the Fraser Institute's 35th anniversary, each issue of *Fraser Forum* in 2009 will look at a different milestone in the Institute's history. This feature looks at the history of the Institute's student programs.

A little over 20 years ago, the Fraser Institute held its first student seminar. For a first-time event, the attendance was remarkable: 60 enthusiastic students from several nearby universities and colleges participated.

Since then, the Institute's student programs have reached over 13,000 students directly and many thousands more indirectly. Its programs have expanded to such an extent that in January 2009, the department was officially renamed Education Programs, reflecting its broadened mandate and extensive reach. With programs for high school and university students, high school teachers, journalists, and other professionals, Education Programs continues to grow—both in size and influence.

What's on your resume?

THE idea for starting up programs for students came to Mike Walker, founding Executive Director of the Institute, from an unexpected source: the resumes of politicians.

While on the speaking circuit, Walker had the opportunity introduce a number of high-level politicians. Reading their biographies, Walker says he was "astonished" at how many of them became active in politics during university through campus political clubs.

"It dawned on me that while we didn't have the resources to reach out to every university student, we could have a reasonable prospect of reaching out to every student who was interested in policy issues," says Walker. With that in mind, the Institute began targeting students in political clubs of all stripes, inviting them to take part in a one-day seminar program.

Though times and topics have changed, the basic structure of the Institute's seminars has remained much the same: the students listen to presentations, have the opportunity to ask questions, and then break off into discussion groups.

"The students could discuss the topics from whichever point of view," Walker says. "We didn't want to impose our views on them, but we did want to impose rules of civil discussion."

Those discussions—particularly in the earlier years—were often heated.

"Not everyone who came to the seminars was 'rah-rah free markets' and believed in the work we were doing. Many of them came to challenge us," recalls Annabel Addington, Director of Student Programs from 1994 to 2007. Addington joined the Institute's events department in 1991, assisting Director of Events Lorena Baran, who was the first student programs coordinator.

Early on, the Institute held only one or two seminars per year, but this soon became three or four and now is often ten or more.



CANADIAN STUDENT REVIEW: THEN AND NOW

CSR is sponsored by the Lotte & John Hecht Memorial Foundation, a long-time supporter of the Institute's student programs.

"We realized that there was a real market for these programs," says Addington, "that the students were loving them because these were ideas that they didn't generally hear on campus or read in their campus newspapers."



STUDENT SEMINARS: THEN AND NOW

Growing up

OVER the next few years, the Institute's student seminars program grew substantially, and by 1992, more than 650 students were attending annually. Wanting to offer further educational opportunities for these students, the Institute launched the Student Leaders' Colloquium, an advanced two-day program designed to give students a firmer grasp of free market principles.

The first colloquium, held in Vancouver in May 1992, was attended by 18 students who had participated in one of the Institute's student seminars.

In this way, says Addington, the student seminars became a "feeder program" for the colloquium—and in time, the colloquium became a feeder program for the Institute's internship program, which was formalized in 1995.

These internships, says Walker, were a "natural outgrowth" of the seminars and the colloquium.

"The point, really, is to give young people an opportunity to get involved in the public policy discussion, to get involved in trying to change the world at the earliest stage possible," he says.

The program started with just three interns, one of whom was Ezra Levant, now a well-known author and free speech advocate. While an intern, Levant wrote the Institute's first book by a student, for students.

"I wrote *Youthquake*," says Levant, "because I had a sense that young people were not as advertised—that is, we weren't all left-wingers, following political conventional wisdom, doing what our political teachers' union teachers expected us to do."

"It was an exciting project for us," Addington recalls. "We didn't have a lot of publications for young people at that time."

One of the existing student publications was *Canadian Student Review*, a newsletter with short articles on public policy issues, which was first published in 1992. Through CSR and the

student essay contest, which began in 1995, the Institute was able to "encourage young writers to get their ideas out there," says Addington.

New venues and avenues

NOT long after its tenth anniversary, Student Programs was poised to expand again, this time infiltrating high schools across Canada with seminars for students—and teachers.

In 1999, the Institute put on its first seminar for high school students, and the response, recalls Addington, was "incredible." As registrations poured in, the Vancouver-based event outgrew the hotel that had been booked for it. With almost 400 participants, it remains one of the largest student seminars to date.

The next year, the Institute followed up with a new training workshop for teachers, which attracted 19 participants.

"The teacher program was a real breakthrough for us," says Addington. "The teachers who came said, 'There is nothing else like this—this sort of professional development opportunity is quite rare.'"

Continuing on in its campaign to improve economic literacy among professionals, the Institute launched a week-long program for journalists in 2007, involving seminars and small group discussions about free market ideas. Twelve journalists attended the inaugural program, and thus far, more than 20 have applied to take part in this year's program.

More recently, Student Programs has expanded beyond the traditional seminar format with the launch of two highly successful web-based initiatives: a student video contest and Ask the Professor, a live online discussion based on a topical essay posted on the Institute's website each month.

"Both of these programs are connecting with students who are interested in economics and public policy using methods that they use everyday," says Vanessa Schneider, current Director of Education Programs. Going forward, Schneider plans to continue to use new media—online videos, blogs, and social networking—to teach people about economics and public policy so that current and future leaders "will be armed with the tools to craft better solutions."

Past and present

OVER the past two decades, the Institute's student programs have given students the opportunity to examine public policy issues from a free market perspective—an opportunity that has, in many cases, been a stepping stone to a career in public policy. Today, there are many politicians, academics, journalists, entrepreneurs, and businesspeople with the Institute's student programs on their resumes.

And that, truly, is Student Programs' biggest success.

—Kristin Fryer

Creating a common security perimeter

Canada's lax security still a concern for US

Martin Collacott

ONE of the issues that arose during President Barack Obama's visit to Ottawa in February was the "thickening" of the Canada-US border, the result of American security measures that have slowed down and increased the cost of cross-border movement.

In the weeks leading up to the talks between Prime Minister Stephen Harper and President Obama, speculation over the issues they were most likely to discuss gave relatively little priority to border security issues. This changed, however, when reports reached Canada that, a few days after taking office, the new Secretary for Homeland Security, Janet Napolitano, announced she had ordered a comprehensive review of security efforts along the border between the United States and Canada, including recommendations on what could be done to improve security.

One report linked her decision to a Department of Homeland Security assessment that, while more attention had been focused on the southern border with Mexico, the terrorist threat was greater on the US-Canada border, given its length and limited law enforcement (Blumenthal, 2009, Jan. 28). Shortly thereafter, an opinion piece that appeared in a number of Canadian newspapers referred to Secretary Napolitano's statement and raised concerns over the impact that further tightening of the border by the United States could have on the Canadian economy (Collacott, 2009, Feb. 3). The article noted that it was curious that the new secretary for homeland security should direct her attention first

to the northern border rather than the southern one, which is far more porous and of whose problems she would be well aware as the former governor of Arizona.

The article speculated that one possible explanation for this was that, in the midst of a rising protectionist sentiment in the United States, tightening the border with Canada could be a convenient way to reduce Canadian competition under the guise of security. It concluded by recommending that the prime minister make the creation of a continental security perimeter a priority issue in his talks with the visiting American president.

The subject of border security did come up during the talks, with President Obama apparently downplaying suggestions that his homeland security secretary was targeting the Canadian border rather than the Mexican one. Secretary Napolitano followed up two weeks later with a teleconference with Canadian reporters during which she said that the review of US-Canada border security she ordered was simply a fact-finding exercise, not necessarily a prelude to tougher border measures, and that the media had misconstrued her earlier remarks (Mayeda, 2009, Feb. 28).

These reassurances from President Obama and Secretary Napolitano notwithstanding, there has already been a significant thickening of our border by the American authorities over the past few years, and there is no guarantee that we will not see more of the same in the future. This does not mean that individual initiatives cannot be implemented to speed up movement of goods and people across the border. The Smart Border

Agreement, signed in 2001, provided a substantial list of such measures, many of which have since been put into place. The fact remains, however, that a common security perimeter would provide the most effective way to ensure that the border remains as open as possible.

Prospects

WHAT then are the prospects for establishing such a perimeter?

The proposal itself is not new. It was suggested in the final years of the Clinton administration by the American ambassador to Canada, Gordon Giffin (Policy Research Initiative, 2001), and by Paul Cellucci (Hunter, 2001, Sep. 13), his successor under George W. Bush.

Reactions here were mixed. Some Canadians quickly grasped the benefits a common perimeter would bring to Canada—particularly since our economy depends much more heavily on our bilateral trade than the economy of the United States does. Others, however, were wary since it would involve harmonizing Canadian and American procedures in areas such as visa issuance and the processing of asylum seekers. In the view of some critics, it would constitute a loss of sovereignty and an erosion of Canadian values as reflected in our liberal approach towards allowing people into the country.

Following these initial expressions of US interest, little further was heard from the Americans regarding the perimeter concept. And while significant progress has been made by the two governments in putting in place various measures for facilitating the movement of goods and

people across the border, the US government has continued to increase security on its side in various ways.

Not all of the changes have had an impact on legitimate cross-border traffic. The increasing use of unmanned surveillance aircraft by the United States, for example, does not impede such traffic and, in fact, benefits both countries by monitoring crossings along a border that is both long and, for much of its length, sparsely populated.

Other measures, however, have thickened the border since 9/11 in a manner that has had an adverse effect on the movement of people and trade. One recent analysis concluded that, because of increased American security requirements, Canadian exports of goods to the United States (excluding energy and forestry products) are 12.5% lower than they otherwise would be (Grady, 2008). Another estimate has put the post-9/11 cost of waiting, processing, and security measures at the border at 2% to 3% of total trade (Moens and Cust, 2008).

Under the circumstances, it seems clear that a major initiative will be required and some sort of comprehensive agreement reached if Canada is to avoid further significant erosion of its trading relationship with the United States due to the increased tightening of the border for security reasons. The most obvious way of achieving this would be through the establishment of a common security perimeter around the two countries.

Hurdles to be cleared

A comprehensive agreement on a common security perimeter would involve harmonized policies in a range of areas including, for example, protocols and standards for the entry of goods into the two countries. For the purpose of this article, however, I will focus only on security issues relating to people, particularly those involving terrorist threats, since these are likely to pose some of the

more formidable obstacles to reaching a comprehensive agreement. I will leave it to others to determine what might be involved in arriving on a common approach in other areas, such as the entry of goods.

With regard to the question of terrorist threats from our side of the border, President Obama reportedly alluded to this when he told Liberal leader Michael Ignatieff that Americans have concerns about Canada as a possible transit point for global terrorism (O'Neill, 2009, Feb. 20).

While this is hardly news, it is not often that a senior American official says this with such candor. There is, in fact, no shortage of evidence that the United States has concerns in this area if one takes the trouble to look for it. In my 2006 Fraser Institute paper *Canada's Inadequate Response to Terrorism: The Need for Policy Reform*, I identified a range of American sources describing the United States' misgivings in this area.

Chief among concerns in Washington are (1) what are perceived as our lax immigration and refugee policies, and (2) Canadian legislation and judicial rulings that make it difficult to exercise effective control over who enters and who should leave our territory.

An example of the latter is the failure, after two years of negotiations, of Canada and the United States to reach an agreement on arrangements to speed up traffic on the Peace Bridge between Fort Erie and Buffalo. The plan was to provide for pre-clearance by American officials at the Canadian end of the bridge for travelers entering the United States. Canada, however, refused to agree to the United States' demands that they be allowed to take fingerprints of such travelers since, under Canadian law, this could only be done in the case of someone charged with a crime. In the words of then-Minister of Public Safety Stockwell Day, "Canada will not consider any proposal that would diminish the basic

individual rights of Canadians" (Kralej, 2007, Apr. 27).

In the last few years, Canada has made significant progress in some areas in dealing with terrorist threats. Shortly after taking office, the Conservative government designated the Tamil Tigers as a terrorist group and has taken steps to seize the property of a front group involved in fundraising on behalf of the organization (Bell, 2009, Mar. 4). In addition, Canada recently handed down its first conviction and sentence under its anti-terrorism laws (Brennan, 2009, Mar. 12), and, in terms of strengthening border security, the government is considering plans to collect biometric information from visitors to Canada (Thompson, 2009, Feb. 27).

The United States, however, continues to have strong reservations about Canada's ability to exercise control over who gets into the country, to ensure that dangerous individuals are removed in a timely manner and that extremist elements are not allowed to operate with comparative ease. In particular, more than a few Americans have voiced concerns about the effectiveness of our immigration and refugee systems. We have, for example, tried unsuccessfully for more than two decades to deport convicted terrorist Mohammed Issa Mohammed (Collacott, 2006: 29). And even when a dangerous individual has been removed, we may invite him to come back again because of legal technicalities.¹

While there are concerns over various aspects of Canada's immigration program from a security point of view, particular attention has been focused on our refugee determination system. The latter has the highest per capita intake and acceptance rates of any refugee program in the world, and has been a major conduit for the entry of terrorists and their supporters into Canada (Collacott, 2006: 87). While Canada is better placed geographically than most countries to avoid large

numbers of asylum seekers reaching our borders, the number who do manage to enter has been increasing in recent years. After a decline in applications following 9/11, applications rose to almost 38,000 in 2008—almost double the number in 2005 (UNHCR, 2007, 2008).

The United States may also have concerns about the extent to which closer cooperation with Canada in terms of guarding against threats from terrorism will be possible in the future. One of the most important facets of such cooperation has been the arrangements under which security and intelligence agencies in the two countries have been able to exchange sensitive information on individuals and organizations that may pose a threat.

The scope of such exchanges, however, has been somewhat circumscribed by the results of the O'Connor commission, which examined the circumstances under which dual Canadian-Syrian citizen Maher Arar was sent to Syria by the United States after being detained at the John F. Kennedy airport in New York in 2002. The commission concluded that Canada had provided US agencies with information about Arar that formed at least part of the basis on which the Americans decided to dispatch him to Syria, and that we should be more circumspect in what we share with US agencies in the future.

Increased Canadian caution in this regard was evident in the Canadian government's recent decision, reportedly under pressure from privacy advocates, to repatriate from the United States a database of personal information on Canadian citizens (Beeby, 2009, Feb. 16).

In addition to the forgoing concerns, other developments in Canada may leave US authorities with doubts about our readiness or ability to bring under control the activities of militants already on our soil. In April 2007, for example, members of the Sikh community in British Columbia publicly venerated the assassins of Indian Prime Minister Indira Gandhi (Bolan, 2007, May 11), and

in March of this year, a public memorial service was held in Toronto for the Tamil Tiger pilots who carried out a suicide attack on the Sri Lankan capital of Colombo (Bell, 2009, Mar. 3).

Another area of concern regarding the capacity of Canadian authorities to deal effectively with security threats is that of resources. Colin Kenny, the chair of the Senate Committee on National Security and Defence, recently declared that his committee had concluded that the RCMP is short 5,000 to 7,000 officers. Its contingent for patrolling the Great Lakes, for example, consists of only 14 officers compared to 2,200 US Coast Guard personnel on the American side. He also reported that the RCMP told the committee last year that it only had the resources to track one third of the Canadian criminal organizations it knows to exist.

Senator Kenny also stated that the Canadian Border Services Agency is short 2,300 employees and that while the federal government is planning to hire 400 more, this would not be nearly enough to keep traffic moving at border crossings while maintaining a high level of security. Nor is the situation much more encouraging at the Canadian Security Intelligence Service, which has fewer employees now than it did 18 years ago, even though it now has more responsibilities (Kenny, 2009, Mar. 12).

Conclusion

WHETHER or not we can reach agreement on a common security perimeter remains to be seen, particularly in light of the obstacles mentioned above. If we can achieve such an accord, it would certainly provide much greater assurances than we have at present that Canadian exports, as well as people, will be able to move relatively easily into the United States. Even if complete agreement is not possible, it would still be worth exploring more thoroughly the concerns the

Americans have with respect to security threats from our side of the border. With such information, we could then examine what measures we could take to alleviate some of these concerns and, hopefully, convince the United States that it does not need to strengthen security along the border in ways that would impede legitimate traffic. If we do not take some sort of initiative in this regard, we will probably have to resign ourselves to further thickening of the border by the United States and the implications that will have for the Canadian economy.

Note

1 A recent case in point is that of convicted gang member, Panchalingam Nagalingam, who was sent back to his native Sri Lanka after various criminal charges and convictions including a brutal attack on two people. After Canada successfully deported him three years ago, the Federal Court of Appeal ruled in April 2008 that there had been a procedural error at his last trial. In February 2009, he was, therefore, allowed to return to Canada and was flown here from his home in Sri Lanka at the Canadian government's expense (Bell, 2009, Feb 27).

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2009 Dr. Harold Walter Siebens AGM Lecture and Luncheon



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Obama's radical remake of the US economy

Jason Clemens

THERE is no arguing that the election of Barack Obama as president of the United States was an historically significant event. In the 2008 election, his Democratic Party not only captured the presidency, but also swept both houses of Congress. The Democrats, led by Obama, House Speaker Nancy Pelosi, and Senate Majority Leader Harry Reid, are now capitalizing on their unified power, the population's willingness to support larger-than-normal changes due to the current economic crisis, and the president's overwhelming popularity. The plans being promulgated and, in many cases, implemented represent nothing short of a radical remake of the US economy. The next few months may very well decide the economic future of the United States—and countries such as Canada, which are dependent on the United States as a destination for its exports—for a generation.

Obama's starting point

IN order to understand the depth of the president's commitment to fundamentally remaking the US economy, it is essential to understand the perilous fiscal position he inherited.

In early 2009, the non-partisan Congressional Budget Office (CBO) calculated that the deficit for 2008 would be \$455 billion (CBO, 2009a).¹ The CBO estimated that the deficit would increase to \$1.2 trillion in 2009. This increase is largely the result of declining tax revenues, due to the recession, and increased

spending. This estimate, however, does not include the recent "stimulus" package or the update to the 2009 budget.

President George W. Bush, in collaboration with the Democrat-controlled Congress, also approved a number of indirect spending initiatives, such as spending by the Federal Reserve and loan-guarantee programs that also need to be taken into account. For instance, the Federal Reserve created a number of backstop guarantees, insuring companies such as Citigroup (\$301 billion),

Despite the president's repeated speeches about fiscal discipline and his much-touted February summit on "fiscal responsibility," Obama has not attempted to rein in federal spending.

Bank of America (\$118 billion), and AIG (\$152 billion) against future potential losses. The Troubled Asset Relief Program (TARP), which was originally designed to remove toxic bank assets, was famously expanded to include "lending" to the "Big Three" domestic auto companies.² The Federal Reserve also created the Term Asset-Backed Securities Loan Facility (TALF), which supports lending for student loans, auto loans, and credit cards. It was originally seeded with TARP funds, but has since been expanded to more than \$1 trillion. Finally, according to the Committee for a Responsible Federal Budget, a total of almost \$1 trillion has been committed to support Fannie Mae and Freddie Mac.³

Team Obama takes over

DESPITE the president's repeated speeches about fiscal discipline and his much-touted February summit on "fiscal responsibility," Obama has not attempted to rein in federal spending. Indeed, as the following summary will illustrate, he and his congressional colleagues have accelerated spending at a nearly unprecedented pace.

The first major legislative initiative of President Obama, in cooperation with

the Democrat-controlled Congress, was the American Recovery and Reinvestment Act 2009, which is commonly referred to as the stimulus bill. The total cost of the package was estimated by the CBO to amount to \$787.2 billion over the next 10 years (2009-2019) (CBO, 2009b). However, that estimate ignores the fact that all of the funds will have to be borrowed. Once borrowing costs are included, the expected price tag increases to \$1.27 trillion over the next 10 years, using current government interest rates.^{4, 5}

It is also important to understand some of assumptions underlying the CBO estimates. There are a host of spending initiatives included in the stimulus package that the CBO assumes will end

in 2011. In other words, the CBO accepts the premise that the increase in spending in health care, education, energy, unemployment insurance, and other programs will not become permanent spending. This assumption is more than a little dubious. A far more realistic assumption would be that much of this “temporary” spending will become part of the baseline for future budgets, thus increasing government spending permanently.

The CBO estimates that the stimulus package will increase the deficit for 2009 by \$185 billion (CBO, 2009b). However, the House of Representatives recently passed additional spending for the current fiscal year (2009). At the time of writing (March 11), both the House and Senate had approved an additional \$410 billion in spending for 2009. In total, this means that government spending will increase by nearly 9% over the level recorded for 2008. Indeed, an updated forecast for the deficit this year (2009) is \$1.75 trillion (OMB, 2009).

President Obama also announced at the end of February, at almost the same time as the House of Representatives passed its additional budget spending, a new \$275 billion program to tackle the housing foreclosure crisis. The proposal includes two principal components. The first component, worth \$75 billion, will finance several new programs, including interest relief and an insurance fund for lenders at the Federal Deposit Insurance Corporation (FDIC). The second component, worth \$200 billion, will go to Fannie Mae and Freddie Mac to assist them in expanding their loan portfolios.

Remaking the US economy

JUST after his speech before a joint session of Congress on February 24, Obama released a “blueprint” for his forthcoming budget plan (OMB, 2009).⁶ The response to the blueprint has been almost unanimous in terms of the plan’s scope and depth of proposed changes. Daniel

Henninger of the *Wall Street Journal* characterized President Obama’s speech and related budget plan as “a radical shift in the relationship between the people and their government” and likened it to Lyndon Johnson’s Great Society project of the 1960s (Henninger, 2009, Feb. 26). David Broder of the *Washington Post*, who is widely acknowledged as a dean of liberal-oriented political commentators, described President Obama’s approach to reform in his first month in office as follows:

The size of the gamble that President Obama is taking every day is simply staggering. What came through in his speech to a joint session of Congress and a national television audience Tuesday night was a dramatic reminder of the unbelievable stakes he has placed on the table in his first month in office, putting at risk the future well-being of the country and the Democratic Party’s control of Washington. (Broder, 2009, Feb. 26)

The following are the key highlights of the president’s plan.

Health care

One of the centerpieces of the president’s proposal is expanded government-financed health insurance coverage. This budget sets aside \$630 billion to be used to finance health insurance coverage over the next 10 years. This amount, however, was characterized as only a “down payment” on additional spending for government-provided health coverage. This move is widely acknowledged as yet another step towards single-payer universal health coverage. The amount will be financed through \$316 billion in projected “health savings” and \$317.8 billion in tax increases over the next 10 years.⁷

Climate change

The president is calling for the establishment of an “economy-wide emissions re-

duction program to reduce greenhouse gas emissions.” The program will take the form of a cap-and-trade system that is expected to bring in \$646 billion in fees (taxes) between 2012 and 2019. The goal is to reduce emissions to 14% below 2005 levels by 2020 and approximately 83% below 2005 levels by 2050. Revenues derived from the program will be used to fund “clean energy” projects amounting to \$140 billion over a 10-year period beginning in 2012.⁸ A series of tax credits and deductions for traditional energy companies, mainly oil and gas, will also be eliminated.

Taxes

The budget blueprint calls for increases in a number of taxes over the next 10 years.

- Some of the Bush tax cuts will be left to expire in 2011, raising the top two personal income tax rates from 33.0% and 35.0%, to 36.0% and 39.6%.
- The value of itemized deductions will be limited to 28.0%, regardless of one’s income bracket. In other words, even if an individual is in a tax bracket above 28%, the value of their itemized deductions, including mortgage interest, will be calculated based on the middle income tax rate of 28%.
- The capital gains tax for individuals earning more than \$200,000 and families earning over \$250,000 will be increased to 20.0%.⁹
- The estate tax for inheritances over \$3.5 million will remain at 45.0%. It was scheduled for repeal in 2010.
- US multinationals will no longer be able to shield foreign earnings from US taxes. This will raise the overall effective tax rate for US companies.¹⁰

TARP

Obama’s plan calls for using the remaining TARP funds, plus an additional \$750

billion (of which \$500 billion is expected to be repaid), to stabilize the US banking system.

There are a host of other areas for which significant expansions of government spending and regulation have been proposed, including education, defence, foreign service, and transportation.

The very structure of the president's fiscal plan has been strongly criticized by a number of economists for relying on overly optimistic assumptions of economic growth.¹¹ These optimistic assumptions have allowed the Obama administration to project sizeable decreases in government spending and the deficit over the next 10 years. For instance, the plan assumes reasonably strong economic growth in the coming years: 3.2% in 2010, 4.0% in 2011, 4.6% in 2012, and 4.2% in 2013. In contrast, forecasters surveyed by Blue Chip Economic Indicators in February have predicted that the economy will experience relatively weak growth through to 2013: 2.1% in 2010, 2.9% in 2011 and 2012, and 2.8% in 2013 (Crutsinger, 2009, Feb. 27).

Indeed, data released by the Commerce Department on February 27, a mere three days after Obama's speech, seems to illustrate the fairy-tale nature of the administration's economic assumptions. The department reported that the economy contracted by 6.2% in the final quarter of 2008 (annualized rate), a much larger decline than the 3.8% retraction predicted by the Obama administration (Goodman, 2009, Feb. 27).

In a similar fashion, the budget plan makes aggressively optimistic assumptions about program savings in the future and likely interest costs. Much of the savings assumed in the 10-year plan are tenuous at best. For instance, if even a small percentage of the so-called "temporary" programs expanded or created by the stimulus bill are made permanent, much of the planned savings will be effectively eliminated.

Combined, these overly optimistic assumptions mean that it will be nearly impossible for the Obama administration to achieve its spending reductions and deficit targets over the next 10 years. It also raises serious doubts about the administration's commitments to no new taxes for the middle class.

Conclusion

THE United States, and indeed much of the industrialized world, is in a perilous economic situation. Citizens are demanding a response. The Obama administration is using the current crisis to implement large-scale changes across nearly every department of government. Some of the changes, such as tax increases, cap-and-trade climate regulation, and massive expansion of government-provided health care, will fundamentally change the US economy if they are actually implemented, and in doing so, will impair economic growth and prosperity in the foreseeable future.

Notes

1 This amount includes a Social Security "surplus" of \$183 billion. In other words, the federal government was operating a \$638 billion deficit before the Social Security funds were included.

2 In total, they received more than \$17 billion in late 2008 to help finance their operations through to March 2009. GM and Chrysler have since requested an additional \$21.6 billion. At the time of writing, Ford had not requested additional monies.

3 For more information on these two organizations, which were designed to promote and facilitate home ownership in the United States and which are at the core of the current financial crisis, please see www.fanniema.com and www.freddiemac.com.

4 See Clemens and Frey (2009) for a discussion of this calculation.

5 This amount will increase to \$1.42 trillion if interest rates increase by even a single percentage point. This is an important con-

sideration given that interest rates appear to have reached or are near the bottom of this cycle.

6 The US budget system is markedly different from those used in parliamentary systems such as Canada's. The president's blueprint is now being considered by Congress. The House and Senate will then craft their own budgets. Once completed, various committees will provide more detailed budget authorizations and spending plans based on the agreed upon budget in each chamber of Congress. The two budgets (House and Senate) must then be reconciled with one another once the authorizations are completed. The budget is then sent to the president for approval.

7 A number of commentators have indicated that the price tag will actually be closer to \$1 trillion, and that the revenues projected from the tax increases are overly optimistic.

8 Much of the remaining funds will be used to finance income transfers to low- and middle-income families.

9 Critically, the budget plan assumes that a higher capital gains tax will result in \$118 billion in additional revenue. This is a questionable assumption given that the US experience has consistently shown that higher capital gains tax rates result in less revenue, and vice versa. For an excellent discussion of this phenomenon, please see Moore and Silvia (1995). For a discussion of the Canadian experience, please see Clemens et al. (2007) and Grubel (2001).

10 This measure is expected to yield \$210 billion in revenues over the next 10 years. However, this estimate assumes that firms will not re-organize their affairs in order to mitigate the effect of this tax change. A far more likely scenario is that US-based multinationals will begin restructuring their businesses in order to manage the tax implications of this change.

11 Economists generally agree on the efficacy of more conservative economic assumptions when crafting budgets.

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Give Quebec workers democratic rights

Niels Veldhuis &
Alex Gainer

WITH another chapter set to end in the United Food and Commercial Workers' Union's (UFCW) long-running efforts to unionize Wal-Mart stores, the Quebec government has again demonstrated that it is more interested in placating unions than in doing what is right for workers.

Back in 2005, the UFCW was "certified" as the exclusive bargaining agent for workers at the Wal-Mart store in Saint-Hyacinthe. After a series of legal proceedings, Alain Corriveau, the arbitrator appointed by the Quebec Ministry of Labour, is now preparing to impose a collective agreement on Wal-Mart and its workers in Saint-Hyacinthe.

The problem is that workers were unionized without the opportunity to show their preferences through a secret ballot vote. In Quebec, a union can automatically be certified if the majority of workers (50% plus one) sign union cards, a process referred to as "card check." That is how the union at the Saint-Hyacinthe Wal-Mart became certified.

The card-check system of union certification has a number of serious problems. First, card checks are inherently confrontational. Union organizers and workers wanting union representation are able to go to the homes of other workers or approach them in parking lots and other public places in order to persuade them to sign union membership cards. If a worker decides not to sign a membership card, union organizers cannot be prevented from repeatedly approaching them.

The confrontational nature of the card-check system can also create hostilities between workers in a company. Given that individual decisions are known by all workers, card checks often create conflicts between co-workers who must ultimately work together after a union certification drive commences.

The card-check system also restricts the flow of information. Under such a system, many employers only become aware of unionization campaigns once they are virtually complete and, as a result, the union is often the only source of information for workers. This makes it difficult for workers who do not have access to a full range of information regarding unionization to make an informed decision.

Supporters of card checks argue that the ability of employers to communicate with workers during unionization campaigns leaves workers subject to intimidation. The reality, however, is that workers are protected under the Labour Relations Code against what is commonly referred to as "unfair labour practices," which include threats of dismissal, wage decreases, or the alteration of any conditions of employment.

Not surprisingly, when workers are given the right to vote for union representation using secret ballots, they choose collective representation much less often.

Professor Christopher Riddell (2004) studied the effects of different certification mechanisms, looking at the experience of British Columbia between 1978 and 1998. In 1984, the province implemented secret-ballot voting and then

reverted to a card-check system in 1993. Professor Riddell found that unionization success rates fell by 19% after mandatory secret ballot voting was introduced and then increased by nearly the same amount when it was eliminated.¹

Similarly, Sara Slinn (2004), examined the impact of changing from a card-check system to secret ballot voting in Ontario. The results of Slinn's study showed that the establishment of secret ballot voting in 1995 reduced the likelihood that a union would be certified by 21%.

In 2005, the Ontario government removed the requirement for secret ballot voting for the construction sector and replaced it with a card-check system. A

new study by Timothy Bartkiw (2008) reveals that the 2005 changes are already having an impact on the volume of union-organizing attempts and their success rates. Specifically, these changes have led to an average increase of seven new bargaining units certified per month. This translates into an overall increase in certification success rates of 10.2 percentage points.²

The research consistently shows that when workers are given the opportunity to make private, anonymous decisions through secret ballot voting, the result is lower levels of union certification.

Quebec is one of only four North American jurisdictions (10 Canadian

provinces and 50 US states) that allow union certification without a formal, secret ballot vote. Without a secret ballot vote, workers cannot choose anonymously or democratically. It's time Quebec workers had democratic rights.

Notes

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

2 This effect was the result of eliminating the requirement for secret ballot voting to approve a union and changes that made it easier for the Ontario Labour Relations Board to remedially (automatically) certify unions.

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Refocusing on the Alberta Advantage

Nadeem Esmail, Niels Veldhuis, & Milagros Palacios

ALBERTA, like most Canadian provinces, is facing a pronounced economic downturn. If the experience of other governments in Canada is any indication, Alberta's government is sure to face tremendous pressure to implement "counter-cyclical" increases in government spending and more activist economic policies. The notion that governments can "stimulate" the economy is a fallacy that Albertans should not buy into. What Alberta really needs to do is refocus on the "Alberta Advantage": the combination of Canada's lowest tax rates, smallest government, and most attractive investment climate.

Despite the government's claim that "prudent fiscal management has positioned Alberta well" (Alberta, 2009), recent fiscal management has been anything but prudent. Massive increases in government spending, financed by volatile revenues, have left the province with a significant deficit, estimated at more than \$1 billion. While raiding Alberta's \$7 billion Sustainability Fund might temporarily help to close the gap, it will not solve the larger problems.

The unfortunate reality is that Alberta has turned its back on the policies that created the foundation of its recent prosperity: limited government and lower taxes.

Profligate government spending lies at the heart of this departure.

In its first budget, the Stelmach government clearly stated, "We just can't keep raising our spending at these levels—even if strong energy prices and

economic growth continue. The facts are clear. Hiking our operating spending by 10%—as we're doing this year—can't continue" (Alberta, Ministry of Finance, 2007: 12).

But continue it did. Last year's budget (2008/2009) increased operating spending by another 9.7%, an increase that was greater than the projected rate of economic growth. In addition, the budget proposed increases in operating spending that exceeded projected economic growth for the following two years (2009/10 and 2010/11) (Alberta, Ministry of Finance, 2008). Exactly how is that prudent?

This ramp-up in spending over the past two years follows imprudent increases in the later Klein years. Between 1995/1996 (the end of strong fiscal restraint in Alberta) and 2006/2007, government program expenditures in Alberta grew 174%, from \$10.7 billion to \$29.5 billion (Alberta, 1996, 2008).

Had the government exercised fiscal prudence and held spending growth to the rate needed to keep up with inflation and population growth since 1995/1996, Alberta's expenditures would have totalled just \$19.8 billion this year (2008/2009) instead of the projected \$37.6 billion—a difference of \$17.8 billion for 2008/2009 alone (figure 1). For a sense of scale, consider that Alberta is expected to raise a total of \$8.8 billion through personal income taxes and \$3.8 billion through corporate taxes in 2008/2009 (Alberta, Ministry of Finance, 2009).

One of the main results of the unabated increases in spending has been a dearth of meaningful tax relief. The absence of tax relief in Alberta has allowed

other provinces, particularly neighbouring Saskatchewan and British Columbia, to reduce the tax gap substantially.

For instance, British Columbia has been aggressively reducing its personal income taxes. Since 2001, BC has reduced its top personal income tax rate by 25% while Alberta has maintained its status quo. BC now has the lowest personal income tax for individuals earning up to \$108,000 of any Canadian province, including Alberta (Veldhuis and Angevine, 2007).

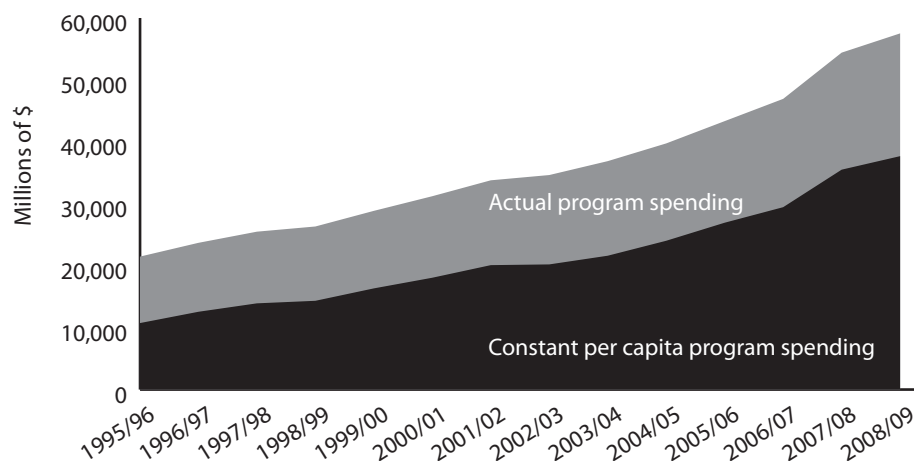
Both Saskatchewan and British Columbia have aggressively reduced their business taxes, and have taken away Alberta's significant advantage of being the only province without a corporate capital tax. While Alberta has reduced its corporate income tax, both Saskatchewan and British Columbia have followed suit (Veldhuis and Angevine, 2007; Clemens and Veldhuis, 2007).

The benefits for the economies of both BC and Saskatchewan have been obvious, while the relative attractiveness of Alberta's economic climate has waned. In fact, economic forecasts predict that those two economies will outperform Alberta's over the next two years (TD Bank Financial Group, 2008; Shenfeld, 2008; Scotiabank Group, 2009).

The time has come for the Alberta government to make the tough choices that these difficult economic times require. That is, it should follow the lead of Albertan families and trim spending.

Meaningful spending reductions coupled with program reform would strengthen Alberta's diminishing tax advantage and re-assert a clear focus on

Figure 1: Program spending in Alberta, 1995/1996-2008/2009 (in millions of \$)



Sources: Alberta, 1996 to 2008; Alberta, Ministry of Finance, 2009; Statistics Canada, 2008a, 2008b; calculations by authors.

the Alberta Advantage. Alberta's government expenditures do purchase a number of important services for Albertans. But it is critical to remember that this spending is not done efficiently.

For example, waiting lists for health care are much longer now than they were in the mid-1990s, despite large increases in health expenditures. In fact, Alberta's health care system ranks among the most expensive universal access health insurance programs in the developed world, but wait times for health care in Alberta rank among the developed world's worst (Esmail and Hazel with Walker, 2008; Esmail and Walker, 2008; CIHI, 2008; calculations by authors).

More broadly, a recent study found that there is approximately 25% waste in Canada's public sector as a whole (federal and provincial) (Tanzi et al., 2007). There is little reason to expect that Alberta would deviate from the national norm.

Clearly, there is room to cut spending without reducing benefits.

Responding to this economic situation with spending and government intervention, as other governments have

wrongly done, will only increase the risk of sustained deficits and delay a much needed refocus on the Alberta Advantage. The time has come for the government to reverse course. Prudent fiscal management coupled with sensible tax relief will provide a true stimulus now and in the future.

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The rising tide of protectionism in the United States

Alan W. Dowd

MANY observers outside the United States expressed concerns about the “Buy American” provision in the supersized “stimulus” package recently passed by Congress. For instance, a European Commission spokesman called the provision the “worst possible signal” and warned that it could have forced the European Union to “take it up with the World Trade Organization” (*BBC News*, 2009, Feb. 3). However, fears of a trade war were tempered by a compromise that kept the “Buy American” language but added an important caveat requiring that the measure be “applied in a manner consistent with US obligations under international agreements” (*Reuters*, 2009, Feb. 12).

In other words, the revised version shields existing trade agreements from the encroaching shadows of protectionism—for now.

Rejecting CFTA

CANADIAN Trade Minister Stockwell Day called the compromise “a great step forward” (*Toronto Star*, 2009, Feb. 9). Similarly, Japanese Cabinet Secretary Takeo Kawamura said Tokyo welcomed the compromise, but added that his government would “keep a close eye” on the situation on Capitol Hill, given that “the whole process leading up to this bill appeared to be rooted in protectionism” (*Reuters*, 2009, Feb. 12).

Indeed, it could have been worse, but the re-emergence of American protectionism should not be surprising to anyone who has been watching American politics.

“Our consensus to advance international trade is frayed,” as US Senator Max Baucus recently observed. “Our faith in the international trading system is badly shaken” (Faiola, 2009, Mar. 10).

The protectionist instinct is powerful among those who constitute much of the leadership of the current Congress and

approve a revamped version of CFTA (O’Donnell, 2009, Mar. 2).

Noting that the Colombian government “has increased democratic reforms ... taken on the insurgency ... [and] is moving that country forward economically and politically,” Prime Minister Stephen Harper admitted to

The re-emergence of American protectionism should not be surprising to anyone who has been watching American politics.

the Obama administration. If a free-trade scorecard compiled by the Cato Institute is any indication, many key congressional leaders are more inclined toward erecting trade barriers than promoting free trade (see www.freetrade.org/congress).

This sentiment was apparent during the debate over the Colombia Free Trade Agreement (CFTA), which the George W. Bush administration concluded in 2006. But the agreement has languished due to obstruction by members of Congress. Then-Senator Barack Obama was one of several senators who ardently opposed the trade deal with Colombia. Then-Senator Hillary Clinton was another, vowing to “do everything I can to urge Congress to reject the Colombia Free Trade Agreement” (*Los Angeles Times*, 2008, Apr. 9).

Allowing Colombia to dangle in the wind has not served anyone’s interests, except perhaps Europe’s. While the candidates pandered and Congress shrugged, the EU saw an opportunity and may finalize its own free-trade deal with Colombia before Washington can

lobbying his American counterpart to move forward on CFTA. “If you don’t support your friends,” he warned, “you are not going to have many friends” (O’Grady, 2009, Feb. 28).

“Fixing” NAFTA

SINCE governing is different from—and more difficult than—campaigning, perhaps the Obama administration will come around to Ottawa’s commonsense view on CFTA. If so, the new president will have traveled a great distance. After all, the pro-barrier view was on full display throughout the 2008 presidential campaign.

During his campaign, Obama voiced his opposition to a free-trade agreement with South Korea. “If South Korea is selling hundreds of thousands of cars to the United States and we can only sell less than 5,000 in South Korea, something is wrong,” he said in 2008 (Montopoli, 2008, June 20). Likewise, while campaigning to be the Democratic nominee

for president, Hillary Clinton, who is now secretary of state, called the Korea-US Free Trade Agreement “inherently unfair” (Wolf, 2007, June 9).

Candidate Clinton used NAFTA as a piñata, lauding its passage during her husband’s administration, but later saying on the campaign trail, “I’ve long been a critic of the shortcomings of NAFTA” (Fouhy, 2008, Feb. 19).

Candidate Obama also criticized NAFTA early and often. “We can’t keep passing unfair trade deals like NAFTA that put special interests over workers’ interests,” the would-be president said in early 2008 (Montopoli, 2008, June 20). He also called NAFTA “an enormous problem” (On the Issues, 2008). Meanwhile, on his campaign website he declared that “NAFTA and its potential were oversold to the American people,” and promised “to fix NAFTA so that it works for American workers” (Obama and Biden, 2008).

At the same time, his staff sent back-channel messages to Canadian leaders that his comments on NAFTA were little more than political posturing (Goldstein, 2008, Mar. 4).

Tapping into fear

It would be wrong to conclude that all of this was simply a function of campaign-season pandering. A 2004 Fraser Institute survey of Canadian exporters found that 95% of respondents “believe protectionist sentiment is growing in the United States,” with 68% saying that the “protectionist sentiment in the United States has already negatively affected their ability to sell into the United States” (McMahon and Curtis, 2004).

That survey, it pays to recall, was conducted when economic times were relatively good and the political environment was calm, which brings us to the American public.

Whether during the back-and-forth of the campaign or in the fine print of

the stimulus bill, American politicians are responding, to a great extent, to what their constituents are feeling. A 2008 CNN poll found that 51% of respondents view foreign trade as a threat to the US economy, up from 45% a year earlier. Likewise, a Pew/Council on Foreign Relations poll found that only 35% of Americans believe agreements like NAFTA are good for the United States. And a poll conducted by *The Los Angeles Times/Bloomberg News* reveals that 50% of Americans believe international trade has hurt the economy, while only 26% say it has helped the economy.

The facts say otherwise. After all, NAFTA has helped generate 26 million jobs in the United States, and “more than 57 million Americans are employed by firms that engage in international trade” (Markheim, 2008). However, the age-old impulse to turn inward when times get tough is a powerful force. As Prime Minister Harper warns, “There will be substantial political pressure, especially as the recession continues in all major countries, whether developing or developed, to widen protectionism as a way of responding.” A cycle of protectionist salvos, according to Harper, will “make this recession far deeper and far longer than it would be otherwise” (O’Grady, 2009, Feb. 28).

Given the economic contraction and convulsion now underway—America’s unemployment rate is 8% and rising, the US economy is expected to shrink by 1.5% this year, and the Dow has shed half its gains since 2007—it seems unlikely that the protectionist impulse in the United States will subside anytime soon.

Politicians are adept at tapping into these feelings of fear. Statesmen, on the other hand, resist them and remind the public about the benefits of trade and about how protectionism in one country triggers protectionism in another.

The statesmen in Washington, Ottawa, and other capitals have their work cut out for them in the months and years ahead.

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Taking action in the Arctic

Canada and US must work together

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THOUGH much of Canada's territory extends beyond the Arctic Circle, the vast majority of the country's population lives along the southern border, and most Canadians know surprisingly little about the Arctic despite its increasing global importance. For instance, polls show a strong emotional attachment to "our north," but no clear sentiment as to how much money or attention the government should devote to Arctic sovereignty, resource exploration, and security (Ipsos News Centre, 2008). The government's policy toward the Arctic region tends to reflect this public sentiment—not much strategic investment in security alongside strong emotional appeals for Canadian sovereignty.

The lack of consistent policy did not matter as much in the past as it will in the future. Thick ice prevented most human activity up north. Cold War-era security in the Arctic came in the form of early warning radar and air defence systems. Ice and harsh climate made shipping and most resource exploration impossible or too expensive to undertake. During these years, Canada and the United States would occasionally squabble about the status of the Northwest Passage, with Canada claiming any sea routes through its archipelago as internal waters, and the United States holding fast to the notion that the passage is an international strait connecting two oceans.

Of course, Canada has never had the military capacity to actually establish

and enforce its sovereignty in the Arctic. Canadian governments have promised to invest heavily in Arctic military and security capabilities at least twice in recent history: during the early years of the Mulroney government and under the current Harper government. However, in both cases, budgetary restraints eroded the plans, leaving Canadians with few assets to deploy in the Arctic (Coates et al., 2008).

But circumstances may yet force Canada to make the necessary investments—and pay the requisite attention—to protect its Arctic territories and claims.

Icebreaker

THERE are at least three interrelated reasons why it is time for Ottawa to do more than talk about Arctic security and sovereignty.

First, the prospect of rising oil prices in the long term and the emergence of highly sophisticated drilling technology provide new incentives and opportunities for exploring this resource-rich frontier. The US Geological Survey estimates that the Arctic may hold 1,670 trillion cubic feet of natural gas and 90 billion barrels of oil, equalling 30% of undiscovered gas and 13% of undiscovered oil reserves in the world (USGS, 2008).

A second factor fuelling Arctic activity—and demanding hands-on Canadian involvement—is the opening of new transit routes. The Northwest Passage, once frozen throughout most of the year and navigable only by heavy-duty icebreakers, is thawing. In fact, the *Wall Street Journal* reported that the

Northwest Passage was ice-free in 2007 (Chazan, 2008, July 29). The US Congressional Research Service notes that an ice-free Northwest Passage could “cut shipping routes between Europe and Asia by 3,000 to 4,000 miles” (Ek et al., 2008). Most major powers in the world, including China, Russia, and the European Union, agree with the American interpretation that an international strait, defined as “a body of water linking one area of the high seas to another” (Coates et al., 2008: 92), runs through the Arctic, whether it be a “Northeast Passage” near Russia, a Northwest Passage near Canada, or an even shorter passage close to

Never much for subtlety or nuance, Moscow has begun training “troops that could be engaged in Arctic combat missions” and increased the “operational radius” of its northern submarine fleet, according to one Russian general (Boswell, 2008, June 25). Plus, Russian long-range bombers have started flying sorties again in the region after nearly two decades of post-Cold War peace.

“We’re concerned about not just Russia’s claims to the international process but Russia’s testing of Canadian airspace,” Prime Minister Stephen Harper said late last year (Reuters, 2008, Sep. 19).

In short, conditions in and above the

of such a lane would be internal Canadian waters and the United States arguing that an international passage linking the Pacific and Atlantic Oceans exists, which in effect limits Canada’s sovereign rights over such a water way. However, their common interests in a secure Arctic far outweigh these disagreements, as officials in Ottawa and Washington are starting to realize.

The key issues for Canada and its closest neighbour are how to extend Canada’s best practices in environmental control of the area and how to develop a security regime for the region that will augment and complement the UN Convention on the Law of the Sea (UNCLOS).

UNCLOS will play an important role in defining borders and boundaries in the Arctic, but like most UN regimes, UNCLOS is inherently weak. Thus, allowing it to be the final arbiter could serve Russia’s interests. Indeed, it appears that Russia plans to use the loopholes of UNCLOS to claim much of the Arctic as its own. Developing a transparent security component seems prudent in a region where maritime traffic—and resource exploration—will dramatically increase.

Article 234 of UNCLOS gives Canada the right to regulate environmental and some security standards. US vessels strictly abide by Canada’s Arctic Waters Pollution Prevention Act, which was passed in 1970 and recently updated to extend to the 200-mile EEZ of Canadian waters.

The Arctic was staked out by the Canadian government in 2006 as one of the key areas for attention in its “Canada First” defence strategy. “To protect the North, we must control the North,” Harper declared in 2008 (Boswell, 2008, Aug. 26). Toward that end, the government has pledged \$3 billion to build eight military patrol vessels with the capacity to break through up to three feet of ice; vowed to add aerial surveillance assets

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the North Pole.

Finally, a newly assertive Russia is reminding Canada, the United States, and other Arctic nations that inaction is no longer an option.

In 2001, Russia claimed almost half the Arctic Circle and all of the North Pole (Idov, 2008, Dec. 9). During a 2007 expedition, Russia planted its flag under the ice—far beyond the internationally recognized 200-mile territorial limit known as the “exclusive economic zone” (EEZ). The lead explorer provocatively declared, “The Arctic is ours” (Clover, 2008, May 27).

Russia’s outsized Arctic claims rest on a dubious interpretation of an “underwater ridge” linking to the Russian landmass (Idov, 2008). Russia argues that this ridge is an extension of its own continental shelf (Chazan, 2008). Denmark disagrees. It’s up to the UN Commission on the Limits of the Continental Shelf to settle the dispute (Maddox, 2009, Feb. 6).

Arctic warrant a more consistent policy approach based on Canada’s national interests. They also call for a review of how Canada and its closest Arctic ally, the United States, may work together on Arctic issues.

Common ground

CANADA and the United States face common challenges both in terms of ascertaining the rights to resources and in determining how to regulate secure and environmentally safe shipping in the area. This is not to diminish their dispute over mining rights to some 60 square miles of the Beaufort Sea or their divergent definitions of the Northwest Passage. The two nations disagree over the precise angle at which the land boundary between Alaska and the Yukon extends into the Beaufort Sea. They also disagree on the status of a possible sea lane through the Western Arctic archipelago, with Canada claiming that the legal status

and increase the size of Canada's Army Ranger units to 5,000; and outlined plans for a new army training centre and a deep-water port in the northern reaches of Canada (Coates et al., 2008: 174; MacAskill, 2007, Aug. 11).

However, the sharp economic downturn and the very high costs of Canada's robust commitment to fighting the Taliban in Afghanistan have already eroded Canada's ability to fulfill some of these military promises aimed at securing the north. But given Russia's actions and words, Ottawa should not sacrifice long-term security investments for short-term savings. Protecting Canadian sovereignty in the Arctic is important enough to allocate defence dollars to the effort. As before, Canada will need to partner with the United States to help defend its northern regions.

Washington seems awake to the challenge. Calling for "a more active" US presence, the recently issued US Arctic Region Policy seems to echo Ottawa's nonsense view on Arctic security. "The United States has broad and fundamental national security interests in the Arctic region and is prepared to operate either independently or in conjunction with other states to safeguard these interests," the policy states (White House, 2009).

Although the United States maintains 20,000 active-duty forces in Alaska, and has the capacity to project its military into any region, it faces its own challenges. It has only three polar icebreakers, and two of these \$800-million ships have exceeded their projected 30-year lifespan. Russia, by contrast, can deploy 20 icebreakers (O'Rourke, 2008).

Moreover, the United States faces enormous budget deficits as a result of the economic crisis and ongoing military commitments in Iraq and Afghanistan. As such, the United States would be well advised to work more closely with its friends and allies in the north.

Canada and the United States are not the only nations bracing for a cold front

in the Arctic. Norway, Sweden, and Finland are developing a Nordic security partnership as a hedge against Russian expansionism in the energy-rich "high north" (Lucas, 2008, Nov. 19). Moreover, NATO Secretary General Jaap de Hoop Scheffer recently raised the prospect of NATO involvement in the Arctic. "I would be the last one to expect military conflict," he said, "but there will be a military presence" (Associated Press, 2009, Jan. 29).

Upgrades

INDEED, conflict with Russia—in the Arctic or elsewhere—is not inevitable. Of course, neither is cooperation, as we are learning on issues as disparate as Georgia's sovereignty, Iran's nuclear program, Europe's gas supplies, and NATO's logistics arteries.

Russia's claims are different from those of other Arctic nations, both in the way the claims are being made and in the nature of the claims: other nations are not laying claim to half of the region or to the entire North Pole; other nations are not flouting the letter and spirit of UNCLOS; and other nations are not making territorial claims in a blatant military context.

Every reasonable effort should be made to include Russia as an Arctic partner. US military commanders, for instance, are pursuing routine contacts with their Russian counterparts to prevent mishaps and misunderstandings in the skies above the Arctic (Schanz, 2008, Aug. 21).

Ottawa and Washington may also want to consider upgrading the Arctic Council, a forum founded in 1996 for dialogue among Arctic countries. Similarly, the United States, Canada, Norway, and Denmark could explore a treaty with Russia to divide resource claims equitably. UNCLOS, as referenced above, is rather weak and does not preclude such a treaty.

UNCLOS itself has bipartisan backing in the US Senate and prospects for its passage look good. In its parting days, the George W. Bush administration called on the Senate to pass the treaty "promptly" (White House, 2009).

Despite the shortcomings of UNCLOS, it is important for the United States to adopt the treaty. First, it is hypocritical for Washington to expect Moscow to abide by the letter and spirit of the treaty if the United States has not ratified it. Second, being a party to the treaty is the best way for the US to ensure its voice will be heard and its Arctic interests addressed. Third, it may be useful in the future to underscore allied solidarity.

Speaking of allied solidarity, if Russia continues down its current path, Canada, the United States, and their Arctic allies will be left with few other options than standing firm and standing together. Sharing the Arctic's bounty—in a transparent manner governed by the rule of law and sound trade practices—makes more strategic sense than allowing Moscow to divide and conquer.

To prevent that unhappy outcome, the allies may need to agree among themselves on borders, transit routes, and exploration rights, and then pool their economic and military resources to protect their shared interests, as they do in other parts of the world.

The United States and Canada should lead the way by resolving their dispute over boundaries in the Beaufort Sea—splitting the difference down the middle seems reasonable—and by recognizing that cooperation on the Northwest Passage provides more benefits than costs. It seems counterintuitive, but it may be in America's strategic interests to support Canada's claim on the Northwest Passage as an inland waterway. Although some in the United States are concerned that such an arrangement could constrain America's freedom of movement and set a problematic precedent, the alternative would seem to invite a greater

risk to US and Canadian security. If the Northwest Passage is deemed to be international waters, any country could send its naval vessels through it or use it as a flight corridor.

With the Northwest Passage dispute put to rest, it seems likely that Canada would welcome American military capability in keeping threats to Canadian territory and US interests at bay.

The North American Aerospace Defense Command (NORAD) could serve

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as a model. In fact, “maritime surveillance” was added to NORAD’s list of responsibilities in 2006 (Gilmore, 2008). Just as NORAD defends Canadian and US airspace, a joint or allied naval arrangement could provide security in the Northwest Passage and other parts of the Arctic.

Whatever path Russia chooses in the Arctic, Canada and the United States would be best served by working together.

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