

# Fraser Forum

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A Fraser Institute review of public policy in Canada

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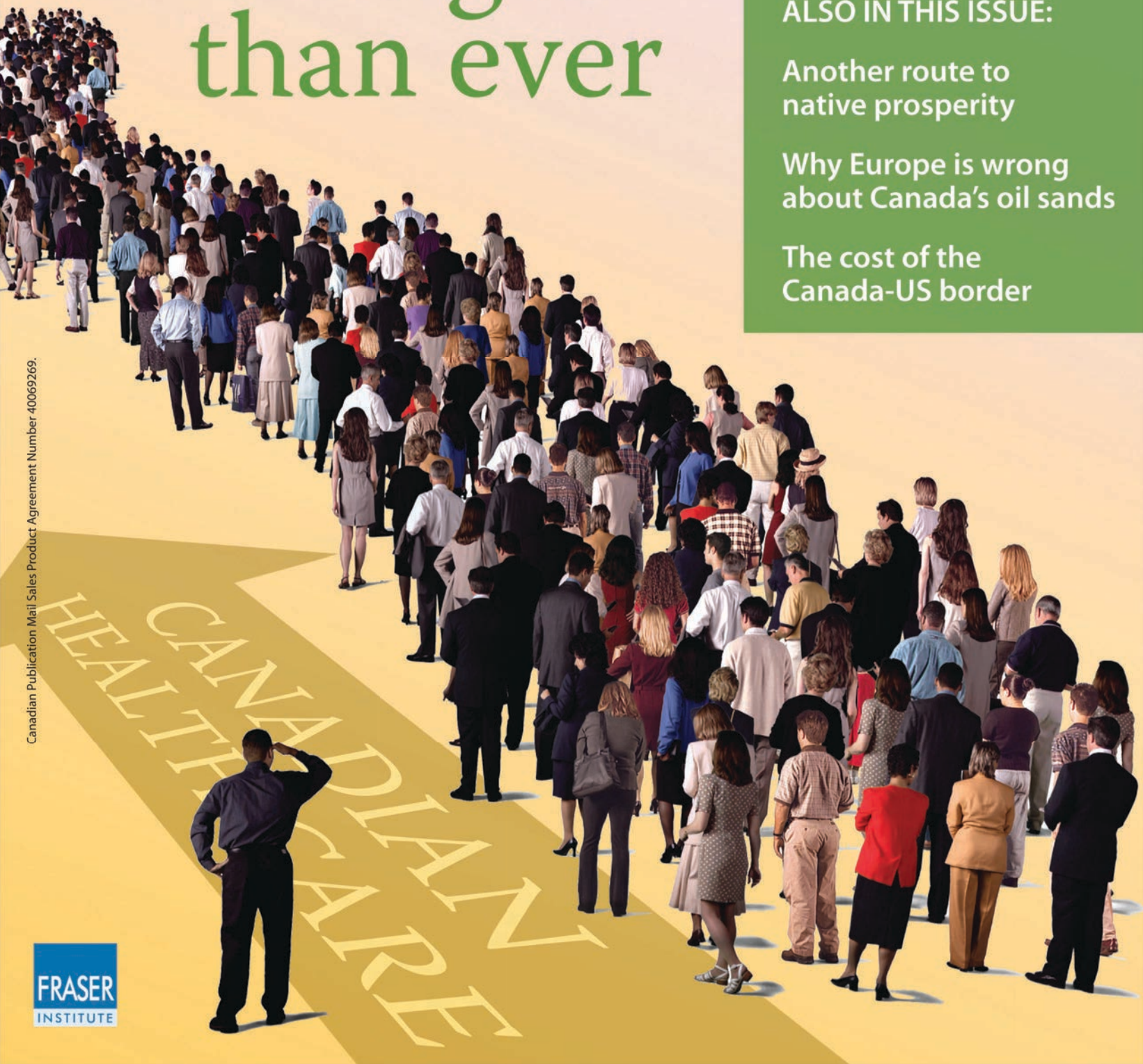
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### **Purpose, Funding, and Independence**

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Recently, there has been much discussion throughout the Western world regarding Canada as an oil exporter. In Europe, Alberta's oil sands were questioned for their possible environmental risks and in the United States, the Keystone XL pipeline from Canada has been delayed by President Barack Obama. In this issue of *Fraser Forum*, Mark Milke questions why the Europeans are not in favour of importing oil from Canada generally, and Alberta specifically (pg.10). Gerry Angevine takes us to the US and answers the question: Why isn't the oil sands bitumen refined, or partially refined, in Alberta rather than in the US? (pg.14)

Our cover story, however, is far removed from oil. In *Longer than ever—a patient's wait for health care* (pg.16), Mark Rovere and Bacchus Barua delve into the amount of time it takes for Canadian patients to receive the care they need. In their annual study *Waiting Your Turn*, they found that in 2011, patients face longer wait times than ever before in the 21 years that the Fraser Institute has been conducting this survey. Both authors ask why this is and what causes a health care system to make its consumers wait too long for specialist appointments and treatments.

In late February, the Fraser Institute will launch a new website devoted to mining information. Alana Wilson, Senior Research Analyst with the Fraser Institute's Global Centre for Mining Studies, introduces the website in *Time for facts in the mining debate?* (pg.9). Later in the issue, in *Quebec risks driving away mining investment with Bill 14* (pg.12), we get a look at what effects the new Bill could have on Quebec and on its strong mining environment for investors.

This year, *Time* magazine named "The Protester" its Person of the Year. In *Bouazizi's revolution* (pg.21), Alan Dowd suggests that *Time* should have been a little more specific and given the title to Mohammed Bouazizi for his actions, which led to the start of the Arab Spring. *The costs of the Canada-US border* (pg.24) looks at the heightened security measures that have been implemented at the Canada-US border since the 9/11 attacks. The authors discuss what monetary losses border security imposes on both consumers and business. In *How can Canadian policy makers combat black market tobacco?* (pg.28), Nachum Gabler sets up a six-point plan to reduce the amount of contraband tobacco sold in Canada.

This issue also includes two articles regarding the Federal government's deficit delay (pgs. 5 and 7); a Quarterly Research Alert (pg.32); a review of *Reckless Endangerment*, a book about the financial crisis in the US and who is truly to blame (pg.35); a column from Walter Williams on the "1%" and whether or not they deserve their fortunes (pg.31); a summary of the Addington Prize winning paper *Sovereignty, Credible Commitments, and Economic Prosperity on American Indian Reservations* (pg.19); and an article about antiquated liquor laws in British Columbia and their consequences to business (pg.34).

— Emma Tarswell

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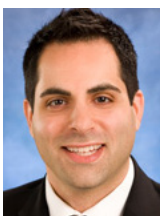
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# Cut now, not later

Niels Veldhuis, Milagros Palacios, and Charles Lammam



Bigstock

When the federal government announced in its November economic and fiscal update that it would miss its target for balancing the budget,<sup>1</sup> it confirmed something that should be obvious to all students of recent Canadian economic history: Crossed-finger revenue forecasts and unrealistic spending growth projections are no basis for sound economic policy.

Ottawa's delay in balancing its budget will result in additional government debt and a much larger bill for the next generation to pay back. So why are virtually all provincial governments poised to follow this same failed strategy?

All provinces save Saskatchewan expect to run deficits over the next several years. British Columbia and Manitoba currently have the smallest deficits among the provinces (0.4% and 0.6% of GDP). At the other end of the spectrum, Ontario has a \$16.3 billion deficit (2.6% of provincial GDP). Ontario's deficit is so large that it makes up more than 64% of the total deficits recorded by all the provinces in 2011-12, even though the province represents 38% of total Canadian GDP (Statistics Canada, 2011).

In addition to the size of their deficits, what's also important is when each province plans to eliminate them. Even for the most aggressive deficit slayers of the bunch—BC, Alberta, Quebec, and Nova Scotia—it will take another three years of red ink (see table 1).<sup>2</sup>

But here's the rub: Nearly all provinces are using optimistic revenue projections with annual growth rates ranging from 3.2% in Manitoba to 7.3% in Alberta. Ontario, where the deficit problem is most severe, is assuming very rosy revenue projections of 4.3% per year for the next seven years.

On the other side of the ledger, the provinces plan to significantly restrain their expenditures by holding the growth of program spending (total spending minus

interest costs) to between 1.4% in Ontario and 1.9% in Quebec.

Given the recent spending history of many provincial governments<sup>3</sup> (even before the 2008 downturn) and the fiscal pressures put on various programs from an aging population, it is unlikely that the provinces will be able to keep spending to these rates over the medium term.

Consider that in the five years before the recession (2003-04 to 2008-09) Quebec increased program spending at an average rate of 4.9%, the lowest average among all provinces. The biggest spender, Alberta, increased program spending at an annual rate of 11.2%. The balanced budget plans of all provinces are currently built on promises to restrain program spending growth to under 2.0% (Canada, Department of Finance, 2011a; Provincial Budgets, 2011). That hardly seems likely.

Combine optimistic revenue projections and unrealistically low rates of program spending growth, and you get balanced budget plans that contain substantial risks—especially in light of the following scenarios.

First, revenues may not materialize as expected due to slower economic growth. Lower than fore-

**Table 1: Growth rates in revenues and spending for deficit provinces (percent)**

Provinces	Revenues	Program Spending	Number of Years to Balance
British Columbia	3.4	1.5	3
Alberta	7.3	1.5	3
Manitoba	3.2	1.8	4
Ontario	4.3	1.4	7
Quebec	4.9	1.9	3
New Brunswick*	n/a	n/a	4
Nova Scotia	0.5	1.8	3
Prince Edward Island*	n/a	n/a	4
Newfoundland & Labrador	0.4	1.8	4

\*Note: The averages presented were calculated over the period required in each province to achieve a balanced budget. NB and PEI did not provide sufficient information in their 2011-12 budgets to allow for the required calculations for inclusion.

Source: Provincial budgets, 2011; calculations by authors.



casted commodity prices would especially hurt provinces that depend on natural resource royalties. For instance, Alberta is expecting average revenue growth of 7.3% over the next three years (Alberta, Department of Finance and Enterprise, 2011). That might be attainable if commodity prices remain strong, but a minor dip in revenue expectations would delay the balanced budget plan.

Second, program spending may increase faster than anticipated for a number of reasons such as natural disasters, political pressure, and higher entitlement spending.

Finally, interest costs may also turn out to be higher than expected, putting upward pressure on government spending.

By relying on strong future revenue growth, most provincial governments are dealing with their fiscal problems using a passive approach. If the economic outlook worsens, and the provinces like the federal government miss their balanced budget targets, Canada will be left with larger deficits for a much longer period and significantly more government debt—both of which are drags on the economy.

Total provincial debt is already expected to reach \$487 billion this year (Gulati and Burleton, 2011). Add this to the federal debt that's currently at \$586 billion and Canadians are leaving over a trillion dollars (\$111,000 per Canadian family) in debt for the next generation to pay (Canada, Department of Finance, 2011; calculations by authors). With the federal government and nearly all provinces expecting deficits into the foreseeable future, the total level of debt will increase significantly.

Politicians from all political parties need to realize the seriousness of the inherent risks in their fiscal plans. Rather than rely on the failed policies of the past, of trying to slow spending growth while hoping revenues rebound sufficiently, provincial governments should be proactive and enact immediate program spending reductions and reforms.

## Notes

1 Canada, Department of Finance, 2011b.

2 The number of years to balance the budget runs from 2011/12 to the year of balance. Saskatchewan was in a surplus position in 2011/12 and is excluded from the analysis. New Brunswick and Prince Edward Island were excluded from the analysis as their 2011 budgets lacked the information required for the calculations.

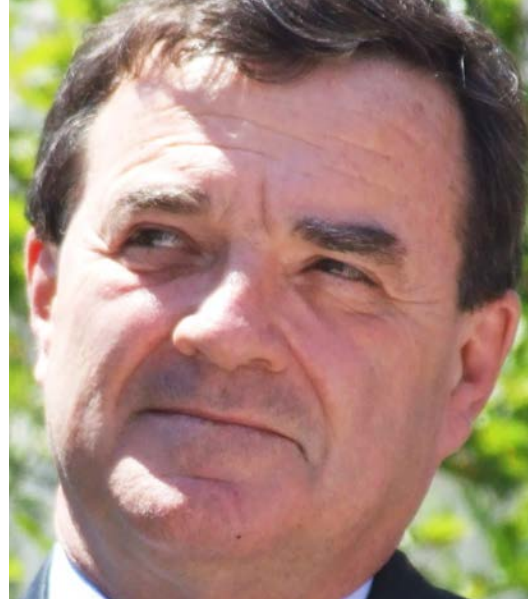
3 See Veldhuis et al. (2011) for an overview of this history.

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# Federal government's deficit delay no surprise

Niels Veldhuis, Charles Lamman, and Milagros Palacios



Joshua Sherurcij

In November, the federal government updated its economic and fiscal plan that it first released in June of 2011. With that update, the federal Conservatives finally confirmed they will not meet their 2015/16 target for balancing the budget.<sup>1</sup> The announcement was no surprise. For nearly two years, Fraser Institute economists have repeatedly pointed out that the government's plan to balance the budget was fraught with risk.<sup>2</sup>

To balance the budget by 2015/16, the Conservatives were hoping for robust revenue growth averaging 5.6% per year, while planning to hold increases in program spending to an average rate of 2.0% (Canada, Department of Finance, 2011b). Given these optimistic revenue projections and the Conservative government's history of excessive spending, our point was simple: their plan was extremely risky.<sup>3</sup>

The Conservative government should have drawn from Canada's history on how not to construct a balanced budget plan.<sup>4</sup> Consider the Progressive Conservative government of the 1980s and early 1990s. During that period, the Progressive Conservatives failed to eliminate the federal deficit because they were unable to restrain spending growth and because revenues ended up being lower than expected. That combination resulted in ongoing deficits, mounting debt, and a serious fiscal crisis in the mid-1990s (Veldhuis et al., 2011).

The economic and fiscal update of November 2011 shows that the incumbent Conservatives could be repeating the same mistakes as their predecessors. In its update, the Conservative government downgraded its inflation-adjusted projections of economic growth for Canada and pushed its target for balancing the budget to 2016/17, a year later than projected in the June budget. Private-sector forecasters, upon whom the government relies, now believe that the Canadian economy will grow at 2.2% in 2011 and 2.1% in 2012, rather than the more optimistic 2.9% and 2.8% used to generate the government's June budget. Over the next five years, projected average economic growth has been reduced to 2.4% from 2.7%. As a result, revenues are projected to be about \$53 billion lower over the next five years<sup>5</sup> and the government is now estimating that a balanced budget will not come until 2016/17—or 2015/16, if it hits its

targeted savings (see figure 1).<sup>6</sup> With lower-than-expected revenues, Canadians can expect larger deficits for a longer time period and higher levels of government debt—both of which are significant drags on the economy.<sup>7</sup>

In the June budget, the Conservatives projected an increase in the federal debt to \$610 billion by 2015/16 from \$533 billion in 2010/11, an increase of \$57 billion in five years (Canada, Department of Finance, 2011b). Just months later, the government's updated projections now expect the debt to reach \$641 billion by 2015/16. Consider what would happen if the global economic outlook were to worsen.

But the government's plan does not account for that. Instead, it continues to base its strategy for achieving a balanced budget on robust revenue growth of 4.6% over the next five years while planning for program spending growth of 2.2%. In other words, there is still significant risk in the Conservatives' fiscal plan.

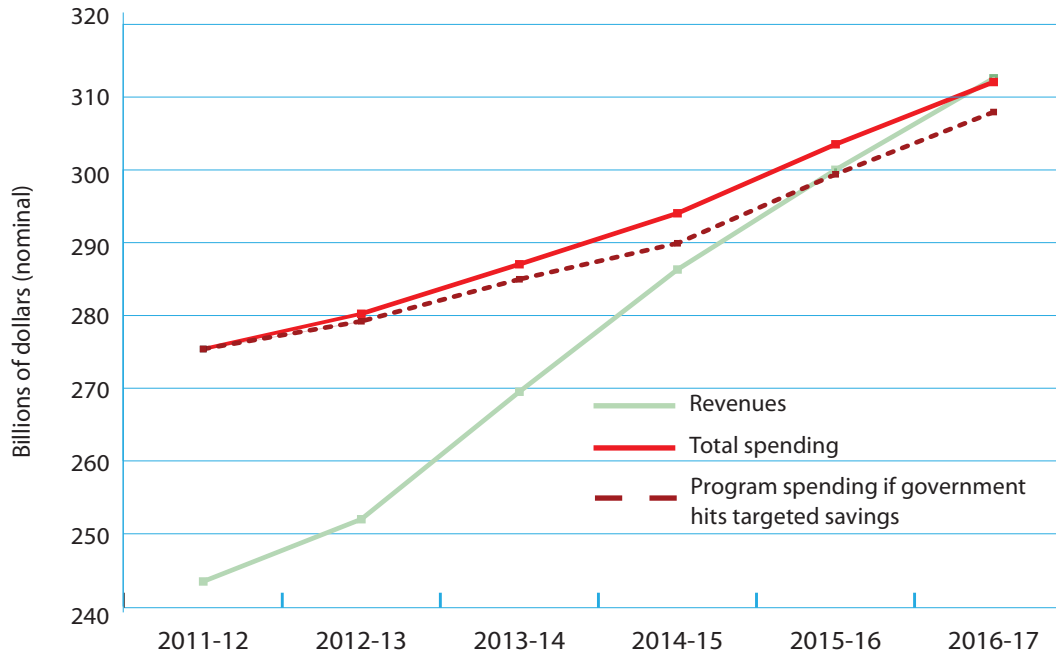
To mitigate the risk, the Conservatives should table an austerity budget in 2012—one that reduces rather than increases program spending and delivers a balanced budget in two years instead of five.

The first step: ensure that program spending is returned to pre-stimulus levels by expanding the government's Strategic and Operating Review. Currently, this review is a one-year evaluation of program spending—excluding transfers to individuals and governments—that proposes to find only \$11 billion in savings from the \$473 billion in departmental spending planned from 2012/13 to 2015/16. An expanded Strategic and Operating Review should prioritize spending so that important areas are spared deep cuts while lower-priority areas carry a greater burden of the spending reductions. For example, the Conservatives could reduce or eliminate subsidies to the Canadian Broadcast Corporation (CBC), axe the Canada Health Infoway,<sup>8</sup> eliminate regional development spending, reform public-sector compensation, and reduce and reform transfers to provincial governments.<sup>9</sup>

A plan for a balanced budget by 2013/14 would substantially reduce the risks of another round of down graded economic projections and leave the Conservatives in a



**Figure 1: The federal government's fiscal plan revenues and spending, 2011/12 to 2016/17**



Note: Spending is the sum of program spending and debt charges.  
Source: Canada, Department of Finance (2011a)

position to implement a much-needed multi-year plan to reduce taxes if revenues do in fact rebound robustly.

## Notes

1 The balanced budget target was originally intended for 2015/16, or 2014/15 if the Conservatives achieved their targeted savings through the Strategic and Operating Review (a one-year review of program spending excluding transfers to individuals and governments). Unless otherwise noted, the data cited in this article are sourced from Canada, Department of Finance (2011a).

2 For example, see Veldhuis and Lammam (2011).

3 The revenue projections in the government's June 2011 budget are optimistic given the present uncertainty in the global economy. With fiscal and economic problems in the United States and Europe, strong revenue growth in Canada may not materialize. Canada is a relatively small economy whose health depends on the strength of others, so if the situations in those larger economic regions worsen, the Canadian economy and government revenues will be at risk. There is additional risk on the spending side. While the government's planned annual program spending growth of 2.0% over five years appears modest, such a target is unlikely given the Conservative government's historical record. Since coming into power in 2006, the Conservatives have increased program spending at an average rate of 6.7%—5.9% over the period before the recession (2006/07 to 2008/09). That is roughly three times the planned rate of growth in the June 2011 budget.

4 See Veldhuis et al. (2011) for an overview of this history.

5 In general, a growing economy characterized by more investment, increased job creation, and higher incomes for workers eventually leads to more government revenue of all types, including personal income tax, GST, and corporate income tax revenues. If the pace of economic growth slows, then revenues will decline.

6 If the Conservatives hit the targets they outlined for spending savings which total \$11 billion over five years, the budget will be balanced in 2015/16 instead of 2016/17.

7 For evidence on the deleterious economic effects of debt accumulation, see Reinhart and Rogoff (2010) and Kumar and Woo (2010).

8 Canada Health Infoway is a federally funded organization tasked with accelerating the development of electronic health records across the country.

9 For more details, see the *Financial Post's* most recent Chopping Block series at <http://opinion.financialpost.com/tag/chopping-block/>.

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# Time for facts in the mining debate?

## Global Centre for Mining Studies to launch mining facts website

Environment

Communities

Economy

**Alana Wilson**

**M**ost Canadians rely on mined metals and minerals every day, often without realizing it. Our food systems depend on mined nutrients; we rely on the minerals in our cell phones and computers to stay connected with one another; and our energy needs are met with hydro, solar, and gas which all use minerals and metals to generate and transmit energy.

The Canadian economy also benefits from mining: 308,000 workers are employed directly in this industry (2% of the labor force) (Canada, Natural Resources, 2011). In 2009, mining and metal processing contributed \$32 billion to Canada's GDP (2.7%) and this sector is expected to remain an important contributor to Canada's economic growth (Canada, Natural Resources 2009).

Canadian mining is also important internationally. According to the Mining Association of Canada, in 2010 there were 1,000 exploration companies active in over 100 countries with more than 4,300 mining projects at various stages of development (The Mining Association of Canada, 2010). Canadian firms also contribute to government revenues through taxes and royalties. Yet despite its significance, the mining industry is poorly understood and debates on its local and global effects are increasingly polarized.

Anti-mining sentiments are growing and are often centred around allegations of environmental damage, community opposition, and increased social conflict over land and water resources. Miners, like everyone else, have a clear responsibility to avoid damage to others or provide compensation when it occurs. Mining, like other activities, has not had a perfect track record. But, paradoxically, such claims are growing even as the industry has increased community engagement, improved environmental protection

and restoration, and extended the economic and social benefits of operations to host communities. For example, many mining companies voluntarily provide communities with infrastructure (electricity, potable water, schools, improved roads), training, and health care as part of their Corporate Social Responsibility programs.

The complexity of the mining industry requires careful analysis that objectively considers the impacts and benefits from different perspectives. Unfortunately, the debate over such issues is often simplistic, biased, or does not reflect current mining practices.

The Fraser Institute's Global Centre for Mining Studies has launched a new project to address this information vacuum. It aims to provide balanced consideration of both the benefits and challenges mining brings. It will explore the issues and debate surrounding the activities of Canadian mining companies in Canada and abroad. It will present information for a general audience and will act as a resource for those communities, citizens, and media who have questions about the impact of mining activity. Its website, [www.miningfacts.org](http://www.miningfacts.org), is scheduled to launch in late February 2012.

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# Why Europe is wrong about Canada's oil sands

Mark Milke



Forest reclamation is lowering the impact on the landscape in oil sands areas.

Bigstock

The European Commission was wrong when, this past autumn, it singled out oil extracted from Canada's "tar sands" by proposing a higher carbon-emissions value for it than for other sources of fossil fuel. On the actual proposed action, the directive would rank oil sands crude as having a greenhouse gas (GHG) value of 107 grams of carbon per megajoule. That would be higher than the measurement applied to conventional oil entering Europe which has an 87.5-gram impact value applied (Penty, 2011: E1).

Given that very little Canadian oil currently makes its way to Europe, labelling it as "dirty" could be largely symbolic.

But such a designation does matter: it would muddy the issues that now surround extraction of Canadian oil and inflame trade tensions. It could also, in the longer term, lead to more imports to Europe from countries that are not paragons of civil, political, and economic rights. But first, some background that, while not the basis for the Commission's proposal, has been detrimental to the debate.

For one, the oft-used term "tar sands" is incorrect. Tar originates from distilling coal (Merriam-Webster, 2011). Canada's oil comes from clay sand, through two processes that are cleaner than distilling coal. In the traditional method, oil is extracted through mining which temporarily scars the landscape. The oil is then separated from the sand using heat. This approach, however, is in decline and only 20% of recoverable oil lies close enough to the surface to be mined. The rest is "steamed" out of the ground through a process that resembles conventional oil drilling, and that method is on the rise (IHS-CERA, 2010a: 2). The impact of oil sands on Canada's landscape is therefore falling.

The proposed European Union action, though, is based on greenhouse-gas emissions. According to a study by IHS Cambridge Energy Research (IHS-CERA), oil derived from sand emits as much GHG emissions as Nigerian or Venezuelan crude oil, but only 6% more than the average crude oil consumed in the United States (IHS-CERA, 2010a: 8).

As IHS-CERA points out, other studies that calculate the gap in GHG emissions between oil sands crudes and other sources of oil have found higher emissions. This is

because the other studies only compare GHG emissions for part of the life cycle rather than the total and more comprehensive "well-to-wheels" emissions calculated by IHS-CERA (IHS-CERA, 2010a, 10-12). This is an important difference if one is to make apple-to-apple comparisons. ("Well-to-wheels" calculations account for environmental impacts associated with all the stages of a product's life from extraction through to processing, manufacturing, distribution, and use.)

For example, while oil produced in Saudi Arabia has fewer GHG emissions than that produced from heavy oil sands in Canada's north, one must take into account that the emissions expelled from transporting Saudi oil to market by tankers adds to the overall GHG emissions. This needs to be considered and added to a well-to-wheels analysis of Saudi oil's GHGs, which brings it closer to the GHG emissions produced by Canada's oil sands, i.e., the 6% gap (IHS-CERA, 2010a: 9).

Also, this overall 6% difference is rendered less significant still by a point that the European Commission misses: most emissions come not during extraction but during usage. As IHS-CERA points out, 70% to 80% of the greenhouse-gas emissions come from the combustion of the fuel in an engine, thus, "the combustion emissions do not vary with the origin of the crude" and the vast majority of emissions remain the same whether the oil comes from Africa, Latin America, or Canada (IHS-CERA, 2010a: 7).

Set against these differences in emissions are three considerations on energy that should also be considered before any country, or the European Commission, decides to try and discourage Canadian oil sands oil: demand, security, and human rights.

Global demand for oil will rise from 89.2 million barrels per day now to 99 million barrels in 2035, according to the International Energy Agency (IEA, 2010: 1-2). The IEA also predicts that unconventional oil—such as Canada's oil sands—will play "an increasingly important role in world oil supply through to 2035, regardless of what governments do to curb demand" (IEA, 2010: 2).

For Europe, the question then is not whether the world will use more oil, but where it will come from. Oil's origin should matter for Europeans who care about their

own security and about others' human rights. Canada, unlike most oil-exporting countries, is politically stable and has a superb human-rights record—unlike, say, Iran, Saudi Arabia, or Venezuela.

For example, in Freedom House's annual survey of the situation around the world, the *Freedom in the World 2011 survey*, contains reports on 194 countries and 14 related and disputed territories (Freedom House, 2011). Each jurisdiction was listed as Free, Partly Free, or Not Free. The designation is determined by the combination of political rights and civil liberties. I matched the Freedom House's results with the world's top 15 oil-exporting countries (US Energy Administration, 2011), and the results are as follows: 10 of the world's top 15 oil-exporting countries are considered "not free," three are considered "partly free," while only two—Norway and Canada—are considered "free."

Given the IEA's point about increasing demand for oil over the next few decades, if the oil isn't produced and exported by Canada (or if roadblocks are thrown up in front of at least some Canadian exports), it's clear that the oil for Europe, the United States, and east Asia will come from countries with a less-than-stellar human rights record. The demand makes that obvious.

However, since European industry faces obligations to reduce its carbon footprint, rather than its human-rights footprint, the Commission's proposal will encourage Europe to focus on greenhouse gases at the expense of

other important measurements such as civil, political, and economic freedoms.

Lastly, the Commission's directive is not worth a trade clash with one of Europe's trade partners. Canada's prime minister, Stephen Harper, and his government have hinted quite clearly that Canada may complain to the World Trade Organization if Canadian oil sands are labelled "dirty," arguing that the designation is protectionism under another guise (Fekete, 2011). Even if the dispute does not deteriorate to that level, an EU directive that discriminates against Canada's oil would add a complication to talks on a comprehensive EU-Canada free-trade agreement, now being negotiated.

Stated bluntly, the EU's directive would send this unfortunate signal: human-rights issues and progress in open trade matter less than marginal differences in greenhouse-gas emissions.

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**Figure 1: Top 15 net\* oil exporting countries and freedom ranking**

Top 15 Countries	Thousand Barrels Per Day	Freedom Ranking
Saudi Arabia	7,614	Not Free
Russia	7,012	Not Free
Iran	2,506	Not Free
United Arab Emirates	2,217	Not Free
Norway	2,125	Free
Kuwait	2,124	Partly Free
Nigeria	1,939	Partly Free
Angola	1,874	Not Free
Venezuela	1,778	Partly Free
Algeria	1,773	Not Free
Iraq	1,764	Not Free
Libya	1,525	Not Free
Kazakhstan	1,299	Not Free
Canada	1,158	Free
Qatar	1,055	Not Free

\*Net: i.e., after a country's oil imports have been subtracted from its oil exports.

Sources: Freedom House (2011) and US Energy Information Administration (2011), based on 2009 data.

# Quebec risks driving away mining investment with Bill 14

Jean-Francois Minardi

Until recently, mining executives around the world saw Quebec as having the best policy environment for mining investment (McMahon and Cervantes, 2010). This is mainly thanks to a predictable regulatory environment, the absence of territorial claims in Northern Quebec, high quality geo-scientific data easily accessible to miners, good infrastructure, a skilled workforce, and an attractive mining tax system (McMahon and Cervantes, 2011). But with the introduction of Bill 14, tabled on May 12, 2011 to amend Quebec's Mining Act, the province is now poised to introduce a high level of uncertainty that may scare investors away and seriously damage the policy attractiveness of Quebec to mining investors.

Bill 14 gives additional power to municipalities to control mining activities in their territories. But giving municipalities control over where and how mining can take place sidelines the provincial government as the sole mining regulator and runs the risk of erecting multiple barriers to mining investment, investment that creates well-paying jobs in many Quebec communities. The mineral sector represents 2.4% of Quebec's GDP and more than 52,000 jobs (including 36,000 direct jobs and 16,000—full-time equivalent—in the Quebec supplier network). The annual net tax revenue totaled \$281 million on average since 2000 for the government of Quebec and the value of exports of the mineral sector grew on average by 8.2% since 2000 to reach \$8 billion in 2008 (AMQ and AEMQ, 2010: 3).

To date, provincial management of the mining sector has been characterized by certainty regarding the rules of the game: a transparent process, timeliness, and predictability, which played a big part in the attractiveness of the province for global investors. It's why Quebec was ranked as the top jurisdiction for mining investment by the Fraser Institute's annual *Survey of Mining Companies* from 2008 through 2010.



Under Bill 14, more than 1,000 municipalities, most of which lack the necessary experience, expertise, and knowledge to do so, will be able to implement different rules for different companies in their respective jurisdictions.

For example, Article 91 in Bill 14 states that, contrary to the current situation, any areas within an urban perimeter and any area dedicated to vacationing is withdrawn from staking, map designation, mining exploration, and mining operations. Article 91 also states that, in order to work on these sites, the holders of claims in areas that have been so withdrawn must obtain the consent of the local municipality concerned. However, no compensation is paid by any level of government for the consequences of the new rule.

This means mining claim holders who have already invested millions of dollars in exploration in a parcel of Crown mineral land may retroactively lose, without compensation, their legally acquired right to explore and develop minerals.

Future decisions regarding mining development in municipalities will run the risk of being politicized because of a municipality's power to veto mining exploration and development and because changing administrations may have different opinions regarding the same mining project. Moreover, with Bill 14 both levels of government (the provincial and the municipal) will have the power to change mining policy.



Courtesy of IAMGOLD Corp.

Miners understand that they have to follow sensible regulations and pay taxes. However, they are alarmed when they face uncertainty over their claims. Mining is a highly cyclical and capital-intensive industry, with a long lead time between initial investment and commercial production. Many exploration companies do not have production revenue and, therefore, must rely on investors who are prepared to support high-risk activities.

Bill 14 is reminiscent of British Columbia's experience in the 1990s where mining declined in the province and its share of Canadian mineral exploration fell to 5.7% in 2001 from 29.2% in 1990 (Association for Mineral Exploration British Columbia, 2009). This was mainly due to the BC government's 1995 decision to halt the Windy Craggy mining project in order to create a park on the site (Webster, 1999). This effectively expropriated the company's considerable investment and created a great cloud of uncertainty over mining policy in BC which left miners afraid to invest, lest their property be, in effect, stolen from them by the government.

Public policy actions can either stimulate or hinder mineral investment. With Bill 14, Quebec's Liberal government sends a conflicting message to investors. It gives the impression that it is actively trying to attract global mining investments in the north (where there is little habitation) of the province for the Plan Nord while discouraging them in the south (where population is more concentrated) to ap-

pease a public opinion increasingly hostile to the exploitation of mineral resources in their backyard. This is a risky strategy that may lead global investors to opt for other jurisdictions and damage Quebec's ability to attract investment.

At the time of publication Bill 14 is still in the committee stage.

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# Subsidization of bitumen upgrading is unwarranted

Gerry Angevine

The construction of the TransCanada Corporation Keystone XL crude oil pipeline, which will increase the capacity to transport raw and upgraded bitumen<sup>1</sup> from Alberta's oil sands to American refining centres, has been opposed by both Canadian and American environmentalists. Some readers may wonder why Canada is allowing the export of unrefined oil at all. Since the oil upgrading and refining process requires capital and labour, and therefore generates employment, income, and other economic benefits, some Canadians believe that we should be upgrading and refining the bitumen right here at home. However, the Alberta government's intent to ensure that a minimum proportion of the raw bitumen produced is upgraded before it's shipped from the province makes no economic sense.

Environmentalists and landowners apparently see no difference in the kinds of oil that pipelines transport from the oil sands. Environmentalists see the oil sands as an unclean and environmentally unfriendly source of oil and, therefore, fundamentally object to any further development of the resource. For the sake of convenience, they are largely ignoring the fact that technological advances are making it possible to mitigate the environmental impacts of bitumen recovery. Their position would be the same even if all the bitumen being sent south were first refined. This also applies to landowners concerned with the impacts of oil spills. In their eyes, any pipelines carrying any form of oil—conventional crude oil, bitumen, upgraded bitumen, or refined petroleum—are grounds for concern.

Others have a quite different view. For example, at their October 31, 2010 annual general meeting, members of the Alberta Progressive Conservative party approved a motion calling on the government to use incentives or legislation to ensure that at least 65% of the bitumen that is produced from the oil sands is upgraded in Alberta (Alberta Progressive Conservative Party AGM Motions, 2010). Party members failed or chose not to recognize that funds for special incentives must come from somewhere. They also don't seem to understand that extracting money from taxpayers to support projects that are not commercially viable generally results in a misallocation of resources. More fundamentally, robbing Martha and Henry down on the farm to permit Alberta Premier, Alison Redford, and Energy Minister, Ted Morton, to provide incentives to reluctant investors is a violation of property rights since Martha and Henry have no say in the matter (at least until the next provincial election when the deal has already been made) and no guarantee of compensation.

All of the bitumen that is being recovered by surface mining combined with heating processes to sepa-

rate it from the sand and rock it is embedded in is currently being upgraded to refinery-ready synthetic crude oil (SCO). But only about 11% of the bitumen that is being recovered using so-called "in situ" (i.e. "in place") technologies that involve drilling wells and injecting steam (or other techniques) is being upgraded. According to the Energy Resources Conservation Board (ERCB) approximately 149.4 thousand cubic metres per day, or about 58% of the 256.3 thousand cubic metres per day of bitumen produced in 2010 were upgraded. That resulted in the production of 126.4 thousand cubic metres per day of SCO (ERCB, 2011).<sup>2</sup>

Based on its assessment of current and expected capital investment in new and expanded oil sands production facilities, the ERCB forecasts that bitumen production will more than double from 2010 to 2020, to reach almost 550 thousand cubic metres per day. The ERCB, however, anticipates that only about half of that production will be upgraded, yielding about 223 thousand cubic metres of SCO per day in 2020 (ERCB, 2011). This would only be about 77% greater than the SCO produced in 2010 in spite of the fact that bitumen production is projected to increase by 214% (ERCB, 2011). One reason to expect that a smaller share of bitumen production will be upgraded in the future is that "in situ" recovery is anticipated to soon surpass surface mining as the more important source of bitumen supply and that, for many "in situ" producers, production volumes are too small to justify capital expenditures for upgrading facilities sufficiently large enough to achieve the necessary economies of scale.

To help ensure that more bitumen is upgraded in the province, the Alberta government has contracted with a new company to upgrade bitumen received under its bitumen royalty-in-kind program. According to the terms of a 30-year agreement between the Alberta Petroleum Marketing Commission (APMC) and North West Redwater Partnership (a general partnership between Northwest Upgrading Incorporated and Canadian Natural Upgrading Limited that is constructing a 150,000 barrel per day upgrader/refinery near Edmonton for start-up by 2014), the government, through APMC, will supply the North West Redwater Partnership with three-quarters of the upgrader's feedstock requirements from Crown royalty bitumen.<sup>3</sup> The government will also pay the Partnership a processing fee to upgrade and refine that bitumen, in effect paying three-quarters of the facility's operating costs including debt servicing charges (Alberta Government, 2011; Penty and Cryderman, 2011). In addition, the government has contracted with the Partnership to market royalty bitumen volumes that are supplied in excess of amounts that are to be processed.





Suncor Energy Inc.

It is likely that the Northwest upgrader/refinery would not be built without the government's long-term commitment to supply it with Crown royalty bitumen and pay three-quarters of the operating costs.<sup>4</sup> Although it is possible that the processing fee and other costs may be more than offset by the increased value of the refined bitumen products relative to that of raw bitumen, what amounts to a subsidy clearly puts taxpayers rather than the project owners (e.g. the investors) at risk.

Bitumen production is projected to increase substantially well beyond the 2020 end point of the ERCB's latest projection. In fact, a recent Canadian Energy Research Institute (CERI) study indicates that bitumen production could be three times greater in 2040 than in 2010 (Millington and Mei, 2011). There will, therefore, be no shortage of bitumen to upgrade.

If investors chose to invest in Alberta upgraders, there is no doubt that the provincial economy would get a boost from spending on goods and services during the construction phases and from employment required to operate and maintain the facilities once they are built. However, according to the CERI study, the capital cost of a stand-alone upgrader capable of producing 100,000 barrels of SCO per day is approximately \$5.1 billion in constant 2010 dollars. For this reason, ensuring that 65% of the bitumen that is produced is upgraded in Alberta could be very costly. If private investors are not prepared to take this risk, it suggests that it is more economical to upgrade and refine much of the bitumen closer to where the refined petroleum products will be consumed.

What members of the Alberta legislature and others who argue for the subsidization of upgraders fail to appreciate is the loss that the provincial economy would have to bear as a consequence, since the taxpayers, who would have to pay for the subsidies, would have less money to spend on goods and services. Worse, if upgraders are not feasible and require government support to be built, more productive investment could be crowded out.

If bitumen producers determine that it makes more economic sense to build upgraders in Illinois, or some other state, than in Alberta there must be good reasons for their decisions. These could include factors such as the availability of skilled workers, lower wages, lower

materials costs, lower state and local taxes, economies of scale, the regulatory climate, or other factors.

The Redford government should be aware that government stimulus via spending is generally not as effective as tax cuts targeted at facilitating private investors to increase investment as market opportunities arise (Alesina and Ardagna, 2009). If the government is really concerned that not enough investment in bitumen upgrading and refining is occurring in Alberta it would be well advised to investigate the reasons and strive to improve the province's competitiveness, rather than attempting to force uneconomic investment. In particular, the Redford government should examine whether it would make a difference if they were to remove or lower non-market barriers, such as regulatory processes and procedures that are unnecessarily time consuming and costly.

## Notes

1 In the context of this article, bitumen is crude oil that is embedded in the Alberta oil sands deposits along with sand and other materials.

2 A barrel of bitumen generally yielded approximately 0.846 barrels of SCO in 2010. In future, the average yield will depend on the technologies that are employed. If the coking technologies that are predominant today continue to prevail the yield is likely to remain about the same.

3 The Alberta Petroleum Marketing Commission is an organization within the Alberta Department of Energy that takes delivery of the province's share of the royalty on oil that is produced and sells it at market prices. The members of the North West Redwater Partnership are private companies.

4 Crown royalty bitumen is the provincial government's royalty share of the bitumen that is produced.

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# Longer than ever

## *A patient's wait for health care in Canada*

**Bacchus Barua and Mark Rovere**

Over the last couple of decades, wait times in Canada have become so political that nearly all of the provinces have established their own wait time's strategies.<sup>1</sup> While it is encouraging that provincial governments are attempting to reduce the amount of time that patients must wait, new research indicates that Canadians are waiting longer than ever to access to medically necessary treatment.

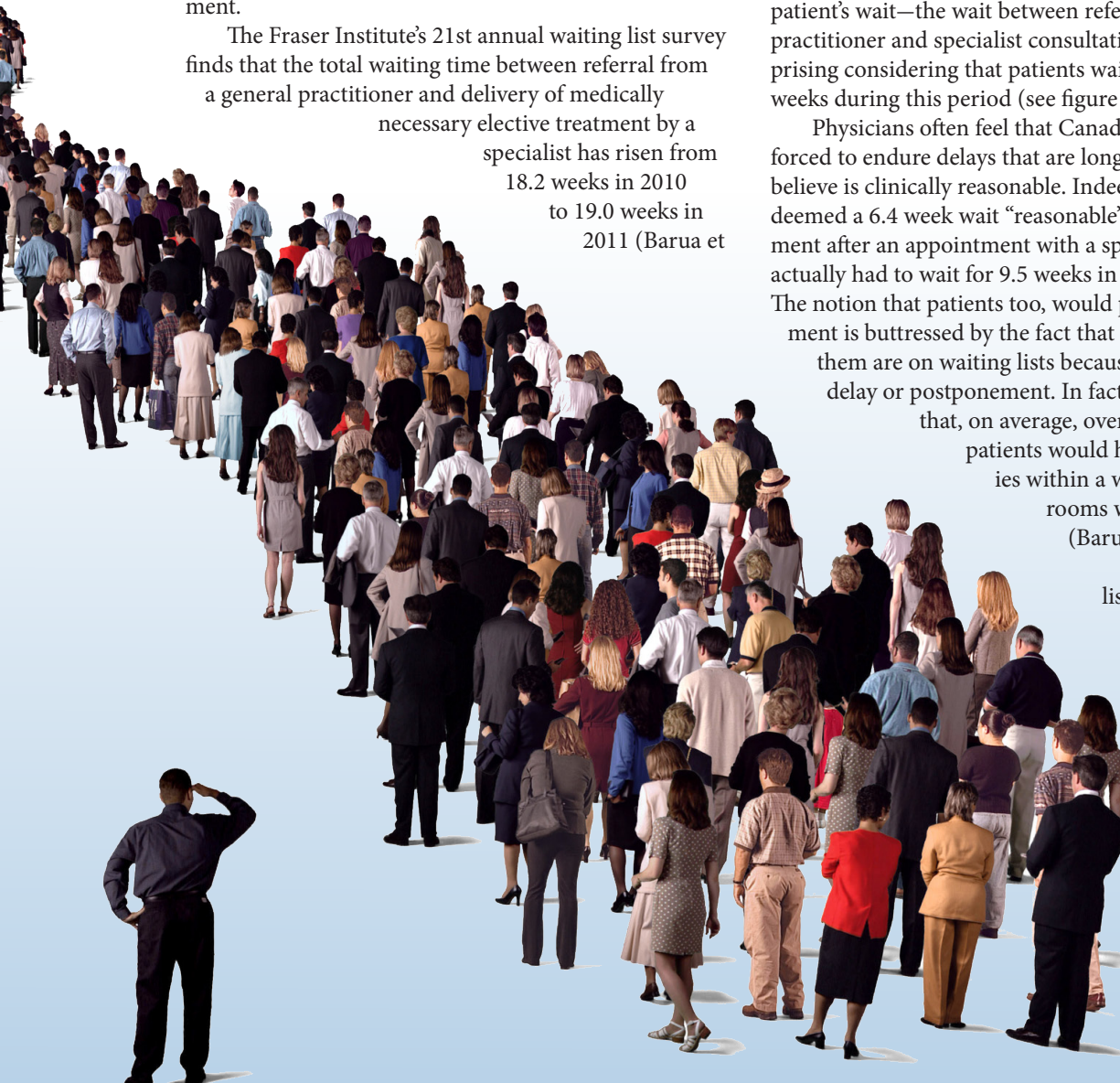
The Fraser Institute's 21st annual waiting list survey finds that the total waiting time between referral from a general practitioner and delivery of medically necessary elective treatment by a specialist has risen from 18.2 weeks in 2010 to 19.0 weeks in 2011 (Barua et

al., 2011). At 104 percent longer than it was in 1993 (9.3 weeks; Miyake and Walker, 1993), this is the longest total wait time recorded since the Fraser Institute began measuring wait times in Canada.

While provincial governments have set up various websites to record the wait between specialist consultations and treatment, the majority of these provinces overlook (or do not report) the first portion of a patient's wait—the wait between referral from a general practitioner and specialist consultation. This is surprising considering that patients wait an estimated 9.5 weeks during this period (see figure 1).

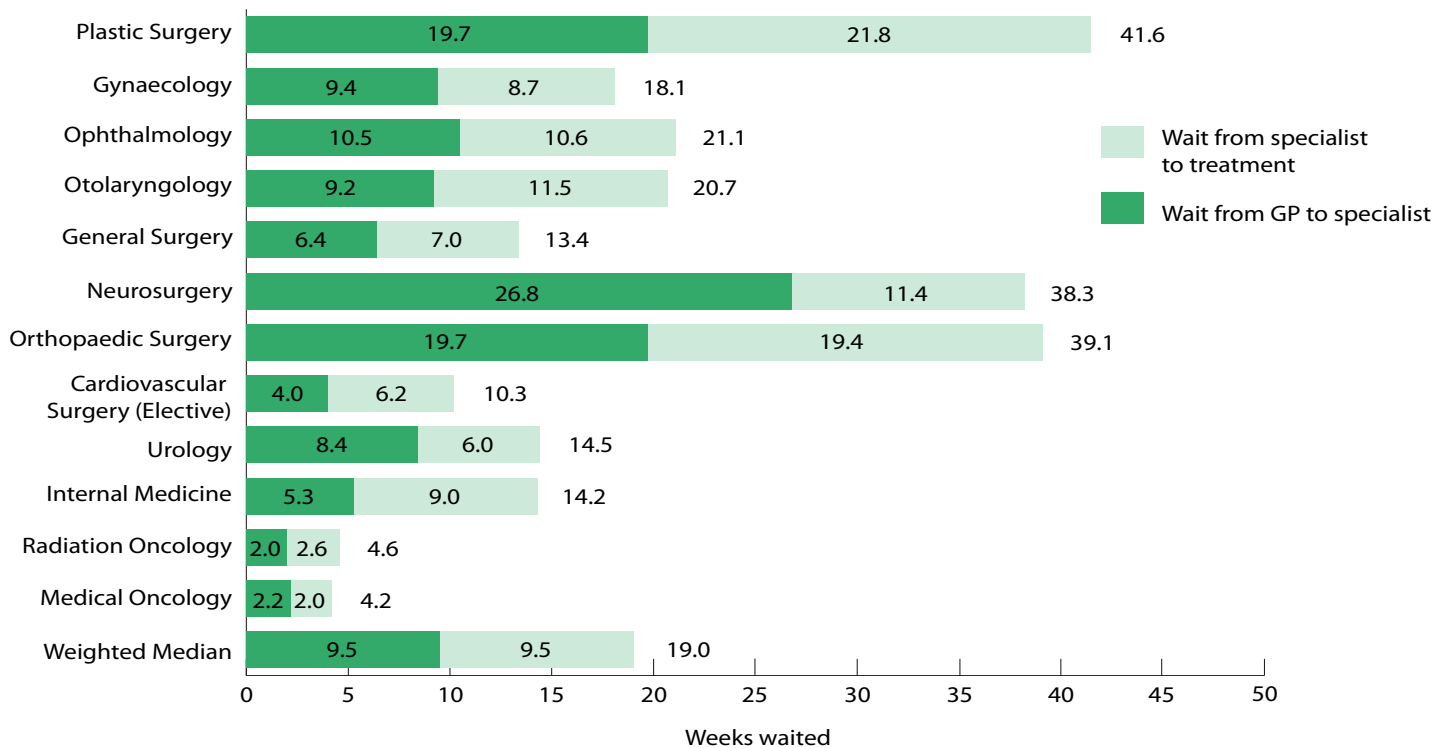
Physicians often feel that Canadians are routinely forced to endure delays that are longer than what they believe is clinically reasonable. Indeed, while they deemed a 6.4 week wait "reasonable" for elective treatment after an appointment with a specialist, patients actually had to wait for 9.5 weeks in 2011 (see figure 2). The notion that patients too, would prefer earlier treatment is buttressed by the fact that only about 9.4% of them are on waiting lists because they requested a delay or postponement. In fact, physicians believe that, on average, over half (52.8%) of patients would have their surgeries within a week if operating rooms were available (Barua et al., 2011).

While waiting lists for access to medical services are obviously undesirable for patients, they also have an economic cost. A study by Esmail (2011a) estimated that



Fotolia

**Figure 1: Median wait by province in 2011: weeks waited from referral by GP to treatment**



the cost of waiting per patient in Canada was approximately \$1,105 in 2010 if only hours during the normal working week were considered “lost,” and as much as \$3,384 if all hours of the week (excluding eight hours of sleep per night) were considered “lost.” Economists Stokes and Somerville (2008) also found that in 2007, the cumulative total of lost economic output in Canada (representing the cost of waiting for treatment for joint replacement surgery, cataract surgery, coronary artery bypass graft surgery, and magnetic resonance imaging (MRI) scans collectively) was nearly \$15 billion.<sup>2</sup> It is therefore in everyone’s best interest to reduce the amount of time that patients must wait for medical treatment.

Several factors contribute to these long waits Canadians face when seeking medically necessary elective treatment. Studies have shown that operating rooms are systematically underused<sup>3</sup>, hospital beds are inappropriately occupied by Alternative-levels-of-care (ALC) patients<sup>4</sup>, and the supply of physicians is insufficient to meet demand under the country’s current system<sup>5</sup>—all of which may be contributing to the long wait Canadian patients endure.

Another factor, is the wait for access to medical technology. In 2011, patients in Canada had to wait approximately 4.2 weeks for a CT scan, 9.2 weeks for an MRI, and 4.6 weeks for an Ultrasound (Barua et al., 2011). Given that the information from these tests is

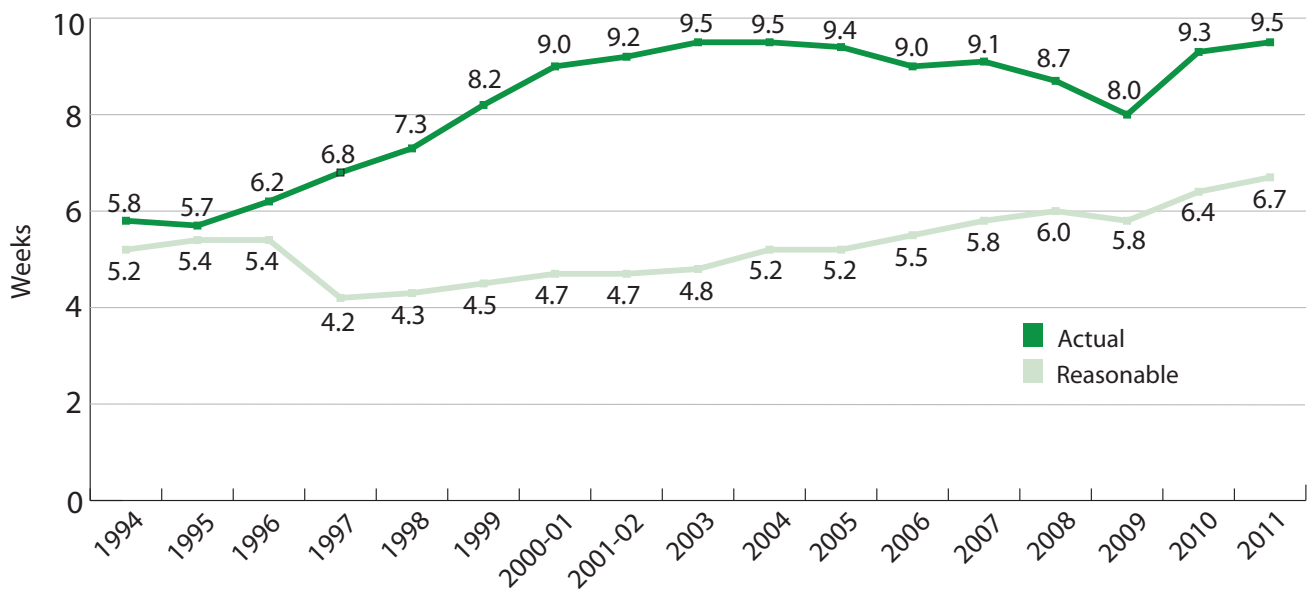
used to determine the urgency of a patient’s case, it is not only unreasonable, but potentially harmful to have patients wait so long for them. This long wait might, however, be partially explained by the fact that Canada ranked 18th (out of 28 OECD countries) for the number of CT scanners per million people, and 16th (out of 27 OECD countries) for the number of MRI units per million people, in 2009 (OECD, 2011).

In addition, when compared to Australia, Germany, New Zealand, the Netherlands, the United Kingdom, and the United States, “Canada ranks last or next-to-last on almost all measures of timeliness of care” (Davis, et al., 2010: 11).

Physician responses to the Fraser Institute’s annual wait times survey also indicate that an estimated 1% (46,159) of Canadian patients received medically necessary elective treatment in another country during 2010/2011. This suggests that Canadians who are unhappy with the long waits they face, or who are willing to pay out-of-pocket to access timely medical care, are already *not* waiting their turn.

Despite the fact that government health expenditures are expected to reach \$140 billion by the end of 2011 (CIHI, 2011), and even though the federal government committed \$41.3 billion (Department of Finance, 2011) of new funding over 10 years in 2004 (under the 10-year Plan to Strengthen Health Care), wait times remain unacceptably long across Canada.

**Figure 2: Canada—Actual versus reasonable waits between appointment with specialist and treatment, 1994 through 2011**



## Notes

1 For example, Canada's provincial, territorial, and federal governments agreed to a set of common benchmarks for medically necessary treatment on December 12, 2005 (Ontario Ministry of Health and Long Term Care, 2005).

2 Three types of costs were considered: patient costs, caregiver costs, and healthcare system costs. The study found that the highest economic costs were generated for total joint replacement surgery (an average of about \$26 400 per patient), followed by MRIs (\$20 000) and CABG surgery (\$19 400), with cataract surgery yielding the lowest costs (\$2900).

3 See Frappier and Laberge, 2007; for example.

4 ALC patients are those who continue to occupy an acute care hospital bed after the acute phase of their inpatient stay is complete (Wait Time Alliance, 2011:10) and are simply "awaiting an alternative level of care in a more appropriate setting" (Walker et al., 2009: 1). It is estimated that, in Ontario, almost "one in six beds is filled with patients who should be cared for somewhere else" (Wait Time Alliance, 2011: 10).

5 See Esmail, 2011b; for example.

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# Property rights

**Terry Anderson and Dominic Parker**

The authors of this essay are the recipients of the Fraser Institute's 2011 Addington Award. The Fraser Institute's annual Addington Prize in Measurement recognizes a person or team who has researched a new, interesting, and important concept in public policy, exemplifying the Institute's motto: If it matters, measure it. The essay summarizes the authors' study *Sovereignty, Credible Commitments, and Economic Prosperity on American Indian Reservations*, which measures the crippling economic consequences resulting from the lack of private property rights on Indian reserves. The paper was published through the Property & Environment Research Center (PERC) in Bozeman, Montana and is available at [www.perc.org](http://www.perc.org).

Canadian First Nations reserves and United States Indian reservations are islands of poverty in a sea of wealth. In 2000, the income of First Nations people amounted to only 39 percent of the income of the average Canadian. In the US, the income of Native Americans living on reservations was only 36 percent of the income of the average American.

A robust explanation for this poverty has remained elusive. As with many explanations of economic development, the poor performance of reservation economies has been mainly attributed to poor land, geographic isolation, and inadequate human capital to manage what few assets First Nations have. To be sure, some reservations have few natural resources and low rates of education and training. But other Native lands are rich with natural resources and have skilled and energetic populations with unrealized entrepreneurial ideas and plans. Why have these physical and human resources not been used for greater economic gain?

Our research focuses on the importance of institutions or the rules of the game under which Native American economies operate as a cause of economic stagnation. We compare economic growth for Native Americans under two systems of governance. On some reservations tribal judiciaries have exclusive jurisdiction over most contracts involving American Indians. On other reservations state legal systems have jurisdiction. The variation is due to a US federal law (Public Law 280), implemented during the 1950s and 1960s, which gave states jurisdiction on some reservations without the consent of affected tribes.

The legislation was controversial because it weakened the sovereignty that tribes have fought long and hard to retain, but, according to our results, that sovereignty has been an economic liability for tribes. After controlling for other important variables, per capita income for Natives on reservations subjected to state jurisdiction grew 30 percent more than per capita

## The legal environment on Native lands is a key reason why poverty persists



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income for those not subjected to state jurisdiction between 1969 and 1999.

Our findings add to a growing consensus in the economic development literature that legal institutions play a fundamental role in discouraging or encouraging growth. For example, countries scoring high on country-level measures of secure property rights and a stable rule of law have higher rates of growth than countries with low scores.

But the reservation setting enables a closer view of institutions than what is afforded by cross-country analysis. On reservations, it is easier to control for the impact of non-institutional factors such as geography, resource endowments, and culture.

Because we can control for these factors, it is quite clear that the legal environment on Native lands is a key reason why poverty persists. In particular, we know that some outsiders perceive tribal courts as biased, incompetent, or even corrupt. This perception will deter businesses from investing resources on reservations and block wealth from entering.

However, another reason may be even more fundamental. Because reservations are poor and sparsely populated—in 2000, the United States only had one Native population exceeding 15,000—it is very difficult for tribal courts to build legal precedent on contract litigation. Will courts hold debtors accountable for repayment? How will courts interpret ambiguities in contracts? Instead of operating in this uncertain legal environment, many would-be investors take their money elsewhere and economic stagnation on reservations persists.

Tribes wanting robust economic growth need court systems that allow their tribal members to commit to adhering to contracts, but this may not require the imposition of state jurisdiction. Some tribes are creating inter-tribal court systems of appeal by forming regional legal bodies that will adjudicate cases arising on multiple reservations.

This federalist system of tribal law could, in principle, work better than forcing tribes under state courts. On one hand, it leaves original authority in local tribal courts where there is the best place-specific knowledge. On the other hand, the system augments precedent on tribal cases because all regional cases will be subject to appeal in a broader court system. The system also provides a check on local corruption and abuse by any particular tribal court.

It is clear: that a secure, impartial, and predictable rule of law is key if reforms are to be successful in creating prosperity.

If this happens and if a band can establish a legal reputation for impartial and predictable adjudication of contract disputes, we have an experiment which can test the importance of institutions for economic development. Our prediction is that such institutional change will build a platform on which Natives in both the US and Canada can begin their climb up the economic ladder and out of poverty. ■



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For more information on Canadian reserves please read Gordon Gibson's *A New Look at Canadian Indian Policy*. (<http://www.fraserinstitute.org/research-news/display.aspx?id=12783>).

# Bouazizi's Revolution



Antoine Walter

Alan W. Dowd

*Time* magazine's Person of the Year has been an annual tradition since 1927. Winners have been peacemakers (Gandhi and Martin Luther King Jr.) and warmongers (Adolf Hitler), heroes (Winston Churchill) and villains (Joseph Stalin), liberators (Dwight D. Eisenhower) and dictators (Ruhollah Khomeini), moguls (Ted Turner) and machines (the personal computer), pop stars (Bono) and politicians (Bill Clinton).

By selecting "The Protester" for 2011, *Time's* editors lived up to their own standard for determining Person of the Year—the person or persons "who influenced the news most, for better or worse." As the magazine explains, "from the Arab Spring to Athens, from Occupy Wall Street to Moscow... the protester once again became a maker of history" (Anderson, 2011). But *Time* could have—and arguably should have—gone one step further and chosen the man who inspired the Arab Spring protests and consequent revolutions, Mohammed Bouazizi. No single person influenced global events or global news—or the political fortunes of so many leaders and the political future of so many people—as much as he did.

## Target: Autocracy

If the name doesn't ring a bell, don't worry. Bouazizi was not a famous inventor or philosopher, military strongman or freedom-fighter. In fact, he wasn't known at all until his death. But his death triggered a geopolitical earthquake that is shaking the Middle East and reshaping how the rest of the world interacts with this vital region and its people.

Bouazizi was a Tunisian street vendor who finally had enough of government regulation and humiliation last December after a police officer confiscated his vegetable cart because he didn't have a proper permit. When Bouazizi tried to pay the fine, the police officer slapped him and spat in his face. He attempted to appeal to the officer's higher-ups for relief, but was dismissed and denied a hearing (Abouzeid, 2011).

The humiliation and hopelessness—caused by government interference in his life and livelihood—overwhelmed Bouazizi to the point that the young merchant set himself on fire. He died on January 4, starting a people's revolution that toppled Tunisia's dictator less than a fortnight later. As the authors of the Fraser Institute's report on economic freedom in the Arab world concluded, Bouazizi's defiant act "highlighted in the most dramatic way the desire for, and benefits of, economic freedom in the region" (al Ismaily, Cervantes, and McMahon, 2011: 3).

The shockwaves have spread across the Arab world. However, it should be noted that just as the Arab world is not a monolith, neither are the revolutions of the so-called Arab Spring: In some instances, there has been a Sunni-Shiite undercurrent; in others, corruption has fueled the revolt; in still others, government indifference has been the driving force. Some of the revolutions have been spurred by the lack of economic freedom, others by the lack of political freedom.

Though the triggers may have been different, the targets were all the same: autocrats.

On January 17, 2011, an Egyptian man, overwhelmed by the grinding poverty and lack of opportunity in his homeland, imitated Bouazizi's horrific act of civil disobedience. Massive anti-government protests then broke out in Egypt. Cairo's Tahrir Square became the new epicentre of the political earthquake. And in the span of three weeks, Hosni Mubarak was toppled—after three decades in power. (A year later, spasms of unrest continue in and around Tahrir Square.)

As Mubarak's one-man rule collapsed, Libyans in Benghazi began protesting Moammar Qaddafi's 41-year reign. But unlike his neighbouring dictators, Qaddafi would not go peacefully. Instead, his regime vowed to crush the Benghazi rebels, triggering a Libyan civil war. A range of factors—Libya's oil wealth, concerns over a tidal wave of refugees washing onto Europe, the ghosts of Srebrenica and Rwanda—compelled NATO leaders to support the rebel force with air and sea power. By June, Qaddafi's reach had shrunk to the city limits of

Tripoli. By August, the rebels had taken Tripoli. And by October, Qaddafi was dead. The Arab Spring had claimed its third dictator.

Although Morocco wasn't scarred by civil war, the protests forced Morocco's reform-minded king to agree to a new constitution.

The unrest wasn't quarantined to North Africa, however. Fueled by social media and satellite television, Bouazizi's revolution jumped across the Red Sea and onto the Arabian Peninsula. Yemen was rocked by violence that spiraled toward a full-blown civil war. Ensclosed as Yemen's autocrat for 33 years, Ali Abdullah Saleh would flee to Saudi Arabia after being badly wounded in battles raging in the capital. Then, after recuperating, Saleh returned to San'a and directed his military forces for several months before finally signing an agreement to transfer power, hold elections, and broaden access to the country's political process (Al-masmari, 2011). Another autocrat had been ousted.

In Bahrain, the chaos forced the government to appeal to Saudi Arabia for assistance. Eager to prevent any threat to friendly autocrats, the Saudis dispatched hundreds of troops and tanks to prop up the Bahraini regime. It was an Arab version of the 1968 Brezhnev Doctrine, the brutal and blunt instrument of coercion used by the Soviet Union to justify armed intervention in communist nations in order to prevent anti-communist revolutions.

Jordan weathered weeks of largely peaceful protests that demanded parliamentary and economic reforms. In response, King Abdullah II, a much more benign monarch than his counterparts in Saudi Arabia and Bahrain, unveiled political reforms that seemed to mollify his subjects—at least for the time being.

In Syria, the revolution arrived late but has lasted the longest. The protests were peaceful at the outset, but Bashar Assad would not permit any challenge to his rule. It's simply not in his DNA to allow for pluralism. (His father, Hafez Assad, slaughtered 20,000 Syrians to staunch a 1982 uprising). So the order came down to smash the protests and disperse the protesters. Assad's henchmen have now killed an estimated 4,000 Syrians. Lacking the stomach to fire on innocent civilians, thousands of Syrian soldiers have switched sides and formed the Free Syrian Army to defend the protesters and dislodge Assad's regime (BBC, 2011). As a consequence, Syria is now edging toward a Libya-style civil war.

## Risks

It has been a year since Bouazizi became so fed up with government intrusion in his life that he concluded death was better. His self-immolation was more than

a condemnation of capricious, intrusive government; it was also a declaration in defense of freedom—and specifically, economic freedom. It pays to recall that Egypt, Syria, and Bouazizi's Tunisia were in the bottom half of the 2011 Economic Freedom of the World rankings. Libya and Yemen weren't even ranked. (Gwartney, Lawson, and Hall, 2011: 9).

Bouazizi may have never read Friedrich Hayek or John Locke, but what he was seeking was economic freedom—the freedom to use and exchange his property as he deemed appropriate, the freedom from arbitrary confiscation or theft of that property, and the protection of that property from physical invasions by others, including the government (al Ismaily, Cervantes, and McMahan, 2011: 1).

As Locke observed, it should be every person's right to "preserve his property, that is, his life, liberty, and estate against the injuries and attempts of other men" (Locke, 1690: 50). Bouazizi understood the importance of this truth because he lived under a regime that did not. That regime is now gone, and the regional order that supported it is crumbling.

Reasonable people can, and do, disagree about whether the Arab Spring has opened the door to a freer Middle East, or to an extremist takeover of the Middle East, or simply to a time of great uncertainty and instability.

On the positive side, the Middle East's revolutionaries are demanding freedom, opportunity, justice, and an end to government corruption and control, not unlike Eastern Europe's revolutionaries in 1989-90. Tunisia, Egypt, and Yemen have ousted their autocrats; Libyans, with an assist from NATO, have dethroned Qaddafi; and Syria's despot is under increasing pressure from within and without.

However, some observers understandably worry about what will replace the old order in the Middle East.

Mubarak's Egypt, for instance, was a moderating influence in the Arab world. It lived up to the aspirations for peace made at Camp David in 1978. As a result, a once-constant source of international instability—war between Israel and Egypt—was taken off the table. Mubarak's Egypt partnered with the West to promote regional stability by opening Egypt's ports and airspace to power-projecting nations like the United States, by serving as a bulwark against destabilizing regimes in Iraq and Iran, and by keeping the vital Suez Canal and Suez-Mediterranean oil pipeline (SUMED) open. It pays to recall that 15% of Europe's oil flows



Bigstock

hold. And it will take time for the children of the Arab Spring to learn the ways of political pluralism, to understand the importance of majority rule with minority rights, to recognize that freedom is about more than going to the polls every few years.

As Mohammed Bouazizi understood, it's also about property rights, economic liberty, and human dignity.

## Notes

1 Islamist political movements advocate reordering government and society in accordance with a strict interpretation of Islam.

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through the canal and that Egypt accounts for 5% of the world's liquefied natural gas trade (Ratner, 2011: 3-4).

Similarly, before the Arab Spring erupted, Saleh had worked closely with Western intelligence agencies and militaries to counter al Qaeda's new power centre in Yemen, al Qaeda in the Arab Peninsula (commonly known as AQAP). Qaddafi had come in from the cold, renounced his terrorist ways, given up his weapons of mass destruction, and opened up his country to trade and development.

Of course, Mubarak ran a tough police state that smothered normal political activity, Saleh stubbornly ignored the will of the Yemeni people, and Qaddafi showed his true colours when his subjects demanded their freedom. In other words, no one should mourn the end of autocratic rule in the Arab world. Libyans, Egyptians, Yemenis, and Syrians, like all people, deserve to be free. But there are risks to revolution. As US Secretary of State Hillary Clinton has observed, "Revolutions have overthrown dictators in the name of democracy only to see the political process hijacked by new autocrats who use violence, deception, and rigged elections to stay in power or to advance an agenda of extremism" (Clinton, 2011).

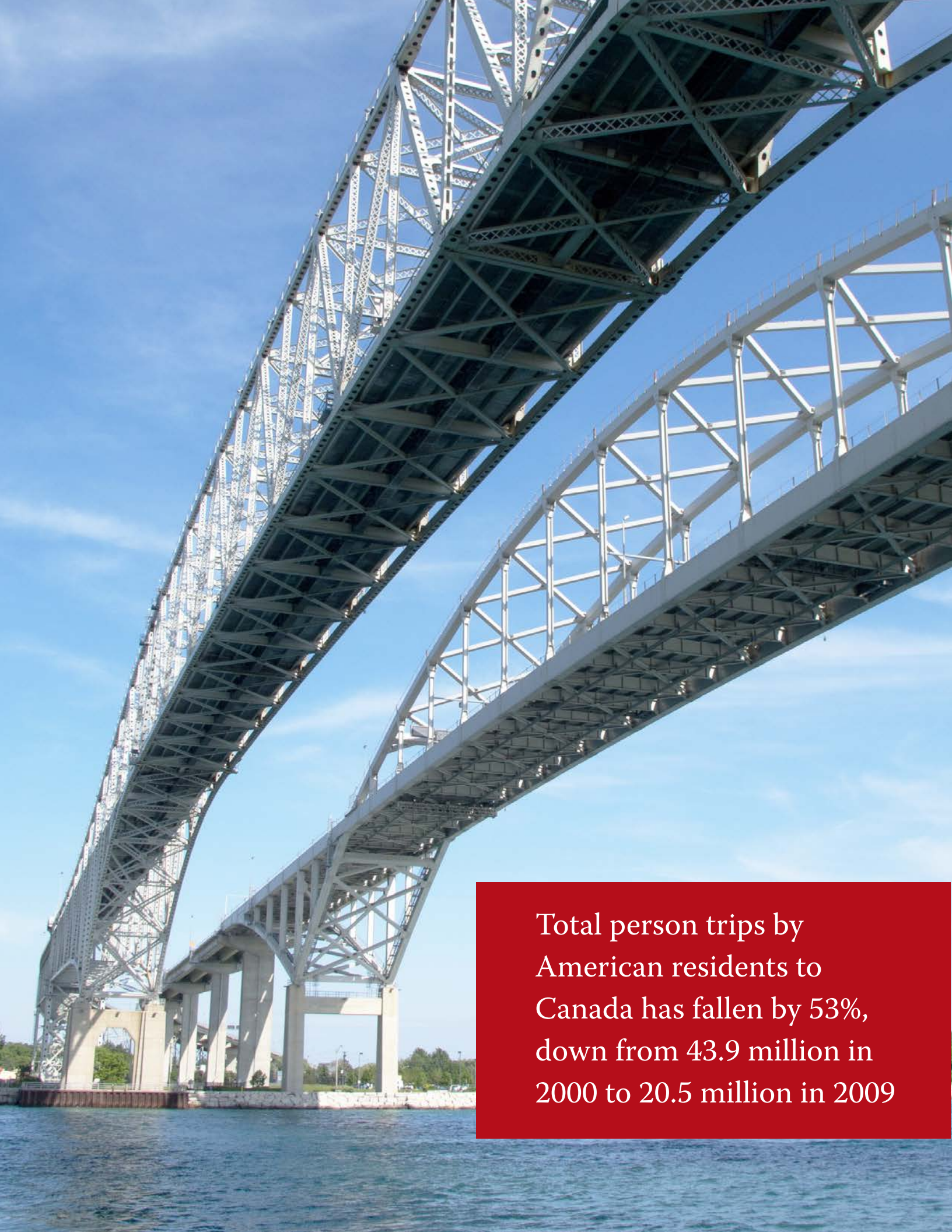
## Learning Freedom

That is why the world so anxiously watches the unfolding revolution. The realists caution that Islamist groups<sup>1</sup> could win at the ballot box and open the door to extremists, that ongoing chaos could roil the region and weaken the global economy, that emergency councils and military strongmen could re-emerge as kingmakers, that fractured polities could descend into tribalism, that jihadists could seize power in one or more of these strategically vital countries.

These are real possibilities. Yet there is a sense, finally, that freedom has a chance in the Middle East.

Even so, it will take years—not just a revolution, not just an election—for freedom to take hold. It will take more than elections for the rule of law to take





Total person trips by American residents to Canada has fallen by 53%, down from 43.9 million in 2000 to 20.5 million in 2009

# The Costs of the Canada-US Border

Alexander Moens and Nachum Gabler

## 9/11 and the Border

More than a decade has passed since the United States suffered the most violent attack ever carried out on American soil. The shockwaves have reverberated across the American political and economic landscape and far beyond. The negative consequences from 9/11 have become deeply entrenched and have led to a new “security-first” orientation that now permeates most branches of the US government, notably the Department of Homeland Security, and has widely infused itself into the mindset of elected representatives in Congress concerning Canada-US border and security issues (Moens and Gabler, 2011).

Border wait times and various security program costs have led to “border thickening” (Goldfarb and Robson, 2003). “Border thickening” refers to the phenomenon whereby national borders become increasingly impermeable to travelers and commercial shippers as a result of multiple layers of security enhancing procedures. The integrated commercial and economic relationship between Canada and the United States has suffered from this new implicit “thickening” on border crossings.

Canadian policy makers, and assorted business and community stakeholders, have spent considerable time and resources trying to overcome the problem. The so-called Smart Border Accord of 2001 with the US and the Security and Prosperity Partnership of 2005 with both Mexico and the US were governmental initiatives that added many new programs and costs to border crossing but that did not deliver significant efficiencies. The Harper government and Obama administration announced in December 2011 a new Beyond the Border Accord that aims to bring more security checks

to the perimeter, rather than on the shared land border, more secure cargo programs, and further harmonization of various regulatory differences in manufacturing and food standards.

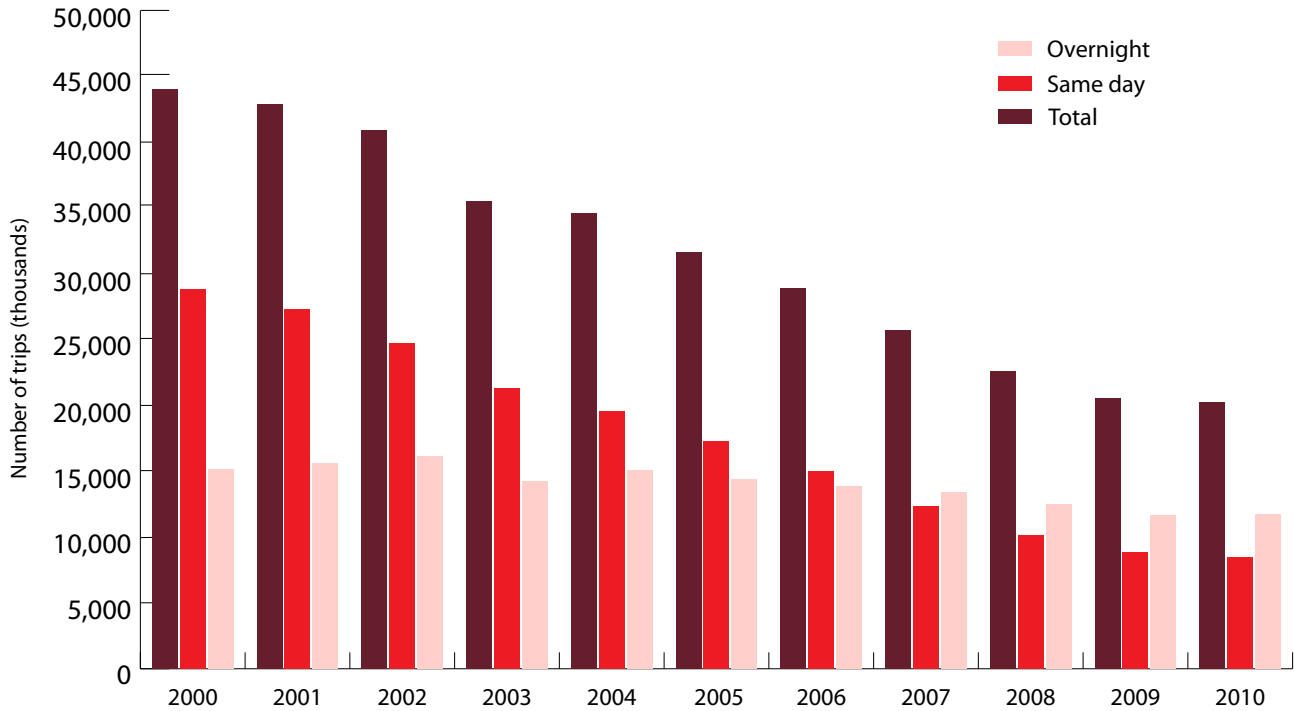
While sovereign countries have an obvious legal right to control their borders, citizens on both sides of the Canada-US line ought to be free to conduct commerce and bolster other cross-border ties. Finding the optimal balance between the two “rights” requires defining what criteria the border should fulfill and what costs are reasonable to meet these “rights.” Given the high degree of compatibility between our two societies and economies, and the long history of deeply integrated commercial ties in numerous sectors which has benefited consumers and producers on both sides of the line, the onus is on governments to prove which border security costs are justified. This mindset has thus far been lacking and needs to be developed.

## Measuring Border Costs

The cost of the border can be measured on three areas: travel and tourism, commerce and trade, and government expenditures in administering border procedures and various new security programs. In an upcoming Fraser Institute report titled *Measuring the Costs of the Canada-US Border* to be released in early 2012, we will publish a detailed attempt at measuring these costs. The following is an overview of our findings. What we measure are the effects of so-called “border thickening.” Canadians are also concerned about the “chilling effect” of crossing the border whereby individual travellers and shippers avoid making discretionary cross border trips whenever possible because they perceive the border crossing experience as intimidating and unpleasant (Peter Andreas, 2003a, 2003b).

The number of overnight American travelers visiting Canada has fallen by 23% over the past decade (Statistics Canada, 2010a, 2010b). The number of same day return trips has declined by 69%. Taken together, total person trips by American residents to Canada has fallen by 53%, down from 43.9 million in 2000 to 20.5 million in 2009 (Statistics Canada, 2010a, 2010b). Obviously, economic troubles in the US and a rising Canadian dollar are important factors in this decline. However, as figure 1 shows, the decline started well before 2008. Most likely border security, including the Western Hemisphere Travel Initiative requirements for American travelers, contributed to the drop. The Western Hemisphere Travel Initiative made passports or enhanced drivers licences mandatory for all American citizens to cross back into the US.

**Figure 1: US residents travelling to Canada**



Source: Statistics Canada 2010a and 2010b

Total payments made by Americans to Canadians for travel and tourism barely fluctuated over the past decade, amounting to \$7.03 billion (nominal) in 2001 and ending 2010 at \$7.04 billion in nominal dollar value (US Department of Commerce and US Bureau of Economic Analysis, 2011). Given that the number of travelers has been nearly cut in half, it is likely that at minimum \$7 billion in potential receipts were lost to the Canadian economy.

Of course the largest cost incurred from the congested and securitized border is borne by business. Ford Motor Company reported recently that on average its trucks involved in cross-border transfers of auto parts wait one hour at the border amounting to an idling cost of \$200 per truck (Ibittson, 2011). Trusted shipper programs have added considerably to the administrative cost of cross-border trade. (United States Chamber of Commerce and Canadian Chamber of Commerce, 2008).

An assortment of literature addresses costs to businesses and bilateral trade, including surveys, case studies, and general commentaries. Most pitch their estimate between 1.5% and 3% of the bilateral merchandise trade value (Moens and Cust, 2008). The most systematic analyses find significant shortfalls in trade flows attributable to new border barriers and costs (Globerman and Storer, 2006, 2008, 2009a, 2009b; Grady, 2009a). American economists

Steven Globerman and Paul Storer calculated that between the third quarter of 2001 and the second quarter of 2005, the total value of the shortfall in Canadian exports to the US equaled USD \$176.08 billion or more than \$40 billion per year on average (Globerman and Storer, 2008).

Besides travelers and business people, the taxpayer also pays for the rising cost of the border. There is no consistent data available that tracks year-over-year costs of border programs and security measures. Researchers can only find snap shots of individual programs or pieces of overall program spending. The government of Canada should make reports of program objectives that are linked to disclosed budgets and provide year-over-year assessments of these goals and their itemized costs public.

Given all the separate and incidental costs for a myriad of programs, we cannot aggregate a total for any one year. However, we estimated the total cost to the Canadian economy by aggregating all of the individual program costs and concluded that “border thickening” costs Canadian taxpayers between \$500 million and \$1 billion annually.

## Conclusion

The cost of border security since 9/11 continues to rise for travelers, businesses, and taxpayers. At this point we cannot know if these costs are warranted. Unless

we measure and evaluate them, border programs will expand through their own policy and bureaucratic momentum. The Harper government and Obama administration have agreed to a new “Beyond the Border” agreement that expands practices introduced earlier, such as the pre-screening of container cargo and adds a new entrance-exit coordination plan. The intent of the new accord is to build up more perimeter security measures and to reduce unnecessary regulatory differences. Both of these are promising features to thin the border. However, we argue that the Canadian government needs to develop specific border goals and cost these out, as would be done with all other government programs, in order to measure and evaluate if the new border costs are warranted.

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# How Can Canadian Policy Makers Combat Black Market Tobacco?

## Six Policies to Counter Contraband

Nachum Gabler

Contraband tobacco is a serious concern for Canadian policy makers and the public. One report estimated that 65 million cartons of contraband tobacco were bought in 2008, equal to approximately 30% of all tobacco bought across Canada (Public Safety Canada, 2009). In 2009, the number of contraband tobacco cartons seized across Canada reached a record high of 975,000 (RCMP, 2010a).

Contraband tobacco poses multiple dangers. Health Canada has warned that cheap and easily accessible contraband constitutes a threat to public health beyond the threat posed by lawful tobacco (Health Canada, 2009). Furthermore, contraband trafficking has drawn in over 100 criminal organizations with links to narcotics and firearms distribution (RCMP 2008, 2009; Public Safety Canada, 2009). Other negative consequences associated with the contraband tobacco trade include the loss of market share for lawful merchants and declining tax revenues (CCSA, 2010; Canada Revenue Agency, 2008, 2009).

Canadian policy makers must develop robust strategies that employ the right policy mix to tackle the contraband tobacco problem. A recent Fraser Institute study, *Combating the Contraband Tobacco Trade in Canada*, examines several of those policies.

### 1. Tax agreements

The participation in the contraband trade of individu-

als and organized groups operating on certain Aboriginal reserves is well documented (RCMP, 2008, 2009). Advocates who defend Aboriginal tobacco commerce claim that these “tobacco entrepreneurs” produce wide spread economic benefits in their communities (Kahnawake Tobacco Association, 2010). Whether or not this is the case, the Aboriginal tobacco trade would be exceedingly difficult to eliminate.

Instead, in an attempt to legitimize Aboriginal tobacco commerce, one option would be for Canadian provinces to implement tax revenue agreements with their local Aboriginal communities that remunerate the band with the full or partial proceeds from the tobacco taxes collected on a reserve.

The benefits of tax agreements include incorporating the Aboriginal tobacco trade into the legitimate market, enhancing the legitimacy of Aboriginal governance by offering band councils a way to generate their own revenues, using tax revenues to finance development projects, and reducing criminality and disrespect for the law associated with black markets. Another benefit of tax agreements from the point of view of the anti-smoking lobby is the restored deterrent effect of taxes on smoking.

Two arguable drawbacks of tax agreements include the loss of revenues for signatory governments and the possible perception that tax agreements constitute a reward for subverting tobacco distribution laws. But, this argument is flawed. It presumes that the tax revenue being collected by Aboriginal merchants would otherwise have been collected by the government; in fact, the tax revenues being collected by Aboriginals merchants were formerly the proceeds of contraband tobacco be-

ing earned by Aboriginal contraband distributors.

Furthermore, tax agreements can only reduce that portion of the contraband tobacco supply controlled by Aboriginal tobacco merchants and not, for example, the sources of contraband originating from American states with relatively low tobacco taxes or counterfeit brand name cigarettes arriving from overseas in commercial shipping containers.

## 2. Tax revocation

There are several arguments for eliminating tobacco excise taxes, primarily, that a drop in these taxes will deter the underground trade in tobacco. The precise cost-benefit between having a flourishing black market and using taxation to discourage smoking and improve public health is unknown. Tobacco tax proponents argue that tax revocation would encourage smoking. However, recent research has found that the deterrent effect of higher tobacco taxation has been waning (Gospodinov and Irvine, 2005; Galbraith and Kaiserman, 1997; Gruber et al., 2003).

Tax revocation opponents also claim that federal and provincial governments would be forgoing a vital source of revenue. However, the revenues being collected by Aboriginal tobacco sellers are not forgone government revenues; the revenues in question are former contraband tobacco sales revenues and profits, as noted above.

A further drawback of eliminating taxes is that it might still prove insufficient in deterring the underground trade in tobacco. Aboriginal tobacco distributors have allegedly accepted prices as low as \$6 per carton in some locales (RCMP, 2008). It is unlikely that the tax-free retail price of tobacco would ever fall so low. Thus, even if tobacco taxes were eliminated outright, there is still reason to believe that Aboriginal tobacco merchants would retain some market share. Even if the black market does not vanish following tax repeal, a complete elimination of excise taxes would reduce the appeal of buying contraband tobacco and the profitability of selling it.

## 3. Tobacco excise tax reduction

The primary incentive driving cigarette smuggling from the United States is the existence of a

significant price difference between cigarettes sold in Canadian provinces and those sold in US states. Eliminating or reducing the tobacco tax difference between Canada and certain US states may require Canada to drop its tax rates to match those in jurisdictions across the border. Government tax receipts from tobacco sales could shrink because of the lower rate of taxation. However, any possible decline in tax revenues may be partially offset by an increase in tax revenues resulting from an increase in lawfully sold tobacco.

## 4. Better record keeping by policing authorities

Eradicating contraband tobacco requires relevant data to be tracked so that policy makers can develop counter measures. Unfortunately, statistics that describe the extent of criminality linked to contraband tobacco markets are essentially non-existent. Canadian law enforcement must begin systematically recording, compiling, and organizing data pertaining to Canada's contraband tobacco trade.

Useful statistics that should be tracked include: provincial tobacco seizures; the number of individuals charged with contraband tobacco related offences and the total number of charges laid against them; the size of law enforcement budgets devoted to anti-contraband tobacco enforcement and how these budgets are being spent; the number of charges laid against alleged offenders as well as charges pertaining to other criminal activities; and the number of people who were simultaneously charged with both contraband tobacco and drug or gun trafficking, for example.

## 5. Campaign to increase public awareness

Another important factor fueling the contraband market is the common misperception among smokers that buying contraband tobacco is consequence-free, the price being the only tangible difference between contraband and lawful cigarettes (Health Canada, 2009).

To counter that misperception, public health officials should develop an anti-contraband tobacco information dissemination strategy stressing the harm associated with contraband tobacco including: the lack of warning labels, the illegality of tax evasion, the link to peripheral crimes and the domination of contraband

markets by organized crime groups, the damage to law abiding tobacco retailers, and the ease of access to contraband enjoyed by young smokers (Health Canada, 2010).

## 6. Increased enforcement against wholesalers and retailers

Several Aboriginal reserves situated near the US border have become important smuggling corridors into Canada. Moreover, there has been a discernible increase in the amount of contraband tobacco entering Canada in freight shipments (RCMP, 2008, 2009 2010b; CBSA, 2010). Attempting to cut off the supply of contraband tobacco where it enters Canada is futile. There are insufficient police resources to stop the traffic using the remote smuggling routes running across the porous Canada-US border. Similarly, it is impossible for customs to detect all of the contraband tobacco entering Canada in shipping containers. Instead, law enforcement should diligently pursue contraband wholesalers and retailers at the wholesale or retail distribution level.

## Conclusion

Contraband tobacco is a difficult problem to resolve. No single anti-contraband initiative in isolation will solve the whole problem. However, adopting an assortment of well-developed policies that have been tailored to overcome the challenges posed by specific aspects of the Canadian contraband tobacco market is a potentially promising approach.

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# Should the rich be condemned?

Walter Williams

Thomas Edison invented the incandescent bulb, the phonograph, the DC motor, and other items in everyday use and became wealthy by doing so. Thomas Watson founded IBM and became rich through his company's contribution to the computation revolution. Lloyd Conover, while in the employ of Pfizer, created the antibiotic tetracycline. Though Edison, Watson, Conover, and Pfizer became wealthy, whatever wealth they received pales in comparison with the extraordinary benefits received by ordinary people. Billions of people benefited from safe and efficient lighting. Billions more were the ultimate beneficiaries of the computer, and untold billions benefited from healthier lives gained from access to tetracycline.

US President Barack Obama, in stoking up class warfare, said, "I do think at a certain point you've made enough money." This is lunacy. Andrew Carnegie's steel empire produced the raw materials that built the physical infrastructure of the United States. Bill Gates co-founded Microsoft and produced software products that aided the computer revolution. But Carnegie had amassed quite a fortune long before he built Carnegie Steel Co., and Gates had quite a fortune by 1990. Had they the mind of the current US president, we would have lost much of their contributions, because they had already "made enough money."

Class warfare thrives on ignorance about the sources of income. Listening to some of the talk about income differences, one would think that there's a pile of money

meant to be shared equally among North Americans. Rich people got to the pile first and greedily took an unfair share. Justice requires that they "give back." Or, some people talk about unequal income distribution as if there were a dealer of dollars. The reason some people have millions or billions of dollars while others have very few is the dollar dealer is a racist, sexist, a multinationalist, or just plain mean. Economic justice requires a re-dealing of the dollars, income redistribution or spreading the wealth, where the ill-gotten gains of the few are returned to their rightful owners.

**"I do think at a certain point you've made enough money."**

—President Barack Obama

In a free society, for the most part, people with high incomes have demonstrated extraordinary ability to produce valuable services for— and therefore please— their fellow man. People voluntarily took money out of their pockets to purchase the products of Gates, Pfizer, or IBM. High incomes reflect the democracy of the marketplace. The reason Gates is very wealthy is millions upon millions of people voluntarily reached into their pockets and handed over \$300 or \$400 for a Microsoft product. Those who think he has too much money are really registering disagreement with decisions made by millions of their fellow men.



In a free society, in a significant way income inequality reflects differences in productive capacity, namely, one's ability to please his fellow man. For example, I can play basketball and so can LeBron James, but would the Miami Heat pay me anything close to the \$43 million they pay him? If not, why not? I think it has to do with the discriminating tastes of basketball fans, who pay \$100 or more to watch the game. If the Miami Heat hired me, they would have to pay fans to watch.

Many see capitalism as benefiting only the rich, but the evidence refutes that. The rich have always been able to afford entertainment; it was the development and marketing of radio and television that made entertainment accessible to the common man. The rich have never had the drudgery of washing and ironing clothing, beating out carpets, or waxing floors. The mass production of washing machines, wash-and-wear clothing, vacuum cleaners, and no-wax floors spared the common man this drudgery. At one time, only the rich could afford automobiles, telephones, and computers. Now all but a small percentage of North Americans enjoy these goods.

The prospects are dim for a society that makes mascots out of the unproductive and condemns the productive. ■



## Tax policy

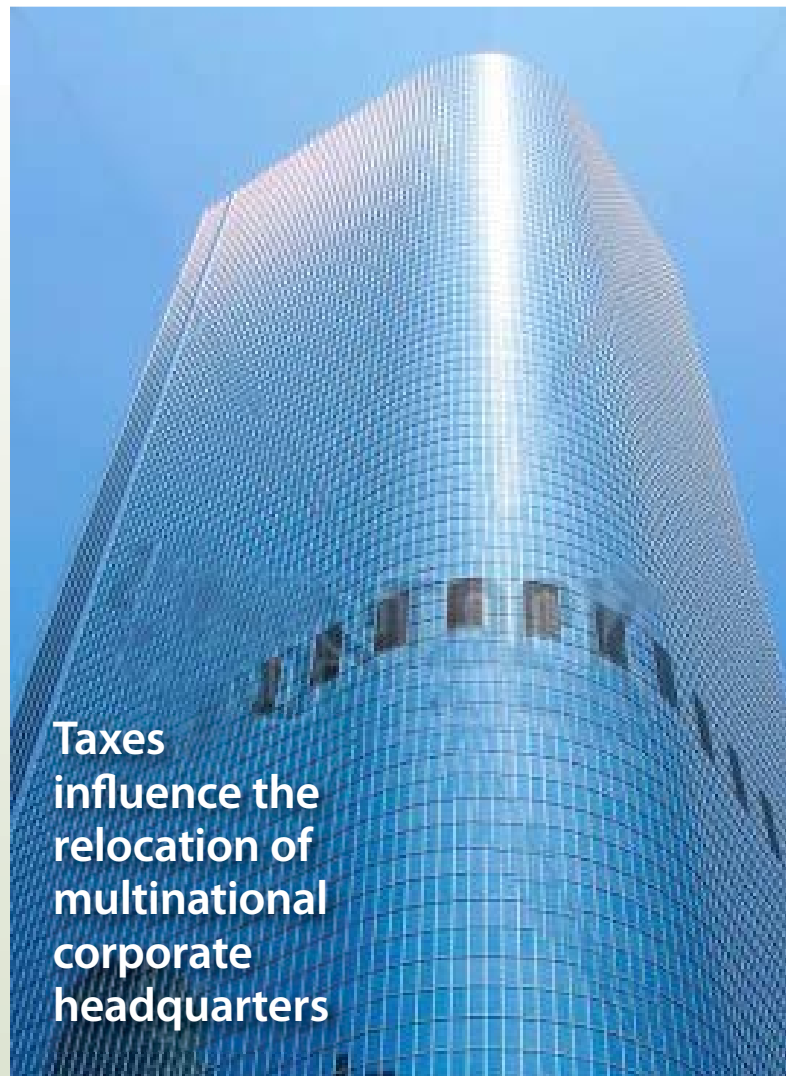
Voget, Johannes (2011). Relocation of headquarters and international taxation. *Journal of Public Economics* 95, 9-10: 1067-1081.

Attracting and retaining multinationals helps local economies by creating jobs, facilitating the adoption of new technologies and innovations, increasing access to capital, and spurring productivity and economic growth. But multinationals often relocate their headquarters to avoid tax rules, such as controlled foreign corporation (CFC) laws, that constrain their ability to form foreign subsidiaries in tax havens and shift profits to those subsidiaries. Multinationals also relocate to avoid paying additional taxes on their foreign-source profits. This paper explores how taxes influence the relocation of multinational headquarters and the extent to which the relocation is driven by tax avoidance. Using a worldwide database of 140 multinationals that relocated their headquarters between 1997 and 2007, and comparing them to 1,943 multinationals that did not relocate, the author finds that CFC laws increase the likelihood of relocations. In addition, multinationals headquartered in countries that provide credits for taxes paid abroad, instead of exempting foreign-source profits from taxation, are more likely to relocate. This reflects their incentive to avoid additional taxation of foreign profits in their home country. The findings suggest that a 10 percentage point increase in this additional tax results in a 2.2 percentage point increase in the share of multinationals that relocate.

— Milagros Palacios

Godbout, Luc, and Suzie St-Cerny (2011). Are Consumption Taxes Regressive in Quebec? *Canadian Tax Journal* 59, 3: 463-93

Unlike income taxes, which have a progressive scale such that the tax rate increases as income rises, consumption taxes have a single rate. As a result, many perceive consumption taxes to be regressive, with lower income families spending a larger share of their income on taxes than those with higher income. The authors challenge this view by estimating the burden of



Taxes influence the relocation of multinational corporate headquarters

Bigstock

the federal goods and services tax (GST) and Quebec sales tax (QST) on Quebec households in 2008. Their results show that these consumption taxes are actually progressive. Indeed, the share of consumption taxes paid by the 20% of households with the lowest income is 2.6% compared to 44.1% for the 20% of households with the highest income. The share of consumption taxes rises with income because certain goods are exempt by the GST/QST (such as basic groceries and prescription drugs) and thanks to the refundable GST/QST credit, which is a payment low-income households receive to offset the impact of the GST/QST. Overall,

the results show that the recent GST rate reduction and QST rate hike benefited all households by reducing their share of income going to consumption taxes.

— **Milagros Palacios**

## Economic policy uncertainty

Baker, Scott R., Nicholas Bloom, and Steven J. Davis (2011). *Measuring Economic Policy Uncertainty* (October 2011). <http://faculty.chicagobooth.edu/steven.davis/pdf/PolicyUncertainty.pdf>.

If businesses are uncertain about taxes, health care costs, and regulations, they may postpone decisions to hire or train workers and invest in capital or adopt new technologies. The result would be slower economic growth. In the United States, there is much debate about whether economic policy uncertainty (on taxes, government spending, and other policies) has deepened the recent recession and stalled the recovery. To explore this issue, the authors construct a new index of economic policy uncertainty and measure its relationship to key economic variables like gross domestic product (GDP), investment, and employment. Their index is composed of: the frequency of newspaper articles that reference economic uncertainty and the role of policy; the number of federal tax code provisions set to expire in coming years; and the extent of disagreement among forecasters about future federal government spending and inflation. The index is measured from 1985 to 2011 with notable spikes in economic policy uncertainty around major elections, wars, the 9/11 attacks, and, more recently, the Lehman bankruptcy and passage of the Troubled Asset Relief Program (TARP) (the US federal government's first stimulus package). The index hit an all-time high during the 2011 debt ceiling dispute. The impact of the index on economic performance sug-

gests that an increase in economic policy uncertainty equal to the actual change between 2006 and 2011 leads to "large and persistent declines in aggregate outcomes, with peak declines of 2.2% in real GDP, 13% in private investment, and 2.5 million in aggregate employment."

— **Charles Lammam**

## Economic freedom

de Soysa, Indra, and Krishna Chaitanya Vadlamanati (2011). *Do pro-market economic reforms drive human rights violations? An empirical assessment, 1981–2006*. Public Choice (forthcoming).

Existing research shows that pro-market reforms, such as increased competition and reduced barriers to trade, typically result in increased economic growth. In this study, the authors examine the impact of such reforms on human rights violations like physical harm, torture, and imprisonment for political beliefs. The impact could go one of two ways: (1) either market reforms benefit the ruling elite at the expense of the majority, leading to social dissent and disarray, and ultimately human rights repressions; or (2) the reforms weaken the state's power and empower citizens by separating economic from political power, leading to better economic performance for everybody while increasing social harmony and peace. Using data from 117 countries over the period 1981 to 2006, including the Fraser Institute's *Economic Freedom*

*Index* as a measure of market reforms, the authors find that competitive market reforms lead to fewer human rights violations and an increase in government respect for human rights.

— **Amela Karabegović**



**Economic  
policy  
uncertainty  
slows growth**

# Beer with your popcorn? Not in British Columbia

Joel Wood

British Columbia has liberalized its liquor laws significantly since inception of the laws in the 1920s following prohibition. However, more reforms are needed since the laws in their current form are logically inconsistent and unfairly favour some businesses over others.

BC's liquor laws have evolved tremendously since they were first implemented. Originally bars were prohibited from playing music, serving food, hiring female serving staff, and allowing women and men to drink together (Campbell, 1991). Bars were also restricted until the 1950s to being located in hotels and member-only clubs (Campbell, 1991). Bowing to public pressure to relax these puritanical regulations successive governments from across the political spectrum reformed the more arcane aspects of BC's liquor laws; however, successive reforming has left BC's liquor regulations inconsistent.

The current regulations, as set out in the *Liquor Control and Licensing Act* and the associated *Liquor Control and Licensing Regulations*, explicitly prohibit three types of establishments from obtaining liquor licenses: Movie theatres,<sup>1</sup> video arcades, and any business whose primary purpose caters to youth. This specific exclusion stems from a revived temperance movement's influence on a newly elected Social Credit government in 1976 (Campbell, 1991).<sup>2</sup>

Being prohibited from serving alcohol usually is not an issue for movie theatres since they generally cater to families and teenagers and may be happy with ticket revenue and mark-ups on popcorn and soft drinks. However, this antiquated exclusion hampers the development of boutique and multi-use movie theatres that cater to a more adult crowd. This was recently exemplified when the Rio Theatre in Vancouver was required to stop showing movies in order to obtain a liquor license (Mackie, 2011, Oct. 26). The Rio is a single-screen, multi-use theatre in urban Vancouver catering to both movie buffs and music fans.

Excluding movie theatres, especially multi-use movie theatres, from obtaining liquor licenses is inconsistent with how other entertainment venues are treated. Any bar in BC can show movies, so long as a liquor control board bureaucrat does not deem the venue a movie theatre. Venues for plays, operas, concerts, and sporting events can all serve alcohol in BC. Even bowling alleys and IKEA serve beer. Yet movie theatres are excluded.

The only justification that seems at all plausible is a concern for minors. Yet if that is the case then the regulation excluding movie theatres is redundant since there is also a regulation specifically excluding establishments that cater mainly to minors. Furthermore, this could obviously be remedied for places like the Rio Theatre by requiring an age restriction on movie theatres that serve alcohol. This is in fact how Ontario has solved the problem and now allows

alcohol to be served in 19+ only movie theatres (Crawley, 2008, Dec. 15; Cineplex, 2011). This approach is common in many US states and European countries. However, even this type of requirement is logically inconsistent with the current treatment of other types of entertainment venues. Concert halls, sporting events, and bowling alleys are not required to restrict entry to patrons who are of age to drink alcohol.

A possible solution is to eliminate the regulation that specifically excludes movie theatres, but leave as is the regulation that excludes businesses that cater mainly to minors. Movie theatres that can prove that they cater to a market that is mainly comprised of adults should be allowed to obtain a liquor license. At the same time, a theatre multiplex that may not be able to prove this claim should be allowed to serve alcohol in some of its theatres if appropriate age restrictions are imposed.

Although liquor laws in BC have come a long way since prohibition, there are still improvements to be made. A clear next step for reform is to allow movie theatres in BC to serve alcoholic beverages.

## Notes

1 As defined under the *Motion picture Act*.

2 The newly elected Social Credit government was responsible for crafting the regulations for the new *Liquor Control and Licensing Act* passed by the previous New Democratic Party government.

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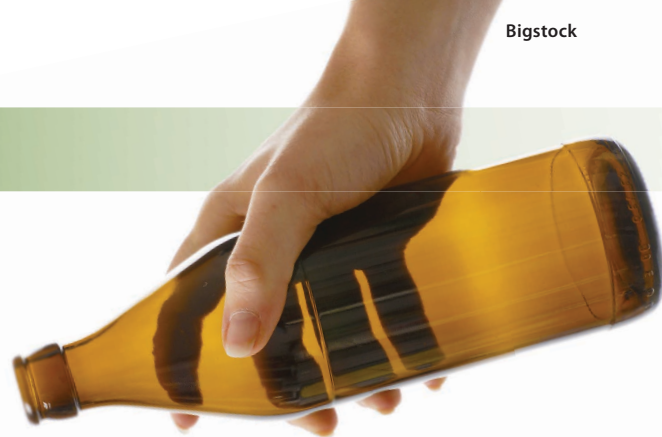
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## Assigning (proper) blame in the last financial crisis

*A review of* **Reckless Endangerment: How Outsized Ambition, Greed, and Corruption Led to Economic Armageddon**

by *Gretchen Morgenson and Joshua Rosner, Times Books 352 pages.*

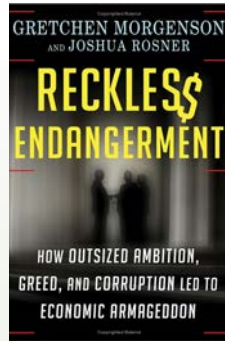
**Mark Milke**

The philosopher George Santayana’s quip that “Those who cannot remember the past are condemned to repeat it” has long been a cliché but no less true for that (Santayana, 1905: 284). Thus, as the world wrestles with the sovereign debt crisis in Europe and America, it is worth reviewing what prompted the last financial meltdown and the ensuing recession in late 2008 and early 2009.

Just after the financial services firm Lehman Brothers collapsed, and as United States mortgage giants Fannie Mae and Freddie Mac declined into a financial morass, US congressmen Barney Frank, the US Representative for Massachusetts’s fourth congressional district, was omnipresent on the nightly news. Frank, then chairman of the powerful House Financial Services Committee, was constant in his blame of Wall Street for the collapse in the American financial and housing sectors; he also blamed other politicians such as President George W. Bush and Republican opponents.

Quoted in a January 2009 *New Yorker* profile, Frank (who recently announced he won’t seek reelection in 2012), claimed he predicted, and might have prevented, the US housing crisis—if only others would have listened to him: “The ‘I told you so’ here is that homeownership is a nice thing but it is not suitable for everybody” (Toobin, 2009).

Frank’s remarks gave new life to the notion of “chutzpah.” The congressman had in fact favoured the practice of ever-expanding home ownership, even to those who might not be able to afford it under more historic, prudent mortgage lending rules. Until the financial crisis hit, Frank had long opposed stripping Fannie Mae and Freddie Mac of their special arrange-



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ment with the US federal government.

Contrary to later claims by Representative Frank and many other Democrats and Republicans, enough American politicians had opposed substantive reforms to the two ballooning financial behemoths, and this was in part due to the efforts of the mortgage giants themselves. However, some early history is first required to understand the context for political involvement in the last financial meltdown.

The Federal National Mortgage Association—better known by its colloquial title, “Fannie Mae”—was founded during the Great Depression in 1938 and set up as a government business enterprise (though it has been publicly traded since 1968) akin to a Crown corporation in Canada. Its purpose was to raise levels of home ownership and the availability of affordable housing. It did this by creating a liquid secondary mortgage market which made it possible for banks and other loan originators to issue more housing loans than they otherwise might, this by purchasing mortgages insured by the Federal Housing Administration (FHA).

Similarly, the Federal Home Loan Mortgage Corporation, better known as “Freddie Mac,” was started in 1970, also by the US federal government but as a private corporation. Its mission was similar to that of Fannie Mae: to expand the secondary mortgage market in the US.

Thus, for the last four decades, these two lenders were technically private. However, and critically, they had always been granted *de facto* government guarantees and other favourable treatment that cut their borrowing costs. For example, federal government capital requirements for Fannie Mae and Freddie Mac were set low, at just 2.5%, compared to a 10% requirement for American banks. The favours were opposed by the rest of the financial sector and also to critics who thought the US government risked a future taxpayer bailout.

The role of Fannie Mae, Freddie Mac, Representative Frank, and other politicians in the American financial and housing debacle, is chronicled in a new book by Gretchen Morgenson and Joshua Rosner, *Reckless Endangerment—How Outsized Ambition, Greed, and Corruption Led to Economic Armageddon*.

Morgenson is a Pulitzer-prize winning business reporter for the *New York Times*; Rosner is now a managing director at a New York-based consulting

company. But back in 2001, he was part of a small six-person boutique research firm where he authored a report critical of the already-easy credit terms with which Americans could access home purchases, backed up by Fannie Mae and Freddie Mac.

In *Reckless Endangerment*, blame for the American financial crisis is properly attributed to both the government and the private sector (Wall Street became “irrationally exuberant” once again, to use a phrase applied in the 1990s by Alan Greenspan) though the former deserves even more blame than the conventional narrative admits.

Government encouragement of high-risk behaviour was everywhere. There is the already-noted lowered capital requirements applied to Fannie Mae and Freddie Mac; the book also explores the Carter administration’s *Community Reinvestment Act* which pushed financial institutions to lend more money to low-income Americans in the inner cities—the notion being that scarce lending in the inner cities was as result of racial discrimination and not straightforward risk calculations.

Some of that ground has been explored before, notably in two other books on the financial crisis: CATO Institute’s Johan Norberg’s *Financial Fiasco*, and the *Wall Street Journal*’s Nicole Gelinas’ *After the Fall*, both published in 2009.

However, a new theme emerges from *Reckless Endangerment*, that of Fannie Mae’s 1990s-era chief executive, James A. Johnson and how, which the authors chronicle in exceptional detail, Johnson engaged in internal high-risk corporate behaviour to massively expand Fannie Mae. In addition, publicly, he relentlessly attacked any critic that sought to cut Fannie Mae’s special government-granted privileges. The two approaches reinforced each other and Fannie’s “special relationship” with the US government: “Johnson’s command-and-control management of the mortgage finance giant and his hardball tactics to ensure Fannie Mae’s dominance amid increasing calls for oversight are crucial to understanding the origins of the worst financial debacle since the Great Depression,” write the authors.

Johnson, and those who followed him at Fannie Mae, spent tens of millions on campaign contributions, grants to potential allies, and lobbying efforts. It all helped thwart any attempt to put the company on a level playing field with other financial institutions. For instance, the company strategically supported a wide swath of American politicians, everyone from the aforementioned Frank on the left to Newt Gingrich on the right.

Also, Fannie Mae gave grants to low-income housing organizations who became reliable support-

ers of Fannie whenever Congress or some oversight agency questioned Fannie Mae’s internal finances. (It later emerged the books were rigged by over \$6 billion to ensure high bonuses for company executives). Such organizations could thus be counted on to block reform when someone raised the query of whether the plethora of Fannie Mae mortgages given to many low-income Americans was prudent.

Johnson moved on from the company in 1999, nine years before the US financial sector imploded, but the authors assert he was a major reason for the later housing and financial sector meltdown. “Johnson’s tactics were watched closely and subsequently imitated by others in the private sector,” Morgenson and Rosner wrote. Whether relaxed lending standards, the elimination of due diligence, repackaging junk loans, and, importantly, supporting disastrous Clinton-era political attempts to push for more home ownership even among those who by any sensible measure, could not afford one, Johnson and Fannie Mae were there first as “pioneers.”

As for the congressman from Massachusetts, when asked in 2005 whether his political blunting of traditional prudence in the financial sector was wise, whether this might not lead to mass mortgage defaults, he brushed off the question: “We’ll deal with that problem if it happens, said Frank.

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