FEDERALISM AND INTERGOVERNMENTAL FINANCIAL RELATIONS IN CANADA

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SCOPE AND CONTENTS: This thesis is concerned with the development and evolution of intergovernmental financial relations from the time of Confederation to the present day. The particular area of interest is the time from 1946 to 1968. The past quarter century has seen a powerful resurgence in provincial influence and increasing demands from the provinces for financial autonomy. The provincial revenues have been very much increased, but so too have their responsibilities. As Federal Government revenues have increased much more rapidly than Federal responsibilities the period has also been marked by considerable increases in payments from the Federal to the Provincial Governments. It is around the conditions attached to these increased payments that the majority of Federal-Provincial conflicts have been concentrated. The increasing degree of variation in economic wealth seen between the provinces, the increasing degree of urbanization,

and the rapid growth of provincial revenues, will all be considered. Possible solutions to the more serious and immediate problems are considered but no 'grand solution' is offered since it seems unlikely that any static solution could hope to satisfy the needs in a society as dynamic as Canada is, and will continue to be, for the remainder of this century.

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Introduction

Since the time of Confederation an important, perhaps the most important and persistent, problem of the Canadian federation has been that of intergovernmental financial relations. Although this area is of vital concern it has attracted very little attention from political scientists. This has been especially true of the period from the Second World War to the present day, perhaps because of the many more dramatic changes seen in Canadian politics during this period. This scholarly neglect is reflected in a dearth of literature dealing with this topic. Practical politicians are, however, well aware of the importance of this area of intergovernmental relations to the future of the nation but, because of the complexity of the subject, the discussions relating to fiscal matters are often obscured by a smoke screen of disagreement ostensibly about other matters, including interpretation of the British North America Act (B.N.A.) and "Provincial rights". The problem of achieving an equitable distribution of both revenues and governmental functions has continued to be, and no doubt will continue to be, the most persistent problem to plague the Canadian federation.

The paper will primarily be concerned with an analysis of the development and possible future of intergovernmental financial relations in Canada. The major hypothesis of the paper is that the wide and increasing variation in economic conditions and fiscal needs of the Canadian Provinces presents a greater threat to the continuation of

Canada as a nation than any other factor.

To demonstrate the changes in Canada since Confederation and to indicate the basis for many recent problems the history of inter-governmental financial relations from 1867 up to 1968 will be discussed. The major area of concentration will be the development of these relationships from the time of the Rowell-Sirois Report.[1] Much has been written about the Report and a study of the Report itself provides the most valuable source of knowledge on the subject of Federal-Provincial relations. The importance of financial arrangements can be judged by the attention paid to them by the Commissioners and by the briefs submitted by the Provinces. The Report provides the most comprehensive study of the Canadian federation ever prepared and the conclusions of the Commission, even if, for political reasons, they could not be implemented, show a great appreciation of the many problems, fiscal and otherwise, which then faced the Canadian people.

Students of Canadian politics interested in the pre Second World War developments would be well advised to consult not only the Report but also the briefs submitted by the Provinces. In addition the minutes of the Dominion-Provincial Conference which met, briefly and bitterly, in January, 1941 to discuss the Report are most valuable.[2] The deep concern of the ten Governments involved and the hostility inherent in the relationships which are the interest of this paper are nowhere better demonstrated than in these minutes. A valuable study of the methods of providing

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[1] The Report of the Royal Commission on Dominion-Provincial Relations. Issued in three volumes by the Kings Printer, Ottawa, 1940.

[2] The Proceedings of the Dominion-Provincial Conference, January 14-15th, 1941. Ottawa, Kings Printer, 1945.

Federal subsidies to the Provinces is to be found in a study by J. A. Maxwell.[1] The development of conditional grants in the pre War period can be traced in the study by Luella Gettys.[2] Among the many studies prepared for the consideration of the Commission, the work by Eggleston and Kraft[3] covers the development of fiscal relations from 1867 to 1939 and well demonstrates the "ad hoc" nature of many of the Dominion-Provincial agreements. The number of final settlements is quite remarkable. Professor Corry's work, also prepared for the Commission,[4] deals with problems of divided jurisdiction. An invaluable source of references dealing with the period from pre-Confederation to 1946 is provided by Wilfred Eggleston.[5] A detailed study of the problems faced by the three levels of government, along with a discussion of the steps taken to maximise the war effort is presented in a 1949 study by A. E. Buck.[6] The massive expansion of government activities, even before the War can be seen in the work by Corry.[7] With the advent of World War Two the

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[1]J. A. Maxwell, Federal Subsidies to the Provincial Governments in Canada, Cambridge, Harvard University Press, 1937.

[2]Luella Gettys, The Administration of Canadian Conditional Grants, Public Administration Service, Chicago, 1938.

[3]Wilfred Eggleston & C. T. Kraft, Dominion-Provincial Subsidies and Grants, A Study Prepared for the Royal Commission on Dominion-Provincial Relations, Ottawa, 1939.

[4]J. A. Corry, Difficulties of Divided Jurisdiction, A Study Prepared for the Royal Commission on Dominion-Provincial Relations, Ottawa, 1939.

[5]Wilfred Eggleston, The Road to Nationhood, Toronto, Oxford University Press, 1946.

[6]A. E. Buck, Financing Canadian Government, Public Administration Service, 1949.

[7]J. A. Corry, The Growth of Government Activities since Confederation, A Study Prepared for the Royal Commission on Dominion Provincial Relations, Study No. 2, Ottawa, 1939.

spate of works abated, and did not recommence with the War's end.

It is clear, therefore, that a considerable amount of scholarly energy has been devoted to the study of the Rowell-Sirois Report and to the period prior to 1946. Since there is this wealth of literature this paper will concern itself only briefly with the years from 1867 to 1946, whereas the area of major concern will be the period from 1946 to 1968. Since the constitutional division of revenue-raising power[1] and governmental functions have proved to be so important it will be necessary to give a brief résumé of these provisions, and subsequent legal interpretation.

Perhaps one of the most serious deficiencies in post war studies of Canadian politics has been the lack of concern shown to the problems of intergovernmental financial relations. There have been periods following Federal Provincial Conferences or the signing of new Tax Agreements when considerable interest has been shown, especially by economists and public administrators, but no comprehensive study has been undertaken since the Rowell-Sirois Report. There is no post War study to compare with those of Maxwell or Eggleston in the 1930's and 1940's. Since this field is so obviously vital to the functioning of a federal nation, as evidenced by the continued conflict in Canada, Australia and the United States, and the more intensive study now being devoted to this topic, especially in the U.S.A., it is to be hoped that political scientists interested in Canada will note the importance of the problem and devote to it the attention it deserves. The rapid and increasing rate of expansion of the

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[1]Especially important is Section 92 (2) of the B.N.A. Act which allows the Provinces to impose "Direct Taxation within the Province in Order to the Raising of a Revenue for Provincial Purposes."

expenditures of the Provincial and Municipal Governments, up to 46.4% of total Government revenues by 1967-69,[1] compared with a much slower growth in Federal Government revenues gives some indication of the changes which are occuring in the Canadian society and gives some indication of the need for substantial readjustment to the existing structure of fiscal relationships. During the same time period the acceptance of the fact that government must now accept much more responsibility than formally in such fields as maintaining a high and stable level of employment and in many social services has meant that, as in all developed nations, considerable adjustments have had to be made in the machinery for intergovernmental and international co-operation.

Reports of Federal-Provincial Conferences, especially the 1969 Conference, give insight to the continuing nature of the problem, and of the manner in which fiscal matters are often confused by political manoeuvering of a high order. The Canadian Tax Foundation often publishes reports of its meetings and also publishes a great deal of literature which deals with the more technical aspects of the division of revenues and expenditure.[2] There have also been articles published in Canadian Public Administration which assist in providing viewpoints, again of a technical nature, which are useful in providing the groundwork for a

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[1] Federal Provincial Grants and the Spending Power of Parliament, Government of Canada Working Paper 1968, P. 8.

[2] A. M. Moore & J. H. Perry, Financing Canadian Federalism, Canadian Tax Foundation, Toronto, 1953. Canadian Tax Foundation, Report of the 1967 Conference, Toronto, 1967. G. V. LaForest, The Allocation of Taxing Power under the Canadian Constitution, Canadian Tax Foundation, Toronto, 1967.

study such as this.[1] The major difficulty encountered in a study of this nature is the dearth of studies undertaken by political scientists. Many works by leading political scientists include a chapter on problems relating to Federal Provincial relations, including the fiscal difficulties, but most pay little attention to the important dynamic aspect of fiscal relations.[2] There are occasional articles in the Canadian Journal of Economics and Political Science which do deal with specific problem areas but Canada lacks a definitive work, by a political scientist, on the political aspects of the system of intergovernmental financial relations in Canada.[3] In addition to articles in the various journals works relating to the general problems of federal finance are valuable. The problems faced by Canada are not unique to her but are present, to a greater or lesser extent, in all federal nations. The study by Heller[4] gives an analysis, primarily from the viewpoint of an economist, of the

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[1]A. R. Kear, "Co-operative Federalism: A Study of the Federal-Provincial Continuing Committee on Fiscal and Economic Matters," Canadian Public Administration, March, 1963. E. R. Black & A. C. Cains, "Different Perspectives on Canadian Federalism", Canadian Public Administration, March, 1966.

[2]See R. M. Dawson, The Government of Canada, Revised by Norman Ward, 4th Edition, University of Toronto Press, 1967. Paul Fox, (ed.) Politics: Canada, Toronto, McGraw-Hill, 1966. J. A. Corry & J. E. Hodgetts, Democratic Government and Politics, 3rd Ed., Toronto, University of Toronto Press, 1959.

[3]R. Dehem & J. N. Wolf, "Principles of Federal Finance and the Canadian Case", Canadian Journal of Economics and Political Science, February, 1955.

[4]W. Walter Heller, New Dimensions of Political Economy, Harvard, University of Harvard Press, Cambridge, Mass., 1966.

problems of taxation and administration in a federal nation. Harold W. Groves has edited an interesting, if somewhat dated, study, on a similar topic seen from the perspective of a public administrator.[1]

Sources of primary material for this study will include submissions to Royal Commissions, Rowell-Sirois and Taxation Commissions in particular, and especially submissions by the Provinces; Debates in the House of Commons and Provincial legislatures will also be of use. The reports of the Federal-Provincial Continuing Committee on Fiscal and Economic Matters provide an ongoing account of the many problems as solutions to them are sought. The minutes and reports of Federal-Provincial Conferences provide probably the best indication of the stress which occurs between the Federal Government and the Provincial authorities, either generally or between a particular Province or group of Provinces and the Federal Government.

Chapter One will involve a brief discussion of the history of Federal-Provincial intergovernmental relations from the time of Confederation to the Rowell-Sirois Report. The more important revenue raising powers granted to the governments by the British North America Act and subsequent judgements of the Judicial Committee of the Privy Council and the Supreme Court will also be considered. The second chapter will be concerned with developments in the field of intergovernmental financial relations since World War Two and with their effects on the Federation. The various methods of financing the federation will be discussed in Chapter Three, as will possible solutions to the more serious

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[1]Harold W. Groves, (ed.), Viewpoints on Public Finance, University of Wisconsin, Henry Holt & Company, New York, 1950.

problems in the area of study. The experience of other federal nations, Australia and the U.S.A. in particular, will be referred to in this chapter.

It is not probable that any comprehensive plan can be drawn up to meet the major problems in this vital, if restricted, field of Canadian government. In fact, given the ethnic, industrial and geographic diversity of Canada the problems may prove to be virtually insoluble. It is, however, possible to suggest ways to allieviate the more serious difficulties in the field of intergovernmental financial relations and thus in intergovernmental relations generally.

I 1867 to 1946: The Basis is Set

The United States of America was probably the most important single force which led to the federation of the Canadian colonies. The military threat of one of the most powerful armies in the World and the example of economic advance based on the frontier were both great incentives for the provinces to unite. Changes within the British Empire which allowed more freedom to the colonies but at the same time removed the protection of Imperial Preference also led the colonies to consider other means of finding expanding markets. The ending of the Reciprocity Treaty with the United States meant that some form of expanded trade links were essential if the provinces were to advance. The Province of Canada needed to expand; she needed access to the sea, the Maritimes were already feeling the effects of competition from the new steam powered boats, and a decline in demand for wood. The first moves towards some kind of union came from the Maritime Provinces, they felt the need for closer links both between themselves and with Canada. The railway was seen as the potential saviour of the colonies. If co-operation could be ensured and a trans-continental railway constructed it was felt that many of the benefits seen in the United States would acrue to a Canadian nation. The ethnic division within the Province of Canada continued to cause great stress, the French fears of cultural and religious absorption led to internal political deadlock. The political ambitions of such men as Sir John A. Macdonald were also most important in bringing about the

Confederation. It was inevitable, then, that the Canadian Constitution would reflect the ethnic diversity of the country, its protection of the French language and religion, in particular, was essential if there was to be a Canadian nation. The many political pressures and negotiations which led to the British North America Act (B.N.A.) are too well known to require reiteration here. It is, however, important that the economic forces which operated at the time should be considered.[1]

In the years prior to Confederation the expansion of the provinces had been somewhat retarded by economic and financial difficulties. The large debts incurred for development by the provinces and their need for yet more credit if they were to continue to expand, had led to their competing against one another on the London money markets. Much of the development, which was concentrated on the railways, was economically unsound, but, spurred on by the example of railway expansion in the U.S.A., provinces continued to lend large sums for railway construction. By 1866 the Province of Canada had loaned $33 million and the municipalities $7 million for railway development. Most of this debt was uncollectable.[2]

The population of the colonies at the time of Confederation was only three and a half million. Eighty % of the population was rural, with Montreal being the largest city, with a population of 100,000 and Toronto next with some 50,000.[3] Manufacturing and handicraft industry was concen-

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[1]See W. A. Mackintosh, The Economic Background to Dominion-Provincial Relations, Appendix Three to the Report of the Royal Commission on Dominion-Provincial Relations, The Kings Printer, Ottawa, 1939.

[2]The Report of the Royal Commission on Dominion-Provincial Relations. Book 1, Page 25.

[3]Ibid. Page 21.

trated in Ontario, but even there they made up only 14% of the work force. Fish still made up to 40% of Nova Scotia's exports and lumber 70% of New Brusnwicks.[1]

Even when it had been decided, that Confederation was economically desirable the means of achieving union were by no means clear. Given the accepted needs for expanding markets to replace those which were, for political and economic reasons, becoming closed to them, it was essential that there be a large free trade area. To maintain and protect such an area, and to prevent inter-provincial customs competition, it was essential that the central government should have exclusive powers over customs and excise revenues. However, all the provinces were heavily reliant on these duties to meet the costs of government. In the fiscal year ended in 1866 the Province of Canada derived 60% of its revenue from these duties, Nova Scotia 80%, New Brunswick 78% and Prince Edward Island 75%.[2] The records of the Quebec Conference clearly show that the Fathers of Confederation were faced with a clear choice between allowing the provinces extensive powers in the field of indirect taxation or of the Dominion government being obliged to pay subsidies to the provinces. The arguments with regard to customs revenues applied, to a considerable extent, to indirect taxation as well since the provinces could have used tax rates competitively. It was therefore decided, reluctantly, that some form of subsidy would have to be paid. The Fathers were convinced, however, that the subsidy need only be small and that

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[1]Ibid. Page 24.

[2]Wilfred Eggleston and C. T. Kraft, Dominion-Provincial Subsidies and Grants, A Study Prepared for the Royal Commission on Dominion-Provincial Relations, Kings Printer, Ottawa, 1939, P. 1.

it could be fixed for all time. The principle of equality of treatment for all provinces was satisfied by the eventual agreement that the subsidy would be on a per capita basis. Once this had been accepted the amount of the subsidy had to be calculated. It was expected that the provinces would be very much the junior governments, little more than "glorified municipalities", and that their expenses would, therefore, not be great. The clear intention was that any Dominion subsidy would be small in amount and of a temporary nature. After some complicated, and most unrealistic, calculations it was discovered that Nova Scotia could, after redistribution of the constitutional obligations, execute her functions fully if the Dominion would meet her deficit of only $264,000. Calculated on the basis of the 1861 population of the Province this was only 80¢ per capita. This sum, it was agreed, would be paid to all provinces based on the population in 1861. A special exception had to be made with regard to New Brunswick since this Province was very much in debt, 38% of her current revenues being required to meet interest payments,[1] and a special grant, limited to a period of ten year, of $63,000 per annum was agreed upon. The Dominion was to assume provincial debt and most assets.[2] Provinces with relatively lower debts than the average were to be compensated by means of a debt allowance. Nova Scotia and New Brunswick had per capita debts of approximately $25 and Canada debts of $27. The allowance was set at $25 but in recognition of New Brunswick's special problems she was

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[1] J. A. Maxwell, Federal Subsidies to the Provincial Governments in Canada, Cambridge, Harvard University Press, 1937, P. 12.

[2] British North America Act (B.N.A.) 1867 Section 111.

granted $7 million instead of the $6.3 to which she would have been entitled if the formula has been fully applied. The provinces were to receive a payment of 5% on the amount by which their debt exceeded it. Allowances were also to be paid to cover the costs of government in each province. Ontario was to receive $80,000, Quebec $70,000, Nova Scotia $60,000 and New Brunswick $50,000.[1]

TABLE 1:1

	Per Capita Subsidy	Grants in Support of Government	Special Grant for 10 Years Only	Total
Ontario	$1,116	$ 80		$1,196
Quebec	890	70		960
Nova Scotia	264	60		324
New Brunswick	202	50	$63	315
	$2,472	$260	$63	$2,795

The division of the taxing powers in the B.N.A. serves to demonstrate the way in which the Fathers had hoped to form a centripetal federation. Direct taxation was not, at that time, an important revenue source, and there was little reason to think that it might become so. It was not considered that the provinces would be in need of any substantial revenues and so, by Section 92 (2) of the B.N.A. Act the Provinces were allowed only to impose "Direct Taxation within the Province in Order to the Raising of a Revenue for Provincial Purposes." The Dominion Government

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[1] Ibid. Section 118.

was, however, to be allowed to undertake "The Raising of Money by any Mode or System of Taxation."[1] Speeches made by leading politicians of the time also indicate their desire to see, if possible, the creation of a strong central government. Galt reflected this desire especially well "We would all have desired a legislative union (i.e. unitary state) and to see the powers concentrated in the Central Government as it exists in England, spreading the aegis of its protection over all the institutions of the land, but we found it impossible to do that at first."[2] This same intent can be seen in the Peace Order and Good Government provision of Section 91 and the enumeration of provincial powers, including "Generally all Matters of a merely local or private nature within the Province."[3] The Dominion Government was to govern, "in relation to all Matters not coming within the Classes of Subjects assigned exclusively to the Legislatures of the Provinces."[4] In other words, unlike the situation in the United States, the federal government was the one which was to be most powerful and was to have the residual powers under the constitution. The powers given to the provinces to regulate Property and Civil Rights[5] did, however, prove to provide the Judicial Committee

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[1] B.N.A. Act, Section 91, (3).

[2] Canada, The Parliamentary Debates on the Subject of the Confederation of the British North American Provinces. Reproduction, Kings Printer, Ottawa, 1950, P. 263.

[3] B.N.A. Act, Section 92, (16).

[4] Ibid. Section 91.

[5] Ibid. Section 92, (13).

of the Privy Council with a convenient method whereby the powers of the provinces could be much extended.

The details of certain of the individual judgements of the Committee will be considered in this Chapter, before we deal with the more complicated matter of many of the intergovernmental fiscal agreements. The majority of cases heard by the Judicial Committee involved areas where the constitution allowed some degree of "overlap" in the jurisdiction of governments. Most conflict of this nature was concentrated on interpretations of Section 91, the Peace, Order and Good Government power given to the Dominion, and Section 92 (13) which allowed the provinces the power to deal with Property and Civil Rights.

In the case of Russell vs. the Queen, 1882,[1] the Committee essentially supported the powers of the Dominion when that Government acted for the purpose of protecting "public order, safety or morals." In later cases the provinces were able to prove that they had considerably more power than was intended by the Fathers of Confederation. In 1883 in Hodge vs. the Queen,[2] the Committee held that provincial legislatures were not "mere agents" of the Dominion but were "supreme within the fields of their respective jurisdiction."[3] Of particular interest to this paper was the ruling in the Bank of Toronto vs. Lambie[4] in which the Committee declared intra vires an Act of the Quebec Legislature

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[1]Privy Council, (1882), 7 A.C. 829.

[2]Privy Council, (1883), 9 A.C. 117.

[3]Peter H. Russell, (ed.), Leading Constitutional Decisions, the Carleton Library Series, No. 23, McClelland and Stewart, Toronto, 1965, P. 19.

[4]Ibid. P. 143.

which imposed a direct tax on a Dominion chartered corporation.[1] The decision in Russell vs. the Queen was to all intents and purposes overthrown by the case of the Attorney General of Ontario vs. the Attorney General of Canada and the Distillers and Brewers Association of Ontario, 1896.[2] This case established that whereas the Dominion had considerable powers, in the event of a national emergency, these powers could not be used to usurp the constitutional powers of the provinces under normal circumstances. Section 91 could not, and cannot, be used to allow the Dominion to legislate on any matter allowed to the provinces simply by declaring that a particular matter affected the peace, order or good government of Canada. By the end of the Century the Privy Council had, by its interpretation of the B.N.A. Act, considerably increased the powers of the provinces. Being bound by the British legal tradition they were bound by the rules of precedent relating to past cases heard before them and relating to all the Empire, and not simply to the Canadian situation. The result was a federal state which was very different from that desired by such men as Galt and Macdonald. Much of the strength, and weakness, of the Constitution and its ability to meet the demands of this Century can be attributed to the manner in which the lines of authority drawn by the B.N.A. Act have not remained as rigid as planned by the Fathers of Confederation. To save later confusion it will be as well to deal here with the Judicial interpretation of the Constitution, from 1867 to the present day, since it has obviously had a profound effect on all aspects of intergovernmental relations.

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[1] Privy Council, (1887), A.C. 575.

[2] Privy Council, (1896), A.C. 348.

The Fathers of Confederation do not appear to have paid any great attention to the matter of judicial review. Even with the example of the United States Supreme Court before them there was little explicit recognition of the importance of the Judicial Committee of the Privy Council which was, of course, to be the final Court of Appeal for Canada. There was some attempt made, following the creation of the Supreme Court of Canada, to restrict appeals to the Privy Council. This, however, was frustrated by politicians who were determined to retain the British connection. As we have seen the early decisions of the Judicial Committee of the Privy Council tended to favour the extension of Provincial powers. There have been many criticisms made of the Committee in this regard, many of them based on the manner in which their Lordships adhered rigidly to the Anglo-Saxon rules of precedent. Thus, by the British legal tradition by which they were bound, the Judges interpreted the very words of the Act, and not the intention of the Fathers of Confederation. Their duty, as they saw it, was 'to interpret, not to enact'.[1] The question was not what was supposed to have been intended but rather what had been said (in the Act). Their Lordships were much more rigid in their interpretation of the B.N.A. Act than were the Justices of the Supreme Court in the United States. Much of the criticism of the Judicial Committee has, however, been exaggerated. Professor Brady has maintained that the early decisions reflected, rather than caused, the upsurge in provincialism. The decisions "[G]ave judicial expression to the upsurge of provincialism, evident from the early eighties to the decade after the First World War".[2]

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[1]Dawson, Op. Cit., P. 145.

[2]Steven Muller, "Federalism and the Party System in Canada", in J. Peter Meekison (ed.), Canadian Federalism: Myth or Reality? Methuan, Toronto, 1968, P. 121.

Most intergovernmental conflict which reaches the Courts in Canada is, as we have seen, based on various interpretations of Sections 91 and 92 of the B.N.A. Act. The decision as to whether a matter of property and civil rights (Section 92) and therefore a provincial responsibility, or one relating to the peace, order and good government of Canada, (Section 91), and therefore a matter for the Dominion Government, is a fine one.

The decision in the Russell case[1] which allowed the Dominion Government considerable power vis a vis the provinces, caused considerable difficulty in deciding later cases. If this decision had stood the Dominion Government would have been placed in a position of extreme dominance. All the Dominion Government would have been required to do, in order to legislate in a particular area, would have been to declare that the matter involved was a matter of concern to the peace, order or good government of Canada, for its legislation to stand. This would have placed the Dominion Government in a position as strong as that which Commonwealth Government in Australia was to acheive under the Australian Constitution at the turn of the century. Such a position would, however, have been quite inappropriate in Canada, divided as the nation is on ethnic and economic grounds. Such a solution would have flown in the face of the wishes of all provinces, and not just those of Quebec, and would, without doubt, have led to an increase in intergovernmental conflict. The sixteen enumerated exclusive powers of the provincial legislatures would, presumably, have been secure in the absence of a national emergency. Dawson felt that the Judicial Committee's ".... enlargement of provincial rights

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[1] Privy Council, (1882), 7, A.C. 829. See Peter H. Russell, Op. Cit., P. 2.

in the decades before and after the turn of the century was not as shocking as many would like to believe, and it appears to have been in substantial accord with the general trend of opinion in Canada."[1]

In the Board of Commerce Case, 1922[2] Lord Haldane suggested that the Russell decision was only justified because of abnormal or emergency conditions. Later cases were, therefore, to be decided on this basis. It was made clear, at this time and in later cases, that the Dominion Government could only use the peace, order and good government power in times of real emergency. As the Judge's interpretation of what was and what was not an emergency did not always coincide with the interpretation of either the governments or the population as a whole conflict was inevitable. The fact that the final Court of Appeal was so removed from Canada also did little to endear it to many Canadians.

The Dominion was, of course, quite secure in the operation of emergency powers during the First World War. In the Fort Francis Pulp and Paper Co. vs. the Manitoba Free Press Case, 1923[3] the Dominion Government action in controlling the price on newsprint was declared intra vires[4] due to the war-time emergency. Viscount Haldane held that, "It is clear that in normal circumstances the Dominion Parliament could not have so legislated as to set up the machinery of control over the paper manufacturers which is now in question."[5] He found that, under conditions

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[1]Dawson, Op. Cit., P. 145.

[2]In Re The Board of Commerce Act, 1919, (1922), A.C. 191. Martha Fletcher, "Judicial Review and the Division of Powers in Canada", in Meekison, Op.Cit., P. 145.

[3]Privy Council, (1923), A.C. 695.

[4]Within the Dominion power.

[5]Russell, Op. Cit., P. 33.

of war, Section 91 of the B.N.A. Act could be interpreted as providing for such an emergency. This did not, of course, remove the provincial responsibility for property and civil rights, or for any of their enumerated powers, but simply increased the authority of the Dominion Government for the duration of the emergency.

A somewhat broader view of Dominion Government powers was given in the Radio Case, 1932.[1] In 1927 the Dominion Government had, without reference to Britain, signed an International Radio Telegraph Convention. This case arose as the result of a reference made by the Dominion Government to the Judicial Committee in order that the right of the Government of Canada in matters of this kind could be made quite clear. Quebec maintained that matters such as this should be decided on the basis of the division of powers under Sections 91 and 92 of the B.N.A. Act. This view was rejected. It was held that, as the Fathers of Confederation could not have been aware of such developments, the powers to make such treaties must be brought under Dominion control via the residuary power of Section 91. This was, of course, an important case in that there could not be reference to precedent, it had, rather, to be decided on the basis of common sense and the political realities of the situation.

Thus, as Canada entered the crucial 1930s the Judicial Committee of the Privy Council had been very influential in setting the pattern of intergovernmental relationships in the country. There had been a considerable clarification of the rights and duties of both major levels of government and guidelines had been laid down by which all governments

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[1] Privy Council, (1932), A.C. 304. See Russell, Op. Cit., P. 133.

could assess as to whether a particular Act of Parliament or a provincial legislature was in accord with the B.N.A. Act. The powers of the Dominion in times of emergency were now also thought to be clear. The difficulty, during the depression, was to decide when an emergency in fact existed. There was some indication, however slight, that the Committee was more prepared to treat each case as it arose and to show a greater degree of flexibility than hitherto. The Judges were, of course, allowed a certain degree of flexibility in their interpretation of the B.N.A. Act. In the formulation of any constitutional document there will be, of necessity, many words of a general and abstract nature. Thus such expressions as 'property and civil rights,' 'trade and commerce,' 'peace, order and good government' and 'any mode or system of taxation,' have all led to conflict between governments in Canada. Each case heard has allowed the Judiciary an opportunity to interpret the wording of the Act and of later decisions. Such interpretations will, of course, alter over time and in the light of developments in the attitude of the society to such matters as social welfare and the role of government in the life of the community. The judgements of the Committee, and of the Supreme Court of Canada in later years, were, in addition, influenced by the very much increased independence of Commonwealth nations which was recognised by the Statute of Westminster, 1931.

The Judges, when asked to decide on an issue between governments, have, firstly, to decide upon the nature of the subject matter involved. Once this has been done, to discover what previous interpretations of the B.N.A. Act and later Acts have been. It would be a most unusual case

in which both these issues were clear. The more usual condition is one in which the final decision reached is only one of several closely competing alternatives. Try to avoid it as they may, and it is doubtful if they all did, the Judges make as well as interpret, law. Even though the Judicial Committee of the Privy Council was considerably more restrained than the Justices of the Supreme Court in the United States it did have a profound effect on the growth and development of the Canadian Constitution, the British North America Act.

The decision as to when the Judges must be narrow in their interpretation and when a more generous interpretation is called for must always be a difficult one. Sir Frederick Pollock has written:-

> "The most delicate problems of judicial craftsmanship is no doubt that of determining when it is wise to decide a matter on the narrowest possible basis and when it is both legitimate and salutary to grasp the opportunity to formulate general principles in the hope that they may have an influence extending far beyond the immediate case. Every great judge from Coke and Marshall to our own day has been confronted with the dilemma and dilemma it will necessarily remain in every successive case in which the problem arises. The skill with which the dilemma is resolved is perhaps the ultimate test of both judicial craftsmanship and judicial statesmanship."[1]

The task of Judges in interpreting the B.N.A. Act during this Century was made more difficult by certain of the Judgements arrived at in the early years of Confederation. In particular the problem of deciding what constituted emergency or abnormal conditions remained. The definition of emergency conditions which was used by the Judicial Committee was to cause

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[1] C. Wilfred Jenks, Craftsmanship in International Law (1956), 50, American Journal of International Law, 32, at PP. 59-60. Quoted by W. R. Lederman, The Courts and the Canadian Constitution, Carleton Library Series, No. 16, McClelland and Stewart, Toronto, 1964, P. 171.

considerable conflict between the Judiciary and Parliament during the depression years. Much of the Bennett 'New Deal' legislation was challenged in the Judicial Committee. The attempts to deal with the depression, in particular the Weekly Rest and Industrial Undertakings Act, the Minimum Wages Act and the Limitation of Hours Work Act, were justified by the Dominion Government on the grounds that there was an emergency situation, the depression, to meet. The Judicial Committee refused to accept this argument and thus many of the steps designed to ease the situation of the unemployed were frustrated. The Employment and Social Insurance Act was also declared invalid since it was held to be in conflict with the provincial duty in relation to property and civil rights.[1]

Many Canadians felt that this 'alien Court' would only allow the Dominion Government to assume emergency powers to meet conditions of war of public drunkeness, (the Russell Case). Their Lordships held that the conditions of the depression were not so serious as to qualify under the precedent established in earlier cases. In the Attorney-General for Canada vs. Attorny-General for Ontario, (Labour Conventions Case),[2] it was held that no overriding emergency existed. Their Lordships stated that:-

> "It is only necessary to call attention to the phrases in the various cases, "abnormal circumstances", "standard of necessity", (Board of Commerce Case (1922) 1 A.C. 191), "some extraordinary peril to the national life of Canada," "highly exceptional", "epidemic of pestilence", (Snider Case, (1925) A.C. 396), to show how far the present case is from the conditions which may overide the normal dis-

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[1]Attorny-General for Canada vs. Attorny-General for Ontario (Employment and Social Insurance Act Reference, (1937), A.C. 355.

[2]Martha Fletcher, Op. Cit., P. 147.

tribution of powers in sections 91 and 92."[1]

The depression may not have qualified as an "epidemic of pestilence" but with unemployment as high as 14.9%[2] in 1933 it must surely have been "highly exceptional" and there was certainly a "standard of necessity".

The importance of the actual wording of a Constitutional Act, such as the B.N.A. Act, can be judged by the different pattern of development seen in two Commonwealth nations, Canada and Australia.

The Australian Constitution, the Commonwealth of Australia Constitution Act, 1900, was very similar to the B.N.A. Act. Chamberlain, speaking in the Westminster Parliament, introducing the Commonwealth Bill said, "I do not think the main features of the Australian Commonwealth will differ materially, after all, from the Canadian Constitution of 1867. It is true that in Canada the general powers are reserved to the Dominion Parliament, while only specified powers are given to the Provincial Parliaments, but the latter have among them those specified powers the widest powers for dealing unreservedly with property and civil rights. Therefore rather technically than in substance is there a difference between the Provincial Legislatures in Canada and the States in Australia."[3] Developments during the depression were to prove, however, that there were quite important differences between both the Constitutions and political culture of the two Nations. The Commonwealth Government in Australia was much better equiped to deal with the problems of the

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[1]Labour Conventions Case, (1937), A.C. 327.

[2]A. E. Graur, Op. Cit., P. 12.

[3]H. S. Nicholas, The Australian Constitution, Second Edition, The Law Book Company of Australia, Melbourne, 1952, P. 12.

depression. As we have seen much of the Bennett 'New Deal' legislation in Canada was invalidated by the Judicial Committee of the Privy Council. In Australia, as we shall see later, quite radical steps were taken in Australia, including the formation of the Commonwealth Grants Commission and the Australian Loans Council, to deal with the problems of the depression and the less developed areas. These changes were eventually to prove to be strong centralizing factors. They were possible not only because of the homogeneous nature of the Australian population but also because of the provisions of the Constitution. It had been the intention of the politicians to create a strongly centralized federation. In this they were successful, much more so than in the Canadian case. In particular Section 109 of the Australian Constitution states that "When a law of a State is inconsistent with a law of the Commonwealth the latter shall prevail, and the former shall, to the extent of the inconsistency, be invalid."[1]

During the War the regional governments in both Canada and Australia lost the all-important right to impose income tax. In Canada, as we shall see in detail elsewhere, this was by agreement under the Wartime Tax Suspension Agreements. In Australia the Commonwealth Government was powerful enough, both under the Constitution and in political power, to force the States to cooperate. Section 109 allowed the Commonwealth Government to declare that it would cease to pay grants to State Governments which continued to impose income tax. This was appealed to the High Court but the appeal was rejected.[2]

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[1]K. C. Wheare, Federal Government, Third Edition, Oxford University Press, London, 1956, P. 112.

[2]Ibid. P. 107, South Australia vs. The Commonwealth (1942) 65, C.L.R. 373.

It may appear that there was little practical difference between the positions of both central Governments during the war years. In fact, during the emergency conditions, the Dominion Government was very powerful indeed. The difference in the strenghts of the two Governments was seen, however, much more clearly in the immediate post-war years. In Australia, by use of the grant power, allowed by Section 96, and by use of Section 109, the Commonwealth Government was able to retain the exclusive use of the income tax power. In Canada the Dominion Government found itself unable to pursuade the provinces to allow it the exclusive use of the income tax. The notable difference, is, of course, that the Dominion Government did not legislate on this matter, but, realizing the probability of intense political conflict if it had attempted to attain its objective by this method, it attempted to pursuade to provinces to cooperate. The pre-war judgements did indicate, in any case, that the Privy Council might well have refused to accept that the war time emergency conditions remained for very long after the war, in which case the provinces would retain their power to impose direct taxation. The Commonwealth Government, secure in its position because of its Constitutional position and High Court Judgements, was able to rely on the legal enforcement of its will.

There was a considerable change in the interpretation of the emergency doctrine in relation to the B.N.A. Act during the post war period. Instead of a rigid requirement that certain extreme external conditions be met it was now the nature of the legislation itself which was to be the basis of the decision. Viscount Simon held that:-

> [T]he true test must be found in the real subject matter of the legislation: if it is such that it goes beyond local or provincial concern or interests and must from its inherent nature be the concern of Dominion as a whole... then it will fall within the competence of the Dominion Parliament as a matter affecting the

> peace, order and good government of Canada, though it may in another aspect touch on matters specially reserved to the provincial legislatures....It is the nature of the legislation itself, and not the existence of an emergency, which must determine whether it is valid or not.[1]

The Supreme Court of Canada, when it became the Final Court of Appeal, in 1949, was faced with a position in which there was considerable doubt as to when the Dominion Government would be entitled to exercise its emergency powers. The precedents, to say the least, were confused. "The Supreme Court is no longer bound to accept Privy Council pronouncements as the premises for its own reasoning."[2] It is too early, as yet, to tell how the Court would react to any Federal attempt to extend its power via the emergency power in Section 91. Thankfully there has been no period of acute emergency since 1949. "The score or so of decisions in the last decade provide reasonable evidence of an intention to adopt a policy of gradual adaption of Privy Council decisions and doctrines."[3]

Mr. Justice Taschereau had called for the application of 'common sense' in deciding as to when there is an emergency situation or not.[4] Two important recent cases have given little real indication of possible future decisions of the Court. The ruling in the National Capital Act was clear,[5] the creation of a 'green belt' around the national capital was

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[1]Martha Fletcher, Op. Cit., P. 148. Attorney-General for Ontario vs. Canadian Temperance Federation, (1946), A.C. 196.

[2]Lederman, Op. Cit., P. 175.

[3]Ibid. P. 175.

[4]Martha Fletcher, Op. Cit., P. 149.

[5]Ibid. P. 150. Munro vs. National Capital Commission, (1966), S.C.R. 663.

obviously a matter of national concern. The Off-Shore Mineral Rights Reference, decided in 1967, was firm in deciding that these rights belonged exclusively to the Federal Government.[1] There has, however, been no major decision as to the interpretation of rights under Sections 91 and 92.

It can be seen, therefore, that any Act of Parliament, the B.N.A. Act included, may be exposed to considerable variations in interpretation over a number of years. It is also clear that neither the Judges nor the Fathers of Confederation operated in a vacuum but were influenced by the political realities of the situation. If the pre-war emergency doctrine had been rigidly adhered to in the post 1946 period it is certain that this could have led to a considerable increase in intergovernmental conflict. The changes seen since the Supreme Court assumed the role of Final Court of Appeal have not been great. There are, however, some indications that there will be a continuation of the trend away from the rigid method of interpretation followed by the Judicial Committee. This is not, of course, to suggest that the Judges of the Supreme Court are politically motivated or biased. They are, however, much more likely to be aware of the pressures and tensions within the Nation than are a group of Judges, however learned they may have been, living thousands of miles away.

Returning to the position in 1867 the acceptance of the unrealistic 80¢ per capita payments, and the payment of the special grant 'for ten years only' to New Brunswick, were supposed to be in full and final settlement of provincial demands. No province in financial difficulty

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[1]Ibid. P. 151. Reference Re Ownership of Mineral Off-Shore Rights, 65, D.L.R. (2nd), 353.

was to expect assistance from the Dominion but would have to bring its revenues and expenditures into line, either by reducing the costs of government or by use of the direct taxing power. With the benefit of hindsight it can clearly be seen that there was little real hope of these intentions being realized. Nova Scotia was soon forced, not by inefficiency but by sheer fiscal need, to seek better terms. In 1869 Nova Scotia was placed in the same position as New Brunswick, for without these better terms her budget could not be balanced.

In the years 1870, 1871 and 1873 the provinces of Manitoba, British Columbia, and Prince Edward Island joined the federation. While paying lip service to the principle of equality of treatment for all provinces, political realities were accommodated by means of generous interpretations of the various provisions and agreements. If a per capita payment of 80¢ had been the actual unit of calculation British Columbia, with a population of 9,000 whites and 25,000 Indians and Chinese, would never have joined the federation. It was therefore "assumed" that the Province had a population of 120,000. This allowed the Dominion to allocate $213,000 a year, which included the per capita payment on the fictitious population and a grant of $35,000 to meet the costs of government.

The total increase in payments made by the Dominion was not, in monetary terms, very great during the 1867 - 1914 period. The importance of the payments lies not in the amounts involved (from $2.2 million in 1867 to $12 million in 1913),[1] but in the fact that a precedent had been set for later demands. The percentage of provincial revenues derived from

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[1]Wilfred Eggleston, The Road to Nationhood, Toronto, Oxford Univer-Press, 1946, P. 82.

the Dominion was approximately 60% at Confederation, about 35% by 1890; by 1920 it was to fall to less than 20%.[1]

The provincial claims on the Dominion were met by a series of ad hoc "final" agreements between individual provinces and the Dominion. There were many such agreements reached before the Great War but little of a comprehensive nature was achieved before 1907. The Dominion Government was concerned that the national economy continue to expand, and to this end considerable debt charges were incurred. When the depression arrived in 1873 these debts meant that the Dominion was unable, even if it wished, to give much assistance to the provinces. Between 1873 and 1895 Dominion revenues rose only from $20 million to $33 million.[2] The gradual upturn in economic activity, from 1895, also led to increased demand from the provinces for Dominion aid. The Dominion-Provincial Conferences of 1887 and 1902 were, in effect, expressions of the continuing fiscal difficulties of the provinces. As the population of the towns grew, the problems of the municipalities, a provincial responsibility, continued to grow and this, in turn, led the provinces to pressure the Dominion for additional assistance. Following the Provincial Conference of 1906 an amendment to the B.N.A. was passed which revised the conditions attached to the payment of provincial subsidies. The population limits of the 80¢ per capita payments (the 1861 population) was altered and provinces with a population in excess of 2,500,000 would now gain 60¢ on

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[1]Stewart Bates, Financial History of Canadian Governments, A Study Prepared for the Royal Commission on Dominion-Provincial Relations, Kings Printer, Ottawa, 1939, P. 3.

[2]Eggleston and Kraft, Op. Cit., P. 30.

the excess population. British Columbia gained an additional special grant of $100,000 per annum, and increased grants to meet the costs of government were made to all provinces.

TABLE 1:2

Changes affected by the 1907 Agreement: ($000)[1]

Provinces	Payments in 1906-07	Payments in 1907-08	% Increase
Ontario	$1,339	$2,129	59
Quebec	1,087	1,687	55
Nova Scotia	433	610	41
New Brunswick	491	621	26
Manitoba	621	751	21
British Columbia	307	522	70
Prince Edward Island	212	282	33
Saskatchewan	1,130	1,218	8
Alberta	1,124	1,212	8
	$6,745	$9,033	34

The relative political strength of the various provinces is reflected in the terms of this settlement. Ontario, Quebec, British Columbia and Nova Scotia obtained 75% of the increase of $2,288,000. The removal

[1]Canada, Federal Subsidies and Grants to the Provinces of Canada, Department of Finance, Ottawa, 1937, P. 16.

of the population limit on the per capita payments also had the effect of boosting the revenues of those provinces which were already in expansion. These agreements, as were those previous, were to be final and unalterable.

The fact that the two most industrialized and prosperious Provinces were able to obtain such large increases served only to exaggerate the problems for the Federal Government in later years. The poorer provinces found that they were condemned to a continual decline in their standard of living while the wealthier provinces were rapidly approaching a situation in which they could, if they so wished, be self sufficient. Their wealth and political influence was to lead to even greater concessions, as the years passed and their populations grew.

The period of "boom" which began, slowly at first, in 1895 and continued, sporadically, until 1913, led all Canadian governments into a period of relative prosperity. In the early stages Canada found that increased World demand for her products led to a favourable trade balance; she exported more than she imported. Much of this surplus was invested in capital goods. This surplus was destroyed by 1902, mainly due to an influx of British capital which was used to finance further expansion of the economy. In the later period, as imports increased, so did Dominion revenues which were still largely dependent on customs revenues. This dependence on customs revenues was potentially quite dangerous. In time of prosperity the level of imports would rise, customs revenues would follow and thus in such a period the Dominion Government would find itself with a surplus. This surplus would be used to finance further capital expansion, which, as we now know, could work to increase inflationary pressures in the economy. The Canadian governments, like other governments all over the World, often ensured that a recession would follow

any period of expansion. Dominion revenues rose from $29,958,000 in 1896 to $135,203,000 in 1913.[1] Provincial revenues increased from $4,301,000 to $12,851,000 in the same period. The provinces which could not but help see that their subsidies had only been increased by some $8,550,000 while Dominion revenues had increased by $85,212,000, decided that some method must be devised which would allow them to share in the increased revenues. In the early years of the boom the provinces had enjoyed a surplus on current account but, by 1912, three of the provinces were in difficulty. British Columbia had pursued a reckless policy of expansion in public works and had incurred a deficit of over $20 million by 1913. Manitoba pressed for, and received, compensation for the continued Dominion retention of land and Prince Edward Island received an additional $100,000 per annum to compensate for the lack of a year round ferry service. The provinces were not to be satisfied with these small increases, neither would they settle for a general upgrading of the kind seen in 1907; they were demanding a comprehensive programme of reform. In 1913 the Provincial Conference asked that they be granted additional payments "equal to 10% of the customs and excise duties collected...from year to year." They (the provinces) wished to ensure that the trend for Dominion subsidies to decline in importance as a percentage of provincial revenues should be reversed. They also felt that they should not be forced to negotiate for each increase in aid but that many rises in aid should become automatic and "as of right." Such a plan was obviously attractive to the provinces in a time of confidence and growth. If adopted the plan

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[1]Report of Royal Commission, Book 1, Op. Cit., P. 86.

would have doubled the subsidies in 1913. What was not considered, however, was the possibility of a depression. In 1914 the additional subsidies would have been $12.6 million, but in 1915 only $9.7 million. In times of real depression the situation could have become catastrophic. In 1929 the "extra" grant would have been $25 million but by 1933-34 it would have dropped to $10 million.[1] Thus the provinces would have found that their incomes would have been falling at a very rapid rate at a time when their expenditures were rising.

The Great War rescued Canada from a severe economic depression. In 1913 the signs were ominous, credit was becoming scarce and expensive and both imports and exports were falling. The massive debts which had been incurred to finance the expansion of the nation and the provinces had produced a large dead weight of interest payments to be met. From 1914 there had to be a drastic change in the allocation of resources. Men and materials, which had been employed in the construction industries, especially railways, now had to be diverted to other, war orientated, occupations. The recession which began in 1913 had, however, left many men and resources idle. Between 1913 and 1914 there had been a significant fall in the value of construction contracts awarded. The high level of demand created by the War soon operated to "mop up" virtually all the unemployment. There were massive increases in exports throughout the entire range of Canadian produce. Merchandise exports rose from $355,000,000 in 1913 to a peak of $1,151,400 in 1917 to $1,239,500 by 1920.[2]

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[1] Eggleston and Kraft, Op. Cit., P. 39.

[2] Report of Royal Commission, Book 1, Op. Cit., P. 92.

The costs of waging war were, however, very high. These costs were at first met by a series of loans, at first from Britain and later from America. Loans from Canadian citizens also provided millions of dollars to finance the war effort. Incomes were high and rising[1] and the need to win the war was obvious. The first loan, floated in November 1915 was so successful that, as the war progressed, three more Victory Loans were floated. The amounts raised by the three loans were $546 million in 1917, $681 million in 1918 and $620 million in 1919.[2] Other revenue increases were obtained by increases in customs duties in 1915 and a very moderate Business Profits War Tax in 1916 (25% of all profits in excess of 7%). This Tax was repealed in 1921. The note issue was increased and its gold backing reduced but the most important development from our point of view is that a Federal Income Tax was introduced in July, 1917. The Tax was to be at the rate of 4% on incomes exceeding $2,000 for single men and $3,000 for married men with a super tax of 2% on incomes between $6,000 and $10,000. This was to prove to be a lucrative revenue source and also one which was to cause more conflict between the Dominion and provinces than any other revenue source. The B.N.A., by allowing the provinces to impose direct taxation had set the Dominion and provincial governments on a collision course. This did not, of course, become apparent until the period following the 1939-45 war when direct taxation, in the form of income tax, became the major revenue source. This meant that both major levels of government were entitled to impose

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[1]But not as fast as the rise in the cost of living.

[2]Bates. Op. Cit., P. 54.

taxes in the same area which would in turn lead inevitably to conflict.

The changed income and expenditure pattern caused by the War can be judged, firstly, by the massive increase in government debt. The Dominion debt in 1913 was $520,837,000 in 1921 $3,520,039,000. The War accounted for $1,648,513,000, with debt from Soldiers Land Settlement reaching $78,293,000. Railway debt had risen from $502,353,000 to $1,850,636.[1] The revenue pattern had also been very considerably altered by the demands of war. Customs and excise revenues rose from $126,143,000 in 1913 to $142,332,000 in 1921. The most significant change, even if the amounts involved were at first small, was the $39,821,000 raised from personal income tax by the Dominion in 1921. Corporation tax raised $64,008,000 in the same year.[2]

The financial picture in Canada at the end of the Great War was, therefore, one of the Dominion having a large dead weight of debt and interest payments to meet. It had also discovered the potential of income taxes on both persons and corporations. Although many of the basic problems of both the economy and the constitution had been submerged in the war effort, they were, of course, to reappear. Canada in the inter-war years demonstrated many of the problems common to all developed nations. The fact that her economy did not show any great degree of diversity was to make her very vulnerable to international changes in demand for primary produce. The conflict between the provinces and the Dominion and the seeming inability for any really national system of economic

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[1] Ibid. P. 56.

[2] Report of Royal Commission, Op. Cit., Book 1, P. 107.

regulation were to accentuate many of these difficulties. The inter-war period is particularly noticeable as being one of increasing disorganization in the tax structure and, eventually, a much belated recognition that the Dominion did have a great responsibility in fields which had been, until the depression, regarded as provincial problem areas. There was also a more honest recognition that certain regions, the Prairies and the Maritimes in particular, did have serious problems which demanded special solutions.

The period from 1919 to 1929 was characterized by massive investment programmes being undertaken by the provinces. The provinces began intensive development of highways. The borrowing undertaken by the provinces did, of course, lead to very high percentages of the provincial budgets being "tied" to interest payments. Interest payments made by the provinces increased by 245% between 1919 and 1929.[1] The introduction of mothers allowances and a gradual increase in the provision of basic social services led to an increase of 154% in the expenditures on these services, while education expenditure increased by 145%.[2] This was a period when the provinces were becoming much more powerful and confident. The revenues of the municipalities and provinces were increased by some $120,191,000 from 1921 to 1930. This increase is of greater significance when compared with a fall in Dominion revenues of $18,465,000.[3] The prosperity of the provinces was, however, based largely on unsound investment. The economy of Canada as a whole, and of certain provinces

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[1]J. A. Maxwell, "The Adjustment of Federal-Provincial Financial Relations," C.J.E.P.S., August, 1936, P. 375.

[2]Ibid. P. 375.

[3]Report of the Royal Commission, Op. Cit., P. 130.

in particular, was bound to suffer severely if there was even a slight downturn in world economic activity, as too many government income sources were dependent on continued expansion. In the absense of expansion they could only collapse. No long term policy existed, at any level of government, to meet either the short or long term fiscal needs of the nation or the regions in the event of a downturn or, for that matter, if expansion continued. No plans had been devised to cater to the needs of the people and areas which suffered from structural or cyclical pressures within the economy.

The trend for the Dominion Government to revert to customs duties as the major revenue source was also to compound the confusion and difficulties of the depression years. Even when the need for anti-cyclical measures was accepted they were to prove difficult to implement in the face of rapidly contracting revenues. The difficulties inherent in large scale foreign borrowing had been well demonstrated in the 1870s and in 1913, but these lessons were ignored. The Dominion depended on customs and excise revenue for 82% of its income in 1913, this fell to 33% in 1921 but rose to 47% by 1928. This was part of a deliberate policy to attempt to return to normal conditions. Other taxes and duties, including corporate and personal income tax and sales taxes were reduced in this period. The Dominion was managing to place itself in an impossible financial position. It had not yet realized the advantages of direct taxation.

Developments not directly related to taxation, but of real concern in the field of intergovernmental financial relationships during

this period, were the early schemes of grants in aid from the Dominion to the provinces. The Old Age Pensions Act, 1927 was the most important development in this regard. The Federal Government offered to meet 50% of the cost of approved provincial pension schemes. At its inception no province had a pension scheme in operation. By 1929 British Columbia, Manitoba, Saskatchewan, Alberta and Ontario were taking full advantage of the Federal offer. The Maritime Provinces could not afford even half the cost of an adequate scheme. A symptom of the declining economy of the region was the fact that the population was becoming increasingly old.

TABLE 1:3

Proportion (per thousand) of population aged 70 or over[1]

	1921	1931
Canada	28.12	33.22
Prince Edward Island	60.24	64.81
Nova Scotia	47.26	50.93
New Brunswick	38.53	41.95

Following the election of 1930 the Bennett Government raised the Federal contribution to 75%. Between 1933 and 1936 all the Maritime Governments had started schemes. The administration of the schemes was in the hands of the provincial governments, with only a slight degree of Federal

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[1]Maxwell. Op. Cit., P. 231.

supervision.

More recent developments in grants in aid schemes will be discussed in Chapter Three. In this period other schemes in which the Federal Government provided funds in return for a provincial guarantee that minimum standards would be maintained covered such fields as technical and agricultural education, an employment service and a system of venereal disease control. The following table indicates the costs of the Old Age Pension Plan.

TABLE 1:4

Cost to Dominion, to March, 1938 of Pension Plan[1]

	Date of Entry	Cost ($0000)
Prince Edward Island	1933	680
Nova Scotia	1934	6,812
New Brunswick	1936	2,202[2]
Quebec	1936	10,731[2]
Ontario	1929	58,849
Manitoba	1928	12,702
Saskatchewan	1928	11,442
Alberta	1929	8,055
British Columbia	1927	11,913

The development of a good highway system was given considerable

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[1]A. E. Graur, "Public Assistance and Social Insurance", P. 70.

[2]Late entry accounts for low figures.

stimulus by the Federal offer to meet 40% of the cost of approved schemes. A total of 8,700 miles of highway was financed by this method.[1]

There were, therefore, quite significant changes in intergovernmental financial relations in the inter war years. The Dominion and Provincial Governments were beginning to become involved in programmes of social welfare and the Dominion had begun the experiment with a few grant in aid schemes. The provinces were, in the early period, stronger than they had ever been before, both in terms of economics and their political influence. The reliance of the Dominion on customs revenues and the lack of planning were to prove serious during the depression. The high level of provincial debt was also to provide a great deal of 'drag' once the need for government action to combat the depression had been accepted. The mere fact that provincial revenues were expanding rapidly, by 139% from 1919 to 1929, blinded many to the fact that debts had also increased in the same period, in fact by 245%. Between 1929 and 1933 provincial bonded debt rose from $848,501,200 to $1,255,713,300.[2] This latter figure suggests that many provincial officials expected that the crisis would be short lived and so indulged in massive short term borrowing to await the time when the 'free flow of the market' would correct the temporary imbalance.

Unemployment was, constitutionally, a provincial responsibility. It had, however, been the practice to allow the municipalities to deal with this problem, perhaps as a remnant of the English poor law tradition,

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[1]Eggleston and Kraft, Op. Cit., P. 45.

[2]Maxwell, Op. Cit., P. 45.

and this practice was at first continued. The onset of the depression coincided with a severe drought in the West which further complicated the issue. The depth of the depression can be judged by the fall in per capita income across Canada. What is of particular interest, as far as this paper is concerned, is the fact that, even at the depth of the depression, the per capita incomes in Ontario and British Columbia were still above the 'normal' per capita incomes in Prince Edward Island and New Brunswick and only a little below the 'normal' for Nova Scotia.

TABLE 1:5

Per Capita Income in Canada, 1928-9 to 1933[1]

	$ per capita 1928-9	$ per capita 1933	% fall
Saskatchewan	478	135	72
Alberta	548	212	61
Manitoba	466	240	49
British Columbia	594	314	47
Prince Edward Island	278	154	45
Ontario	549	310	44
Quebec	391	220	44
New Brunswick	292	180	39
Nova Scotia	322	207	36
Canadian Average	471	247	48

It gradually became apparent that the depression was not a temporary

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[1]Report of the Royal Commission, Book 1, Op. Cit., P. 150.

phenomenon and that neither the provinces nor municipalities could deal with a task of this magnitude. The level of Federal aid, when it did start, rose rapidly. From the 1931 figure of $3,160,000 it rose to $51,507,000 in 1936-7 and to $55,000,000 by 1937-8. The level of conditional grants had reached $30,750,000 by 1938-9.[1] Many of the schemes financed by the grants in aid were of the 'make work' variety. The level of unemployment was 12.4% in December, 1932 and reached a high of 14.9% in April, 1933. It varied for the next three years between 8.8% and 13.9% and had fallen to 6.8% by August, 1937.[2]

The Dominion position with regard to revenue sources was still most unsatisfactory at the outbreak of the Second World War. High debt charges still had to be met and customs duties still continued to fall. These revenues fell from $131 million in 1930 to $84 million in 1936, with only a slight rise to $99 million in the immediate pre war period.

The gross inefficiency seen in all levels of government during the depression, and in particular the plight of the Maritime and Prairie Provinces, led to increasing demands for some kind of formal inquiry into government policies and intergovernmental relations. During the winter of 1936-7 the Premiers of Manitoba and Saskatchewan asked the Dominion Government to agree to an examination of those provinces finances prepar-

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[1]Eggleston and Kraft, Op. Cit., PP. 64-5.

[2]A. E. Graur, "Public Assistance". Op. Cit., P. 12.

[3]Canada. Dominion of Canada and Provincial Governments Comparative Statistics and Public Finance, 1913, 1921, 1925 to 1939, Appendix One to the Royal Commission Report, Kings Printer, Ottawa, 1939, P. 49.

atory to their making an appeal to the Dominion for increased financial aid. The Prairies, in addition to the strains of lost markets and widespread unemployment which affected all Canada, had suffered severe periods of drought which had made their position intolerable.

An investigation made by the Governor of the Bank of Canada resulted in a strong recommendation that a Royal Commission be appointed to study Dominion Provincial relations. On 14th August, 1937, the Prime Minister announced that a Commission would be appointed. The Commission was charged with the investigation of:-

(a) the constitutional allocation of revenue sources and governmental burdens.

(b) the charactor and amount of taxes.

(c) debt provisions.

(d) Dominion subsidies and grants.

Although the terms of reference were wide there were to be four major areas of concentration. These were to be studies of the economic background to Dominion Provincial relations, the constitutional aspects involved, methods of taxation and the financial history of Canada. The Commission visited all the provinces but was not received by all the governments. Those provinces most in need, Manitoba and Saskatchewan, presented well prepared and argued briefs. British Columbia, one of the wealthy provinces, proved to be less than cooperative but did at least present a brief. Alberta refused to recognize the Commission and so the Commission was reduced to accepting, as the major brief from that province, the brief from the Edmonton Chamber of Commerce. Ontario was little more hospitable but did present a reasonably comprehensive brief. The Maritimes

were mainly concerned that this should not be simply another occasion when their problems were either ignored or misunderstood. Their major position was that grants were not enough and that fundemental changes in the allocation of revenues and responsibilities of governments was called for. They were tired of being second class provinces and realized that their position was at least in part due to the Canadian tariff policy, which, of course, worked to the benefit of the Central Provinces. Remission of income tax rights to the provinces would be of no value to the Maritimes. The level of per capita incomes in these provinces was so low that the revenues raised would not be sufficient to finance the level of government activity demanded by the conditions in the region. As we will see in later chapters the conditions in the region have not been substantially improved. Quebec decided not to appear before the Commission but did meet members of it in an informal manner. The division between the reaction of the provinces was quite remarkable. Those provinces most in need were the most cooperative, others, such as British Columbia and Ontario, refused to accept that there was a need for a Commission. All that was required, they felt, was that the Federal Government should cease meddling in their affairs. They would have liked to see the powers of the Federal Government very much reduced in contrast to the less fortunate provinces which wished to see the Federal Government in a position to assist them.

During the two and half years which elapsed between the creation of the Commission and the publication of its report great changes had occured in Europe. The Second World War had begun, and this was to seriously affect the reception of the Report. Taken all together the Report offered

the most exhaustive and comprehensive study of the Canadian federation from 1867 to 1939. It remains the only comprehensive study of inter-governmental relations yet produced.

As could be expected in a Report covering such a vast field, there were many recommendations made, which, while making sound sense to an economist or fiscal expert, would not be acceptable to the wealthy provinces. Pressures exerted on provincial politicians were, and are, exerted because of the very considerable variations in the level of economic development of the provinces. For a realistic level of assistance to be given to the poor provinces would involve, naturally, a sacrifice by the more wealthy. This would not, of course, be politically popular in these provinces and so is resisted by their political representatives. It has been this conflict which has dogged the Canadian federation from the time of its creation, and it continues, at a greater intensity than ever before, to the present day. It is to be expected that the conflict will increase as the level of economic advance increases. Post war developments seem to confirm this. Was it to be expected that Ontario and British Columbia would be prepared to reduce their rate of expansion or reduce the level of their services in order that the Maritimes could be assisted? If the principle of 'fiscal need' and basic minimum national standards were accepted this would be inevitable.

The Commission was well aware that the provinces were afraid that the Federal Government desired to extend its power. They were opposed to the creation of a centripital federation. Since they were aware of these provincial reservations the Commission took great pains to assure the

provinces that the solutions they proposed, while extending the power of the Dominion to raise taxes, would nevertheless provide the provinces with adequate guarantees against Federal usurpation of provincial powers. Thus the provinces would be secure as far as expenditure responsibilities were concerned and would be guaranteed a definite level of revenue. The provinces most in need would be assisted but, of course, the other provinces would have to make moderate sacrificies.

The major recommendations of the Commission can be quickly summarized. The Dominion was to be responsible for the whole relief of the employable unemployed and their dependents. The Dominion was to assume the dead weight of provincial (but not municipal) debt. This would, of course allow the provinces to assume a much more flexible approach in future policies. These two recommendations were, however, of quite minor importance when compared to those regarding revenue raising powers. The Dominion had already, during the later years of the depression, assumed an increased amount of responsibility for unemployment relief. The provinces would not be reluctant to pass this burden on to the Dominion. Opposition could have been expected, and did in fact occur, when the Commission suggested that the provinces surrender the major revenue sources to the Dominion. The recommendation that the Dominion should be granted exclusive rights in the fields of direct taxation, was not acceptable to the provinces. All governments by now fully appreciated the growth potential of the income tax as a revenue source. The massive growth in revenues seen even during the early war period, along with developments in other countries, convinced the provinces that they should not sacrifice these fields.

Pre-War

The minor tax fields allocated to the provinces in the Report did little to ease their suspicion that it was a cover for the Federal Government's centralizing tendencies. The events before the war and the rapid recognition of income taxes as a, and perhaps the, major revenue source meant that the provinces would be unlikely to accept what was the major recommendation of the Commission.

It was suggested that the Dominion would pay what were to be known as National Adjustment Grants to certain of the provinces. The level of the Grant, and the decision as to which provinces were to receive any such grant would be based on the concept that all provinces, rich and poor alike, should be in possesion of sufficient revenues to provide, if they so wished, basic minimum services which did not fall below the Canadian national average, without need to impose higher levels of taxation than the national average. This was not to say that the provinces were to be forced to use the money as the Dominion saw fit. If a province decided that it did not wish to maintain standards in a particular area that would be a matter between the provincial legislature and its electorate. It would not affect the level of Federal payment to the province. The Commission was clearly intent on preserving a considerable degree of provincial autonomy on the expenditure side even if it could not be preserved on the revenue side. Talking of the need to provide for the health of the population the Commission stressed that this was a field in which the Federal Government might be tempted to coerce the provinces. The Commission felt, however, that "Mere importance of a service

does not justify its assumption by the Dominion."[1] The provinces would, therefore, have received a considerable amount of autonomy if these recommendations had been accepted. The grants were to be unconditional and, because of their pronounced equalization bias, would have assisted the less wealthy regions at the same time that Federal control of provincial expenditures was reduced. The Report was quite explicit in its concern that the provinces should have a high degree of independence in deciding how they should spend its revenues. The provinces should continue to have considerable political independence. The Commission stated that:-[2]

> "No control of provincial expenditure is contemplated. Every province would be quite free to improve its services, by specially heavy taxation, or to have specially light taxation by reducing its services, or to develop some services in excess of the Canadian average at the expense of others which would remain below it."

Since the aim was to ensure that all provinces had sufficient funds, it followed that certain of the wealthy (and politically powerful) provinces would not qualify for a National Adjustment Grant, since they already had funds in excess of the Canadian average. As can be seen from the following table British Columbia, Alberta and Ontario would not qualify for a grant at all. This was, of course, because the Commission had taken the very sensible step of moving away from population as the main determinent of provincial need or the basis for the calculation of Federal grants.

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[1] Report. Op. Cit., Book 11, P. 34.

[2] Ibid. P. 86.

The move away from the per capita basis was sound. It would have allowed the poorer provinces an opportunity to lift themselves up from the level of grinding poverty which had been their lot for such long periods from 1867. However sound from an economic and fiscal point of view these recommendations were, it was not likely that the more wealthy provinces would accept them.

The Dominion was to assume very large financial responsibilities in return for the tax fields which were to be vacated by the provinces. The concept of a 'surplus' of funds which would be available to a province to spend as it wished after it had met its constitutional obligations was also utilized. This surplus above fiscal need could be used to finance any scheme on which the provincial government placed a high priority. Even without the payment of a National Adjustment Grant the richer provinces would still have a surplus above that of the Maritimes. Had the plan been accepted the poorer provinces would still not have been able to expand at the same rate as the richer, and it was unrealistic to expect that they could have improved their position.

The Dominion Provincial Conference which met in January, 1941 soon ended in complete failure to reach agreement. Ontario, British Columbia and Alberta all firmly opposed the Report. The only provinces which accepted the bulk of the Report without hesitation were Prince Edward Island, Saskatchewan and Manitoba. Quebec did not reject the report but felt that such a large scale revision should not take place in war time. The most vehement opposition to the Report came from Premier Aberhart of Alberta, who, of course, had his own ideas on fiscal and monetary reform.

Mr. Aberhart suspected that the Eastern monied interests had played an undue influence on the findings of the Commission and was violent in his opposition.

TABLE 1:6

Abstract of Financial Recommendations in Rowell-Sirois Report[1]

	Dominion Responsibilities[2] $000	National Adjustment Grant $000	Surplus[3] $000
Prince Edward Island	901	750	260
Nova Scotia	4,375	800	800
New Brunswick	3,786	1,500	2,250
Quebec	23,489	8,000	1,000
Ontario	37,100	nil	4,700
Manitoba	7,185	2,100	1,300
Saskatchewan	15,959	1,750	2,300- 2,950[4]
Alberta	9,124	nil	2,200
British Columbia	12,551	nil	900

It can be seen that even if the Report had been accepted the poorer provinces would not have been able to advance at the same rate

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[1]All figures from Book 11 of the Report, PP. 77-107.

[2]Would include assuption of provincial debt and full responsibility for unemployment relief. Savings to province by loss of sinking fund and tax collection duties are also included.

[3]Available for the expansion of education, welfare and developmental expenditure, either directly or through the municipalities. Available funds in excess of fiscal need.

[4]Increase expected between 1936 and 1939 due to operation of emergency grants which would be continued and improvement in provincial revenues.

as the more industrial provinces. Some assistance would, however, have been given. It is quite possible that the strain placed on the federal structure by the economic diversity of the nation would have been very much reduced if these payments, limited as they were, had been made. As the stagnation of regions continued it became even less likely that it would ever been reversed. As seen above[1] the population in the Maritimes was becoming increasingly old, due both to a low birth rate and a loss of young people to the other, more prosperous, provinces. This, of course, means that it is even more difficult to stimulate the economies of the less developed regions. Since the majority of young people do not leave the region until they have completed their education this means that the poor regions are subsidizing the rich via the educational costs incurred in educating people who do not long remain in their home province.

These points were not, of course, accepted by the most influential provinces. The Federal Government was also insistent that the recommendations be considered as a whole. There was a strong feeling among the opponents of the Report that the Federal Government was using the emergency conditions of the war to attempt to force the provinces to sacrifice their rights in the income tax fields. Many of the conditions which had led to the creation of the Commission, falling prices and massive unemployment, no longer existed, due to the stimulus provided by the war. The provinces now felt much stronger than they had only a few months before. The Conference was especially notable because of the high degree of competition

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[1]See Table 1:5 above.

between the rich and poor provinces and the extreme bitterness of much of the debate.

Following the failure of the Conference the Federal Government was still faced with the task of financing the most expensive war effort in history. The Government decided that it must enter the field of direct taxation to a very large extent. Even without the agreement of the provinces the Government decided to press on and impose that level of personal and corporate income taxes that they would have if the provinces had not been occupying the same tax field. They were 'squeezing' the provinces from the income tax field, though only for the duration of the war. Compensation was offered to the provinces under the Wartime Tax Suspension Agreements. They could choose between receiving an amount equal to the yield of these taxes in the fiscal year 1940 or 1941 or the net cost of their debt charges, less sucession duties in the same year. In addition any province, which could prove that its lack of revenues would place it in a condition of fiscal need, would be entitled to a subsidy. Under these Agreements payment at the rate of $86.2 million a year were made between 1940 and 1944.[1]

Dominion revenues from income taxes rose from $145,279,511 in 1939 to $1,335,863,754 by 1943.[2] Dominion debt rose from less than $4 billion in 1937 to $13 billion by 1946, at which time it was still increasing.[3]

When peace eventually came the relative strengths of the levels of government were very much changed. The provinces now had what appeared to be a strong economic position. The war had removed the problems of

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[1] Dominion-Provincial Conference, April, 1946, Proceedings, P. 4.

[2] Canada Year Book, 1948-49, P. 1011.

[3] Dominion-Provincial Conference, 1946, P. 6.

unemployment and the major economic difficulties of the inter war years. The Dominion was limited in its freedom of action due to the massive war debts. Nevertheless the public had become accustomed to looking to Ottawa for decisions and action during the war years and had been impressed with the speed with which the challanges of the emergency had been faced. The level of intergovernmental cooperation had been much increased and it was hoped that this would continue. The Dominion Government, by the provisions of the B.N.A. Act had very wide powers under any emergency conditions. With the end of the war many of these powers were lost. What had been acheived by compulsion, it was hoped, could now be consolidated by cooperation.

There were considerable fears that the chaos which followed the First War would now reappear. As the Prime Minister said in 1945,[1] "There are men and women who almost dreaded the coming of victory because they feared that depression and unemployment migh come in victory's train". The Dominion Provincial Conferences of 1945 and 1946 were called so that this problem could be met and, if possible, a reallocation of governmental responsibilities and revenues arranged. Utilising the experience of the 1941 Conference the Federal Government abandoned the principle of fiscal need and returned to the per capita payment as the principal unit in the calculation of Federal grants. This, while making the Federal proposals more acceptable to certain provinces, meant that the hopes for the poorer regions which had been offered by the Rowell-Sirois Report was now lost. The Federal Government had been forced to capitulate

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[1] Dominion Provincial Conference, 1945, Proceedings, P. 6.

to the interests of the wealthy provinces.

The Federal Government still wished the provinces to continue the basis of the wartime agreements. In return for compensation the Federal Government wished the provinces to allow all revenues from personal and corporate income and sucession duties to accrue to the Federal Government, initially for a period of three years. The Dominion would make per capita payments of $12[1] as compensation. The statutory subsidies, for support of government etc., would continue. The Dominion would also guarantee not to enter certain tax fields and not to increase its rates of tax in others. There were many other proposals relating to planning and public investment programmes which would have called for a considerable degree of intergovernmental cooperation and increased provisions for the payment of conditional grants to assist the provinces in the field of public health. The Dominion would assume all responsibility for unemployment insurance and old age pensions for all over the age of 70, and would assume 50% of the cost of a pension plan to cover those between 65 and 70. The cost of Federal payments to the provinces would, it was estimated, amount to $198.2 million by 1947 if all provinces accepted the offer. This contrasted with a sum of $124.5 million in 1944.[2]

The major difficulty, as could be expected, was that the provinces still suspected that the Federal Government wished to centralize power in its own hands. Since the provinces were restricted to direct taxation

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[1]Increased to $15 during the Conference.

[2]Dominion Provincial Conference, August, 1945, Proceedings, P. 4.

they feared that a concentration of Federal taxes in the same area would leave the provinces nearly 100% dependent on the Federal Government for revenues. The Federal claims that this was not, in fact, their intention did little to still these fears. The Conference lasted a little more than nine months and then ended without agreement being reached. No province could accept all the Federal proposals and some, including Ontario, British Columbia and Alberta could accept very few. The Federal Government, at this stage, intended that all the 'package' be accepted. It was not yet ready to negotiate each item seperately.

The Conference failed in May, 1946 having achieved very little except to demonstrate the depth of the problems which now faced Canada. The motives behind the refusals to accept the proposals were, of course, many and varied. Quebec's traditional concern for provincial autonomy might, on the surface, seem to explain her rejection to the plan. However, none of the provisions would have affected provincial responsibilities with regard to education, religion or civil rights. At least part of the motives for her refusal of this offer must have been of fiscal, not cultural domination. Ontario, British Columbia and Alberta all complained that the compensation offered was not as great as the revenues they were being asked to sacrifice. They could not accept the obligation to the poorer provinces which the Federal Government was again trying to place on the nation as a whole. The difficulties seen in this regard, and the eventual rejection of the Federal offer, meant that the division between the rich and poor regions in Canada would not only continue but would increase during the post war years of very rapid expansion. The developments of

the 1946 to 1968 period will be discussed in Chapter Two, suffice it here to say that the pressures on the Canadian federal structure were very much increased by the expansion of the economy in the years since the war. Provincial budgets were strained by the massive growth of the cities and the flow of immigration. The economic advance was not uniform and so the regional diversity, and all the problems inherent to it, continued unabated.

II 1946 to 1968: The Growth in Provincial Power

In Chapter One the development of intergovernmental financial relations during the period from 1867 to 1946 was the main area of concern. It was seen that, even at the time of Confederation, there were very considerable variations in the wealth of the provinces and that this had been reflected in variations in the political influence of the provinces. The present chapter will show that not only did this diversity continue but that the relative gap between the worst hit provinces, the Maritimes, was hardly improved at all by the ad hoc solutions attempted by the Federal Government.

The period between 1946 and the present has been marked by a continuation of the economic disparity and by a much increased level of provincial power. The federation has become very much more centrifugal. The provincial revenues have been subjected to very much increased pressures, as we will see, and have been able to weaken the Federal Government's control over them. The growth in the cities has been very spectacular, as has the rate of immigration. The majority of immigrants become city dwellers.

The Federal attempt, in the early post war period, to perpetuate the centralization of the war, failed. The Federal Government could not persuade the provinces to allow it exclusive use of the income tax field and so one of the major Federal objectives was frustrated. The relative strenghts of the governments were altered by the events of the war. The

Federal Government had incurred very great war debts and did not have much room in which to negotiate with the provinces. The provinces were, of course, much stronger than they had been for many years. The Dominion attempt to continue the Wartime Tax Agreements failed. The Dominion-Provincial Conference of 1945 demonstarted that the provinces, or the wealthy ones at least, did not intend the Federal Government to retain the dominant position it had taken during the war. The Dominion proposals at the Conference reflected not only the fear of a severe post war recession but also an increased awareness at the Federal level of the economic theories of Lord Keynes. Briefly stated the Federal proposals would provide the Federal Government with all the powers a modern government was then thought to need in order to control an expanding economy in a complex nation. They included (1) exclusive Federal use of taxes on incomes, corporations and inheritances. (2) payment of an old age pension to all at the age of 70, by the Federal Government. (3) Federal assistance to the provinces with health insurance grants equal to 60% of the cost. (4) Payment of assistance to the employable unemployed, and (5) timing of Federal grants to assist provincial and municipal capital expenditure programmes. It can be seen that there are elements of the Rowell-Sirois recommendations in the Federal proposals, but the all-important concession to the wealthy provinces, the per capita grant calculation, wasstill very important. The poorer provinces had lost the opportunity to achieve the kind of drastic restructering of revenues and responsibilities which they had assured the Rowel-Sirois Commission was essential. The gross inequalities were to continue.

The Federal proposals were made in the form of a 'package deal'. The Federal Government hoped that the provinces would be persuaded to accept all, or at least the majority, of the package. Complex negotiations which lasted a total of nine months eventually ended in failure. The wealthier provinces, Ontario and British Columbia in particular, rejected the extension of Federal power into areas of provincial jurisdiction. During the Conference, the Federal Government had claimed to be negotiating with an open mind but in fact it seemed determined that the centralization seen during the war would be continued for as long as was possible. This was not simply due to the central government's love of power, although this may have played its part, but also to the increased economic knowledge of the Government. Contemporary economic thought emphasized the need for a unified economic and fiscal system, and the Federal Government was determined to achieve this. The determination of the Government to have the package adopted more or less complete brought it into direct and bitter conflict with the major provinces. Unlike the Australian situation, the Federal Government in Canada could not force agreement on the regional governments, neither did it have the same constitutional rights in this matter as the Commonwealth Government.

In the Federal budget of 1946 an offer was made to 'rent' provincial rights with regard to direct taxation, but the comprehensive social welfare measures were no longer included, the package had been split. The ad hoc nature of pre war negotiations was already beginning to appear. A noticeable change had occured in the attitude of the Federal Government. Following the failure of the Conference, the Federal Government assumed

a policy of negotiating direct with individual provinces. The direct attempts to coerce the provinces were now to give way to an attitude of 'take it or leave it'. It was quite obvious that the Dominion was unable to persuade all the provinces. The Federal offer would have allowed the provinces a little more tax 'room' than they had had previously. The Government calculated that a province could meet its constitutional obligations if it imposed income tax at 5% on both people and corporations and succession duties at 50% of the Federal rates. This amount of 'room' was therefore offered to the provinces in the 1946 offer. The Federal Government had to reject the demand, made at nearly every Dominion-Provincial Conference since, that it withdraw from the field of income tax. As was pointed out at the time the Federal Government had a very serious obligation to the poor as well as to the rich areas in Canada. Some form of transfer payments to these provinces was essential.

Manitoba, Prince Edward Island and New Brunswick expressed immediate interest. British Columbia was interested but was very concerned that the West should get some relief of their debt obligations incurred during the depression. Eventually the Federal Government met British Columbia on this point, only to find that the other provinces were complaining of unjust advantage for British Columbia. A new set of agreements were then drawn up, putting all provinces on an equal footing. Options were allowed to accommodate, in a very modest way, the differences between the provincial interests. The First Option offered was:-[1]

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[1]Dominion-Provincial Tax Rental Agreements Act, 1947. See Canadian House of Commons Debates, 1947, PP. 5276.

1. $12.75 per capita on the 1942 population of the province.

2. 50% of the revenue in the province from corporation and income tax.

3. The statutory subsidies payable to the province in 1947.

The Second Option was:-

1. $15.0 per capita on the 1942 population of the province.

2. The statutory subsidies payable in 1947.

The Third Option was:-

A flat payment of $2,100,000.

The third option was specifically designed to meet the needs, to a very limited extent, of Prince Edward Island. Such a small sum could obviously do no more than to ensure that the level of stagnation in that province was no more rapid than it had been before the war. Saskatchewan and Nova Scotia accepted the second option. As expected Ontario and Quebec decided not to enter the agreements. British Columbia, Manitoba, New Brunswick, and Alberta, as expected, accepted the first option. The total cost to the Federal Government was to be $206.5 million.[1]

Even though the provinces did not sign the agreements the residents of Quebec and Ontario would be allowed a tax credit of 5% of the Federal rate if the province imposed an income tax. The Federal Government would collect the tax for them if it was on the same base as the Federal tax. The fact that neither province did impose an income tax indicates that the provincial politicians were reluctant to incur the displeasure of their electorates. This was true even when the actual cost, to the taxpayers

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[1]A. Milton Moore and J. Harvey Perry. Financing Canadian Federation., Tax Paper No. 6, Canadian Tax Foundation., Toronto, 1953., P. 35.

of Quebec and Ontario, would be nil if the provincial income tax had been at only 5%. We will see later in the paper that when the provincial demands for Federal withdrawal from the direct taxation fields were met to a very considerable extent the provinces were very reluctant to enter the field themselves.

TABLE 2:1

Guaranteed Payments under Tax Rental Agreements, 1947 ($ million)[1]

	1946 offer	1947 offer	% increase
Prince Edward Island	2.0	2.1	5.0
Nova Scotia	8.9	10.9	22.5
New Brunswick	7.0	8.8	25.5
Quebec	50.9	56.4	10.8
Ontario	58.3	67.2	15.3
Manitoba	10.9	13.5	23.9
Saskatchewan	13.4	15.3	14.2
Alberta	11.9	14.2	19.3
British Columbia	18.1	18.1	-----
Total	181.4	206.5	

There was no intense tax competition between the non agreeing provinces and the Federal Government, although it had been expected. They both imposed corporation taxes at an effective 8 1/2% and maintained their succession duties but refused to impose a personal income tax. According

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[1] Ibid. P. 35.

to the Federal Minister of Finance the "Central Provinces acted with reasonableness and restraint".[1]

In return for the guaranteed Federal payments the provinces agreed not to impose any income tax and to restrict company tax to 5% of the Federal rate. If they did impose a company tax it would be collected by the Federal Government at the same time that its own collection was made. The provinces were not to impose succession duties. If they did so the Federal Government would allow a tax credit and deduct the amount from the grant to the province.

The agreements broke new ground and indicated that the Federal Government was now prepared to adopt a somewhat more flexible approach. The options allowed for only very moderate improvement in the position of the poorer provinces and could in no way be described as substantial. The concept of guaranteed minimum payments was, of course, valuable to all.

The relative lack of intergovernmental conflict during the early period must have been partly due to the fact that provincial revenues were fairly bouyant. Provincial revenues from company taxation rose from $2 million in 1946 to $146 million in 1950. Indirect taxes rose from $549 million to $948 in the same period. Total provincial and municipal revenues rose from $2602 million to $2965 million.[2]

The provinces found that, as the war time conditions were removed, considerable financial strain was felt. Canada was now beginning to feel

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[1]Conference of Federal-Provincial Governments, 1950, Proceedings, P. 139.

[2]National Accounts, Income and Expenditure 1926 - 1956, PP. 74-75.

the strain of rapid development. The population of some of the provinces was rapidly increasing, due to immigration. The majority of the immigrants were attracted to the cities, especially in Ontario and British Columbia. The municipalities, of course, are a provincial responsibility. Many public works which had been neglected for years because of the depression and the war now needed urgent attention. The need was, of course, all the greater in the more rapidly developing areas. The level of economic diversity was becoming so great that the federal structure itself was subject to stress. The financial arrangements were again in need of redrawing. It was no surprize, therefore, that when the Prime Minister wrote to all the provinces in December, 1949 to propose the holding of a Federal - Provincial Conference, in order to discuss problems of mutual concern, he found that all the provinces demanded that provincial finance should be on the agenda. Mr. St. Laurent noted that there "...was a consensus of view that the discussion of fiscal matters would be of fundemental importance."[1] It seemed that the Federal Government had hoped, in 1949, to be in a position to offer more attractive terms at the Conference and so, perhaps, to attract the two non agreeing provinces in to a new set of agreements. War, however, intervened to frustrate the ambitions of all the governments involved.

The war in Korea, in which Canada was involved, was to lead to a massive increase in defence spending. At the 1950 Federal-Provincial Conference the Minister of Defence stated that the Federal Government would spend $750,000,000 on defence in 1950 and perhaps $1 billion in 1951.[2]

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[1] Federal - Provincial Conference, 1950, Proceedings, P. 4.

[2] Ibid. P. 14.

Under these circumstances it could not be expected that the level of Federal aid would be much increased. What is of especial interest is not so much the technical details of the Federal offer, important though they are, but the fact that the Prime Minister felt obliged to apologize for not being able to satisfy the province's demands. The older days in which a province had to prove its case with great detail had been replaced by a situation in which they were being tempted by the Prime Minister.

The new agreements were essentially similar to those of 1947. They were to run from 1952 to 1956. An attempt was made to make the payments more closely related to changes in population and in G.N.P. The Prime Minister offered:-[1]

(1) The yield of a personal income tax at 5% of the Federal rate applying in 1948, applied to the 1948 population of the province.

(2) The yield of an 8 1/2% corporation tax.

(3) The average revenues received by the province from succession duties.

(4) The statutory subsidies.

To make the payments more sensitive to actual changes in the provincial economies the grants were to be calculated on the basis of the previous years' figures relating to the provincial population and G.N.P. The practice prior to this was for the figures relating to an average of the previous three years to be used. Federal Government payments were thus to be increased from $368.5 million to $423.8 million.[2]

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[1] Ibid. P. 142.

[2] Moore and Perry, Tax Paper No. 6, Op. Cit., P. 47.

TABLE 2:2

Guaranteed Minimum Payments 1947, 1952 and Annual Adjusted Payments 1952-3[1]
($000,000)

	1947 Agreement	1952 Agreement	Annual Adjusted Payment 1952 - 3
Newfoundland[2]	6.2	9.2	12.3
Prince Edward Island	2.1	3.0	3.9
Nova Scotia	10.9	15.3	20.2
New Brunswick	8.8	12.6	16.6
Quebec[3]	56.4	85.1	115.0
Ontario[4]	67.2	101.8	137.2
Manitoba	13.5	18.6	24.7
Saskatchewan	15.3	20.0	25.6
Alberta	14.2	21.0	29.4
British Columbia	18.1	29.6	41.4
	212.7	216.2	426.3

The new plan, like the old, was not based on any realistic calculation of provincial need. The insistance on retaining the per capita grant as the basis of calculation, even when tied to the provincial G.N.P., would obviously work in favour of the more wealthy and expanding provinces.

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[1] Ibid. P. 48.

[2] From 1949.

[3] If either agreement had been signed.

[4] If 1947 agreement signed.

J. Harvey Perry wrote, "The three bases ... have neither consistency nor principle; about all that can be said of them is that they produced the amount of money that each province required as its price for entering the agreement."[1] Given the relative political power of the governments little more could be expected. All the provinces were concerned with obtaining the maximum possible revenues from Ottawa and not, it seems, with ensuring that all Canadians should be able to enjoy basic minimum standards in terms of government services. All the agreements represented political strenghts, not fiscal needs.

After months of negotiations Ontario entered the 1952 Agreements. The terms were essentially the same as for the other provinces except that Ontario would continue to collect her own succession duties. There would, of course, be an equivalent reduction in the Federal payments to the province. The Federal Government had now achieved its major objective, the most wealthy and populous province was now bound by the same agreement as eight of the other provinces. This, of course, did have the very undesirable side effect of isolating Quebec. The situation with regard to Quebec - Canada relations now took a distinct turn for the worse, due in very large part, to the policy pursued by the Federal Government.

Prior to the 1952 Agreement provinces which had not entered the Tax Rental Agreements were not subject to a financial penalty. They could maintain a level of public service equal to the Canadian average without need to impose taxes higher than the average. This pattern was to change after 1952. The fact that it was Quebec which was isolated quite obviously

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[1] J. Harvey Perry, "Federal Provincial Tax Negotiations", Tax Paper No. 10, 1956, P. 55.

made the problem much more sensitive. It also makes the Federal policy difficult to explain.

Due to the change by which the calculations were based on the previous year's provincial income and population the payments to those provinces which were in a process of rapid economic advance were to be considerably increased. The more industrialized the province became, and the faster the growth of its population, the greater were the Federal benefits. Quebec now found that she was suffering a substantial loss by not being party to the Agreements. M. Duplessie had, however, made it quite clear that his province would not enter the Federal plan. ;The alternatives now open to the Federal Government were clear. They could either increase the payments to Quebec, via a change in the equalization formula, or they could attempt to coerce Quebec, by financial pressure, to enter the agreements. Unfortunately for Canada, they chose the latter.

The action of the Federal Government in 1953 of increasing the rate of corporation tax credit to 7% from 5% only made the situation worse. Quebec was the only province which had imposed corporation tax at this level prior to 1953. The result of the increase of 2% on the credit allowed for increased benefits to all provinces but Quebec. The terms of trade were now turning, or being turned, against Quebec. Given the past history of Quebec - Canada relations considerable conflict was inevitable if the province appeared to be suffering from the effects of Federal discrimination, which she now quite clearly was. The Federal claim that uniformity of taxation was essential must have sounded very hollow in Quebec.

The conflict was heightened by the report of the Massey Commission[1] which recommended that the Federal Government should provide substantial financial aid to the universities. This was not a novel suggestion, the Rowell-Sirois Report mentioned that such a step might be desirable, but had been too wise to suggest methods. The Massey Commission suggested that Federal payments to the universities should be in the form of a grant paid direct to each university on the basis of the proportion that its enrollment had to total university enrollment in the province. All education is, of course, the responsibility of the provinces, and education had been a particularly sensitive area in French - English relations. Nevertheless the Federal Government accepted the Report. The Federal Government began to make payments to the universities in 1952, at the rate of 50¢ per capita of the provincial population. Quebec universities accepted the grant for the first year of its operation, which was, of course before the change in the corporation tax credit, but refused to accept the grant, on the instructions of the provincial government, for the years following. A battle was brewing. M. Duplessis was now, of course, able to use the Federal actions with regard to both the universities and the corporation tax as evidence of discrimination against Quebec. The conflict was to grow so intense, as we shall see later, that it brought an end to the Tax Rental Agreements.

The increased amount of flexibility allowed in the 1952 Agreements did mean that a non agreeing province could cause serious difficulties for

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[1] The Report of the Royal Commission on the National Development in the Arts, Letters and Sciences, 1951, Kings Printer, Ottawa.

the Federal Government if it so wished. Just how severe these difficulties could become was demonstrated in 1954 when the Quebec Government stated its intention to raise a provincial income tax at 15% of the Federal rate. The province's stated position was that a provincial tax would take precedence over a Federal tax, a claim which had no basis in law but which was to prove to be of great political value. M. Duplessis made the quite valid point that if the Federal Government made a tax credit of even 15% on personal income tax it would still cost it considerably less than if Quebec had entered the Tax Rental Agreement. After considerable negotiation the Federal Government agreed to a tax credit at the increased rate of 10%.

There were many reasons why the Federal Government was reluctant to make this concession. The most important consideration was the possible effect of any agreement on the other provinces, especially Ontario. If Quebec could have a tax credit of 10% or 15%, then why not Ontario; and if Ontario could, then why not British Columbia, or any other province which thought that this would increase its revenues? The Federal Government acted to forestall action by the other provinces by offering to allow credits at the same rate as for Quebec to all provinces and by calling a Federal Provincial Conference almost immediately.

Many problems had to be faced if the new agreements were to provide anything more than transitory relief from the intergovernmental conflict. It was especially important the more tax 'room' be allowed the provinces and that the level of Federal coercion be reduced. The continuing financial strains on provincial revenues, due either to massive growth in industry

and population or to the long standing stagnation in other regions, had to be accommodated to the maximum possible degree. It was essential, of course, that no province should suffer, financially, under any new agreement.

The minutes of the Conference show that all provinces considered themselves to be in a position of fiscal need. They all required either increased Federal grants or additional tax room. The Central Provinces were, as could be expected, more interested in gaining increased tax room, as was British Columbia. Those provinces with low per capita incomes sought increased grants. The attitude of the Federal Government had undergone a significant change. The Government of Canada was no longer appearing to be anxious, as previously, to gain the agreement of all the provinces to the agreements. J. Harvey Perry felt that the Federal Government had learned that the provinces would suspect and resent "...the big player who was too eager to take over the whole game. Now the Federal Government is letting the provinces come to it; and they are coming."[1]

The preliminary meeting of 26th April, 1955, allowed all governments to state their views and express their needs. British Columbia and Ontario were especially concerned by the pressures created by the continuing growth of their cities. The municipalities are, of course, the responsibility of the provinces. The provinces will not, of course, surrender these responsibilities to the Federal Government and will not welcome Federal aid which by-passes the province and goes direct to the cities.

At the Conference Premier Frost, of Ontario, stated that the 1944 provincial budget had allocated $18 million to municipal assistance,

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[1] J. Harvey Perry, Tax Paper No. 6, Op. Cit., P. 9.

but that this figure had risen to $165 million by 1954.[1] The limits to increases in municipal taxation were such that no large degree of assistance could be expected from that source. From 1945 municipal revenues from indirect taxation had risen from $305 million to $911 million in 1956.[2] In Canada as a whole provincial payments to the municipalities grew from $63 million to $340 million in the same period.[3]

During the full Conference held in October both the Manitoba and Ontario proposals were discussed at length. Ontario proposed that a province should be allowed to impose a personal income tax at 15% of the Federal rate, succession duties at 50% and corporation tax at 15%. If a province agreed to allow the Federal Government to collect these taxes it should receive compensation. The essential difference between the Manitoba and Ontario proposals was that the equalization payments were to be calcualted to the national average under the Ontario plan and to the average of the yield of the taxes in the most wealthy province in that of Manitoba. Both, of course, used the 15 - 15 - 50 formula. If the Ontario plan had been adopted the equalization payments to the less wealthy provinces would have been considerably reduced, since the national average is bound to be lower than the level of the most wealthy province. The increased cost of the Manitoba proposal, if the 15 - 15 - 50 formula was accepted by the Federal Government, would have been $141,871,000 over

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[1] Federal Provincial Conference, Preliminary Meeting, April 26th, 1955, P. 21.

[2] National Accounts, 1926 - 56., Op. Cit., P. 75.

[3] Ibid. P. 77.

that of the Ontario plan.[1]

The Federal offer was for a new type of agreement, to be called a Tax Sharing Arrangement, rather than a Tax Rental Agreement, and it incorporated elements of both the Ontario and Manitoba proposals. The Arrangements were to be based on (1) Grants based on current tax revenues; (2) Equalization payments and (3) Stabilization payments. In place of the 15 - 15 - 50 formula proposed by the provinces the Federal offer was for 10% personal income tax, 9% corporation tax, and 50% of succession duties. Thus a province which accepted the full Federal offer would not impose any of the three standard taxes. It would receive, as compensation, payments based on the 10 - 9 - 50 forumula. If a province wished to collect its own taxes its residents would receive tax credits to the rate of the new formula. Instead of the equalization payments being based on the national average yield of the three standard taxes, as under the Ontario proposal, or the average of the yield in the most wealthy province, as suggested by Manitoba, the Federal offer was for the payment to be calculated on the basis of the yield in the two most wealthy provinces. Under this arrangement Ontario would receive no equalization grant, British Columbia only a moderate amount and all the other provinces would be sure of some grant. A considerable degree of stabilization was offered by the Federal guarantee that the revenues of a province would not be allowed to fall to less than 95% of the average for the previous two years.

Quebec decided to continue her own tax collection. She was not

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[1]Federal Provincial Conference, October, 1955, Proceedings, P. 60.

prepared to surrender any of her rights to the Federal Government, and was still under pressure because of the university grants dispute which had still to be settled. M. Duplessis was not a man to surreneder under pressure and he did have considerable support within Quebec. This was, of course, a period of considerable tension between Quebec and Ottawa, and between M. Duplessis and the Prime Minister, M. St. Laurent. The internal pressures in Quebec associated with the growth of industries and considerable urban expansion were very great indeed. As with the other provinces expansion was bringing in its wake pressures and tensions which had been unknown before. In the case of Quebec these problems were increased by the need to adapt the educational system and by the continued dominance of Anglo Saxons in many of the provincial elites. The provincial government had campainged long and hard for its fiscal freedom but, in hard cash terms, it had acheived little. M. Duplessis had been prepared, in the name of provincial autonomy, to allow Quebecers to suffer financially. This, of course, had served to increase the pressures and tension within the province and between Quebec and Ottawa. Much of the difficulty would have been removed if the Federal Government had realized, as it did eventually, that there was little to gain but a lot to lose by following policies designed to coerce provinces into a uniform national fiscal system.

The submissions of Quebec at the Federal Provincial Conference stressed the need for a realignment of powers and revenues between governments in order that the many problems which resulted from the rapid rate of expansion of the economy could be met. The Federal payments to the

provinces were increased from $216.2 million under the 1952 Agreement to $626.4 million under the 1956 Arrangements.[1] The changes, while being substantial in financial terms, had not been substantial as far as principle was concerned. The 1956 arrangements were to prove incapable of accommodating the very rapid changes seen in Canada during the next few years.

The conduct of the St. Laurent Government in relation to the question of university finance is in many respects inexplicable. The actions of the Federal Government during this period seem to indicate that the plan was put into operation without much prior consideration as to possible political consequences. The recommendations of the Massey Commission were accepted and put into operation very quickly indeed. It is quite possible that if the Quebec Government had not been provoked by the Federal increase in corporation tax credits that the university finance crisis would never have occured. It almost seemed as if the Prime Minister, like Mr. Diefenbaker after him, equated provincial autonomy with increased Federal aid. Given the continued policy of M. Duplessis in relation to Federal interference in provincial matters the conduct of the Federal Government is inexplicable. Constitutionally the field of education is reserved exclusively to the provinces. One of the major reasons for this division in the B.N.A. was the need to assure Quebec that her unique educational system would not be exposed to attack by the English majority. By seeming to break this division of responsibilities the Federal Government offered M. Duplessis a valuable political weapon. He could now attack the Federal

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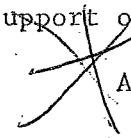
[1]Federal Provincial Conference, 1955, Proceedings, P. 60.

Government, and with considerable justification, on the grounds that they were attempting to destroy provincial autonomy, an attack which had the support of many Canadians.



After Quebec's refusal to accept the grants, or rather the Provincial Government's refusal to let her universities accept them, the Federal Government refused to alter the terms of the grant in any way. In particular Quebec's request for an unconditional payment was refused. The Federal Government obviously hoped that the fact that the grants were cumulative, and thus not lost to the universities if not claimed in the current year, would produce sufficient pressure on the Quebec Government to force their acceptance. If the situation had not been so serious it might have been comical, for here we see a Federal Government going to great pains to force a Provincial Government to accept a fairly large amount of money! What had begun as a generous Federal offer was now developing into a matter of principle, on both sides. The increase in the Federal payment from 50¢ to $1 per capita of the provincial population served only to heigthen the conflict. The action of the Federal Government in naming the National Conference of Canadian Universities as the (independent) administrators of the grant assistance was seen as a mere subterfuge.

The grants offered to the universities were unlike any other form of Federal financial assistance offered, as they were made, not to the provinces but to provincial institutions which were under the jurisdiction of the Provincial Governments. In the first place they were to be paid by an outside agency direct to Provincial institutions. Secondly there

was no question of the Provincial Governments being consulted, it was not a joint Federal - Provincial scheme at all. It is difficult to see what the Federal Government could hope to gain by prolonging the conflict. It is easy to see that they could not afford to be accused by the other provinces of favouring Quebec. It is also clear that a fairly simple solution could be found, as indeed it was when Mr. Diefenbaker took office. The payments could not be justified by reference to the Federal responsibility regarding economic and employment policy. They were not anti-cyclical since they were being made in a time of considerable inflation. Neither could they be justified as being equalizing in nature, since they were paid to all provinces on the basis of population. It may well be that the Federal Government was correct in its assumption that the universities were in need of additional financial assistance, indeed the Massey Commission had found this to be the case. Perhaps a more realistic solution would have been for the Federal Government to have offered a block grant for the general purpose of assisting education.

In an area such as education where the provinces have exclusive powers under the B.N.A. the provinces must be allowed to decide their own priorities. It is difficult to think of any other area, apart from religion, in which apparent Federal intrusion could be expected to create a greater degree of conflict than their intrusion into education.

This issue, which, in financial terms, was not great, kept the relationship between Quebec and Ottawa at a high level of tension over a considerable period of time. M. St. Laurent, by allowing a principle to develop over the matter, effectively manoevered himself into a position

from which he could not retreat. This, of course, provided M. Duplessis with an ever ready proof of the bad designs of the Federal Government, which he did not fail to use to his own political advantage. Even Liberals who were generally sympathetic to the Federal Government found that, on this issue, they were forced to support M. Duplessis. As Mr. Trudeau had said:-[1]

> "...[I]n other words the Federal Government collects funds from all ten provinces and redistributes it to all ten provinces, to finance a field which is not within its jurisdiction. This may be called centralization, but certainly not equalization".

How long this stalemate would have lasted if the Liberals had remained in power is difficult to say. The raising of the per capita payment to $1.50 in 1958 threatened to exacerbate the conflict but the new Progressive Conservative Government decided that the conflict should end. It was conceeded that the Federal Government would increase the level of the corporation tax credit from 9% to 10% for the residents of Quebec only. Quebec would not seek any additional aid for her universities. If the 1% credit resulted in Quebec gaining aid in excess of the amount under the Massey grants her equalization payments would be reduced by the amount of the excess. If the credit produced less, the equalization payment would be increased accordingly. The Quebec universities were quick to accept the grants which had been held from 1952.

Soon after being elected the Diefenbaker Government was placed under considerable provincial pressure to honour its pre election pledge to

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[1] Pierre Elliott Trudeau, Federalism and the French Canadians, Macmillan, Toronto, 1968, P. 82.

'restore provincial autonomy'. In particular the provinces wished to see a 15 - 15 - 50 formula in operation. The Federal Government could not be persuaded to go this far but did increase the credit of personal income tax from 10% to 13%. The Government also recognized the special problems of the Atlantic Provinces by bringing the system of Atlantic Provinces Adjustment Grants into operation. These grants equaled $25 million between 1959 and 1961-2, and has since increased to $35 million per year. The Royal Commission on Newfoundland Finances recommended that an additional payment of $8 million per annum be paid to that province, and despite considerable opposition from the Central Provinces, this was put into effect.

The changes seen in the rate of growth in all three levels of government can be seen from the following figures. Municipal revenues rose from $496 million to $1,463 million between 1947 and 1956,[1] and to $2,523.8 million by 1964.[2] Provincial Government revenues rose from $700 million in 1947[3] to $4,207.5 million in 1965.[4] Federal Government revenues grew from $2,602 million in 1947[5] to $7,180.3 million in 1965.[6] It again was becoming quite obvious that considerable readjustments to the pattern of intergovernmental relations were needed. Mr. Diefenbaker

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[1]National Accounts, 1926 - 56. Op. Cit., P. 75.

[2]Canada Year Book, 1968, P. 1055.

[3]National Accounts, Op. Cit., P. 75.

[4]Canada Year Book, 1968, P. 1047.

[5]National Accounts, Op. Cit., P. 75.

[6]Canada Year Book, 1968, P. 1030.

had indicated that this would receive a very high priority.

In theory these adjustments could be in the division of governmental functions as well as to their fiscal relationships. At the Dominion - Provincial Conference held in July, 1960, proposals were made, which would not only allow the provinces a considerable increase in tax room, but which also would bring about a significant change in the relationship between the provincial legislatures and their electorates. As mentioned above the provincial politicians were well aware that legislation designed to impose taxation, especially direct taxation of incomes, was, and is, always unpopular. Due partly to this knowledge and to the nature of the agreements since the war the governments had allowed a 'drift' to occur in their financial responsibility. The practice had been for the Federal Government and Parliament to become responsible for the raising of the majority of all governments revenues, and the provincial governments would take much of this money, via Federal grants and payments, and then spend the funds on provincial functions. It was not important that this practice broke the cardinal 'rules' laid down by academic experts in the field of federal finance, namely that each government should be responsible for the raising of its own revenues.[1] What was important was that the fears of the experts were being realized. It has never been possible for the governments in Canada to achieve this ideal. The division of responsibilities laid down by the B.N.A., and the revenue rights of the governments specified in the Act, have made this impossible. It is doubtful if any modern

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[1]See B. P. Adarker, Principles and Problems of Federal Finance, London, P. S. King & Son, 1933 and K. C. Wheare, Federal Government, Oxford University Press, Third Edition, 1953. For a more recent view see W. C. Hood, "Economic Policy in Our Federal State" Canadian Tax Journal, Vol. X11, 1967.

federal system in an advanced nation could acheive such a clear division of powers and revenues so as to ensure that no overlap of either occured.

Earlier writers have claimed that there was, in the early years of the Union, such a situation in the U.S.A.[1] More recent work tends to cast considerable doubt on these claims.[2] What is certain is that the situation no longer exists in any modern, advanced, federal nation.

It is quite possible that any attempt to acheive this ideal would bring an end to Canada as a nation. It would, for example, involve the termination of transfer payments from one level of government to another which, in turn, would mean that the standard of living in certain of the provinces would decline rapidly. It would seem to be inevitable that the Atlantic Provinces would be only capable of very limited governmental activities and that nearly all social services would prove to be too expensive for the provincial governments to operate.

The situation with regard to the other provinces, especially the most wealthy, also brings one to believe that such a division would be fatal to Canada. If these provinces found that they could provide a level of service which was acceptable to their electorates without Federal aid the value of staying within the federation would soon be brought into focus. It seems unlikely that defence would be a major problem and the G.N.P. of particular provinces already exceeds that of many independent states.

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[1]See A. H. Birch, Federalism, Finance and Social Legislation, Clarendon Press, Oxford, 1957.

[2]See Daniel J. Elazar, "Federal - State Cooperation in the 19th Century United States", in American Federalism in Perspective, Aaron Wildavsky, (ed.), Little, Brown and Co., 1967.

The principle, as often stated, also tends to ignore the role of a federal government in the control of an advanced economy. If the Federal Government is to be responsible for full employment, economic growth and stability it must have access to revenues in excess of those it needs to finance its own functions. If the Federal Government cannot decide, as a matter of economic policy, that a national surplus or deficit is required, it cannot control the economy.

Whilst it is accepted that the ideal would allow all governments the maximum amount of revenue room and would force all governments to be directly responsible to their electorates for the raising and spending of government finance such a method could not operate within the Canadian structure.

Mr. Diefenbaker did attempt, in a moderate fashion, to reaffirm the political and financial responsibilities of the provincial governments. At the 1960 Conference he insisted in future that all provincial governments would have to legislate their own direct taxes. Referring to the earlier agreements he said,[1] "I think it is fair to say that to some extent these agreements have transferred the interest of Provincial Premiers and their treasurers from their provinces to Ottawa". This was, of course, seen as a sign of the Government's intention to honour its election pledge to end the centralization process seen in Canada in the post war years. By the Federal - Provincial Fiscal Arrangements Act, 1961, which gave statutory authority to the agreements reached, largely in camera,

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[1] Federal - Provincial Conference, July 26th, 1960, Proceedings, P. 9.

at the Conference, the provinces were now committed to legislating their own personal income tax, succession duties and corporation tax. As far as the ordinary tax-payer was concerned there had been little change. The provinces could still appoint the Federal Government to be the collection agency. It was, however, one step towards bringing more financial responsibility to the provincial governments. The Federal Government no longer 'rented' tax rights from the provinces, instead it abated (i.e. withdrew) from certain tax fields up to a specified level. Another most important change was that a province which did not wish to enter a fiscal agreement with the Federal Government would be no longer placed in a position in which financial sanctions could be used against it. In addition a province could now impose direct taxation in excess of the Federal Rate. The Federal Government would still collect the provincial taxes, free of charge, on the province's behalf. This represented, in effect, the Federal Government calling the bluff of the provincial governments. It was not expected that there would be any sudden upsurge in provincial income taxes. This expectation was correct. The provincial governments have shown that they are not prepared, as yet, to accept the political consequences which might flow from their imposing a level of income tax much above the average. All provinces have, of course, been very quick to fill the 'room' left by the very considerable abatements allowed by the Federal Government over recnt years. No province has yet dared to impose an income tax much in excess of the Federal Abatement of 28%. This rate of abatement was raised from 13% to 16% in 1962. It was agreed that it would be further increased to 20% by 1966. In 1964 a new agreement allowed

for yet another increase to 24% in 1966 it was agreed that the abatement be increased to its present level of 28%. It can be seen, therefore, that there has been a most pronounced swing in favour of a high level of fiscal autonomy for the provinces. The Liberals have continued the trend of allowing increased abatements. It now seems impossible that the level of abatement could be reduced in the absence of some major national catastrophe.

As mentioned above the freedom allowed to the provinces to increase the level of their income tax has not had any noticeable effect on provincial finances. Since Quebec takes full advantage of the abatement points, described in detail later, she imposes income tax at the rate of 50%. Manitoba and Saskatchewan impose income tax at 33%, which is of course, 5% above the Federal abatement. This means that residents in these two provinces pay 5% more on income tax than do their neighbours. All other provinces impose income tax to match the level of the Federal abatement at 28%.

The claims made by the Diefenbaker Government that they had been able to end centralization do not bear close examination. Mr. Diefenbaker told the House of Commons,[1] "We have restored the inherent principles of the constitution, and this is something we undertook to do. We are ending centralization". In support of his claim to be increasing the degree of autonomy allowed the provinces the Prime Minister stressed that the provinces could now impose income tax at any rate that they wished. As we have seen the importance of this step was more symbolic than real.

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[1]Canadian House of Commons Debates, Vol. 8, 1960-1, P. 9002.

The level of Federal abatement was, after all to be constant across the nation. The Prime Minister's conception of decentralization and the province's view of autonomy could hardly be expected to coincide. The fact that the provinces receive any payments from the Federal Government at all indicates that their autonomy is less than absolute. Mr. Diefenbaker at times seemed to confuse a high level of Federal aid with provincial autonomy. In the debate on the Fiscal Arrangements he cited a rise in unconditional grants from $29 1/2 million in 1956-7 to $35 million by 1957-8. Conditional grants rose from $7,700,000 to $27,000,000 in the same period.[1] The increase in conditional grants at the expense of unconditional does not indicate a high degree of provincial autonomy, in fact the reverse is true. The total level of Federal contributions, including tax abatements, equalization grants etc., had risen from $689 million in 1956-7 to $1,470 million in 1960-1.[2] A Quebec Member, M. Chevrier, felt that the arrangements under M. St. Laurent had been preferable to the Diefenbaker plan. He claimed that, under the Liberal Government, "There was no centralization in the Tax Rental Agreements. Even during the war they were voluntary".[3] Later in the same speech he was moved to accuse the Government of "arrogant domination" over the provinces.

The Federal abatement in respect of succession duties was increased to 75% in April, 1964. The method of calculating the equalization payments

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[1] Ibid. P. 9005.

[2] Ibid. P. 9006.

[3] Ibid. P. 9008.

was also considerably changed. The national average yield of the standard taxes was now to be the basis of calculation but revenues from natural resources were also to be used. This reflected a desire to see equalization payments more in line with the actual resources of the provinces and was to be followed, eventually, by including all major government revenues in the calculations. In later agreements the practice of taking the average yield of the two most wealthy provinces as the basis of calculation was reverted to. This was, of course, a convenient method of increasing the payments to all but the most wealthy provinces and was of especial value to the poor provinces. Natural resource revenue was still taken into account. Any province which received natural resource revenue in excess of the national average had its equalization payment reduced by the amount of the excess. If a provinces' revenues from this source were less than the national average an equivilent increase would be made to the equalization payments. Stabilization was ensured by the Federal guarantee that the provincial revenues would be maintained at a level no less than 95% of the average over the previous two years.

In 1962-63 the Federal per capita payments in support of the universities were raised from $1.50 to $2.0. This meant that the 1% abatement in respect of corporation tax allowed to Quebec would produce less revenue than the per capita payments to the other provinces. The difference was to be made up via the equalization grant. Primarily because of the conflict over payments in this way the Federal Government decided that it would cease the per capita payments as from 1967. Following negotiations with the provinces it was agreed that the Federal Government would

either allow abatements or give cash grants equal to $15 per capita, or 50% of the cost of post secondary education, which ever was the greater. Thus a point of major intergovernmental conflict was removed. Total payments under this arrangement were $70,955,000 in 1967.[1] Much of the conflict seen over this issue could have been avoided if the Federal Government had not acted in a rather provocative manner in an area of clear provincial jurisdiction.

The extent of the changes seen in the relative levels of activity of the two major levels of government, and of the increased degree of independence allowed the provinces, can be judged by the changes seen in the calculation of abatements and grants over recent years. The provinces are now in a stronger position, economically and politically, than they have ever been. The Canadian federation is becoming increasingly centrifuagal in character, as each year brings an increase in population and a rapid rise in both the urban population and the G.N.P. The expansion of the cities and of industry in Quebec are now making the pressures on the government of the province very great indeed. Even by 1955 M. Duplessis was stressing the pressures created in his province by the expansion and growth of the municipalities. His call for increased tax room was not at all unlike the demands being made by the Premiers of Ontario, Alberta and British Columbia. In fact the general tone of the Quebec delegations' remarks was much less extreme than those made by Mr. Bennet. M. Duplessis stressed that access to independent revenues was essential for the provinces. He felt, of course, that the special problems of Quebec had

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[1] Canada Year Book, 1968, P. 380.

not been given sufficient attention in the past. He said: "Fiscal power is all the more indispensable in the case of a province, such as the Province of Quebec, which is developing itself with great strides; development which greatly enriches Canada, but which exacts on the part of the Provinces, numerous and additional outlays for new schools, new hospitals, for social legislation and for other provincial services."[1]

Whether the disparities in wealth and strength will produce stress too great for the federal structure to withstand in one of the most fascinating, and important, questions facing Canada in the remaining years of this Century. The stress now existing is very great and, as the population and G.N.P. continue to expand, it will without doubt continue to increase. The weakening of Federal power seen over the past decade has not been due solely to the pressures generated by the Quebec situation, which is itself a result of the economic changes seen in Canada and the provinces, but rather to the massive increases in revenues and responsibilities at the provincial level. No Federal Government which attempted to stem this flow would survive long. The changes seen in more recent years and their possible consequences will be discussed in Chapter Three, but it is important to note here that these pressures have had widespread effects on intergovernmental relations since the war. Too many political scientists have chosen to ignore what may be the most important aspect of Canadian federalism in the post war period.

It seems that the only possible manner in which the federation can be preserved, is that means be found to accommodate these changes by

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[1] Federal-Provincial Conference, October, 1955, Proceedings, P. 38.

allowing the provinces sufficient tax room and revenues with which to finance their ever increasing functions; while at the same time allowing the Federal Government sufficient powers to control the national economy.

That this process is already underway can be seen by the changes in provincial revenue structure. The 1957 formula of a simple abatement of 10 - 9 - 50 has now been replaced by a much more realistic and flexible series of agreements. The provinces now have much more freedom to 'opt out' of agreements and Federal schemes than ever before; and without financial penalties being incurred. The specific details of the opting out procedure are given later, but suffice it to say here, that there are two basic groups of programmes involved. If a province decides to opt out of a Categary One Programme it will be compensated by a Federal abatement which will allow it access to equivalent revenues. If a Categary Two Programme is involved the province will be compensated by Federal cash grants. Under Categary One the abatements now offered by the Federal Government are, in percentage points of personal income tax:-[1]

Programme	Abatement Points Allowed[2]
Hospital Insurance	14
Old age assistance, Blind and disabled allowances	2
Welfare portion of unemployment assistance	2
Specified technical education operating costs	1 (expired March, 1967)

[1] The National Finances, 1968-9, Canadian Tax Foundation, P. 139.

[2] One abatement point is equivalent to the average yield of 1% of personal income tax in two most wealthy provinces.

Health Grants 1

Categary Two Programmes which offer cash compensation

Agricultural Lime Assistance

Forestry Programme

Hospital Construction

Campgrounds and Picnic Areas. Roads to Resources Programme

Provinces which do opt out must be prepared to provide audited accounts to the Federal Government, and guarantee standards of performance. As could be expected, Quebec has made the maximum use of the right to opt out of Federal programmes. Quebec receives abatements in respect of all Categary One Programmes, and cash compensation for her contracting out of the Forestry Programme in Categary Two. Quebec therefore now receives a personal income tax abatement of 50% from the Federal Government.

The major change seen in the Federal Provincial Fiscal Arrangements Act, 1967 was a move to make the calculation of equalization grants more in accord with a province's actual needs by taking into account a wider cross section of government revenues received by provincial governments. The earlier decision to include natural resource revenues had, of course, been a step in this direction. The new method involves the consideration of sixteen, rather than three or four, sources of government revenue. The sixteen sources are:-

Personal Income Tax

Corporation Income Tax

Succession Duties and Estate Taxes

General Sales Tax

Motor Fuel Tax

Motor Vehicle Revenues

Alcoholic Beverage Revenues

Forestry Revenues

Oil Royalties

Natural Gas Revenues

Sale of Crown leases and reservations on oil and natural gas grounds

Other Oil and Natural Gas Revenues

Mineral Resource Revenues

Water Power Revenues

Other Taxes

Other Revenues

The actual method of calculation is quite complicated and does not strike at the root problem of regional disparity.[1] The aim of the arrangements was to allow all provinces to receive revenues sufficient to give them funds equal to the national average per capita yield from all sixteen sources. Using the sixteen sources of revenue as the basis of calculation Ontario, British Columbia receive no equalization grant. Newfoundland receives $48.7 million, Prince Edward Island $13.8 million, Nova Scotia $57.6 million, New Brunswick $54.1 million, Quebec $285.6 million, Manitoba $40.1 million and Saskatchewan $2.4 million.[2]

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[1]For an explanation of the arrangements and their defects, in relation to certain provinces see, Richard W. Collins, "Equalized Unhappiness" Canadian Tax Journal, Vol. 14, No. 1, Jan. - Feb., 1966.

[2]National Accounts, 1968-9, Op. Cit., P. 145.

The stabilization guarantee was 95% of the revenue for the year immediately previous to the year of calculation.

The most rapid 'shift' in favour of provincial autonomy may appear to have occurred during the time of the Diefenbaker Government. Indeed Mr. Diefenbaker's statements both before and after the elections that this was his goal and contribution to Canada make the picture somewhat confused. In fact the Federal reaction to the increased provincial pressures to allow for more flexibility and tax room to the provinces considerably pre-dates the election of Mr. Diefenbaker. The Federal withdrawal in the face of pressure from the provinces has been almost continual since the end of the Korean War. Given the massive changes seen in Canada during this period it is almost impossible to believe that the Federal structure could have survived if these changes had not been made.

The Liberal administration of Mr. St. Laurent had taken very important steps to allow the provinces a greater degree of freedom and room in their revenues to allow them to deal more effectively with their problems. It seems to have been that Government's sensible intention to avoid a head on clash with the provinces at any price which would allow Canada to remain a nation. The role of Quebec in this was, of course, very important but should not be overstated. Given the relative growth rates in government expenditures and revenues and the massive growth in the G.N.P., considerable conflict and change was inevitable. The rate of growth in the municipalities and the increased recognition of the social and welfare role of all levels of government had to lead to a reallocation of revenues. It was very unlikely that responsibilities would have been reallocated, for a great many reasons,

some of which are discussed later. The Federal Government's acceptance of the need for change was made clear during the 1955 Conference, with Prime Minister St. Laurent in the chair.

Mr. Campbell, of Manitoba, stressed the nature of the changes seen in the decade prior to 1955 by looking at the data supplied by the Conference Reference Book. The changes seen in the pattern of government expenditures must, he insisted, be met by a new type of Federal-Provincial agreement. The changes in government expenditures had been very rapid and extensive.

TOTAL GOVERNMENT EXPENDITURES 1945 TO 1955[1]

$000

Governments	1945	1955	% increase
Federal	4,526,710	4,773,065	5.5
Provincial	383,993	1,504,997	291.9
Municipal	343,857	1,292,887	276.0

It is, of course, important to remember that the municipalities are the responsibility of the provincial governments.

It was decided at this Conference that the changes which were occurring were so great that they required a much more sophisticated and sensitive system of intergovernmental consultation and cooperation. The Continuing Committee on Economic and Fiscal Matters resulted from these

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[1]Federal-Provincial Conference, October 3rd, 1955 Proceedings, P. 59.

talks. This Committee, which is composed of Ministers and officials who act as the official representatives of the Federal and Provincial Governments, has been of great value in the field of intergovernmental financial relations since the time of its creation. The type of agreement made between the governments have become much more complicated and of a more technical nature in recent years. This has been due, in large part, to the work of this Committee. While this has led to a more realistic set of arrangements, there are certain disadvantages. One of the most important of these has been the increased importance of permanent, full time, experts and officials at both levels of government. The increased bureaucratization of intergovernmental relations has led to a decline in debate, and the lack of clear answers, in debates within Parliament. The details of many of the arrangements are now so often highly specialized and jargon-ridden that the lay-man or ordinary M.P. is placed in a difficult and unequal position.

The increased need for flexibility, and the Federal recognition of this need; along with the realization that the provinces were becoming much too powerful to submit to Federal coercion are reflected in the following statement made by M. St. Laurent, made at the opening of the 1955 Federal-Provincial Conference.

> "[E]ach province might be free to decide whether or not it wished to use any of the three direct taxes itself -personal income tax, corporation tax and succession duties - or to rent them to the Federal Government. In a province that wished to use one or more of the direct taxes itself, our rates would be reduced by the amount of the standard rates and the province would tax those within its jurisdiction at whatever rate it

is possible to select."[1]

When viewed in this light the changes which took place during the Diefenbaker years were not as remarkable as they may appear at first sight. The changes were, in very large part, a continuation of the trend begun since the end of the war. It would seem that this trend will continue at an increased rate, at least in the absence of recession or war. It seems to be very unlikely that the extensive reapportionment of powers needed to reverse the present trend will be possible to achieve. The provinces, especially the more powerful and wealthy provinces, will never lightly agree to any diminution of their powers.

The Diefenbaker election platforms were very much in favour of provincial rights. He vowed that the provinces would be returned their constitutional rights which previous governments had denied them. This platform was not specifically chosen to appeal to Quebec, in fact the reverse was true. The Conservative M.P. Mr. Gorden Churchill had persuaded Mr. Diefenbaker that his major efforts should be concentrated in the West and the Maritimes. There are many historical reasons to explain the traditional anti-Conservative feelings in Quebec and Churchill's advice was for the Party to 'reinforce success, not failure'.[2] Diefenbaker's emphasis on a policy of decentralization paid great electoral dividends. Newspaper reports well demonstrate just how strong were the "Chiefs"

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[1]Federal-Provincial Conference, October, 1955, Proceedings, P. 17.

[2]Peter Reganstrief, The Diefenbaker Interlude, Rochester, Longmans, 1965, P. 29.

promises were in this regard.[1]

> "We will bring about a new, or at least a revised, fiscal system, to aid the provinces and municipalities which cannot now adequately discharge their responsibilities. We will bring an end to this centralization complex."

The Union Nationale Party in Quebec did, it is true, support the Conservative Party workers in the election campaign but this was not due to any sudden change in the long run political loyalties of the people of Quebec. It seems that M. Duplessis acted more against the Liberals than for the Conservatives. The help given the Conservatives was in retaliation for the intervention of Federal Liberal M.P.s on behalf of Liberal candidates in the Provincial Election of 1956.[2] The 1958 swing in the province, while quite remarkable, was not essential to the Conservative's electoral success and was not the result of hard campaigning by the Conservatives. The loss of St. Laurent, a native son of the province, as leader of the Liberals must have had some effect since Pearson was an unknown quantity as a possible Prime Minister. It is impossible to be sure how much appeal Mr. Diefenbakers' statements regarding the decentralization of power had in Quebec. It is quite possible that the rapid solution of the University grants question was of at least some electoral benefit to the Conservative Party. It is, however, quite clear that many of the pressures operating inside Quebec were based on very similar problems, increasing urbanization and economic advance, as in certain other provinces.

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[1] Globe and Mail, Toronto, November, 16th, 1957.

[2] Reganstrief, Op. Cit., P. 113.

It would be superfluous to attempt a full discussion here of all the changes seen in Quebec politics since the 1950's, but it is quite clear that the new forces operating to radically change Quebec-Ottawa relations are closely related to the economic advance within the province. The urban problem alone presented the provincial government with very severe financial difficulties. Between 1951 and 1961 the population of Quebec City increased by 29.4% and that of Montreal by 43.3%.[1] Between 1955 and 1965 Quebec provincial expenditure increased by 270% and provincial debt by 120%.[2] These increases were, proportionately, greater in Quebec than in any other province.

It is not suggested that the unique problems of Quebec, related to ethnicity and religion, have diminished in importance but rather that these problems are now bound up with problems that are common to several of the other provinces.

By the mid 1950s a reaction was developing, not limited to Quebec, against the continued centralization of power in Ottawa. For several years after the war many provincial politicians accepted, though with great reluctance, the claims of the Federal Government that it needed a dominant position in relation to government revenues in order to execute its anti cyclical policies. Many politicians and officials remembered the depression and were prepared to accept some constraints to ensure that this situation did not reoccur. The slow down in economic activity seen in

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[1] Canadian Facts, Toronto Dominion Bank, Toronto, 1967, P. 54.

[2] Donald V. Smilely, The Canadian Political Nationality, University of British Columbia, Methuan, 1967, P. 67.

the mid 1950s led government officials at the provincial level to reconsider the role of the Federal Government in relation to its control of the economy. The pressures on government revenues within all provinces were much greater than for many years. The growth in provincial governments expenditures was making it essential that the economic effects of provincial expenditures on the national economy be considered. The era of the rigid application of simplistic Keynsean theory to the national economy was drawing to a close. In a nation with very large variations in wealth and rates of growth between regions the economic policies suitable to one region may not be applicable to another. A national policy of deflation, for example, has always resulted in a much larger increase in unemployment in those areas, such as the Maritimes in Canada, which are already economically depressed.

Given the constitutional division of powers, which are not likely to change in the short term, the growth of certain provinces at the expense of others can only serve to increase the pressures on governments at all levels. All Federal Governments in recent years have attempted to relieve the plight of the poorer provinces by use of the equalization grants. As seen elsewhere, however, these payments are sufficient only to prevent the poorer from declining too rapidly, they are not sufficient to allow for much improvement. The other changes in the type of agreements, which have allowed for a great flow of power from the centre to the wealthy provinces, have done little to assist those provinces most in need. The political power of the industralized provinces has been too great to allow the Federal Government to render any high degree of aid to the depressed

regions.

It seems very likely that the Federal Government will continue to withdraw from the field of direct taxation. In fact, considerable additional abatements were offered during the 1968 Federal Provincial Conference. If a province was willing to assume all the costs involved in certain of the hospital insurance, health grants and the Canada Assistance Plan, and to guarantee performance to the national level, the Federal Government would allow an additional abatement of 17% on the personal income tax. No province has yet accepted this offer. Recent developments have served to show that increasing tax abatements do not necessarily indicate that the Federal authorities are prepared to allow the provinces the degree of freedom they now demand. Since the Federal Government's taxation powers are, constitutionally, unlimited, there is nothing that the provinces can do to prevent a determined Federal Government from raising the level of existing taxes, or, for that matter, inventing a new one. The imposition of a 2% Social Development Tax, to be collected along with, and at the same rate as, the personal income tax, is a case in point. This Tax, imposed in 1969,[1] has provoked considerable conflict between the Federal Government and the provinces, especially the more wealthy provinces. The tax will be used to raise revenue for social welfare programmes such as, for example, medicare. Since it is collected along with personal income tax it is payable by the residents of all provinces. This, in turn, means that if a province decides not to participate in those programmes financed by the Tax the residents of that province are denied benefits

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[1]By authority of An Act to Amend the Income Tax Act, 1968. See Canadian House of Commons Debates, Vol. VII, 1967-8., PP. 7673-7671.

to which they have contributed. What may be even more important, from the point of view of a provincial premier, is that the residents of the province will be aware both of the increased taxes they are paying and the fact that they are not receiving the benefits. This 'blackmail' or 'Machiavellian scheme'[1] has caused more tension between certain of the provinces and the Federal Government than any other single tax in recent years.

There has been some considerable conflict between certain of Mr. Trudeau's statements relating to the matter of provincial autonomy. On the university grants question Mr. Trudeau was clear in his opposition to Federal intervention in provincial affairs. He maintained that the provincial governments should be allowed the maximum possible freedom and should be allowed sufficient guaranteed funds in order to execute their functions in any manner that they saw fit.[2] However, even before becoming Prime Minister, Mr. Trudeau intimated that he would be in favour of a Federal medicare programme. "The Federal Government is still preparing (and has been since 1919!) a medicare program; when it is completed, you will see nationalists protesting that it should really come under provincial jurisdiction. You might think that in the meantime they would clamour for rapid provincial action to prevent terrible cases of deprivation. But do they? Not a bit of it: they claim that health is not the business of the state at all, but of 'intermediary bodies.'[3]

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[1]Premier Robarts, Globe and Mail, Toronto, February 12th, 1969.

[2]Trudeau, Op. Cit., P. 80.

[3]Ibid. P. 94.

It would appear that Mr. Trudeau had decided some time ago that, in the absense of adequate provincial programmes, health and welfare are so important as to be of national concern. This being the case national action would be justified. In effect health and welfare is receiving treatment as a 'special case'. The wisdom of this decision is difficult to assess and calls more for political judgement than fiscal theory. One effect of the Social Development Tax, examined elsewhere, has been to demonstrate that the Federal Government can still, when the need arises and the Government is determined, assert its authority to a very considerable extent.

The minutes of the Federal - Provincial Conference of 1969 demonstrate just how deeply the Provincial Premiers felt about the Tax. It had not been the Prime Minister's intention to have fiscal matters take up a major part of the discussions at the Constitutional Conference. All the provinces were, however, adamant that they should be, and that the talks should include discussion on posssible realignment of taxation sources for the Federal and Provincial Governments. The fact that the Conference was being televised live may account, to some extent, for the more colourful language and exaggerated claims and proposals made by certain of the Provincial Premiers.

Premier Bertrand, of Quebec, was particularly bitter about the growth of grants in aid, the conditions attached to the Federal abatements, and the Social Development Tax. The large amount of tax room posessed by Quebec, 50% of personal income tax, did not give the province the freedom to establish its own priorities, as it wished and was entitled to do. "The present Federal Government, strengthened by its lions share of tax

funds, a situation which we can never protest too strongly as unjust and contrary to the legitimate aims of the provinces, thinks it can meddle everywhere".[1] Quebec would not be satisfied until the constitution was rewritten to allow that province her 'fiscal freedom'.[2]

Premier Robarts, of Ontario, expressed his views very strongly both inside and outside the conference room. Addressing Mr. Trudeau he said, in relation to medicare, "If we don't succumb to your blandishments and yield to your pressures, the taxpayers of Ontario are not going to share in the money they are going to pay."[3] However, pressure inside the province must have been quite considerable, since it was announced in June, 1969 that the province would now enter the scheme in October, 1969. Ontario joined the other provinces in demanding that there be a fundemental re-drafting of revenue rights under the constitution.

The British Columbia Premier, Mr. Bennet, is of the opinion that the B.N.A. Act should be amended so that the Federal Government withdraws completely from the major fields of direct taxation. When this had been done "... it is our view that the constitution should restrict the spending power of the Federal Government to those matters under its jurisdiction."[4]

All provinces stressed the need for greater study of the problems and for an attempt to be made to realign revenues and responsibilities.

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[1] Federal - Provincial Constitutional Conference, 1969, Proceedings, P. 31.

[2] Ibid. P. 32.

[3] Globe and Mail, February 12th, 1969.

[4] Federal - Provincial Constitutional Conference, February, 1969, Proceedings, P. 88.

TABLE 2:3

SHARE OF TOTAL GOVERNMENT REVENUES COLLECTED 1967-69[1]

	Total Revenue of all Governments ($000,000)	Federal Government Percentage	Provincial and Municipal Percentage
Consumption Sales Taxes	$ 5,193	57	43
Personal Income Tax	5,115	71	29
Property Taxes	2,591	0	100
Corporation Income Tax	2,426	75	25
Customs Revenue	747	100	0
Natural Resource Revenues	513	0.4	99.6
Estate Tax & Succession Duties	217	24	76
Miscellaneous & Revenues from own sources	2,779	46	54
	$19,581	53.6	46.4

In a nation which has reached the stage of development where total government revenues, as a total of G.N.P., has risen from 15.7% in 1929 to 34.4% in 1967[2] it is to be expected that considerable friction will develop between the levels of government. This friction would occur in any nation, unitary or federal, which was undergoing such massive changes,

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[1]Federal-Provincial Grants and the Spending Power of Parliament, Government of Canada Working Paper, 1969, P. 8.

[2]National Finances, 1968-9, Op. Cit., P. 7.

but the nature of the differences seen in the nature of the Canadian regions, both with regard to variations in economic wealth and ethnicity, are bound to further complicate the problems. The provincial revenues, again as a percentage of G.N.P., rose from 5.9% in 1946 to 14.0% by 1967.[1]

Before considering in more detail recent developments in the field of intergovernmental financial relations, it may be of value to consider recent statistics of Canadian government finance. Of particular interest is the manner in which the various government revenues are divided between the provinces and the Federal Government. It must be remembered that, in addition to their tax revenues, the provinces are in receipt of considerable transfer payments from the Federal Government. It can be seen, therefore, that the Federal Government does not, in fact, dominate the revenue sources to the extent claimed by many provincial officials.

In fact if a province did decide to accept the abatements now in operation in Quebec, the level of abatement on personal income tax would be 50%, and if the province also accepted the abatement offer made at the 1968 Conference, the level of abatement could be 67%. This would, of course, mean that the province would have to contract out of a very wide range of Federal social welfare programmes, which might be unpopular within the province. But the option remains. The Federal Government would, however, still retain considerable control via the requirement that the level of service be maintained at a reasonable level and the Federal audit.
As with any politician, provincial leaders are well aware that taxes, and direct taxes in particular, exact a political price at the polls, which

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[1] Ibid. P. 7. This figure includes transfer payments from the Federal Government.

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many provincial politicians are reluctant to incur. In many cases it is preferable to have the Federal Government impose taxes and collect them. It may well be that "... the taxpayer of Canada does not particularly care which government, Federal or Provincial, taxes him."[1] But what is certain is that any taxpayer, Canadian or otherwise, will react to taxation which he considers to be unfair or excessive.

The total expenditure pattern of Canadian governments indicates why, given the constitutional division of powers and revenues under the B.N.A. Act there is so much conflict between the provinces and the Federal Government. Defense expenditure takes only 11% of total government revenues. Defense is, of course, a Federal responsibility. The other major areas of government expenditures are, however, in areas of provincial jurisdiction. Thus education takes 17%, social welfare 16%, transportation 12%, and health 10%[2] of total Government revenues.

It is accepted that, as Canada continues to develop, the trend towards urbanization will also continue. This will inevitably result in continued and increasing pressures on the provinces and this will be reflected in increased demands for more tax room or unconditional grants from Ottawa. The provinces do realize that the Federal Government has important obligations to meet. Many of these obligations, defense and control of the economy, for example, cannot be met by the provinces. Louis Robichaud, of New Brunswick, recognized these needs and brought a note of reality to the 1966 Federal Provincial Conference. He noted

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[1] Premier Robarts, Federal - Provincial Conference, 1969, Proceedings, P. 19.

[2] National Finances, 1968-9, Op. Cit., P. 12.

that:-

> "The Federal Government surely requires effective control of certain tax fields to ensure economic stability and to promote vigorous national growth. The Provinces need increased funds if they are to fulfil their constitutional responsibilities. On a purely fiscal basis the problems are insoluble... we can hope for nothing more than a fiscal compromise."[1]

The exact percentage of tax revenues which the Federal Government needs to possess in order to be a position to impliment anti-cyclical policies is not yet known. The Federal guarantee to maintain provincial revenues at 95% of the previous year's level provides a valuable measure of stability, not only for the provincial governments, but for the national economy also. It is, however, quite obvious that the Federal Government must have access to very considerable revenues before it is in a position to make a guarantee of this kind. This guarantee alone, however, would be of little assistance in the event of a severe downturn in the economy. It would prevent the reoccurence of certain of the worst aspects of the 1930s, but, by itself, it is not enough. Any major downturn in the Canadian national economy is unlikely as it is the consequence of a similar situation in the U.S.A. In such a situation the Federal Government, or rather all governments combined, would need to impliment coordinated and comprehensive programmes to counter the recession. A stockpile of public works and construction of all kinds needs to be 'kept on the shelf' so that unemployment could be allieviated and the business cycle restored. The present situation in Canada leaves much to be desired in this respect.

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[1] Federal-Provincial Conference, 1966, Proceedings, P. 104.

There are doubts that the Federal Government has sufficient control of the economy to reinforce monetary policies. Even in the absence of a serious decline in the level of economic activity the Federal Government is well aware, if certain of the provincial politicians are not, that constant week to week adjustments have to be made in order to preserve high levels of productivity, employment and growth. The situation has already been reached in Canada where certain economists doubt that the strength of the Federal Government is sufficient to exercise the degree of control necessary in an advanced economy. "Anti-recessionary fiscal policy is now less capable of providing support for monetary policy than at any time since the war... [T]he provinces have so strategic a role in both tax and expenditure policy by virtue of the relative weights of their budgets and from the fact that much of the initiative for change now rests with them."[1] The diverse needs in the regions are so great that it has proved impossible for the provinces to cooperate to the point where a comprehensive policy could be agreed to.

The hopes of the Founding Fathers, that Confederation was only to be a temporary phase in the development of the Canadian nation, have been dashed. The French factor may have been important, and probably the most important, reason for the creation of a federal state, but variations in regional economic conditions will ensure that the Canadian Federation remains, at best, a very loose structure indeed. Given the degree of diversity it is unlikely that a close federation on, say, the Australian pattern, could ever be acheived. When economic diversity is compounded

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[1]W. C. Hood, "Economic Policy in Our Federal State", Canadian Tax Journal, Vol. 12, 1964, P. 394.

by ethnic diversity there is even less chance of this occuring. "Federalism [in Canada] is not a stage on the path to the creation of a unitary state."[1]

The claims made by the wealthy provinces in Canada, to the effect that they are entitled to 'autonomy' in fiscal matters simply cannot be met within the Canadian federation. If transfer payments to the poorer provinces were to cease, a very severe fall in the standard of living would result. This is especially true of the Atlantic Provinces. The demands which certain provinces have made, to the effect that the Federal Government should withdraw completely from the field of direct taxation, would, if implemented, place the existence of Canada in danger. If Mr. Bennet's demands were met, the Federal Government would lose revenues worth $6,510 million out of a budget of $11,730, in the 1968-9 tax year.

The provinces do not have, never have had, and cannot have, within the Canadian Federal structure, fiscal autonomy. "Financial autonomy exists when there is no pressure on a Province, either directly or through conditional grants, to make expenditures or perform actions which it would otherwise not wish to do."[2] Given the Federal obligations relating to the less developed regions, to social welfare and employment, it is impossible for this situation to exist in Canada. It may well prove to be matters relating to economic and fiscal matters which will provide more conflict within the nation than the conflict between the two founding races.

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[1]National Finances, 1968-9, Op. Cit., P. 37.

[2]R. Deham and J. N. Wolfe, "The Principles of Federal Finance and the Canadian Case", C.J.E.P.S., February, 1955, P. 65.

The intense feelings of frustration, of being neglected, and of being misunderstood or ignored by the majority of the nation, are in no way limited to the residents of Quebec. Neither is the feeling that certain regions and provinces are suffering hardship because of their membership in the Canadian Federation. The Atlantic Provinces, as we have seen, have suffered a severe economic decline since the time of Confederation. This decline has been characterized by an increase in the average age of the population and a decline in incomes and employment. The industrial provinces all benefit from the tariff but the poorer provinces, being less developed industrially, suffer by it. Little has been done to stimulate industry in the area or to releive the financial pressures on the provincial governments. As Mr. Robert Stanfield pointed out, the principle of equalization as it operates at present is insufficient for the needs of this region. Even with the Atlantic Provinces Adjustment Grants, only the most basic level of provincial government services can be maintained.[1]

There has been over the past few years, a very noticeable change in the attitudes of several of the provinces to the question of intergovernmental financial relations. Mr. Bennet, of British Columbia, has grown much more ambitious as his province has expanded. Content in the late 1950s with requests for larger Federal abatements in the direct tax fields he has, of late, been demanding that the provinces should gain the exclusive rights to these fields. The conflict between Mr. Bennet and the Premiers of less wealthy provinces, especially Mr. Smallwood, has, at times, been quite bitter. The attitude of Quebec seems to have moderated

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[1]Robert Stanfield, "Nova Scotia Speaks", in Canadian Federalism: Myth or Reality? J. Peter Meekison (ed.), Toronto, Methuan, 1968, P. 227.

somewhat of late, although, of course, it would be rash to make any kind of prediction as to the future. The fact that the Prime Minister is French Canadian and is popular inside Quebec may be considerably important factors. There has been an increased concentration by the province on attempts to convince the Federal Government of the need for increased provincial autonomy and fiscal freedom. The present Quebec Government has, however, shown an acceptance of the principles of "economic interdependence, mutual support and cooperation between states and provinces, with every regard to the country's binational charactor."[1]

It is difficult, as yet, to see what the effects of the present Government will be on intergovernmental relations. Mr. Trudeau is perhaps unfortunate in having written so much about federalism, before becoming Prime Minister. It would seem that at one time the Prime Minister was very much in favour of a considerable degree of provincial autonomy.

> "[From these principles] it inevitably follows that the total resources available to the Canadian Treasury must be divided among the federal and provincial governments in such a way as to allow each government to look after the common good as it sees fit."[2]

The history of the medicare conflict indicates that the Prime Minister may have changed his mind.

The Tax Structure Committee provided a valuable report which, in a very few pages, outlined the crisis that Canada is now facing. It indicates that considerable changes in the pattern of intergovernmental

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[1]Government of Quebec, "What Does Quebec Want?" Ibid., P. 354.

[2]P. E. Trudeau, Op. Cit., P. 80.

relations and, perhaps, to the B.N.A. Act, will have to be made within the next few years. The Report stated:-

> "The expenditures rise as projected, and if tax rates and Federal transfers to the provinces remain as they were when the projections were made, the financial position of the provinces and municipalities would worsen and that of the Federal Government would improve. On these assumptions, and depending on whether G.N.P. grows at 6 or 7 per cent the provincial municipal deficit would increase from the present level of $900 million to about $2.4 or $2.1 Billion. The Federal Government's position would move from an approximate balance in the current year.... to a surplus of about $325 million or $725 million, depending on the rate of growth of the economy."[1]

G.N.P. has, in fact grown by an average of 5.9% in real terms.[2] It can be seen by the contents of the Report that it has been the rate of expansion of the economy which has produced strains on the system of government in Canada which are greater than ever before.

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[1]Report of the Tax Structure Committee to the Conference of the Federal-Provincial Governments, 1966, P. 123.

[2]Canada Year Book, 1968, P. 1058.

III Contemporary Problems, the Poor Provinces

As can be seen in previous chapters the problem of extreme economic diversity has placed great strain on the Canadian federal structure since the time of Confederation. As yet no concentrated effort has been made to solve the deep economic problems of the Prairie Provinces or the Maritimes. In all the developed provinces the problems of the cities continues to place great financial strain on the provincial governments. This problem is now national in scope. The population of Toronto increased by 18.3% between 1961 and 1966, that of Montreal by 15.5%, Edmonton 18.9%, Regina 16.9%, Saskatoon 21.3% and Vancouver 12.9%. Winnipeg had a population increase of 16.9%, Halifax an increase of 7.7% and St. John 5.9%.[1] Thus even in areas of relatively slow economic growth the provincial and municipal governments have severe problems to face. The older urban centres such as Toronto and Montreal have, in addition to expansionary pressures, to deal with severe problems relating to urban decay.

The problems associated with the rapid growth of the economy and the persistent inequalities seen between the regions are very important, perhaps more so, to the future of Canada, than the problems associated with French-English conflict. It is certain that the 'Quiet Revolution' and

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[1] Canada Year Book, 1968, P. 197.

the continuing conflict between Quebec and Canada are very largely a result of the economic disparity between that Province and the major English provinces. A failure to deal with the problem of economic diversity is just as likely to lead to a break up of the Federation as is a failure to resolve the matter of the cultural and linguistic conflict. The evidence suggests, not only in Canada but also in other federal states, that a system of government which allows and encourages a balance in the level of regional wealth and development will result in the elimination of substantive regional disparity and is a powerful stimulus for national unity and cohesion. The problems of particular regions and provinces in Canada are now so great that they present a truly national problem.

The major criticism of Canadian governments in relation to this area is that they have failed to recognize just how serious the problem could become. There have been many steps taken to alleviate the more acute of the problems but these have tended to be of a temporary and ad hoc nature. The principle of 'equalization' is paid lip service to by all leading politicians but the equalization grants paid to the less wealthy provinces do not provide a sufficient excess of funds to provide any appreciable stimulus to provincial government revenues. The major complaint with regard to past policies designed to assist these provinces is quite simple. They have not worked. Mr. George McClure of the Programme Development agency of Nova Scotia recently emphasized this point:

> "The disturbing fact is that the relative economic gap has remained constant for forty years or more. At the same time the absolute income gap has continued to widen--

> where in 1951 the difference between the average family income in the region and Canada was $1,200, it is now $2,400--despite numerous public efforts to redress the situation."[1]

The depth of the problem can be demonstrated by a wealth of data. The wide variations in per capita incomes, rate of expansion and urbanization all show that the post war period, especially from the mid 1950s, has placed great, perhaps intolerable, strains on provincial governments. These problems should not be considered in isolation but rather within the overall framework of national problems. The economic fragmentation in Canada could eventually lead to the loss of what degree of social cohesion and political identity which exists at present.

The regions which present the major difficulties are British Columbia, Quebec and the Atlantic Provinces. The problems of the Prairie Provinces are in a special category since it is the over-dependence of the region's economy on wheat which produces the major stress. The lack of an overall, comprehensive, national policy in relation to these problems serves only to accentuate the difficulties. The persistent problems of the Maritimes and of Eastern Quebec, are associated with a slow rate of growth and a very slow and belated transition from an economy which is resource orientated to one in which industry plays a more important role. The situation in British Columbia is, of course, quite different. The difficulties in this Province are related to the very rapid expansion of the provincial economy. Geographically isolated from the rest of Canada

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[1]Canadian Tax Foundation, Report of 21st Taxation Conference, 1968, (Toronto, 1969), P. 184.

and suspicious of the Central Provinces, British Columbia has adopted a policy which leads it increasingly into close economic ties with the United States.

The following tables indicate two measures of inequality between the provinces. Table 3: 1 indicates the growth of incomes throughout Canada since 1949. The wide variations in the rate of economic growth in the provinces can be seen by reference to Table 3: 2 which shows the growth in the number employed in each province since 1950.

TABLE 3:1

PROVINCIAL PER CAPITA INCOMES 1949 TO (ESTIMATE 1970)[1]

Per Capita Incomes (dollars)

Province	Average 1949-53	Average 1954-58	Average 1959-63	1964	Estimate 1970
Newfoundland	658	785	909	1002	1233
Prince Edward Island	745	820	1000	1168	1541
Nova Scotia	938	1049	1180	1272	1546
New Brunswick	863	937	1042	1164	1330
Quebec	1077	1197	1324	1461	1722
Ontario	1496	1629	1752	1886	2209
Manitoba	1276	1347	1509	1634	1940
Saskatchewan	1395	1251	1465	1544	1826
Alberta	1421	1465	1570	1645	1921
British Columbia	1517	1684	1750	1877	2178
Yukon & North West Territories	1000	1267	1216	1195	1787
TOTAL	1277	1387	1515	1640	1933

[1]Nariman K. Dhalla, These Canadians (Toronto: McGraw-Hill, 1966) P. 30.

TABLE 3:2

GROWTH IN PROVINCIAL LABOUR FORCES 1950 TO 1965[1]

Thousands	1950	1965	%increase
Atlantic Provinces	524	611	16.6
Quebec	1433	2022	41.1
Ontario	1826	2614	43.2
Prairie Provinces	951	1228	29.1
British Columbia	429	666	55.2
Canada	5163	7141	38.3

Other measures of provincial inequality include the aging population in certain provinces, low levels of industrial advance and decline in industries already established. Even differentials found in the salaries of government personnel and teachers are indicative of the different standards across the nation. A male graduate teacher in British Columbia could, in 1965-6, expect to earn in the region of $7,691, whereas a person with similar qualifications teaching in Newfoundland would earn $4,745. In Ontario 79.7% of secondary school teachers are university graduates, 75.6% in British Columbia and only 49.9% in Newfoundland.[2]

The steps taken by the provinces themselves to relieve their situation cannot, in reality, be expected to achieve any high degree of success. The Nova Scotia Voluntary Planning Organization, the Quebec Advisory Council and the Ontario Economic Council may all fulfill margin-

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[1] Ibid. P. 65.

[2] Canada Year Book, 1968, P. 374.

ally useful functions but they cannot, in the absence of a truly national policy, hope to solve the basic problems of the economy. To the extent that these bodies are competative they may well be detrimental in that they may serve to increase the differential between the provinces. The developments in relation to the Atlantic Development Board indicates that the Federal Government is belatedly attempting to stimulate the economy of the region. By March 31st, 1967, expenditures totalling $98,714,000 had been approved and some $54,069,000 had actually been spent to cover the cost of hydro-electric plants, highways, water supplies and harbours.[1] Another $1,253,875 had been expended to finance detailed studies of the economic needs of specific areas within the region.[2]

Other steps such as allowing increased depreciation allowances for taxation purposes to firms which locate in areas with high levels of unemployment will also be marginally useful. They cannot be expected to solve the problem.

Post war developments in other nations including the U.S.A., Italy, Eire, France and Britain could all provide valuable guidelines for the Federal Government. Such devices as 'tax holidays', provision of factory buildings and labour training schemes have all proved to be of great value. The difficulties in obtaining provincial consent and cooperation would, of course, be great. It at least possible that a prolonged Federal programme of persuasion would work.

The Agricultural Rehabilitation and Development Agency (ARDA)

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[1] Ibid. P. 1106.

[2] Canada Year Book, 1968, P. 1107.

which was established in 1961 is concerned with the efficient use of land. Its special concern is with the use of marginal land and unproductive acreage. It will be of only slight benefit to the Maritimes but is proving to be valuable as far as the Prairie Provinces are concerned. All the agencies above could serve a valuable role, and certainly be more useful than they are at present, if the level of inter-governmental cooperation could be increased. If and when the governments make the political decision to stimulate the economies of the depressed regions, up to the point where levels of unemployment and per capita incomes are not appreciably below the national average, such agencies would increase in value. They cannot, however, achieve much until such a decision has been taken. Canada does not lack the economic resources to take this decision, as yet she has lacked the political unity to make it. It is obviously very difficult to make a realistic estimate of what costs would be involved in effectively allieviating the problems of structural unemployment within the regions. Whalen estimates that the direct costs would be "about equal to the Canadian contribution to the St. Lawrence Seaway" with only minimal indirect cost, "certainly less than the annual hidden cost of the Canadian tariff".[1] The indirect costs of the tariff are estimated at about $1 billion a year.[2]

It is quite obvious that extensive changes are called for. It is not all clear that they can be achieved within the very loose federal structure of Canada. Considerable restructuring of constitutional re-

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[1]Hugh Whalen, "Public Policy and Regional Development: the Experience of the Atlantic Provinces", in Abraham Rotstein (ed.) The Prospect of Change, University League for Social Reform (McGraw-Hill, 1965), P. 109.

[2]Ibid. P. 118.

sponsibilities is essential if the changes are to be accomplished. The continued growth of the cities will increase the tension within the Federal structure by placing much increased financial burdens on provincial revenues. It is expected that the population of Canada will reach 25,000,000 by 1980; the urban population will be 81% of that figure.[1]

The decline of the old established occupations continues. Between 1950 and 1965 the number of agricultural employees fell by 41.7% while the number employed in fishing and trapping fell by 41.0%. The massive changes in the economy are also reflected by increases in the number of employees in financial, insurance and real estate, 97.2%, and in mining, quarrying and oil, 78.7%. The number employed in power utilities increased by 67.4%.[2]

That changes such as these can produce considerable pressures within any political system is undoubted. Within a federal state with the geographical area and ethnic composition of Canada these pressures are magnified. In a survey published in MacLeans Magazine in 1964, 29% of a sample of 1,042 Canadians favoured political union with the U.S.A. It is notable that those people with low incomes and poor education were more strongly in favour of such a union. Within the 29% national figure 39% of the people in the Maritimes favoured union, 33% in Quebec, 24% in Ontario and 29% in British Columbia and the Prairie Provinces.[3]

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[1]Canada Year Book, 1968, P. 1101.

[2]Dhalla, Op. Cit., P. 66.

[3]Ibid. P. 311.

These feelings may, of course, have changed in the five years since the survey was taken. However, there has been no dramatic improvement in the position of the provinces in the past five years. In a survey of 750 people in Quebec there was a distinct division between old and young on the question of succession from the Federation. Of French speaking Quebecers over the age of 25, 11.2% wished to see succession. Under that age the figure was 43%.[1]

It does not seem possible that a once and for all settlement to the problems of intergovernmental financial relations will be found. The intensity of the problems is great and will not decline in the near future. The expected growth of the G.N.P. and the increased level of government activity are bound to demand a great degree of cooperation between governments. Table 3: 3 indicates the probable rates of growth of the various levels of government in Canada.

TABLE 3:3

NUMBER EMPLOYED IN GOVERNMENT SERVICE, 1966 TO 1981[2]

Government Level	Actual	Estimated		
	1966	1971	1976	1981
Federal	228,325	270.049	315,912	365,227
Provincial	257,115	346.616	462.704	597,770
Municipal	224,715	301,708	400,493	515,516
TOTAL	710,155	918,373	1,179,109	1,478,513

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[1] The Weekend Telegram, (Toronto, Saturday, 28th June, 1969).

[2] J. E. Hodgetts and O. P. Dwivedi, "Growth of Government Employment in Canada", Canadian Public Administration, XXII, No. 2 (Summer, 1969), P. 234.

All advanced nations, federal and unitary, have been faced with serious problems of readjustment since the Second World War. The 'post industrial age' incurs costs as well as benefits. Other federal states have attempted to deal with the problems of intergovernmental relations in ways that are significantly different than the Canadian practice. In Australia institutions established during the years of the depression have played a decisive part in the post war period. In America the Federal Government has been able to consolidate its already strong position by its use of the income tax power and massive business interests.

It has been suggested that bodies similar to the Australian Loan Council and the Commonwealth Grants Commission would help to allieviate certain of the Canadian problems in the field of intergovernmental financial relations. There are, of course, many similarities between Australia and Canada. There are in both countries large areas as yet undeveloped with the population very largely concentrated in urban centres. Australian industry, like Canadian, is protected by a tariff wall which benefits certain regions at the expense of others. The constitutional position of the Commonwealth Government is basically similar to that of the Dominion except that the Commonwealth is responsible for old age pensions, invalid welfare, maternity and mothers allowances, and many social services. The States have less responsibilities relating to social services than do the provinces. The states are responsible for education, public health and hospitals.

As in Canada the regional governments are heavily dependent on the central government for revenues. In the 1956-7 fiscal year Common-

wealth grants made up 50% of New South Wales revenues, the figure was 54% in Victoria, 57% in Queensland, 53% South Australia, 66% Western Australia and 52% Tasmania.[1] The states are responsible for the administration of the municipalities.

The two bodies of major interest here are the Commonwealth Grants Commission and the Australian Loan Council. The Commonwealth Grants Commission was created in July, 1933, primarily to deal with the problems of the states with persistantly depressed economies. These states had been very badly hit by the depression. In the early part of 1933 Western Australia had voted 2:1 in referendum to seceed from the Commonwealth. The main achievement of the Commission was the recognition of the special needs of the claiment states' South Australia, Tasmania and Western Australia. The Commission accepted the principle that States should not be expected to impose very high rates of taxation or very low levels of service in order to balance their budgets. The Commission reported in 1934 that it found that the "net adverse effect of the Federal trade policy on the finances of the states is considerable for South Australia, still greater for Western Australia, but doubtful for Tasmania."[2] To compensate the states special grants of £1,400,000 to South Australia, £600,000 for Western Australia and £400,000 for Tasmania were to be paid. Thus the claiment states were recognized as being a national problem which demanded national action to deal with it. By recognizing that the Federal tariff policy did benefit certain states with an industralized economy at the

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[1]E. J. Hanson, Australian Commonwealth Grants Commission, Canadian Tax Paper No. 20, (Toronto: Canadian Tax Foundation, September, 1960), P. 10.

[2]E. J. Hanson, Op. Cit., P. 42.

expense of the rural areas the Commission had laid the way to national assistance to the badly hit states. The Commission accepted that no really scientific method existed by which they could measure the costs and benefits involved but they were able to recognize the need and reach reasonable recommendations in a pragmatic manner. Had the Atlantic Provinces been able to gain this recognition it is at least possible that conditions would by now be much improved. The success of the Australian experience can be judged by the fact that in 1959 South Australia had so improved her economic position that she no longer needed to be treated as a claiment state. In that year the special grants to the claiment states had been, on a per capita basis, £6 in South Australia, £14 in Tasmania and £17 in Western Australia.[1] All states receive compensation for the exclusive Federal occupation of the income tax field, which it was able to retain against bitter opposition from the states, following the last war.

The Loan Council, established in 1927, is the only government body allowed to raise funds on the international money market. All the states have equal representation with one vote each, but the Commonwealth has two votes in addition to its vote as chairman. This body decides how funds are to be raised, at what rate of interest, and how the money so raised will be distributed between the central and regional governments. From the time of its creation the Council and its operations have led to a large increase in centralized power in Australia.

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[1]E. J. Hanson, "Federal-State Financial Relations in Australia", Canadian Public Administration (March, 1962), P. 18.

The Australian federal structure is therefore, very centralized indeed. The Commonwealth Government has exclusive access to the field of income tax and a very strong voice in the control of loan revenue.

There has been a noticeable trend since the mid 1950s for grants from the Commonwealth to be in the nature of "block grants", which do allow the states some degree of latitude in planning their expenditure. The negotiations to decide on the distribution of revenue, both from the central government direct and via the Loan Council, are made at the annual meetings of the premiers. The state governments are, because of the centralized financial control, very much the junior members. It is by uniting that they can exercise persuasion on the Commonwealth. The lack of a developed system of local government in most of Australia means that the states assume responsibilities for, or administer Commonwealth schemes in, many of the areas of activity which are the responsibility of municipalities in Canada and America. The highly centralized federation in Australia is only possible because of the relative homogeneity of the population and the time of settlement. The fact that the central government does have control over the economy, to the degree that it does, allows it to control public expenditure to a very considerable extent and so enables it to cope with economic problems effectively. As Australian industry develops this may well prove to be of great value. Policies designed to deal with cyclical fluctuations in the economy can be dealt with rapidly, without the need for long consultations with the states. The considerable business operations of the states do, to a considerable extent, increase the economic importance of this level of government. How appropriate such

bodies as the Loan Council or the Commonwealth Grants Commission would be Canada is difficult to assess, although the fate of the Rowell-Sirois recommendations may give a fair indication. The granting of special status to the claiment states was very similar, in principle, to the proposal made by the Royal Commission that National Adjustment Grants be paid to the provinces. As seen in chapter one it was the wealthy provinces which would not have received such a grant which refused their cooperation and so prevented the implementation of the most important recommendation of the Commission. In effect British Columbia, Alberta and Ontario prevented the remaining six provinces, seven after 1949, from achieving the status of 'claiment' provinces.

Australia is, racially, a very homogeneous country. The influx of post war immigration has not significantly altered the political culture in this respect. Canada, on the other hand, in neither racially homogeneous nor possessed of sufficient political unity to tackle the economic problems of her less well developed regions in the Australian manner. The English-French conflict has been very important in the development of intergovernmental financial relations and will no doubt continue to be important in the future. The increasing ethnic diversity of the nation will also increase in importance. The percentage of non-French, non-British Canadians is now 53% in Saskatchewan, 49% in Alberta, 48% in Manitoba, 29.6% Ontario and 23.7% in British Columbia.[1] The long term effects of this diversity are impossible to assess. The later immigrants have entered a society in which the political culture has to a very large extent

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[1] John Porter, The Vertical Mosaic, Carleton University (Toronto: Toronto University Press, 1967), P. 77.

already become established. It seems doubtful that the 'mosaic' will produce as much strain on the federal structure as the level of economic diversity. It was, after all, the 'British' provinces which frustrated the implementation of the National Adjustment grants.

There can be, for Canada, no independent body to decide on the allocation of revenues between the governments or to decide which regions are in need of special assistance. The provinces act out of economic self interest and the Federal Government lacks the political power to impose its decisions upon them. Unlike the Australian situation, the regional governments still possess the power to impose their own income tax and this fact alone vastly increases their power at the bargaining table.

Despite the cultural similarities seen between the U.S.A. and Canada the Federal system and methods of government are very dissimilar. By the terms of the American Constitution it is the states which possess the residuary powers but the Federal Government, by its use of the tax powers has been able to influence the expenditures of the states. In particular it has been the Federal use of the income tax power which it shares, according to the Constitution, with the states which has led to claims that the growth in Federal Government activities is destroying states rights and destructive to democracy. The Federal Government has been able to effectively squeeze the state governments from the field of income tax. States revenues from income tax is only about 5 - 8% of the Federal total.[1]

There is a considerable degree of centralization within the

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[1]W. Walter Heller, New Dimensions of Political Economy (Cambridge, Mass., Harvard University Press, 1966), P. 127.

USA

American Federation, though not as great as seen in Australia. By the use of its taxing powers and its massive extension into the business life of the nation the Federal Government has been able to greatly increase its influence since World War Two. There has been a very considerable growth in Federal funds to the states in this period, mostly in the form of conditional or specific grants. In the 1920s the states received 3% of their revenues from the Federal Government, in the late 1940s 19% and up to 15 - 20% by 1965.[1] The indications are that this trend will continue. The Federal Government has increased its activities in the fields of pensions, education, and unemployment in much the same way as the other federal governments. By the Employment Act, 1944, it assumed the responsibility of ensuring that a high and stable level of income, employment and producitivity was maintained. The business interests and defence contracts have also served to increase in Federal influence. By use of its contact powers it is able to control the location of industry to a considerable extent and this, of course, can be a very valuable political tool. In 1963 the Department of Defence, the National Aeronautics and Space Administration and the Atomic Energy Commission spent on goods and services, excluding construction expenditure, $33 billion. This sum exceeds all expenditure on non residential private construction at $21 billion and exports at $31 billion.[2]

As mentioned above much of the Federal aid in the United States is in the form of conditional grants. The states are usually expected

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[1] Ibid. P. 143.

[2] Clopper Almon Jr., The American Economy to 1975, (Cambridge, Mass., Harper and Row, 1966), P. 86.

to match these grants with revenues of their own and so the influence of the Federal government is further increased. The operation of the various regulartory commissions and the virtual exclusion of the states from the income tax field are also significant certralizing forces. Australia and Canada face similar problems associated with a large and rapid growth in post war immigration and urbanization. In the United States the practice has grown for the Federal Government to deal directly with the municipalities. This has, of course, created considerable conflict between the states and the Federal Government. It is claimed that this practice serves to weaken the states politically and reduces the financial responsibility of the state legislatures. There is very little doubt that the Canadian Federal Government will be careful to avoid this trap. The municipalities are the constitutional responsibility of the provinces and they would not tolerate being by-passed in this way. Premier John Robarts, attending the 1969 Provincial Conference in Quebec, warned that the Federal Government must not 'leap frog' the provinces in this way. He accepted that the problem was serious and national in scope.

> "The cities themselves certainly do not have the funds to deal with such problems as inadequate housing, transportation and other services, and slum clearence (But) We can't have the Federal Government leap-frogging over the provinces and disturbing all their planning and priorities."[1]

Unlike the U. S. Federal Government the Canadian is not powerful enough to by-pass the regional governments. The wealthy provinces in Canada

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[1]The Telegram, (Toronto, August 16, 1969).

are too strong, from both the economic and political aspect, to allow the Federal Government to extend its powers and influence via the municipalities. By Section 92(8) of the B.N.A. Act. The provinces have the clear responsibility for the municipalities. It is inconceivable that this section would be amended without the consent of the provinces, and just as inconceivable that this consent would ever be given.

Given the diversity of Canadian society, and the economic diversity of the regions, the degree of centralization seen in both Australia and the U.S.A. would be unacceptable, in peace time at least. The major defect in relation to Canadian intergovernmental financial relations has been the lack of clear policy on the part of the governments. It is essential that the objectives of governmental financial arrangements be defined. The Federal Government has, over recent years, appeared to be reluctant to 'spell out' its objectives, perhaps because it has been reluctant to provoke the provinces. There has been little or no informed debate even within Parliament.

One major objective of policy which is accepted by all governments has been the preservation of a high level of employment and national income. Immediately following the war it was accepted that these policy decisions would necessitate the Federal Government having a great deal of control over direct taxation in order that it could operate anti-cyclcal policies. This is no longer accepted as readily by the provinces nor insisted on as strongly by the Federal Government. It is recognized that regional rates of growth are also very important in this regard.

The principle of 'equalization' has also been accepted for a great

number of years by all levels of government. Little clear thinking seems to have taken place in the post war era, however, as to what precisely is meant by 'equalization'. Are the Atlantic Provinces and the Prairie Provinces simply to be maintained at their present unequal position or are they to receive sufficient revenues and assistance from the rest of Canada with which to develop their economies? Are transfer payments to be regarded as mere hand outs or as reasonable economic investments for the national good? If the former, the present payments will suffice, if the latter, the payments will have to be greatly increased.

The conflicts within a federal state in which both levels of government are entitled to impose the same taxes is complicated by the fact that the division of responsibilities involving expenditures, i.e. the allocation of government functions, is much more easily achieved than the division of revenue sources.[1] The constant provincial demands that the B.N.A. Act should be extensively amended in order that their revenue sources would be increased, so that they may be able to finance all their own functions without reference to the Federal Government, will almost certainly not be met in the near future. The difficulties involved in arriving at an acceptable formula to allow for amendment are great. It is unlikely that the Federal Government will voluntarily surrend the resource fields demanded by British Columbia, Ontario and Quebec. Before discussions relating to the amendment process can have any real meaning, it is necessary that the future roles of all governments be considered. In particular the

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[1]James H. Lynn, "Federal-Provincial Fiscal Relations", in J. Peter Meekison (ed.), Canadian Federalism: Myth or Reality?, (Edmonton: Methuen, Toronto), P. 202.

circumstances under which the Federal Government may intervene in provincial affairs, either directly or by means of grants, is in need of clear definition.

Such factors as the Parliamentary system of government would presumably be sacrosanct, although it may be at least in part responsible for the lack of articulation of regional interests. The Parliamentary system mitigates against the formation of interest groups, regional or otherwise, which cross party lines. Hodgetts found that:

> "There are few genuinely spontaneous regional interests in Canada that have an independent impact on policy; and where they do exist our political system, working through disciplined parliamentary parties, only permits them to be aggregated and articulated within conventional regional boundaries."[1]

Even when the regions and provinces have been able to articulate their demands, often at extra Parlimentary meetings such as Federal-Provincial Conferences and the various continuing committees, the measures taken to meet the problem are often inadequate. It is also very difficult to measure the impact of Federal aid schemes and expenditures designed to assist provinces.[2] In many cases it is doubtful if the funds are used to the best possible use.

It is also important that the role and effects of the political parties in Canada be briefly mentioned. The national organizations of the major parties do appear to be gaining in influence, due, in large

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[1]J. E. Hodgetts, "Regional Interests and Policy in a Federal Structure", C.J.E.P.S., XXXII, No. 1 (February, 1966), P. 13.

[2]Thomas N. Brewis, Carleton University, in Report of 21st Taxation Conference, Op. Cit., P. 189.

part, to their control of campaign funds, but they are still relatively weak. Parties are still not to be regarded as national in character. The provincial parties continue to be the most important units of the party system. These parties will join together at election time, and will receive at least some financial assistance from the national organization, but cannot be regarded as being under the control of the central organization. It may well be that "[N]ormally the maximum cooperation and friendliness can be expected when Dominion and provincial governments are controlled by the same party,"[1] but there is no guarantee of this. The relationships between Premier Robarts and Prime Minister Diefenbaker, and between Premier Hepburn and Prime Minister King indicate that niether major party is immune to intra party strife.

It is difficult to assess if it is more advantageous for a provincial party to be of the same party as the Federal Government or not. If the provincial and Federal Governments are of the same party the provincial party may find itself considerably restrained in its power to criticize, in public at least, the actions of the Federal Government. Much of the tension within the party structure stems from the fact that there is essentially two party government at the Federal level and a multiplicity of parties at the provincial level. The fact that a party has the same name at both levels does not imply that one controls the other. It may be, in fact, that a provincial party which is seperate in identity from any Federal party will still render assistance at election time. Thus the Union Nationale in Quebec has cooperated with the

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[1]Dawson, Op. Cit., P. 526.

Progressive Conservative Party.

By the very diversity of the nation the demands from the provinces, and the pressures on the provincial parties, are themselves diverse. One factor is, however, to a very large degree constant. All provinces are in need of Federal subsidies in order to execute their functions and the success of a provincial government will be measured, by many of the electorate, by the amount of aid it is able to attract from Ottawa. The provincial demands will continue no matter which party is in power at the Federal level.

A provincial government which is of a different party to either the Government or opposition in Ottawa is, in many ways, at a considerable advantage over the other provinces. Such a party is in a position to bargain with both major parties and to trade one off against the other. Thus the Western Provinces are able to make extreme demands of the Federal Government; see, for example, Mr. Bennet's proposals relating to taxation, without fear of political embarrassment within their own governing party.

The divisions, ethnic and economic, within the nation are naturally reflected in the scatter of provincial parties and in the accommodative nature of the two major Federal parties. Any Prime Minister would, for partisan reasons, like to see all provinces under the control of his own party. There is some doubt, however, that this would be of any real advantage. It would be impossible for the Federal party to discipline or control the provincial parties, even if they did all share the same name. Dealing with this problem Engleman and Schwartz found that a Conservative Government in Ottawa need not be on good terms with Conservative governments

in the provinces. In fact the reverse might be true:-

> "Certainly, there is nothing like a Commons-like party division at federal-provincial conferences. If Premier Bennet of British Columbia is one of the chief demanders at these, he is so as spokesman of a heavily demanding province, showing more similarity to his Liberal colleagues, Lesage of Quebec and Smallwood of Newfoundland, than to his Social Credit colleague, Manning of Alberta."[1]

The present scatter of provincial parties provides a valuable 'safety valve' which allows for the articulation of diverse provincial interests without endangering the stability of the Federal Government. "By voting Social Credit into provincial power, for example, the voters of British Columbia can effectively express sectional interests, albeit in the guise of provincial identity, without necessarily damaging thereby the delicate balance of national unity....It may well be that this fact offers a vital flexibility, not only to the voters of the provinces, but to the entire national party system".[2]

The provincial parties do provide, therefore, a very valuable vehicle of organized opposition to the Federal Government. They have not, however, replaced to official opposition as the major vehicle of this opposition.[3] They are, rather, supplemental to it. We have seen elsewhere that the Parliamentary system itself makes it difficult to articulate regional interests inside the Federal parties and thus the provincial parties and the Federal-Provincial Conferences have a vital role to play.

By and large it is true to say that Federal parties have had little

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[1]F. C. Englemann and M. A. Schwartz, Political Parties and the Canadian Social Structure, Prentice-Hall of Canada, Ltd., 1967., P. 202.

[2]Steven Muller, "Federalism and the Party System in Canada", in Meekison, Op. Cit., P. 131.

[3]Englemann and Schwartz, Op. Cit., P. 202.

influence on provincial leadership or policies. "In Federal-Provincial negotiations, the nature of the conflict between the two levels of government, and not the partisan make-up of the provincial government, is the chief determinant of the relations between Ottawa and the provinces."[1]

Pressures on the federal structure are not only generated by the problems of the poorer provinces, there are also problems common to all the provinces. All the provinces would, for example, welcome a large increase in unconditional funds, but there are many areas in which provincial interests are divergent. In particular British Columbia, Ontario and Quebec have acute problems related to the very rapid rate of growth in these provinces, and the Atlantic provinces continue to suffer the chronic problems of structural unemployment and a very slow rate of growth. The economic problems of the Prairie Provinces related variations in the demand and prices of primary produce, create their own internal and inter-governmental pressures. The minimum objective of any federal financial arrangement must be to permit all governments sufficient funds to finance their operations at a reasonable level, having regard to the national standards obtaining and the expectations of their electorates. Public expectations do, of course, vary quite considerably over a period of time. It has been the increased expectations relating to health, welfare and employment that have led directly to much of the post-war disputes between governments in Canada. The need to maintain some minimum national standards is generally accepted. The problem of arriving at an acceptable method of financing these national minimum standards has as yet, defeated all attempts. It has been suggested

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[1]Englemann and Schwartz, Op. Cit., P. 203.

that all provinces should be guaranteed tax revenues equal to some national standard. This would involve considerable transfer payments and is unacceptable to the wealthier provinces. To talk of a national average tax structure makes little real contribution to the discovery of a solution in a nation, such as Canada, which is divided by extreme variations in regional wealth. The sacrifice demanded of those wealthier provinces are too great for them to accept. As Harvey Perry has pointed out, "[T]he average may not be a structure which is imposed anywhere or that anyone would agree to impose".[1]

The changes which could, in theory, be made to achieve an equitable distribution of revenue rights and responsibilities for expenditure are many. The strict delineation of taxing powers has from time to time has been suggested as one means by which Federal-Provincial conflict could be reduced. By this method one level of government would gain the exclusive use of a particular tax field and the other level would be assigned exclusive jurisdiction in another. It could be that the provinces would gain exclusive use to the field of indirect taxation and the Federal Government all direct taxes. This would achieve little under the present circumstances since the Federal Government would gain all the most bouyant tax revenues while the strain on the provincial revenues would increase as never before. Grants would still have to be made from the centre, and so the conflict would continue. The Premier of British Columbia has recently suggested that the reverse solution should apply, namely that the provinces should gain

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[1]J. Harvey Perry, "What Price Provincial Autonomy?", C.J.E.P.S., (November 1955), P. 439.

exclusive use of direct taxation. Thus the provinces would impose personal income tax, corporation tax and succession duties. If Mr. Bennet's suggestions were accepted, the Federal Government would be restricted to sales taxes and customs revenues for its income. The Federal Government would thus be deprived of $1.6 billion in 1968-9 and a sales tax of 21% would have to be imposed.[1] In addition the Federal Government's ability to carry out anti-cyclical policies would be very much reduced. The major advantage of such a division would be that competition, within tax fields, would be avoided. The disadvantages would be so great, however, that such a suggestion can not be taken seriously. The Federal Government would never consent to such a division since it would then lose the ability to continue the transfer payments to the poorer provinces and the ability to introduce national schemes of any major importance. The provinces have requested that they be allowed to enter all tax fields that the Federal Government now possesses. They have, in other words, requested concurrent taxing powers. Thus all governments would compete with one another for revenues. The history of direct taxation would indicate that this would serve to greatly increase intergovernmental conflict. The Federal Government would undoubtably still be in a position to squeeze the provinces from a particular tax field, if it was determined enough, and little would be achieved by such a move unless a considerable degree of intergovernmental cooperation was forthcoming. It is, of course, quite possible that the Federal Government would be prepared to allow the provinces to enter certain tax fields at present under its jurisdiction in return

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[1]R. Deham and J. N. Wolfe, "The Principles of Federal Finance and the Canadian Case", C.J.E.P.S., (February 1955), P. 14.

for provincial concessions in direct taxation rights. This would, however, involve an amendment to the B.N.A. Act. The major problem is that no one solution is acceptable to all ten provinces. The provinces are jealous not only of Federal incursion into areas in which they hold jurisdiction but also of other provinces receiving revenues which they do not. The provinces do not have a tradition of united opposition to the Federal Government in the same way that the states in both Australia and America. That this is not simply due to the Parliamentary system is indicated by the fact that the Australian system is also Parliamentary. It seems that the answer is to be found in both the ethnic and economic diversity of Canada. It is essential that any new arrangements still permit the Federal Government to make transfer payments to those provinces most in need of them, since, as D. V. Smiley says, "[I]t is doubtful whether the Canadian Federal system would last a decade if the Federal transfer payments were withdrawn".[1]

A system whereby the Federal Government retains its rights in the field of direct taxation, especially personal income tax, yet still allows the provinces the maximum possible freedom is one possible solution. Thus, in an emergency, the Federal government would still have the authority to act rapidly, either to put the economy on a war footing or to introduce anti-recessionary measures, while still allowing the provinces freedom in more normal times. The use of Federal abatement has much to recommend it. As seen in chapter two, the provinces are now entitled to impose personal income tax to whatever level they wish. The level to which the abatement

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[1]Donald V. Smiley, "Conditional Grants and Canadian Federalism: The Issues", in Meekison, Op. Cit., P. 263.

could safely go is open to some dispute. The Carter Commission[1] recommended that abatement should not exceed 50%, the present level allowed Quebec, in order that the Federal Government be able to fulfill its obligations regarding the national economy. All governments accept that the Federal Government has this responsibility and that, under certain conditions, the need for a national policy would be so great that individual provincial rights would have to be sacrificed but only, of course, for a limited period. The surrender of the income tax during World War Two was an example of this. Of course the problem of deciding what is and what is not a national emergency, or more importantly under normal circumstances, what is of sufficient national importance to justify Federal intervention, is a very delicate question. No theory of federalism can hope to cover all eventualities and the Federal responsibility for the general welfare of all Canadian and unlimited taxing powers does leave considerable room for the extension of centralized power.

Considering post war developments it would be inadvisable for the Federal Government to increase its intervention in provincial affairs. It is important that the legislative responsibility of the provinces be maintained. It should be only on matters of really national importance that the Federal spending power should intervene between the provincial legislatures and their electorates. If these principles are not respected, not only will the level of intergovernmental conflict increase, but also the financial responsibilities within the provinces will become even more

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[1]Canada, Report of the Royal Commission on Taxation (Ottawa: Queen's Printer, 1966), I, P. 48.

confused. When the Federal Government gives a conditional grant it is in effect legislating within a field of provisional competence.[1] The provincial governments naturally resent the conditions which are attached to many Federal aid programmes and this can result in a considerable loss of good faith in other negotiations. The Quebec-Ottawa battle over Federal aid to the universities was concerned not only with university finance but with the provinces right to use revenues to use as it saw fit. The hostility to centralized power is not restricted to the more wealthy provinces. Premier Smallwood of Newfoundland recently expressed his fears in relation to his authority in the Province. He said:

> "We were a colony of Britain for five centuries, long enough to know all about it. I don't think that it is any improvement to be a colony of Ottawa. They expect us to be seen and not heard, to take the crumbs and be grateful. But we are too independent to be told that father knows best."[2]

In the twenty years since entering the Federation Newfoundland has depended on the Federal Government for 45.4% of its revenues.

Even allowing for the pronounced swing towards a centrifugal federation since the 1950s the Federal Government still, in the final analysis, holds the 'whip hand' in negotiations. Unless a province can make a realistic threat of succession, for which it would need to be self sufficient financially, the Federal Government is aware that its preponderance of revenues will eventually win the day. The recent pattern of negotiations indicates that certain of the provinces are now in a

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[1] Donald V. Smiley, "The Rowell-Sirois Report, Provincial Autonomy, and Post War Canadian Federalism", C.J.E.P.S., (February 1962), P. 61.

[2] Globe and Mail, (Toronto, July 1, 1969), P. B1.

financial position in which they could, if need be, support themselves without need of Federal subsidies. This is reflected in the much stronger line taken by the provinces at Federal-Provincial Conferences and in the press. There are, of course, many other factors than the economic to be considered before a province would even consider succession, but the Federal Government has recognized the depth of the provinces desire for an increased say in their own affairs.

The question of provincial autonomy continues to be of the greatest importance in Canada. The provinces do not object so much to the level of Federal aid as the conditions which are attached to the funds. It is certain that any attempt made to extend conditional grants, and therefore to reverse the present trend to a very loose, decentralized, federation, would be met with very strong provincial opposition. H. F. Angus explains the provincial opposition to conditional grants in this way:

> "If the Federal Government uses a source of revenue to which the provincial governments feel that they have a prior claim and collects a fund in excess of its own needs (including in these needs assistance for distressed provinces) it holds money which in equity belongs to the provinces."[1]

If the Federal Government then returns the revenues to the provinces in the form of conditional grants "....it may appear to be stealing, rather than buying, control".[2] If intergovernmental conflict is to be minimized it would seem to be advisable that conditional grants are used only under

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[1]H. F. Angus, "Two Restrictions on Provincial Autonomy", C.J.E.P.S., (November, 1955), P. 446.

[2]Ibid. P. 466.

conditions where it is essential that basic national standards are preserved.

'Fiscal need' will continue to be an important concept in future Federal-Provincial negotiations. As long as the Federal Government continues to raise revenues in excess of those needed in order for it to meet its own constitutional responsibilities grants, conditional and otherwise, will continue to play an important part in provincial government revenues. The calculations related to grants to the provinces are based, in large part, on arbitrary decisions as to the needs and responsibilities of the provinces. Scientific techniques by which fiscal need may be accurately measured are not, as yet, available. The calculation of grants to be paid include consideration of the population income and other revenues available to the provincial government. The revenue potential is more ameanable to scientific measurement than fiscal need. The potential can be measured by reference to the yield, in a particular province, of the national standard taxes. Equalization payments will be made to compensate the province for any deficit between it's yield and the average yield in the two most wealthy provinces.

It may be suggested that some form of independent body, perhaps on the style of the Grants Commission in Australia, should be established to calculate the revenues needs of all governments and that this body's decision should be binding on all. The diversity of resources, loyalty and interests demonstrated elsewhere in this paper show that a body such as this would be impossible within the Canadian federal structure. Even if restricted in scope to the level of the Loan Council it would never

gain the cooperation of the provinces. Rich and poor alike would resist. Decisions relating to government finance are political decision with enough emotional impact to split the nation. The widely divergent stances adopted by the Provincial Premiers are not simply the result of political manoevering or personal characteristics of the Premiers but are indicative of the vastly differing interests of the provinces. Uniformity of income and opportunity cannot be imposed upon a nation which is as divided as Canada.

Given this situation it appears impossible to devise such a division of revenue sources and governmental responsibilities which would enable the Canadian federation to operate without a great deal of Federal-Provincial conflict and without requiring a great deal of Fedral-Provincial cooperation and consultation. In J. A. Corry's opinion:

> "It is most unlikely that any constitution could be devised which would enable each (government) to perform its specific functions adequately wihtout impinging seriously on the others. So their activities are inevitably intermingled and cooperative arrangements must be worked out."[1]

There has, in fact, been a quite considerable growth in intergovernmental cooperation and consultation during recent years. This has occured at the Federal-Provincial, the Provincial-Municipal and Interprovincial levels. In 1957 Dr. K. W. Taylor listed sixty-four Federal-Provincial committees which met on a more or less regular basis. By 1965 there were 125.[2] The

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[1]J. A. Corry, "Constitutional Trends and Federalism", in R. M. Clark (ed.), Canadian Issues: Essays in Honour of Henry F. Angus (Toronto: University of Toronto Press, 1961), P. 20.

[2]Edgar Gallant and R. M. Burns, The Machinery of Federal-Provincial Relations (Toronto: The Institute of Public Administration of Canada, 1965), P. 3.

number of committees had doubled in eight years. There has also been an increase in the number of informal contacts between officers of all levels of government.

The more important continuing committees, including representatives of all governments, are the Continuing Committee on Fiscal and Economic Matters and the Conference of Ministers of Welfare. The Federal-Provincial Conferences are the most important meetings at this level. There has been a very considerable growth in advisory committees which operate to provide expert assistance to governments. The Continuing Committee on Economic and Fiscal Matters is not able to formulate long term policy on its own initiative but has a successful record of dealing very effectively with short term solutions to specific problems.[1]

With the expansion of intergovernmental consultation Smiley has noted that there has also been a change in the nature of the negotiations. He feels that the negotiations have become akin to negotiations between separate states rather than between different levels of government within the same nation.[2] Also noticeable has been the increased number of specialist, well trained, officers at the provincial level.[3] It is, of course, true that there have been developments in this direction and that Quebec, in particular, would like to see intergovernmental discussions treated as negotiations between 'states', but the fact remains that the

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[1]See A. R. Kear, "Cooperative Federalism: A Study of the Federal-Provincial Continuing Committee on Fiscal and Economic Matters", Canadian Public Administration, (March, 1963).

[2]Donald V. Smiley, "Public Administration and Canadian Federalism", Canadian Public Administration, (March, 1964), P. 374.

[3]Ibid. P. 377.

Federal Government employs four hundred full time diplomats to deal with international affairs but relatively few to deal full time with internal intergovernmental relations.[1]

The changes brought about by Mr. Diefenbaker in forcing the provincial governments to legislate their own direct taxes have not had any great practical effect. Given the very large amount of funds emanating from Ottawa provincial officials still tend to be as concerned, if not more so, about their relationship with Federal officials than with their own legislatures.[2] As the nation continues to develop and G.N.P. to grow the revenues from direct taxation will also increase. If considerable reallocation of revenue sources is not made, and it is difficult to believe that it will be, the revenues of the Federal Government will be increasing at the same time that internal pressures in the provinces, related to the growth of cities and industry, are also much increased. The gap which at present exists between the provinces in relation to the varying degree of urbanization and wealth will also increase. If the Federal Government's role in the control of the national economy is accepted that Government cannot acceed to the provinces request that it withdraw from the field of direct taxation. This being the case, the only manner in which the trend towards provincial autonomy can be accommodated (there seems little chance of it being reversed) is by an increase in the level of unconditional grants to the provinces. In 1968-9 $1,616.9 million was paid to the provinces

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[1] Gallant and Burns, Op. Cit., P. 6.

[2] Donald V. Smiley, in Canadian Tax Foundation, Report of the 1964 Conference, (Toronto, 1964), P. 220.

in conditional grants and $865.0 million unconditional grants.[1] In the face of the increasing pressures from the provinces it is highly probable that the level of unconditional aid will increase and that of conditional fall.

It is, of course, important that the special problems of Quebec be not ignored. It is also important, however, that the basis of much of the provincial unrest be understood, and dealt with as well as is possible within the loose federal structure of Canada. It should be appreciated that many of the Quebec problems are common to all the provinces in economic expansion. As Rene Levesque has said, "Our great weakness (individual and collective), and the source of nearly all the others, is economic. That, in my opinion, is the No. 1 problem."[2] Much of the disagreement associated with the problem of Quebec has tended to detract attention from the problems of the other provinces. It has also served to exagerate an already serious problem. Gerard Pelletier, referring to the reports of the 1963 Federal-Provincial Conference, complained that:

> "Never a word was heard about the objections of Ontario, Saskatchewan or Manitoba, but as soon as Quebec was mentioned, 'oh, that block-head again! Any opposition became obstruction."[3]

Only one point emerges with any clarity after following the complicated history of intergovernmental financial relations in Canada. If Canada does survive as a federal nation, as she probably will, the conflict between the Federal and Provincial Governments will also continue.

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[1]Canada, Federal-Provincial Grants and the Spending Power of Parliament, Government of Canada Working Paper, (Ottawa: Queen's Printer, 1969), P. 8.

[2]Rene Levesque in Frank Scott and Michael Olivers, (eds.), Quebec States Her Case, (Toronto: Macmillan Company of Canada, 1964), P. 135.

[3]Gerard Pelletier, Ibid., P. 161.

There is no single 'great solution' to the issues. What will be required in the years to come will be a great degree of patience and caution on the part of those who wish to preserve the nation.

IV Conclusion

Perhaps the perfect form of federal state would be one in which both the responsibilities of each level of government were clearly defined and the available revenue sources were divided in such a way that each government could execute its functions without financial assistance from any other. It has been seen that it was the clear intention of the Fathers of Confederation to create a federation in which the central government was dominant. If it had been possible to create a unitary state they would have done so. It may well have been that if Quebec had not existed as a concentrated ethnic block that a unitary state would have been created. It is, however, doubtful if British Columbia would have been part of that state. The fact that Quebec did, and does, exist has had a vital effect not only on the conditions laid down in the B.N.A. Act but also on the history of intergovernmental relations ever since. If, however, one looks at indications of dissent within the federal structure it soon becomes apparent that Quebec has not enjoyed a monopoly of serious conflict with the Federal Government. Appeals to the Privy Council, cases heard in the Supreme Court, submissions to Royal Commissions and debates in provincial chambers and the House of Commons all show that each province has been concerned with the maximization of the benefits of membership of the federation while at the same time attempting to minimize

the costs. It can clearly be seen that many of the more acute provincial problems are related to finance. The demands on the Federal Government are more often than not for increased provincial revenues, in particular for an increase in unconditional revenues or more tax 'room'. The post war 'swing' in favour of provincial rights has been, in very large part, due to the rapid expansion of the cities. Not only has the post war swing been of a greater magnitude than ever before, it has also been much more persistent. The situation has now been reached that it seems that nothing, short of war or a serious recession, can reverse the trend.

The major areas in which governmental activity is increasing, and, of course in which their expenditures are growing very rapidly, are in the fields of education, welfare, social assistance, and the most acute problem area, the municipalities. The provinces will not surrender these responsibilities to the Federal Government and the Federal Government, because of its economic obligations, cannot surrender the major revenue sources to the provinces. In the past the Federal Government has been able to use its massive revenue sources to coerce the provinces to accept Federal priorities. That it still has the power to do this can be seen by the recent medicare developments. Provincial resistance to the Federal Government is, however, now very strong, and will probably become even stronger as the provinces, or at least the more wealthy of them, develop their own revenue sources more fully.

The restructuring of the constitution and the realignment of revenues and responsibilities so often demanded by the provinces would be very difficult to achieve. It has not yet, after all, been possible

for the governments to agree on a formula whereby the B.N.A. Act can be completely amended without reference to London.[1] It is, of course, essential that the objectives of all governments be as clearly defined as possible before actual amendments are discussed. Perhaps one of the greatest mistakes made in discussions of this type is to refer to the position of the provinces as if the problems were uniform. It makes little sense to talk of provincial demands in this way since the diversity within the nation and between the provinces is so great that all ten provinces wish to achieve different objectives, many of them in conflict with the wishes of the other provinces and the Federal Government. In other words the most acute difficulties arise because it is eleven government which are involved in negotiations, and not just two levels.

The political and economic power of the major provinces, Ontario, British Columbia and Quebec, with Alberta also important, has allowed them to preserve their advantageous position in relation to the other provinces. The calculation of equalization payments does not provide sufficient revenues to the poorer provinces to allow them to substantially improve their position. These provinces are, in many respects Canada's claiment states but, as seen in Chapter Three, the political strength of the wealthy provinces has been such that they have not accorded the provinces in need the special status they need. It has been impossible for even reasonably objective calculations of provincial needs to be acceptable to the more powerful provinces. Thus there can be no body

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[1]See G. Favreau, Amending the Canadian Constitution, Queen's Printer, Ottawa, 1965. See also P. E. Trudeau, Op. Cit., PP. 40-51, for a discussion of this problem.

such as the Australian Commonwealth Grants Commission for Canada. The level of diversity is too great. The National Adjustment Grants recommended by the Rowell-Sirois Report could not be accepted for the same reason. Neither could the Federal Government force the provinces to accept the recommendations regarding income tax. This, of course, is in very strong contrast with the situation in Australia where the states, like the provinces, lost the power to impose income tax at about the same time as the provinces. In Canada the provinces were powerful enough to regain these taxing powers, in Australia the states loss became permanent.

The assistance given to the provinces most in need, while being welcome, can only be regarded as palliative, it is no solution. The Atlantic Provinces are not, of course, the most volatile in their politics, neither are their votes essential to success in a Federal election. They are, therefore, in a very weak position. The effect of the Parliamentary system in making for difficulties in the articulation of regional demands has been mentioned elsewhere but should be born in mind. The fact that the Prairie Provinces are politically volatile serves to bring more attention to their problems.

What, in the fact of increasing centrifugal pressures on the federation, can be done to ease the situation and ameliorate inter-governmental conflict? Perhaps the worst thing that could happen would be for the Federal Government to decide that the present trend should be rapidly reversed. It would seem highly likely that such a move would stimulate a resurgence of the 'quiet revolution' in Quebec, or at least increase support for the seperatists, and would also create massive

opposition in all the other provinces. The only provinces which might benefit financially from such a move would be those in financial difficulties. But we have seen that these provinces are also demanding their fiscal freedom.

It might be thoughtthat the very high rate of economic advance and, therefore, the increased rate of economic interdependancy, would operate to bring about greater, rather than less, feelings of national unity and a growing acceptance of the need for a strong central government. The history of Canada from the 1950s, however, clearly indicates that this is not necessarily the case. Political integration does not always result from a high degree of economic interdependancy. The fact that certain provinces have continued their rapid advance whilst others have stagnated, is itself, a most divisive force. Even within those provinces which are in rapid expansion the fact the expansion is very largely financed by American capital brings to the fore fears of cultural assimilation, both of the provinces individually and of Canada as a whole.

The political decisions which have to be taken by the Federal Government in deciding which policies are so important, from a national point of view, that even vigorous provincial protests must be ignored will continue to be the most difficult task of any Federal Government. That intergovernmental conflict can be avoided or reduced by the Federal Government allowing the provinces sufficient fiscal means to finance their own schemes is undoubted. The developments in the fields of university finance and health and social assistance show us that much. By such means provincial diversity can be accommodated and national standards still

maintained. A possible compromise between the conditional grants in aid favoured by the Federal Government, and the provincial demands for 'fiscal freedom' could be achieved by use of departmental block grants. By this means grants would be paid to the provincial governments for use under general headings such as, for example, education, municipalities, social welfare, highways, health and sanitation. It is, of course, true that the Federal Government would still, to a considerable extent, be influencing the pattern of provincial expenditure but, since there would be no obligation on the part of the province to 'match' the Federal money the worst aspect of grants in aid, the distortion of provincial budgets, would be avoided. Once such an unconditional payment had been made the manner in which it would be spent would cease to be a Federal concern, provided only that it was spent within the provincial department receiving the grant. Within the general headings, the priorities decided upon would be a matter between the provincial legislatures and their electorates, not between the provincial politicians and officials and their opposites in Ottawa. Such a change would, however, require a considerable alteration in the philosophy on the part of many Federal officials. The feeling that the Federal Government must, in the national interest, make all the major governmental decisions, even those outside its legitimate jurisdiction, or in Mr. Smallwood's words, "That father knows best" is, perhaps, reflective of the English belief in strong central government. Given the present state of the Canadian nation that may be the most inflexible, and therefore unsuitable, for Canada.

There are also, of course, steps which the provinces can take

to ease their own situation. If there is such intense pressure on provincial revenues, why do not the provinces increase their own rates of personal income tax? As the situation stand at the moment there is no Federal constraint on their doing this. The Federal Government has even offered to collect the provincial income taxes, free of charge, and remit it to the province. Why is it that only three provinces impose income tax above the Federal rate, and even then only be a very small amount? The answer is, quite obviously, that the Premiers are aware that any party which dared to impose a much higher rate would suffer at the next provincial election. No one likes to be taxed and taxes on income, being so visible, are objected to with great force. At the moment, therefore, the Federal Government is undertaking a task which relieves the provincial parties from a politically embarrasing task. It seems unlikely, at least in the short term, that there would be any significant change in the rates of income tax if the Federal Government did as it has been requested to do by certain of the provinces and withdrew from this field entirely. As was seen in Chapter Two the Federal Government has offered to increase its abatement in this field to 67% if the provinces, individually or collectively, agree to assume the costs of certain health and welfare schemes. No province has yet accepted the offer. Ontario, which first suggested the change, has shown little interest. The provincial politicians quite obviously understand that financial autonomy involves the risk of political unpopularity, and seem, in the main part, reluctant to incur the risks. This understandable reticence, does, of course, provide the Federal Government with a valuable

political weapon with which to counteract provincial demands.

The much increased level of consultation and cooperation seen between governments, and the increasing professionalization of provincial officials, are perhaps the most encouraging signs seen in the past ten years or so. These changes indicate that the view of Canadian governments as being in a hierarchy, with the Federal Government necessarily at the top, is giving way to a view that recognizes that a federal state in which regional interests can be expressed, and in which provincial governments play a leading role, may in fact be stronger than a highly centralized federation.

Federalism is, by its very nature, a compromise between those forces which unite the constituent regions, economic needs and strategic considerations being very important, and those which divide them. In the latter category are wide differences in the ethnic composition within the regions and variations in the economies of the regions. The balance between the centrifugal and centripetal forces within a federal state can never be static. In a federation exposed to a very rapid rate of growth, especially if, as in Canada, it is very uneven between the regions, the balance will at times be perhaps dangerously unstable. The written constitution or the intentions of the framers of the constitution, or of amendments, shed little light on the actual state of intergovernmental relations. Considering the importance of this field of study and the fact that the changes which will no doubt be made in Canada within the next twenty years it is perhaps unfortunate that this field is ignored by the majority of political scientists because it is thought to be 'dull'.

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