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Mr. Yvan Loubier

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• (0800)

[Translation]

The Chair (Mr. Yvan Loubier (Saint-Hyacinthe—Bagot, BQ)): Good morning everyone. Welcome to the House of Commons Subcommittee on Fiscal Imbalance. The subcommittee has been travelling throughout Canada for approximately one month and a half.

The Clerk of the Committee (Mr. Richard Dupuis): For two months.

The Chair: For two months, then. The committee's mandate is to table a report and recommendations to the House of Commons before June 2 outlining sustainable solutions to the fiscal imbalance.

It is our pleasure to welcome this morning Mr. Pierre Beaulne and Mr. Pierre Séguin from the CSQ, and Mr. Luc Godbout and Ms. Karine Dumont from Sherbrooke University.

Mr. Beaulne and Mr. Séguin, you have 12 minutes in all to share your perspectives with us. The same goes for Mr. Godbout and Ms. Dumont. We will then proceed with a round of comments and questions. Members of the various political parties of the House of Commons will then have the floor.

Mr. Séguin, you may proceed.

Mr. Pierre Séguin (Vice-Président, Centrale des syndicats du Québec): Thank you very much.

We would like to begin by thanking the chairman and the members of the subcommittee for having us and for giving us the opportunity to express our opinions about the fiscal imbalance.

You realize that the Centrale des syndicats du Québec feels very strongly that this situation must be dealt with, especially considering that a clear consensus has emerged in Quebec, at both the social and political levels, that there is in fact a fiscal imbalance. The perspectives underlying this social and political position and the arguments that clearly illustrate it can be found in the report that was drafted and presented to the Commission on Fiscal Imbalance by Mr. Yves Séguin in 2001-2002.

The Centrale des syndicats du Québec participated very actively in the work of that commission. It provided its own opinions and comments. Overall, its own presentation was consistent with the recommendations that were included in the commission's report.

Following that process, we were also involved in supporting the provincial premiers in their demands in Ottawa to the effect that the government provide financial transfers, even though we preferred tax transfers.

We also submitted our opinions and proposals to the Romanow Commission and made the same arguments to that commission.

Before dealing with the substance of the issue, we would like to begin by providing you with some background analysis which enables us to support our contention. As you know, we are currently in a situation of catching up in terms of public services and social programs.

Due to the focus on deficit eradication by the Government of Quebec, and also by all provincial and territorial governments in Canada, we have ended up, in Quebec among other places, losing people who are specialized in various sectors, for example health and education. Deficit control has had consequences and has even threatened the maintenance and restructuring of our various systems, in health as much as in education. We feel that deficit control has caused a delay in the development of social services and has had very serious consequences, especially in the areas of health and education. We feel that the cuts that were made were very severe. They had a major impact on access to services for the general population.

Given that context, even though over the past decade, governments started investing again in health and public services, we feel that those investments have simply maintained levels of access to services. They made up for deficits from previous years. We would point however that it is interesting that additional amounts were provided. However, we note that those amounts did not lead to an increase and improvement in the services as such.

Despite cuts that were made and despite the economic situation which prevailed at the time, the Government of Quebec did innovate in some respects by establishing a day care system and the infrastructure for a drug benefit plan as well as a system for people without group plans to benefit from an insurance plan. The government also established a parental insurance plan.

We are aware of those developments. They provided a certain amount of recovery even though they did not improve the situation with respect to the fiscal imbalance.

• (0805)

The years between 1999 and 2001 were very good ones. The government was accumulating surpluses from year to year, but the provinces, on the other hand, were experiencing the opposite: problems such as revenue loss were accumulating from year to year. Thus, this year again, there is no certainty that there will be a fiscal balance for the Government of Quebec's financial year. If there is, it may be at the cost of public services.

We feel that this situation is due to the decrease in equalization payments that have been made over the years. The Quebec government has lost \$1.5 billion over two years and that is due to the changes that were made within the review of calculations methods. Furthermore, because of shortcomings within those calculation methods, the Government of Quebec must now reimburse equalization overpayments of \$2.4 billion.

Even though the agreement on health and equalization adjustments will provide for \$1.5 billion in 2005-2006, they will not necessarily improve the fiscal imbalance. Quebec's situation, in terms of revenue, will be more or less the same as that of 2003. Despite changes to the health agreement, the Government of Quebec will have a half billion dollars less in 2005 than it had in 2003.

For the fiscal year 2004-2005, that is from April to January, the Government of Canada had a surplus of \$13.4 billion, that is, \$5.3 billion more than for the same period in 2003-2004. Given the current situation, we feel that it is absolutely unacceptable that the government is accumulating this revenue while putting the Quebec government, as well as all the other provincial and territorial governments, in a situation that makes it very difficult to meet any budgetary savings targets.

We will attempt to show that for 2004-2005, the Canada Health Transfer and the Canada Social Transfer will have accounted for, respectively, 69 per cent and 31 per cent of the total transfers. We feel that this is truly cause for concern. We think that these percentages are going down overall. Furthermore, for 2010-2011, we see these percentages being 73 per cent for the Canada Health Transfer and 27 per cent for the Canada Social Transfer. That includes of course the children's support programs.

The Centrale des syndicats du Québec therefore recommends that the federal government increase cash transfers under the Canada Social Transfer in order to bring that percentage of transfers back to 38 per cent by 2007-2008.

• (0810)

Now with regard to equalization, Quebec, for the period 2006-2013, has been offered \$3 billion, despite the fact that the Government of Quebec asked for \$15 billion over five years. In our opinion, the agreements concluded with Newfoundland and Nova Scotia are a form of inequity because royalties from oil are not included in the formula to determine equalization. We consider that to be unfair. At the end of the day, the Government of Quebec, could more or less demand the same sort of treatment under equalization of its hydroelectric resources. Instead, we are recommending that the Government of Canada thoroughly review the equalization system in the context of a broad review on the desirable changes that would need to be made to correct the fiscal imbalance.

Given what we said to you earlier about the Government of Canada seeking repayment of a \$2.4 billion overpayment under equalization, it has become apparent for some time now that the various agreements entered into with Quebec government have ended up delaying the repayment of this \$2.4 billion.

Given the current situation, including new equalization agreements and the surpluses that the federal government has accumulated over the years, it would seem appropriate to recommend that the federal government cancel the Quebec government's obligation to refund the \$2.4 billion.

On the matter of child care and early childhood, we are fully aware that the agreement that has just been entered into is of major importance and is good news in and of itself given that Quebec will be able to use monies paid to it as it sees fit. However, given that over the years, Quebec has implemented a reduced fee child care system for its citizens, Quebecers are not eligible for the federal government child care credit. This saves the Canadian government between \$200 and \$250 million annually. In this case, we recommend that Quebec be compensated due to the shortfall resulting from this reduced reliance on child care fee deductions under the federal taxation system, which is the result of the implementation of reduced fee child care in Quebec.

On the matter of housing, Mr. Chair, we are fully aware that the Government of Canada has invested about \$2.3 billion over the years. However, in the current context, this money is not enough to meet the existing needs. There are huge ongoing difficulties when it comes to funding social housing. This is why we would like the federal government financial support of social housing to be increased from 1 to 2 per cent of its total revenue. Therefore, we are recommending that the federal government double its investment in social housing.

To conclude, we would like to highlight some of the federal government's initiatives such as the sharing of a portion of the gas tax with municipalities and the funding of a parental insurance system. The Government of Canada is sending out the right signals concerning the direction it intends to take on these files. In our opinion, the injection of \$5 billion over five years to municipalities is an excellent step towards sharing more tax room. The same is true for the parental insurance system which will soon be implemented in Quebec. We feel that this demonstrates that sharing more tax room is a positive approach and we hope that it will continue.

Thank you very much.

• (0815)

The Chair: Thank you very much, Mr. Séguin, you have been very disciplined. We will have to invite you to the Block caucus so that this discipline rubs off onto my colleagues. It was very kind of you.

Mr. Godbout, you are a professor at the University of Sherbrooke. Is Ms. Dumont also a professor at this university?

Professor Luc Godbout (Fiscal Policy Teacher, Research Chair on Taxation and Public Finance of Sherbrooke University, As an Individual): Ms. Dumont is a researcher.

The Chair: Welcome, Mr. Godbout, you have 12 minutes.

Prof. Luc Godbout:

First of all, thank you for inviting us to share our perspective on the fiscal imbalance. Karine Dumont and I, from the Research Chair on Taxation from the Université de Sherbrooke have prepared a 50-page brief that we submitted this morning, but we have decided to present some excerpts that illustrate the fiscal imbalance. We do, nevertheless, invite you to refer to the longer version if need be.

Here is the fiscal imbalance in three acts.

First act: deficit control. It is quite easy to see that the deficit was reduced thanks to a 33 per cent decrease in transfers for health and social programs. It also involved reforms to unemployment insurance, which became employment insurance, and resulted in another 20 per cent cut in three years. So the federal deficit was eliminated for the most part by reducing these transfers, but that had negative effects on the provinces' public finances. While health costs rose, the transfer payments from the federal government used to fund them went down.

Fiscal imbalance, act two: the appearance of the federal surplus. After having balanced its budget, what did the federal government do with this surplus? We saw that the government had started cutting transfer payments to the provinces to balance its budget. Once that was done, what did the government do? One hundred and forty-three billion dollars were reinvested in federal program spending, while \$64 billion went to paying down the debt, and \$42 billion were earmarked for increases to federal transfer payments. Although federal transfer payments had been the main source of revenue to balance the budget, that is not where the money was reinvested once the budget had been balanced.

Act three: the future. What does the future hold? The most recent federal budget shows how the money will be allocated over the next five years. Between 2005 and 2010, federal transfer payments to the provinces will increase on average by 3.2 per cent per year; other federal government programs spending will increase by 4.6 per cent and anticipated growth in GDP is 4.9 per cent. Once again, federal transfer payments will increase more slowly than other government expenditures and GDP. In terms of their relative importance, that means that federal transfer payments will continue to go down.

● (0820)

Ms. Karine Dumont (Researcher, Research Chair on Taxation and Public Finance of Sherbrooke University, As an Individual):

Let us now look at the flaws in federal transfers. They are one of the causes of the fiscal imbalance, as is the CHST. After having dropped dramatically between 1994-95 and 1998-99, the share of federal funding for health and social programs was increased to 15.3 in 2003-04, which is considerably lower than what it was in 1994-95. In 2004-05, the CHST was split into two parts, one for health and the other for social programs. That decision brought the federal contribution for health to 22 per cent, because the recent investments dealt exclusively or mainly with health. Consequently, the contribution for social programs was reduced to 13.3 per cent. At present, there are no plans to increase that.

Now, let us look at the flaws in equalization. It is often said that today, Quebec receives a smaller share of equalization, because it has gotten wealthier. That is true in part, but the federal government has also changed the equalization calculation standard. In 1982, in order to prevent program costs from rising, the federal government chose the 5-province standard, instead of the 10-province standard, to calculate the comparison standard. In doing so, it removed wealthy Alberta and the Maritime provinces from the calculation. As you can see on the graph, that led to a reduction in program costs of about 2 per cent, which in proportion to federal revenues, represents \$4 billion in 2004-05. We can also see that if the 10-province standard had been maintained, the program cost, in proportion to federal revenues, would have been maintained over that period.

To measure the impact of using the 5-province standard instead of the 10-province standard, we can also analyze the weight of equalization in GDP: it has continued to drop since 1982-83, going from 1.5 per cent to about 0.8 per cent of GDP.

Prof. Luc Godbout: We have seen the flaws in federal transfers for health care and social programs and equalization payments. If we look at them together, we see that although they have increased in the last 10 years, they have not increased in similar proportions in all the provinces. While all federal transfers together increased by 57% over 10 years in Ontario and by 48 per cent in eight other provinces, they increased by only 13.8 per cent in Quebec.

Why did Quebec get less? This happened mainly because of the change in the standard used to calculate the CHST. Formally, the standard was based on the concept of need, but the federal government decided unilaterally to replace it with a simple concept of demographic weight. We can see the consequences of this decision.

Let us now look at the impact on each resident over a 10-year period. Some people claim that even though Quebec gets less in health care transfers, this is largely offset by the equalization payments it receives. Others say that the reason Quebec received less in recent years is that its demographic weight is increasing less quickly than that of the other provinces.

Quebec is now receiving \$137 more in federal transfer payments than it was receiving 10 years ago. Even though Ontario does not receive equalization payments, it is getting \$226 more now than 10 years ago. All the other provinces are receiving \$384 more. That means that the changes in the way the federal transfer payments are calculated have been particularly harmful to the government of Quebec.

How can we correct the fiscal imbalance?

We will deal with a number of points. First, the time has probably come to lay out the principles of fiscal federalism. The last time this was done in Canada was in 1966. The Liberal Finance Minister of the day, Mitchell Sharp, set out a series of criteria that should be taken into account to ensure the smooth operation of fiscal federalism.

A number of pages in that document go into detail on this matter. I will simply tell you that consideration must be given to fiscal capacity, respect for jurisdictions, accountability, foreseeability and, of course, federal-provincial cooperation.

I think that setting out the proper principles of fiscal federalism could not help but lead to good federal-provincial relations and how to correct the fiscal imbalance. Consequently, your subcommittee should engage in this exercise.

Of course, the equalization system will have to be reviewed and improved. If we want to correct the fiscal imbalance, it is essential that the equalization payment system be improved.

First of all, we think last October's draft agreement on equalization should be dropped. The changes put forward in this draft agreement take equalization further away from its constitutional objective, which is to equalize the fiscal capabilities of the provinces. The overall envelop is set. Some see this as a good feature. However, if it is a floor, it is also a ceiling. So this is in no way based on the real differences in the wealth of the provinces. The promised annual indexation of 3.5 per cent may seem attractive at first glance. On the other hand, it is below the actual growth in federal revenues, below the growth in current federal expenditures and below the growth of the GDP. In the long term, the size of equalization payments can only diminish. Moreover, the standard tells us the size of the pie—\$10.9 billion for 2005—but we do not know how the pie will be split up among the provinces. This decision has been left to a group of experts.

For all these reasons, I think this draft agreement should be dropped, that is the federal offer on equalization. We also have to ask whether the offer was generous. When we compare the amounts of money that the federal government was planning to devote to equalization in its October 2002 economic update to the offer made in October 2004, we find that it has saved \$2 billion a year. So, this offer is not generous.

There are other factors that should be taken into account for equalization as well. Naturally—Mr. Séguin spoke about this earlier—dropping individual agreements can only cause confrontation among the provinces. In addition, this leads to political negotiations between one province and the federal government. We could have gone into this aspect in greater depth, but, inevitably, we must return to the 10 province standard. If we really want to take into account equalization and varying levels of fiscal capability, it is essential that we return to the best possible standard.

Finally, there must be a way of setting up an averaging device. Provinces must know ahead of time how a drastic reduction in their equalization payments will be handled. We should not wait until there is a sudden reduction and then have the provinces negotiating individual agreements with the federal government. So we need to know how sudden reductions in equalization will be handled.

Finally, in order to correct the fiscal imbalance, the federal government could also transfer tax room. That is the option we prefer.

• (0825)

We have seen the flaws in the Canada Health and Social Transfer. These programs could be abolished and replaced by a transfer of tax room to the provinces so that they can finance themselves the services they are required to provide. This would prevent the federal government from arbitrarily reducing its cash transfers to the provinces in the future, thereby guaranteeing foreseeable funding.

In addition, it would increase provincial transparency and accountability with respect to the services they provide.

Tax room may be transferred in the area of income tax, corporate tax, or the GST, the consumption tax.

Why should the consumption tax be chosen, as the Séguin's commission recommended? First, one of the advantages is that the entire area would be transferred. This would ensure that the federal government will not be able to reinvest in the area in the future. Moreover, the GST increases as the economy goes. So this would be a stable source of revenue for the provinces. As well, there would be less fiscal competition between the provinces with respect to the consumption tax than there can be, as we know, with respect to income tax. For all these reasons, if there is a transfer of tax room, it should be done first in the area of the GST.

For your information, other federations have done just this. For example, Australia has a GST similar to the one we have in Canada, and the revenues from this tax, which is collected by the federal government, are redistributed in full to the states of the federation. It is therefore possible to imagine a GST which would be used to fund provincial social programs.

Finally, in order to get out of the fiscal imbalance impasse, one of the two levels of government must make an official, detailed proposal which is acceptable to both parties. When your report is tabled, if the federal government offers nothing to the provinces, it will be up to either the Council of the Federation or to the government of Quebec itself, on behalf of the provinces, to make a detailed, acceptable proposal. That is probably the only way out of the current impasse.

In closing, what do people think about this? We have illustrated the fiscal imbalance and we have suggested some possible solutions. A CROP poll was done for our research chair in recent months and it shows that three Quebecers out of four would be in favour of having part of the income tax they pay to the federal government transferred directly to the government of Quebec in order to solve the fiscal imbalance problem.

We can therefore say in conclusion that the report of the Fiscal Imbalance Commission, which appeared in 2002, convinced the people of Quebec that the fiscal imbalance did exist. People support the solution recommended in the report.

Thank you.

• (0830)

The Chair: Thank you, Mr. Godbout and Ms. Dumont.

We will now move to the questioning.

Ms. Ambrose, for five minutes.

Ms. Rona Ambrose (Edmonton—Spruce Grove, CPC): Thank you, Mr. Chairman.

I would like to thank you for being here this morning. I appreciated your presentation and found it most interesting. I think it is important for you to know that our party, the Conservative Party of Canada, and our leader, Stephen Harper, have acknowledged the existence of the fiscal imbalance for a long time, the gap between the federal government and the provinces. I acknowledge that the fiscal imbalance result from the fact that the federal government collects more income tax than it requires to meet its needs. This has contributed to the federal government's recurring surpluses and to the provincial governments' deficits.

I think it is also important for you to know that at our recent convention, delegates passed a motion stating that a conservative government, working with the provinces, will do away with the fiscal imbalance by increasing transfers to the provinces and by lightening the tax burden or by transferring tax points to the provinces.

I have a question for Mr. Séguin. Could you go into more detail about the problems caused by the fiscal imbalance with respect to Quebec's ability to look after its social responsibilities?

Mr. Pierre Séguin: If I may, I will ask Mr. Beaulne to answer this question, Madam.

Ms. Rona Ambrose: Fine.

Mr. Pierre Beaulne (Economist, Centrale des syndicats du Québec): Thank you, Mr. Chairman.

In the document we submitted, we pointed out in the chapter on equalization in particular that because of the formula itself, the Quebec government is supposed to have received an overpayment of \$2.4 billion and must repay this amount to the federal government, because there has been a review of the calculations.

We also note that the total amount transferred from the federal government to Quebec has decreased from \$9.7 billion in 2004 to \$7.4 billion in 2005. That is \$1.5 billion less. There have been agreements on health care as well as some changes to equalization last fall which will mean that \$1.5 billion will be paid to Quebec. That means that we are at the same point two years later, in 2005, in terms of financial transfers to Quebec, as we were two years ago. In other words, there has been no improvement whatsoever in financial support from the federal government for Quebec in recent years. The Quebec government actually has to pay back \$2.4 billion. This is a completely deplorable situation which prevents the Quebec government from properly carrying out its constitutional responsibility in the area of social programs and public services.

Ms. Rona Ambrose: I have another question for Mr. Beaulne.

The federal government has set up an expert group to study equalization and the financing formula for the territories. Do you think this expert group will have a significant impact on the determination of the next equalization formula?

● (0835)

Mr. Pierre Beaulne: As far as I know, the mandate of this group is to determine how the new equalization funds arising out of last fall's agreement will be allocated. Their task is to look at the allocation of the funding, not to review the equalization formula. So the mandate is very limited. This will not provide an overall solution to the problem of equalization, which is increasingly dysfunctional

and deserves a comprehensive review in order to redefine the formula to establish whether there should be a single criteria or rather 33 tax bases, with constant revisions, and to determine whether the federal government should be involved, whether the provinces should be involved, whether this should be in the form of an agreement rather than a federal program where the federal government determines alone what the final allocation will be.

All of this must be reviewed starting now. In my view, this will require a rather more structured institutional entity than the committee you mentioned.

Ms. Rona Ambrose: Thank you.

The Chair: Thank you, Ms. Ambrose.

Mr. Bell.

[English]

Mr. Don Bell (North Vancouver, Lib.): Thank you.

I appreciate your presentation, and I'm looking forward to getting the translated version so that I can follow it a little more closely. I took notes through the translation, as it was going on, but I may not be able to get into the detail I would like here.

To Mr. Séguin, you mentioned the health care shortfall, which I wrote down as a half-billion dollars. Then I think you said it was less than 2003, and a few minutes later you made reference to 2000.

Can you take me back to that? If there's a section in the presentation that perhaps you could refer me to, in terms of what segment you're referring to, I may be able to follow the figures, if not the translation.

[Translation]

Mr. Pierre Beaulne: At the top of page 4 of our document, we mention that the equalization payments to Quebec in 2005 will be \$500 million less than they were in 2000. This is a program that is supposed to help the have-not provinces. This federal program will provide half a billion less in 2005 than in the year 2000. We find that quite deplorable.

The Chair: Mr. Bell.

[English]

Mr. Don Bell: I heard the reference to 2003, and that's what threw me. I was trying to understand that. Thank you.

Next, I heard again a reference to the gas tax. You were saying that this was the right message and the right step, the \$5 million over five years to municipalities. I want to know, do you agree with the concept, then, of the sustainability criteria that go with those transfers, that they're used for green, sustainable projects—in other words, that conditions are applied?

[Translation]

Mr. Pierre Séguin: We fully agree with the precepts whereby, in connection with the introduction of green programs, the same procedures could apply. We agree on that.

● (0840)

[English]

Mr. Don Bell: Thank you.

You also mentioned, for health, the \$3 billion for Quebec in 2006, that Quebec asked for \$15 billion over three years, I think you said. What are the details here? What is the shortfall? I guess \$15 billion would be \$5 billion a year, and you're getting, as I understand the statement, \$3 billion for 2006.

So I'm trying to get the figure. Are you getting \$3 billion instead of \$5 billion, or are you getting \$3 billion instead of the \$15 billion that you wanted?

[Translation]

Mr. Pierre Beaulne: It's about equalization. These are the government of Quebec's figures. In one of the documents published along with last year's budget, the Quebec government indicated that, by virtue of the changes made to the equalization formula last fall, the Quebec government would receive \$3 billion by 2013, so over about 10 years, whereas it had asked for \$15 billion over five years. This request was based on the 10 province standard and on a review of the definition of the property tax base in particular. These two factors would have substantially increased Quebec's revenues, compared to the revenues it obtained under the review conducted last fall. So over a comparable period, instead of \$3 billion, it would be \$1.5 billion, compared to \$15 billion. That's 10 times less.

The Chair: Thank you, Mr. Bell.

The document in question is entitled *Correcting Fiscal Imbalance*. It was tabled with the Quebec government's 2004 budget.

Mr. Côté.

Mr. Guy Côté (Portneuf—Jacques-Cartier, BQ): Thank you very much, Mr. Chairman.

Thank you for your very interesting presentations. You have given us an eloquent description of the way the federal government, beginning in the mid-1990s, financed its budget deficit on the backs of the provinces and of Quebec, and on the backs of all Canadians and all Quebecers. You repeatedly told us about various changes made to the equalization payments which resulted in less money for the provinces. You also mentioned the fact that the Canada Health and Social Transfer was split, which once again led to a loss of revenue for the Government of Quebec. You also showed us how, over the last several years, the equalization formula is not being applied in the spirit of the Constitution, and how, more recently, specific agreements were reached which, once again, undermined even more the equalization system.

In the meantime, the government in Ottawa had increasingly big surpluses. Naturally, this immediately reminds us of last year's budget. The government had forecast a surplus of \$1.9 billion, but at the end of the year it was \$9.1 billion. In the meantime, the Minister of Finance invented all kinds of reserve funds, such as a contingency reserve or an emergency reserve. To repeat the way one of my colleagues put it, these are anxiety reserves. The government has even indulged in creative math: as you perhaps know, the finance committee has made budget forecasts with the help of independent forecasters. But just six weeks after the tabling of the budget, it became clear that the government's projected surpluses were completely far-fetched and its surpluses would be much higher than projected.

Things are not going very well. There are 200 elected members in Quebec, including 125 at the National Assembly and 75 at the federal Parliament, and only 21 of these members, namely the federal Liberal members, refuse to acknowledge the existence of the fiscal imbalance. It seems to me that, after having heard the two presentations made here today, that it would be impossible to deny the facts.

Given this situation, Mr. Godbout, I've discovered an interesting trend. Among other things, you said that as the federal government was eliminating its budget deficits on the backs of the provinces and all Canadians and Quebecers, since 1997-1998, it increased program expenses by \$143 billion.

What exactly were the increases in program expenditures?

• (0845)

Prof. Luc Godbout: First, the \$143 billion represents the combined amount. We added all the increases since 1997-1998, and took the 1997-1998 budget as our standard. We followed the changes and added the amounts up to 2004-2005. The amount includes military expenditures, old age security pensions, employment insurance benefits, even though they did not increase significantly. Those are basically expenditures which do not include provincial transfers. We also isolated every unexpected surpluses which occurred at the end of the year and which were used to pay down the debt, which after all still represent \$64 billion from the time the budget was balanced.

Mr. Guy Côté: So what you are ultimately telling us is that the government used the money to finance its deficits, to pay down its debt and to increase its expenditures. We also talked about more recent programs, such as in the area of early childhood education. The money was also often spent in areas of provincial and Quebec jurisdictions.

Prof. Luc Godbout: Yes. Take the millennium scholarships, for example. That was good or bad news. Some people also have mixed feelings about the national child care system, but that in fact represents an intrusion in an area of provincial jurisdiction.

Mr. Guy Côté: As you said in your presentation, since 1997-1998, we have witnessed a decrease in the Canada Health and Social Transfer of 33 per cent. Today, we are still far from the amounts transferred in 1994, if we consider what is forecast for 2009-2010 and based on an increase in expenditures of 3.2 per cent.

Is it possible to predict when we will make up for lost ground? When will transfer payments be at the same level as they were in 1994, for instance?

Prof. Luc Godbout: In nominal terms, we have reached that level this year. The amounts which were transferred are the same as in 1994-1995. However, they have to be put into perspective in relation to expenditures which have kept on growing since 1994-1995.

Mr. Guy Côté: Fine.

Prof. Luc Godbout: As far as health is concerned, the transfers are more or less back to what they were in 1994-1995, but that happened to the detriment of social transfers.

There was no agreement last October on social programs, although we know that health expenditures will increase by a certain percentage over the next 10 years. As regards social programs, there is no indexation mechanism for now. We do not know how much the federal government will provide next year or in the following years. We have no idea.

The Chair: Thank you, Mr. Côté.

Ms. Wasylycia-Leis, please, you have five minutes.

Ms. Judy Wasylycia-Leis (Winnipeg North, NDP): Thank you, Mr. Chairman. I would like to thank our witnesses for their very interesting presentations. I have three questions for each witness.

As Mr. Côté indicated, we have a very interesting situation. The federal government, at least the federal minister, has continued to deny that there is a fiscal imbalance. How can you explain this, given all the statistics you have presented today? Is there anything you can tell us to persuade the federal government that there really is a fiscal imbalance?

I will stop there if you let me ask other questions later on.

The Chair: Mr. Séguin, you may reply.

Mr. Pierre Séguin: Indeed, many people in Quebec, but also throughout the rest of the country, are perfectly aware today that there is a fiscal imbalance. Minister Yves Séguin made representations during the meetings of the Commission on Fiscal Imbalance of 2001-2002. We are convinced that more and more people recognize the existence of a fiscal imbalance.

The Government of Canada must now make amends and admit to the existence of this fiscal imbalance. It has to make changes to the equalization formula as soon as possible for the entire country, so that each province can respect and adequately meet its provincial obligations.

A good way of making the Canadian government aware of the situation is, among other things, to raise the issue in committees such as this one. All politicians from other parties can also put pressure on...

• (0850)

Ms. Judy Wasylycia-Leis: Yes.

Mr. Pierre Séguin: ... to help the Canadian Government understand the significance of the situation and to bring about changes.

Prof. Luc Godbout: I don't have a dogmatic approach. If they don't want to use the expression "fiscal unbalance", but would prefer "undue financial pressure", I don't have a problem with that. They can use whatever expression they want; "undue financial pressure" will do just fine. However, there is a difference of opinion as far as solutions are concerned. We are proposing fairly clear solutions. In fact, if you analyze the federal government's attitude, you will see that its preferred approach is to say that it will inject more money, but with conditions attached. That's the main difference. Since 1997-1998, which was the first year in which there was a balanced budget, the federal government redistributed money to the provinces, but

with strings attached, and that if the provinces did not agree to the conditions, they would not get the money.

So if we want a solution, the money will have to be transferred unconditionally. That is why I prefer a transfer of tax room, rather than an increase in federal transfer payments with strings attached.

Ms. Judy Wasylycia-Leis: Thank you. It's true that there is a crisis as far as the equalization program is concerned. The prime minister is in the process of negotiating a bilateral agreement with the province of Ontario. This comes after the bilateral agreements with Nova Scotia and Newfoundland and Labrador.

I agree that we should throw out last October's agreement, but if we want to renegotiate an agreement and come back to the 10 provinces standard, should we include all revenue sources, including oil revenues? What is your recommendation in that regard?

Mr. Guy Côté: There are three aspects to our approach. First, we are asking the federal government to cancel the \$2.4 billion recovery from the Quebec government. Second, we would like last fall's negotiation to continue with a view to changing the criteria because we insist on having the 10 provinces standard. Third, we believe that there should be a forum to re-examine the entire formula; that would help us to determine whether we actually need 33 different tax bases—including revenues from natural resources—or whether we need a more simple formula, based on an indicator. Experts and specialists are debating the different approaches on that subject, and creating a forum would be the right opportunity to review the entire equalization formula. We admit that it may take some time. However, we still want some short term results which will allow us to, for instance, improve the system for provinces which need help.

The Chair: Thank you, Ms. Wasylycia-Leis.

Ms. Judy Wasylycia-Leis: Could the two other witnesses answer the question?

The Chair: If you could just answer the question in a few seconds, Mr. Godbout.

Prof. Luc Godbout: In my opinion, we must go back to the 10 provinces standard. As for the tax bases, the ideal would be to include all sources of revenue, even if there are 33 or 35 of them, including oil revenues. Rather than having ad hoc agreements with Newfoundland claiming money on account of its offshore revenues, a better alternative, that some have suggested and which I do not entirely agree with, would be that so long as Newfoundland does not spend that money on programs, its offshore revenues would be put into a trust fund, and that money would not be included in the equalization payment equation. It would only be included in the equalization payment calculations when it is used, and not when it is received. It should be put into a trust fund, as it is done in Alberta, for future generations.

Ms. Judy Wasylycia-Leis: Thank you.

The Chair: Thank you, Ms. Wasylycia-Leis.

Ms. Folco, this is the second round. You have three minutes.

● (0855)

Ms. Raymonde Folco (Laval—Les Îles, Lib.): First, let me thank you and apologize for arriving a bit late. In the part that I missed, you may have dealt with the topic I want to raise. Both levels of government, federal and provincial, have access to the same sources of revenue for funding their activities. And we note that the provinces have much larger revenues than does the federal government; it has been so for the past 20 years. Here I have a chart that shows that in 2003-2004, provinces and territories received \$37.4 billion in cash transfer payments from the Canadian government, plus \$16.5 billion in tax points under the Canadian Health Transfer and Canadian Social Transfer Programs.

Here is my reading of these figures: transfer payments to provinces—and I mean the provinces in general—are at an all-time peak. Would anyone volunteer to give their reactions to what I said?

Mr. Pierre Beaulne: The figures that I read are not the same as yours.

Ms. Raymonde Folco: I am not surprised.

Mr. Pierre Beaulne: The Quebec government budget figures show that federal transfer payments fell from \$9.7 billion in 2003-2004 to \$7.4 billion in 2005-2006. The \$7.4 billion amount will be supplemented with a further \$1.5 billion, following the agreements concluded last fall. In any case, I see no increase in federal transfer payments to Quebec. To the contrary, Madam, federal transfer payments are strangling Quebec's public funds. We represent members who work in the public service in education, health and other social services, and we are very much disappointed with this turn of events.

Prof. Luc Godbout: There are three parts to your question.

First, as you mentioned, you have to take tax points into account to know whether federal transfer payments have increased. Should they be taken into account? It is unclear.

Quebec's position, in general, is not to count them. But if you do, you should also recognize tax points which the provinces handed over to the federal government during the Second World War. The provinces also transferred tax points to the federal government. Logically, one shouldn't include tax points: once the transfer is completed, you should forget about them. Consequently, we should stop thinking that the federal government is funding 50 per cent of health care because there was a tax point transfer, and this situation should be examined after it has taken place.

Moreover, the federal government likes to state that there is no fiscal imbalance because the provinces have access to the same sources of revenue. Legally speaking, it is true that the provinces can increase their taxes. However, that is a debatable argument, because the provinces, just like the federal government, cannot levy taxes in isolation. They have to take into account the total amount taxpayers can afford to pay, instead of looking at it from one single vantage point.

Ms. Raymonde Folco: Absolutely, because we are overtaxed in Canada.

Prof. Luc Godbout: That's correct. So, we shouldn't say that the provinces simply have to increase taxes if they're not satisfied. They

have to bear in mind the total amount of taxes paid by their taxpayers.

It is true that if you set aside tax points, there has been a recent increase in transfer payments, but that simply offsets the effect of cutbacks made 10 years ago, as was stated earlier. Moreover, according to the new trend—which I consider deplorable—there are more and more strings attached. Money is being granted for a reduction in waiting lists; or on the condition that daycares are created. There are always strings attached. From the mid-1960s to the mid-1990s, there were no conditions attached to federal transfer payments. Provinces had more leeway.

There is more money now, but if that money is conditional, it can be harmful to provinces rather than helpful as they attempt to reach a fiscal balance.

The Chair: Thank you, Ms. Folco.

Thank you, Mr. Godbout.

Ms. Ambrose, you have three minutes. By the way, your French is impeccable.

Ms. Rona Ambrose: Thank you, Mr. Chairman.

I have a question for Mr. Godbout.

Recently, you released a study according to which 79 per cent of Quebecers believe that there is indeed a fiscal imbalance between the federal government and the provinces.

How important is this in the eyes of Quebecers? Could you give us more information as to what most people consider the best solution to the fiscal imbalance?

● (0900)

Prof. Luc Godbout: In January 2002, the Commission on fiscal imbalance asked the following question: Do you believe there is a fiscal imbalance between the federal government and the provinces? We thought it would be interesting to put this question to Quebecers once again, in order to see whether they believed that, following last September's health care agreements, the fiscal imbalance had lessened. On the contrary, 71 per cent said yes in 2002 compared to 79 per cent today.

The effect of the commission's report was such that Quebecers now consider the fiscal imbalance to have worsened. On the issue of a possible solution, as you see, three out of every four Quebecers believe that part of the taxes they send to the federal government should in fact be sent to the Government of Quebec in order to solve the fiscal imbalance. They suggest transferring tax points to correct the fiscal imbalance.

The Chair: Thank you, Ms. Ambrose.

Ms. Rona Ambrose: Thank you.

The Chair: Mr. Côté, you have three minutes.

Mr. Guy Côté: As the chair pointed out earlier on, in the last two months we've been on a cross-Canada tour. We see that the fiscal imbalance translated differently from one province to another.

Ontario considers that it is paying more than its share and is looking for a specific agreement; Saskatchewan also would like to have a specific agreement in order to improve the situation on the equalization front; in Quebec, there is talk about tax point transfers but that would not correct the fiscal imbalance in a province such as Prince Edward Island; British Columbia has huge infrastructure needs.

Meanwhile, the federal government is running a surplus. I mention this because it's at the very heart of the problem. You can't work in isolation, as we've stated. Is the government overtaxing or is it not transferring enough money to the provinces? Where does the problem lie? How come the federal budgetary revenues are so significant when all provinces, or almost all—apart from Alberta that is doing quite well for itself—are dealing with this imbalance? Is the government overtaxing or is not transferring enough?

The Chair: Mr. Beaulne, you have the floor.

Mr. Pierre Beaulne: I have a comment to make. There are at least three reasons for the fiscal imbalance.

First, the current division of powers in Canada has led to an increase in expenditures in provincial areas of jurisdiction that is far superior to that in federal areas of jurisdiction. So there is added pressure there.

Second, because of the size of its debt and so long as it aims to achieve fiscal balance, the federal government is able to show a surplus which is far superior to that of the provinces. It can also, therefore, increase its own expenditures more quickly.

Third, the federal government has a greater revenue-raising ability than the provinces, because the federal government is able to avoid a migration of the tax base. That is the case for instance when it comes to corporate income tax. It has greater fiscal capacity and less responsibilities in terms of expenses. The opposite is true in the provinces, resulting in the fiscal imbalance.

Ms. Folco was asking a question to this effect earlier on. The system that exists leads to a structural fiscal imbalance generated in Canada by this combination of factors. In our opinion, solutions must revolve around a better distribution of the tax base rather than around the federal government transferring its tax room to the provinces, because of its superior revenue-raising abilities.

● (0905)

The Chair: Thank you, Mr. Côté.

Ms. Wasylycia-Leis, you have the floor for three minutes, go ahead.

Ms. Judy Wasylycia-Leis: Thank you, Mr. Chairman. It seems to me that there is indeed a fiscal imbalance in this country. It's clear in my opinion. The focus for all members of the committee is now on a solution.

According to your recommendations, it seems to me, there needs to be a new agreement on equalization. We have to resume negotiations.

I'm not sure about your recommendations on the issue of transfer payments. There is a big difference between increasing tax points and cash transfers. Those are two different things.

What would your recommendation be on cash transfers? In my opinion, we have to increase them. Do you have a preference for this solution, for the transfer of tax points or for the transfer of tax room, as you indicated?

Prof. Luc Godbout: If we could increase the Canada Health and Social Transfer in its present form to eliminate the conditions and to ensure that its growth would be foreseeable and based on needs, at least in part, and not just on demographic weight, I see no problem with leaving the transfers in their present form. However, at a minimum, these three conditions must be met.

If these three conditions cannot be met, it would probably be preferable to abolish these transfers and replace them with tax room, which would at least be predictable for the provinces, without their having to meet certain conditions in order to be entitled to it.

That is the advantage of transferring tax room, if we cannot improve the Canada Health and Social Transfer to eliminate the conditions, and make it predictable and based on needs, and not just on demographic weight.

Ms. Judy Wasylycia-Leis: And what is the view of the Centrale des syndicats du Québec?

Mr. Pierre Séguin: If the Government of Canada were to make cash transfers and these were linked to conditions regarding their use, which would impact on the constitutional powers of each province, we could agree with such a proposal.

We think it would be preferable to have tax transfers and that each province, as part of its constitutional responsibilities, be able to ensure the provision of services to which its citizens are entitled. And this should be done without any conditions being imposed by the Government of Canada.

The Chair: Thank you, Madam Wasylycia-Leis.

I would like to thank you very much for your contribution, Messrs. Séguin, Beaulne, Godbout and Dumont. It was very pleasant and informative to hear from you today.

We will now take a five-minute break.

● (0908)

(Pause)

● (0915)

The Chair: Ladies and gentlemen, good morning and welcome to the Subcommittee on Fiscal Imbalance. We have to report to the House of Commons by June 2nd and to recommend sustainable solutions to correct the fiscal imbalance problem.

We have the distinct honour to have with us today Mr. Michel Audet, who is an MNA and the Minister of Finance of Quebec, and Mr. Benoît Pelletier, who is an MNA and the Minister of Canadian Intergovernmental Affairs, as well as the wonderful team from the Ministry of Finance, which initiated the whole debate about fiscal imbalance three years ago. Of course, the team from Intergovernmental Affairs has also been very involved with this issue in recent years.

Mr. Audet and Mr. Séguin, you have between 15 and 18 minutes to present your comments and analyses.

Mr. Michel Audet (Minister of Finance, Government of Quebec): Each or together?

The Chair: Together. However, you will have an opportunity to clarify your position, because we will have two rounds of questions.

Mr. Michel Audet: I would just like to say that this will be difficult, because my presentation will last between 15 and 20 minutes.

The Chair: Since I know what a nice person you are, Mr. Audet, I will be very flexible. So you will have all the time you need to make your presentation. However, we have only one hour and 15 minutes in all for your presentation.

You have the floor, Mr. Audet.

Mr. Michel Audet: My colleague from Canadian Intergovernmental Affairs, Benoît Pelletier, will start by making some opening remarks. I will then make a PowerPoint presentation to provide you with more information and to go into detail about Quebec's position on the important issue of fiscal imbalance.

The Chair: You have the floor, Minister Pelletier.

Mr. Benoît Pelletier (Minister for Canadian Intergovernmental Affairs, Government of Quebec):

Thank you, Mr. Chairman and distinguished committee members. With me today is my chief of staff, Mr. Olivier Marcil, and the Deputy Minister from the Canadian Intergovernmental Affairs Secretariat, Mr. Camille Horth. Of course, there are other people in the room who are also with me today.

Mr. Chairman, throughout the history of the Canadian federation, the issue of the division of revenues and tax resources between governments has given rise to discussions and debate between the various partners in the federation. This is only natural. A fair division of financial resources is a fundamental element in the proper functioning of our federation. However, for several years now, a problem we generally refer to as the "fiscal imbalance" has significantly disrupted the operations of the Quebec government and that of other provinces and has upset the way federalism works so much so that it has become the most fundamental issue in federal-provincial relations.

As Minister responsible for Canadian Intergovernmental Affairs, I would like to tell you about my view of this issue, which is crucial to the future of Quebec and the Canadian federation. More specifically, I will be presenting some facts and principles which are essential to understanding the fiscal imbalance phenomenon and that must guide us in evaluating the solutions that could help solve this problem.

However, before I go any further in this direction, I would like to give you a brief sketch of the background to the fiscal imbalance between the federal government and the provinces. This imbalance is more accurately called the vertical fiscal imbalance.

Year after year, the federal government has been generating exorbitant budget surpluses, for close to 10 years now. This began when it made some unilateral drastic cuts in the transfer payments for health care and social programs. Moreover, during the same period of time, generally speaking, the provincial governments have

had to deal with a strong growth in social spending and many difficulties in order to balance their budgets. Many of them run the risk of falling back into a deficit every year.

The rapid growth in the federal government's revenues has enabled it not only to operate its regular programs and to pay down the interest on its debt, but also to reduce taxes and to pay down some of the capital on the debt. Moreover, if that were not enough, the federal government has extra resources available to spend in areas of provincial jurisdiction. The provinces, for their part, have had to work miracles in order to deal with rising costs, particularly for health care, which far exceeded the growth in their revenues. Because of this, the provinces had to reduce their budgets for other government activities. The provinces have very little latitude to introduce new programs, to lighten the tax burden or to pay down their debt. And yet, everyone would agree that these are things the provinces should be doing. The main victim of this dysfunctional structure is undeniably the budgetary and decision-making independence of Quebec and the other provinces.

I will complete this quick overview of the situation by pointing out that the have-not provinces are facing increased difficulty in offering comparable high-quality public services at comparable taxation rates. The fact is that there are still significant discrepancies in the fiscal capacity of the various provinces, despite the equalization program. These discrepancies have been accentuated by the arrival of the new equalization program introduced—not to say imposed—by the federal government at the federal-provincial-territorial conference last October. My colleague, Minister Audet, will demonstrate how this situation, which we describe as the horizontal fiscal imbalance, has a very particular impact on Quebec.

Of course, it is not enough to say that the financial situation of one government is better than that of another or that one government has surpluses and the other deficits in order to automatically conclude that there is a fiscal imbalance problem. We make no such claim.

In order to properly understand the vertical fiscal imbalance phenomenon that exists between the federal government and the provinces and in order to understand its consequences, I would invite you to consider the following five factors.

First, we must realize that this is a structural, overall problem that is destined to continue in the future.

● (0920)

A study carried out by the Conference Board clearly demonstrated that the issue is one of structural imbalance, which is set to worsen in years to come if no changes are made to Canada's current model of fiscal federalism. This study shows that if significant changes are not made to current fiscal policy, the federal government will continue to accumulate budget surpluses while the provinces and territories will find themselves facing ever-worsening deficits. The Conference Board predicts that by 2019-2020, the provinces' net debt could go up by more than 50 per cent to reach more than \$400 billion, while the federal government's net debt could be reduced by almost 75 per cent.

Here, we are not so much interested in the accuracy of the figures, but in the marked tendency which the Conference Board study reveals. Like the work carried out by the Commission on Fiscal Imbalance, Conference Board studies confirm not only that the imbalance is structural in nature, but that the trend will worsen if corrective measures are not taken.

Fiscal imbalance is a problem across the board. In fact, to fully understand the scope and complexity of its ramifications, it is important to take into consideration a range of factors, including federal transfer mechanisms: equalization, the Canada Health Transfer, the Canada Social Transfer, and all other transfers linked to programs stemming from intergovernmental agreements.

The second factor which must be kept in mind in order to understand fiscal imbalance is, of course, the division of responsibilities. Beyond simply recognizing that one of the two levels of government enjoys healthy surpluses while the other struggles to stay out of the red, it should be noted that fiscal imbalance arises primarily from the fact that one of the two levels of government, in this case the federal government, has revenue which proportionally exceeds its constitutional responsibilities, while the opposite is true for the other level of government, in this instance the provinces and territories.

The problem of fiscal imbalance cannot be understood in the unidimensional context of a single national economy, but must be considered within the specific context of Canadian federalism. A comparative bidimensional analysis recognizing that both levels of government have full sovereignty within their respective jurisdictions is therefore required. Ensuring that the share of the tax base adequately reflects the division of powers is a *sine qua non* condition to the success of the federation. Canadian federalism is more than just a theory; it is more than a bunch of principles, provisions, documents and ancient texts to be applied subject to the whims of the federal government and the vagaries of public opinion. Canadian federalism and the regulations which govern it are, rather, part of everyday reality and must be faithfully adhered to by the various members of the federation.

Both the provinces and the federal government have their own areas of jurisdiction under the Constitution. Both levels of government must have sufficient revenue to enable them to adequately meet their responsibilities. However, the federal government takes more of taxpayers' money than is required to fund national defence, old age security, federal debt repayment, and all other expenditures which fall under its jurisdiction.

The most glaring proof that Ottawa's revenue surpasses that required to meet its constitutional responsibilities is that the federal government is spending more and more money in areas which fall exclusively under provincial jurisdiction. The last federal budget was a case in point: \$5 billion for child care, \$5 billion for municipalities, \$800 million for various federal health care initiatives, money which, incidentally, was invested without regard for the September 2004 agreement, and so forth.

These initiatives are in addition to the raft of new councils, foundations and institutes, such as the Health Council of Canada and the Canadian Council on Learning, which have been implemented

over the past few years, and, more often than not, whose mandates encroached upon areas of provincial jurisdiction.

● (0925)

As for the provincial governments, most of them are in the opposite situation. They will have to face ever-increasing fiscal pressures over the coming years because of the aging population and the impact that will have on the cost of health and pharmacare.

Because the provinces, as a whole, take in more money, the federal government denies the existence of the fiscal imbalance. To make that kind of statement without comparing the federal and provincial expenditures is pure sophistry. A simple comparison of the federal fiscal balance compared to that of the provinces would be enough to counter the federal argument.

I might point out that the expenditures in health and education currently represent 60 per cent of Quebec's budget revenue. This proportion rises to almost 84 per cent when we add the funds related to professional upgrading and employment activities and family and income security, 11.4 per cent, and funding the public debt, 12.7 per cent. We can easily imagine the extent of the difficulties that the Quebec government will face when we see that only 16 per cent of the revenue remains to take care of the government's other responsibilities, including culture, the environment, regional development, agriculture, etc.

The third factor that must be taken into account in examining the fiscal imbalance is the taxpayer's ability to pay, something which, as we know, is not unlimited.

In the entire debate on fiscal imbalance, our federal counterparts regularly put forward the argument according to which this imbalance cannot exist because the provinces have access to essentially the same independent revenue sources, as does the federal government. It is true that, with the exception of customs and excise taxes, the provinces do have the same sources of revenue as the federal government. Some have even suggested that the provinces are free to increase their sales and income taxes to generate more revenue.

That argument is disingenuous. Indeed, beyond the range of mechanisms that the governments have to raise income and sales taxes, there is one basic truth that no one will challenge: there is only one taxpayer who pays taxes to the federal and provincial governments, and that taxpayer's ability to pay has its limits.

The federal and provincial governments share a tax base that is limited by the citizens' capacity to be taxed without greatly reducing their consumption of goods and services or the country's general economic output. The governments' capacity to tax is also limited—and everyone knows this—by the necessity to ensure that our tax situation will compete favourably with that of our neighbours, whether the Canadian provinces or the American states.

Therefore, if the Canadian government unfairly takes too great a share of the tax base, it is automatically detrimental to the provincial share.

The fourth factor to consider involves paying down the debt. The fact that the federal debt is proportionally higher than that of the provinces in no way justifies having the federal government all alone in paying down its debt. Here again, a certain number of things must be put into perspective.

It has been clearly demonstrated that the federal government has more than enough revenue to fund the programs for which it has a constitutional responsibility, to pay the interest on the federal debt, to spend ever-greater amounts in areas of provincial responsibility, and, at the end of the year, end up with large surpluses that can be used to reduce the debt. The provinces, with the exception of Alberta, have barely any leeway to reduce their own accumulated debt. If it is desirable in terms of economic efficiency for a government to reduce its accumulated debt, then it should be just as desirable, not only in terms of economic efficiency but also in terms of fairness, for all of the governments in Canada to also refund their accumulated debt.

I should also point out that a significant part of the federal debt is the result of deficits that Ottawa has had in the past. The provinces should not have to pay for the lack of care demonstrated in the past by the federal government and must not put up with having it be the only government to reduce its accumulated debt. The Conference Board is undeniably eloquent in its study that demonstrates that an increasing fiscal imbalance would result in a situation where the federal government would see its debt reduced while the provincial debt would increase.

● (0930)

Is the federal government not highlighting its own turpitude when it declares that the fiscal imbalance is non-existent because the federal debt is proportionately higher than that of the provinces? Let us not forget that this debt is, in large part, the result of the federal government's centralizing designs and its abusive use of its so-called spending power in areas of provincial jurisdiction.

The fifth and last factor that one must consider is that the fiscal imbalance serves as a powerful tool for the federal government to further infringe on areas of provincial jurisdiction.

One must understand that, without a doubt, the fiscal imbalance serves the interests of the federal government by giving it the means to exercise what some call its spending power. Needless to say, the federal government has succeeded at stealthily disrupting Canada's federative formula and distorting the principle that each level of government is free in its choices when legislating within its own areas of jurisdiction. The current division of fiscal resources between the two orders of government results in a situation where the federal government wields considerable financial means, out of proportion

to its responsibilities, and enhances its predisposition to act in areas that do not fall under its constitutional jurisdiction. An increased fiscal imbalance would therefore only aggravate the problem of federal spending power.

The underlying logic of the concept of federal spending power is simple: it enables the government to intervene financially without any regard for the sharing of constitutional jurisdictions. By multiplying expenditures in crucial areas, such as social services, health care, education, and municipalities, and by creating several councils or Canadian institutions that deal specifically with issues falling within the mandate of the provinces, the federal government distorts how provinces carry out budgetary choices by favouring certain areas or certain approaches to the detriment of other options.

The report of the Commission on Fiscal Imbalance is clear: the federal government's ability to spend in our areas of jurisdiction is directly fueled by the fiscal imbalance. In so doing, the federal government restricts the provinces' independent and budgetary decision-making process. In addition, it is important to understand that these expenditures are made possible because the federal government has overabundant resources at its disposal. It ends up indirectly changing the sharing of powers to its advantage, without having to resort to proper constitutional reform.

It is nonetheless surprising to hear federal officials deny the existence of a fiscal imbalance on the one hand, while promoting massive federal investments in provincial areas of jurisdiction on the other. Are these indirect acts of federal intervention not in and of themselves solid evidence that the Government of Canada has more money than necessary to adequately manage its own business, to the extent that it can now manage the business of others? Each time the Government of Canada infringes on a provincial area of jurisdiction, because it is strategically or politically advantageous, the government demonstrates that it is collecting more money than it needs, and as such, confirms the existence of a fiscal imbalance.

There is only one conclusion to be drawn: a new sharing of the tax base and a review of federal transfers, including equalization, is necessary to make sure that each government is able to fully assume its respective responsibilities.

I believe that it is essential to refer now to the principles that must drive the creation of a new formula to apportion fiscal resources between the different levels of government in Canada. Regardless of the means used to get there, whether it be increased federal transfers, transfers of tax points, major changes to the implementation of federal programs such as equalization, the following principles must prevail.

Principle one: there must be an appropriate balance between the constitutional responsibilities and the revenues of each level of government, so that each level can properly fulfil its mandate.

Principle two: provinces need stable and predictable revenues. The problem of the fiscal imbalance must be resolved with a permanent and long-term solution ensuring that the provinces enjoy the predictability, stability, and financial independence they need to properly discharge their constitutional responsibilities.

● (0935)

Principle three: stemming from these first two principles, it is not enough to only resolve the vertical imbalance between the federal government and the provinces, but it is also necessary to resolve the horizontal fiscal imbalance by bringing about true improvements to how the equalization program operates.

Up until now, the federal government has been ducking the issue of the vertical imbalance, by refusing to discuss it with the provinces. It must now set aside this close-minded attitude and agree to engage in a constructive dialogue with the provinces. The means to resolve the fiscal imbalance exist, by increasing cash transfers and tax points. For its part, Quebec is open and willing to contemplate and discuss solutions. It is essential that the Government of Canada be willing to do as much.

In conclusion, if nothing is done, the fiscal imbalance will only worsen and the federal government will acquire an increasing share of Canada's fiscal resources. Increased centralization of fiscal resources will only lead to political centralization that would destroy the federal formula.

Under the Constitution of Canada, the two levels of governments are of equal status, one cannot be subordinated to the other. Each level of government is sovereign in its areas of jurisdiction. As such, each must have the required resources to carry out its responsibilities, without having to turn to the other order of government for financial aid or handouts.

Because of the fiscal imbalance, the provinces are financially handcuffed, and find themselves in an unjustified and vulnerable position before the federal government, which increasingly seems to want to impose its priorities.

Mr. Chairman, in the mid-50s, Pierre Elliott Trudeau wrote, in his book entitled *Federalism and the French-Canadians*:

[...] if a government has such a superabundance of revenue that it undertakes to provide part of the common wealth which does not fall under its jurisdiction—that government is conspicuously guilty of going against the principle of proportional taxation.

Obviously, Mr. Chairman, the government of Canada has not learned this lesson.

I will now give the floor to the Minister of Finance, who will paint a clear and detailed portrait of what this problem of the fiscal imbalance entails for Quebec and for our government.

The Chair: Mr. Audet, you have the floor.

Mr. Michel Audet: Thank you.

Thank you, colleagues. I think that my colleague has just given you a very specific outline of the national political context surrounding the fiscal imbalance in Canada. As Minister of Finance, I would like to address the daily effect of the fiscal imbalance on the government's fiscal management, especially these days, as we are preparing the 2005-2006 budget.

The fiscal imbalance has a major impact on the capacity of provinces to offer services to the public, be it in health, education, road infrastructure, the environment, or community services for which the provinces are responsible and which are growing.

My objective today is not only to show that such a fiscal imbalance exists, but to make suggestions for concrete and applicable solutions to deal with several facets of this imbalance in the short and medium term.

The year 2004 was marked by several federal-provincial first ministers' meetings. These meetings led to progress in resolving the fiscal imbalance between the provinces and the federal government. However, there is still considerable ground to be covered. Important processes were launched in 2005. I want to commend the House of Commons for setting up the committee in which were are participating today. There will also be the Council of the Federation's committee on fiscal imbalance, as well as the federal government's panel on equalization.

My presentation will be divided into four parts. First of all, I will make some comments on the underlying reasons for the fiscal imbalance. Then I will talk about the transfer programs to the provinces for health, post-secondary education, and social assistance—which my colleague referred to as the vertical imbalance—and equalization—which he referred to as the horizontal imbalance, and which we could also call the imbalance in the wealth among provinces.

I will speak to the recent amendments made to these programs, as well as to the issues that continue to exist. In conclusion, I will summarize the solutions being proposed by Quebec to put in place a financially balanced and fair federation.

Let us start with a brief look back at the past 50 years. Here is a slide that is somewhat difficult to read from far away, but which summarizes how the situation has evolved. Here what is caused the situation we are facing today. In the 1950s and 1960s, the main social programs we know today were set up. Initially, the federal government, in creating these programs, was often a major and important partner. The federal government had committed to funding half of the provinces' expenditures in health, post-secondary education and social assistance, for example. That was the very foundation for these programs. It had the means to do so, since, as we know, the provinces had let the federal government be responsible for taxation to fund to war effort during the Second World War.

Gradually, the federal government moved out of cost-shared programs and replaced them with block funding, which means that the amount paid to the provinces was no longer linked to the level of spending that it was funding. That was the case for health and post-secondary education in 1977-78. That was also the case for social assistance, and that is a major factor in the evolution that we described earlier.

In 1996-97, when the Canada Social Transfer was set up, the first important phenomenon, the federal government gradually withdrew from any financial risk associated with delivering the social programs that it had encouraged the provinces to put in place using cost-shared funding formulas. Today, the provinces are alone in bearing these significant financial risks and the risks associated with their growth.

The second phenomenon that I want to address—and slide 2 illustrates it very well—is the way in which the federal government put its fiscal house in order in the early 1990s. After having reached \$38.5 billion in 1993-94, the federal deficit was completely wiped out four years later, in 1997-98. Two factors explain this quick and exceptional turnaround in the federal government's public finances.

• (0940)

It is very clear that federal revenues increased by 31.1 per cent between 1993-94 and 1997-98, whereas overall federal expenditures decreased by 3 per cent. However, in breaking down this 3 per cent decrease in federal expenditures, it becomes clear that transfers to the provinces went down 23.9 per cent, or almost 24 per cent, while other federal expenditures, including debt servicing, increased by 1.5 per cent. So that is really where the fiscal imbalance between the federal government and the provinces got bigger. The table clearly illustrates that.

Slide 5 shows what has happened to transfers to the provinces since then. Despite a slight improvement in recent years, the share of federal revenue allocated for transfers to the provinces remains well below what it was in 1993-94. The federal government allocated 23.2 per cent of its revenues for transfers to the provinces in 1993-94, whereas it allocated only 13.5 per cent in 1997-98. This shows that the reduction in federal transfers has an impact, of course, on the weight of these transfers, in overall expenditures. This share gradually increased, thanks namely to additional amounts earmarked for health, to 19.9 per cent in 2004-05. As you can see, the federal share will drop slightly again in the years to come.

By way of illustration, for provincial transfer payments to represent the same proportion of federal revenues in 2004-05 as they did in 1993-94, they would have had to have been \$6.4 billion higher over the past year. I think that figure clearly illustrates the shortfall that must be made up.

Slide 6 clearly shows that the federal government has the leeway it needs to increase its transfer payments to the provinces. Earlier on, my colleague mentioned the surpluses of recent years. More importantly, and more eloquently, the federal government's most recent budget shows that the federal government anticipates more than \$93 billion in leeway for the next five years. So we do not need any more studies like the one conducted by the Conference Board: In its most recent budget, the federal government has provided us with the answer to our question: Does it have leeway? The answer is clear. The recent federal budget has illustrated the fiscal imbalance much more clearly than any study on this topic, even studies by the Conference Board. I noted that the night the budget was brought down.

Slide 7 deals with transfers for health, post-secondary education, and social programs. This is the second part of my presentation. The September 2004 health accord resulted in gains for the provinces, especially for Quebec, because the provinces banded together to convince the federal government to increase transfers for social programs, especially health. Since we were elected, thanks to Mr. Charest's leadership within the Council of the Federation, and thanks to my colleague, the Minister for Canadian Intergovernmental Affairs, the provinces were able to speak with one voice and presented a common front to improve their position, especially in

this area. This consensus led to the September 2004 health accord. This asymmetrical agreement represents a gain of \$502 million for Quebec in 2004-2005, and a gain of about \$700 million for the following years.

The federal contribution to post-secondary education and social programs has been put on the back burner in recent years because of the federal government's priority to fund health. This is on slide 9. There have been some improvements; that is good news. Funding for health is almost \$10 billion higher than it was 10 years ago. The bad news, and few people realize this, is that federal funding for post-secondary education and social programs, over the same period, went down by \$2.2 billion. This can be explained in part by the federal government's decision, which I described earlier, to separate the Canadian Health and Social Transfer into two separate transfers in 2004-2005, based on a recommendation by the Romanow Commission. However, the federal government did not fully implement the Romanow Commission recommendation. The Commission recommended earmarking 43 per cent of the social transfer to health and 57 per cent to funding for other social programs.

• (0945)

In fact, the federal government decided to allocate 62 per cent of the Canadian Health and Social Transfer to health and 38 per cent to other social programs, thus artificially inflating support for health. Basically, the block funding was moved around to illustrate a stronger increase in health, but this had repercussions on other transfers.

On slide 10, taking into account these changes, we can see that federal transfers for health now represent 22.3 per cent of provincial spending in this area. However, federal transfers for education, social assistance and other social programs represent a mere 11.5 per cent of provincial spending.

Moreover, we must harshly criticize the creation—as my colleague stated earlier—of a host of federal programs in areas of provincial jurisdiction at a time when the federal government was reducing its contribution to the social programs. The Canada Millennium Scholarship Foundation and the Canada Foundation for Innovation are but two examples of this.

As slide 11 clearly illustrates, the federal government has, in recent years, amended the allocation formula for some transfers to the provinces. For Quebec and the less prosperous provinces, a major change occurred when the decision was made to move from a social transfer based on the costs of social assistance to a per capita transfer.

I can confirm that this had a major impact. I think I am going to take a few moments to describe it. Until 1995-96, as I may have indicated at the start of my presentation, the federal government was funding 50 per cent of the bill each province faced. Today, it is a per capita amount. The result of this formula is that the federal contribution for persons on social assistance in the provinces is 18 per cent higher for Ontario than it is for Quebec. Alberta receives three times more than Quebec does for each social assistance recipient.

In conclusion, the figure is quite clear. In terms of dollar amounts for social assistance recipients, Quebec currently receives \$2,848 for each social assistance recipient identified, whereas at the other extreme, Alberta receives \$9,422 for each person identified. So you can see the gap. Basically, for each social assistance recipient identified in Alberta, the total contribution is higher than federal assistance, whereas in Quebec, it represents less than half of the average cost. I think this gap clearly shows the perverse effect of the decision that was made about 10 years ago. That decision was made in 1995-96. It is unfortunate that Quebec was not a more aggressive negotiator at the time.

Given this context, you will agree with me that a major reform is needed. This is illustrated on slide 12. As regards post-secondary education and social assistance funding, the level of funding, the formula for allocating the amounts among the provinces, as well as an adequate indexing mechanism must be analyzed and proposed. I am convinced that there will be a consensus among the provinces, especially with Ontario, to build a very strong common front on the specific issue of funding in these areas.

The third part of my presentation deals with what we referred to as the transfer to correct the horizontal imbalance, in other words equalization. I am referring to the federal equalization program.

I am going to remind you of recent developments in this program. Quebec made some very specific recommendations designed to improve the equalization program during the five-year renewal that ended on April 1, 2004. Given the federal government's refusal to implement these improvements, the provinces requested a new discussion on equalization at the same time as the discussion on funding for health, last fall.

However, instead of implementing the corrective measures for equalization as Quebec requested, the federal government unilaterally decided—and my colleague mentioned this earlier—to make substantial changes to the program, in a very authoritative way.

This new framework, the reforms determined unilaterally last September, had not been discussed with the provinces. The overall level of equalization entitlements in Canada has been set arbitrarily at \$10 billion in 2004-2005, and at \$10.9 billion in 2005-2006. Starting in 2006-2007, the overall level for equalization entitlements in Canada will be increased by 3.5 per cent per year.

• (0950)

Of course, a panel of experts has been chosen to provide an opinion by December on the provincial allocation of the total envelope for 2006-2007 and the following years. But this new framework put forward by the federal government represents a completely inadequate reform of the equalization program, in our opinion.

Why? Because the cost of the equalization program as a proportion of GDP, which is an indicator of the relative size of the program, currently stands at 0.8%, which is well below the historical average over the last 35 years, of 1.1% of GDP. However, the federal government could have adopted a very simple improvement to the equalization formula used as the program standard: the fiscal capacity of the 10 provinces, rather than the five-province standard in use since 1982.

At the time, the federal government claimed not to have sufficient resources to adopt this standard, but today has ample means with which to meet its obligations. If the federal government were to use the 10-province standard from now on, the cost of the equalization program as a share of GDP would regain its historic level of 1.1% of GDP.

On slide 16, we can see how the principle of the closed equalization envelope eliminates the last financial risk to which the federal government was exposed in terms of transfers to the provinces. This approach also limits the ability of the program to adjust to changes in the relative fiscal capacity of the provinces. Equalization will increase by 3.5% per year in Canada, regardless of fluctuating disparities in fiscal capacity between the provinces over the course of the next few years. This rate of growth is lower than that forecast for the Canadian economy, which therefore implies that the relative size of the program will diminish.

If a significant and sustained increase in oil prices—which in fact we are seeing today—were to happen and to continue, this would bring about a significant change in the fiscal capacity of the provinces. Within a normal equalization program, the total payments made to the provinces would be adjusted to correct such a phenomenon. With the new equalization framework, this desired adjustment will not take place, because the program envelope is closed. Therefore, the significant disparities in fiscal capacity between the provinces will not be compensated for, which goes against the objective of the equalization program as it is entrenched in the Constitution.

Not only is there a limit that runs counter to the principle enshrined in the Constitution, but added to that are the recent bilateral agreements signed between the federal government and some provinces which truly distort the equalization system. Newfoundland and Nova Scotia—and I do not wish to criticize the provinces; good for them if they have been able to profit from this—will not have to suffer a decrease in equalization payments because of their increased revenue from offshore oil resources.

The federal government's panel of experts has already indicated in its preliminary studies that they intend to study the impact of these agreements on the program's ability to reach its objective.

Furthermore, because of the one-time adjustments that are part of the federal framework, Saskatchewan and British Columbia will not have to pay back their equalization overpayments in 2004-2005. Once again, I do not want to criticize the gains obtained by the provinces, but Ottawa must be fair towards all the provinces.

Indeed, some will say that Quebec has signed a bilateral agreement on equalization. But in our case, the overpayments of \$2.4 billion represent an account payable, as the Auditor General has just reminded us. This \$2.4 billion amount serves to correct decreases in equalization payments that would have been dramatic for government finances. And yet, these decreases have occurred in contexts that are quite similar to the other provinces.

Up until now, I would like to point out that despite these shortcomings, the former equalization formula did respect the fundamental objective of equity. We can see this on the following slide: the fiscal capacity disparities among the provinces were reduced thanks to the equalization formula, and all of the provinces receiving equalization had the same fiscal capacity after equalization.

On the following slide, we see the effect of changes and of recent agreements. I stated that the new framework provides an inadequate and arbitrary level of support for the poorer provinces. I also said that the closed envelope is contrary to the program objectives, but the most harmful consequence of the federal reform, in my opinion, is that it breaches the fundamental principle of equity toward the provinces. The new framework and the bilateral agreements exacerbate the fiscal capacity disparities between the provinces, as is clearly shown on this chart. The role of equalization was specifically to minimize these disparities.

● (0955)

Clearly, as regards equalization reform, the federal government had to go back to the drawing board.

I would like to remind you of something to which my colleague drew your attention earlier, and which I believe to be important. In subsection 36(2) of the Constitution of Canada, it is stipulated that the provinces must receive “[...] sufficient revenues to provide reasonably comparable levels of public services at reasonably comparable levels of taxation.” In order to meet such an objective, the equalization program has to be based upon clear principles applicable across the board.

Broadly speaking, Quebec believes there to be four such principles, and we will have the opportunity to further define them at the various forums in which we will participate over the coming months.

The first principle to which we would like to draw your attention is that the standard used as the point of comparison for establishing the relative fiscal capacity of the provinces must, at the very least, correspond to the average level of the ten provinces, as was the case with the former equalization formula. Otherwise, the equalization-receiving provinces will be unable, by definition, to offer services of comparable quality at a level of taxation comparable to the average of the ten provinces. Furthermore, a calculation based on the average of the ten provinces will inevitably render obsolete the fixed envelope approach to equalization which the federal government decided to implement last fall.

The second principle is that in order to compare the provinces' capacity to fund the public services that they provide, all sources of revenue must be taken into consideration. These sources include revenues of municipalities, school boards and any other entity under the authority of the provinces, as well as revenue from renewable and non-renewable natural resources. Otherwise, equalization will compensate provinces on the basis of a partial, biased and inaccurate reading of their true fiscal capacity.

The third principle for reforming equalization is that the fiscal capacity of the provinces to fund public services must be measured on the basis of their actual, measurable taxation practices rather than

on arbitrary statistical approximations. Otherwise, real disparities in the capacity to fund public services will remain uncompensated, while artificial disparities will be compensated, something which is contrary to the objective of the program.

Finally, the last principle is that the equalization program, by definition, must be equitable. We must ensure that, after equalization, the fiscal capacity of the recipient provinces is comparable to or the same as that of other provinces. Furthermore, it goes without saying that equalization must remain unconditional, otherwise the less affluent provinces will be more constrained in exercising their constitutional responsibilities than the affluent provinces.

Quebec therefore intends to closely monitor the work of the federal government's expert committee on equalization. We plan to make very precise and very firm proposals on this subject.

To conclude, I would like to briefly review the solutions proposed by Quebec to create a financially balanced and equitable federation.

In the short term, from this year forth, we will be proposing major improvements to the federal funding of post-secondary education and social assistance.

In the short to medium term, the federal government must also make fundamental changes to the way in which it approaches equalization, and introduce an equalization program consistent with the stated objectives of the Constitution.

In the long term, as my colleague mentioned earlier, the federal government will have to review the division of financial and tax resources so that provincial revenues better reflect their responsibilities.

However, fiscal imbalance means that Quebec is unable to meet these objectives alone. The federal government has the means to do its fair share and has to do just that. Quebec intends to take advantage of the various processes implemented by the House of Commons, the Council of the Federation on fiscal imbalance, and the federal government, to ensure that concrete progress further to that made over the past two years is achieved.

Thank you, Mr. Chairman.

● (1000)

The Chair: Thank you very much, Mr. Audet and Mr. Pelletier for your excellent presentations.

We are now going to begin our first, and probably our last, round of questions. We will start with Ms. Ambrose of the Conservative Party.

Ms. Ambrose, you have five minutes.

Ms. Rona Ambrose: Thank you, Mr. Chair.

Mr. Audet, Mr. Pelletier, thank you for your presentation. I would like to thank you for coming along this morning. I greatly appreciated your presentation and found it to be most interesting.

It is important for you to know that the Conservative Party of Canada has long recognized the existence of vertical fiscal imbalance between the federal government and the provinces. Our party has also long recognized the existence of horizontal fiscal imbalances between the provinces.

During the last election campaign, Mr. Stephen Harper, the leader of the Conservative Party of Canada, promised that our party would work with Quebec and the other provinces to remedy this problem, which has already been going on for too long. I also feel it is important that you know that this promise was reiterated at our national convention in Montreal where the party adopted a motion stating that, together with Quebec and the other provinces, a Conservative government would work to redress fiscal imbalance by increasing transfers to the provinces, by reducing their tax burden, or by transferring tax points to the provinces.

The Conservative Party of Canada understands that fiscal imbalance allows the federal government to unilaterally intervene in several areas which are solely of provincial jurisdiction. Furthermore, our party understands that this encroachment by the federal government results in the federal government determining priorities for provincial policy, and thus places the provinces under increased fiscal pressure.

I have a question for Mr. Pelletier. The federal government has struck an expert committee on equalization and the funding formula for the provinces and territories. Do you believe that the work of the expert committee will have a significant impact on the way in which the next equalization formula is defined? What avenues would you suggest that our committee explore in an effort to find a solution to the problem of the equalization formula?

• (1005)

The Chair: Mr. Pelletier.

Mr. Benoît Pelletier:

Thank you.

Let me begin by saying that we had noted the Conservative party's open-minded attitude to the problem of fiscal imbalance. This attitude is, of course, one which is shared by some other federal political parties, but not by everybody.

Firstly, I should say that I fail to comprehend why some people still endeavour to deny the problem and to ignore what I would call proof. There is clearly a problem of fiscal imbalance. It is evident in every single federal budget with their ever-growing surpluses. In fact, the issue is becoming something of an embarrassment for the Government of Canada, which is running out of ways to hide its budget surpluses and the fact that the problem of fiscal imbalance exists.

Secondly, I would like to take this opportunity to remind you that, believe it or not, in the last Speech from the Throne, the federal government stated its intention to undertake the most far-reaching reform of equalization since its inception. We are still waiting for this reform. We hope that we are not simply dreaming, and that the Government of Canada will indeed undertake the most far-reaching reform of equalization since its inception, as Mr. Martin promised. Furthermore, when the system is reformed, it ought to be done in the way that my colleague Michel Audet described earlier. I should imagine that Michel would want to add a few words.

Allow me also to point out that the federal government's committee of experts on equalization rejected both of the proposals which were drafted by the Canadian provinces. We hope to see evidence of a more open-minded attitude. We are certainly willing to

have a dialogue on the matter, but it has to be an equitable dialogue between equal partners. An open-minded approach to the problem is still lacking.

Mr. Michel Audet: Allow me to add that I found my colleague's remarks to be particularly pertinent in light of what I said earlier. I am aware that far-reaching reform is planned; however, a decision to cap equalization payments would go against the very principle of the equalization program. By definition, equalization payments are based on calculations relating to the equalization of fiscal capacity. If, from the outset, \$10 billion dollars were to be earmarked for equalization payments to be shared amongst the provinces, regardless of other factors, the equalization program would once again become a capped program which would allow the federal government to avoid increasing its expenditure on equalization, a program designed to equalize the fiscal capacity of the various provinces. That is the very opposite to what the formula seeks to do.

In answer to your question, I would say that I see something of a contradiction between the objectives of equalization and the decision to enshrine in legislation the fact that the formula will henceforth include capped payments.

• (1010)

The Chair: Thank you, Ms. Ambrose, Mr. Audet and Mr. Pelletier.

If you share your time, Mr. Bell, you will each have two and a half minutes.

[English]

Mr. Don Bell: To Mr. Pelletier, you talked about responsibilities. I have a municipal background, and as a former mayor of a municipality and member of the Federation of Canadian Municipalities, I dealt with mayors from Quebec as well. I'm just curious about this relationship to the imbalance. We've heard from some experts, in testimony at other hearings we've had, that there is an imbalance as well between provincial and municipal.

I'm kind of interested in the feeling of Quebec with respect to municipal government. The Federation of Canadian Municipalities has taken the position that municipalities should be either a third or fourth order of government, whichever you relate to. You've mentioned the concerns about the pressures on municipalities as well for some of the services, and I'm wondering whether you accept the concept that one way to relieve the provincial area of responsibilities currently within the definition of the Constitution would be in fact to recognize municipalities.

Mr. Benoît Pelletier: I can give you a few comments on this issue. First of all, I'd like to say that there is a fiscal pressure on the municipalities, a financial pressure, that's for sure. But it's also one of the consequences of the fiscal imbalance between the provinces and the federal government.

Because the provinces have, I would say, maybe not enough money to assume all of their responsibilities fully, and to pay their debt, and to invest in some fields under their jurisdiction, then of course they don't have enough money for the municipalities. If you give the provinces more fiscal or financial resources, then there's a possibility for them to transfer some of these resources to the municipalities and to overall improve the situation of the municipalities fiscally.

That said, don't forget that municipalities are, by virtue of the Canadian Constitution...and I think the Constitution means something. I hope it also means something to the current federal government; I think it means something to the Quebec government. So by virtue of the Constitution, municipalities are under Quebec's jurisdiction. We're not open to having a new order of government constitutionally recognized. However, we do feel it's important that municipalities be considered partners, full partners, with regard to the development of the provinces. This is very important, that there is a sane relationship between the provincial governments and the municipalities.

Now, with regard to eventual agreements we may get with the federal government concerning municipalities, let me tell you that all we want to do is protect our jurisdiction. So we are open to some transfers of money in favour of municipalities, but we insist on the fact that these transfers of money should be done, with all due respect, with regard to the jurisdiction of the provinces.

Mr. Martin said that he is open to respect the jurisdiction and the competence of the provinces, including the competence of Quebec. So we feel that we are in a good mood, I would say, in order to find a viable agreement with regard to municipalities concerning the current federal government.

Mr. Don Bell: Thank you.

[Translation]

The Chair: You have two and a half minutes, Ms. Folco.

[English]

Mr. Don Bell: My 2.5 minutes are done? Okay.

[Translation]

The Chair: It is your turn, Ms. Folco.

Ms. Raymonde Folco: Thank you, Mr. Chairman.

Thank you, Mr. Bell, for sharing your time with me.

First of all, I do not know whether we should be welcoming you, because we are in Quebec City.

I have two comments. The first is to Mr. Benoît Pelletier. Mr. Pelletier, you say that the federal government hides its figures, that it wants to hide the fiscal imbalance. The federal government may calculate the imbalance differently with each province, but to actually say that it hides the figures... The figures are public. We may calculate things differently from the Quebec government, and perhaps also differently from the other provincial governments, but in my opinion, that is not the same as hiding the figures. That was a comment.

My question is to Mr. Pelletier.

Please feel free to answer it as well, Mr. Audet.

The issue of asymmetrical federalism was put forward by Premier Jean Charest and was accepted by all of the provinces in the context of the Council of the Federation. I think the federal government, which we represent, is following in Mr. Charest's footsteps, particularly with respect to the agreement Mr. Martin signed just recently with Newfoundland and Labrador.

In this case there was an agreement with the province, and this agreement meets its needs and takes into account this horizontal imbalance you both mentioned, particularly Mr. Pelletier. I do not agree that this agreement with Newfoundland and Labrador—to take just one example—will be harmful to provincial unity, and divide the provinces.

I would like to hear what you have to say about this, Mr. Pelletier or Mr. Audet.

● (1015)

The Chair: You have the floor, Mr. Pelletier.

Mr. Benoît Pelletier: Thank you, Mr. Chairman. My colleague, Mr. Michel Audet, will reply to one aspect of Ms. Folco's question.

What the federal government hides each year—and I was not referring to the figures with respect to the fiscal imbalance between the provinces, that is, the horizontal fiscal imbalance—are its budget surpluses. It no longer knows how to hide them. At some point, it has no choice, it has to announce the surplus. For at least 10 years now, the federal government has been underestimating its budget surplus every year by several billion dollars.

Again this year, we're clearly headed for further success. The budget surplus announced by your Minister of Finance will probably be far below the actual figure at the end of the year. All of this confirms the fiscal imbalance theory.

Of course, you are very proud to stand up every time your Minister of Finance announces these budgets surpluses. I have seen you—you all stand up and applaud loudly. You're very proud. And then you come to Quebec and deny the existence of the fiscal imbalance. You have a hard time using this expression.

You tell us that there must be dialogue with the provinces, that there must be an attempt made to see how we can reach a financial agreement that will make federalism healthier and more acceptable. But that is not what you do. You deny and you rake in the surpluses.

You announce expenditures in areas of provincial jurisdiction. There is an increasing temptation to attach conditions to these transfers and you think that Canadian federalism is going to be strengthened by this. In my view, you are mistaken.

The Chair: Thank you, Ms. Folco.

Thank you, Minister.

Mr. Michel Audet: May I make a brief comment on a different matter? It is important.

The Chair: Yes, you have a few seconds.

Mr. Michel Audet: In the case of health care, the fundamental difference, Madam, is that the calculation was done in the same way for everyone, but the conditions were different. This is precisely why Quebec had a special agreement. It was not necessarily supposed to meet any conditions. The agreement had fewer conditions, and therefore was different. However, the calculation was done in the same way for everyone.

The issue in the case of these special agreements signed with Newfoundland and Labrador, with Nova Scotia and with other provinces, is that each province had an agreement in the context of a debate in which the calculation was no longer done in the same way at all.

In the case of Quebec, it was supposed to pay back \$2.4 billion over ten years. In the case of Newfoundland and Labrador, however, it was decided that everything was all right and the matter would be dealt with in this way. So there is a problem here of different treatment for different provinces. This is a fundamental difference.

In the case of health care, Quebec did not receive more than the other provinces. It had different conditions attached to the money, because of its unique concerns, specifically with respect to its powers. That is why the agreement was described as asymmetrical. But it was not asymmetrical with respect to the amounts received by Quebec.

The Chair: We cannot say that we did not try to help Messrs. Goodale, Manley and Martin, Minister. In fact, the last time I tried to help Mr. Goodale, I offered him a calculator. He turned it down. It might have helped him evaluate the surpluses better, but that is another story.

Mr. Côté, of the Bloc Québécois, for five minutes, please.

Mr. Guy Côté: Thank you very much, Mr. Chairman. Thank you very much for your very instructive presentation, Minister Audet and Minister Pelletier.

As you mentioned, Mr. Pelletier, the fiscal imbalance is a fundamental issue. You have established beyond any doubt that the problem does exist. You have given a good demonstration of how the dynamic in place over the last 30 years was such that we moved from a situation where program costs were shared 50-50 by the federal government and the provinces, including Quebec, to a situation in which the federal government pays 22.3 per cent of health care costs and 11.5 per cent of other social spending.

We have seen that these problems have gotten worse in the last 10 years. Since 1994-95, provincial governments, Quebec in particular, have had to manage this drop in federal transfers. Similarly, and you demonstrated this very well, despite occasional gains, we are continuing to see the federal government make decisions unilaterally. Here, I'm thinking of course of the health care agreement. The last agreement on equalization and the special agreements with other provinces are also an example of this. At the same time, there has been reduced accountability and transparency on the part of the federal government. We have talked a great deal about the federal surpluses.

The fact is that the federal government can still make unilateral decisions which increasingly encroach upon Quebec's jurisdiction and that of the other provinces, thereby limiting what they can do.

Is your presentation not a demonstration that it is impossible to reform comprehensively the pan-Canadian fiscal system? As long as the federal government can act unilaterally, we will always find ourselves in much the same situation.

Mr. Audet, you say that in the short term, one of the solutions is to correct federal funding for post-secondary education and welfare

beginning this year. That will not deal with the fact that the federal government acts unilaterally. In the longer term, would the solution not be to eliminate completely federal transfers in areas of provincial jurisdiction in exchange for tax points or tax room, for example the transfer of the GST and a comprehensive reform of equalization? Naturally, I'm thinking of the 10-province standard, and including all the revenues in the calculation.

• (1020)

Mr. Michel Audet: If I may, I want to clarify that we are making our suggestions based on the hypothesis that federalism can be more effective. That is clearly our perspective. That is clear to us, and we are convinced that we can achieve that. The fact is that we did achieve that last year by signing the health accord.

Instead of talking only about overall figures, today we presented a way of fixing components of these transfers in order to obtain adequate funding. That is the aim of the proposal. Some people clearly wonder what our chances of success are. I think that we were successful last year. This year, we are putting together a common front on post-secondary education. Of course, everyone is aware of the figures that I presented earlier. All of the provinces are facing this situation. I therefore believe that there will be a consensus and that the strength of the provinces' negotiating position is their ability to put together a common front. It could be presented at the Council of the Federation and the negotiations that will take place in that context. I will let my colleague complete my answer.

Mr. Benoît Pelletier: Mr. Chairman, I fully agree with my colleague. I do not think that reforming our fiscal system in Canada is impossible. I do not agree. On the contrary, I believe that progress can be made. We are not making quick enough progress now. We missed a good opportunity, last October, during the conference on equalization. The Government of Canada should have stepped up its efforts to make it a big success, with an agreement that was advantageous for both the federal government and the provinces. Unfortunately, the federal government adopted a different attitude.

Having said that, I am very convinced that progress can be made. I believe that it is possible to reform our system. Bear in mind that to do so, we must truly deal with the structural nature of things.

Some people say that the federal government should cut taxes; the provinces could then take the area it vacates. That may be true from the tax base point of view. The fact remains, however, that that is an ad hoc approach, whereas the problem with the fiscal imbalance is that the provinces need predictable funding. So that means dealing with the very foundations of the tax base, with long-term allocations, based on everything we have presented.

The main objective of my presentation today is to clearly illustrate that we are facing a multi-dimensional problem. Very often, current federal ministers tell us that the fiscal imbalance does not exist, because the provinces have the same sources of revenue as Ottawa, which is entirely true, apart from customs and excise, the provinces have more or less the same sources of revenue as Ottawa. But that is not where the fiscal imbalance is: it is in the allocation of the tax base between the federal government and the provinces, in a context where the provinces need to be less dependent on federal transfer payments and unilateral decisions made by Ottawa, and where they need more predictability.

To understand the fiscal imbalance, the capacity of each level of government to pay down its debt in the future must also be assessed. The assessment must include not only equalization, but also funding for health, post-secondary education, and social programs. In short, a host of factors must be examined. The constitutional responsibilities of each level of government must also be considered. A link between that and the federal spending power must also be established.

The fiscal imbalance coupled with federal spending power in areas of provincial jurisdiction, is, in the long term, a recipe for disaster for a federation. We must be aware of that.

A host of factors enable us to determine whether or not the fiscal imbalance exists. I have yet to see a federal minister with the courage to sit down and examine the entire issue. We often hear arguments that deal with one small part of the problem.

• (1025)

The Chair: Thank you, Mr. Côté.

Ms. Wasylycia-Leis, please, you have five minutes.

Ms. Judy Wasylycia-Leis: Thank you, Mr. Chairman, and thank you, Mr. Audet and Mr. Pelletier, for your very interesting presentations.

I have the impression that we are currently seeing the death of equalization. The situation is very critical, very urgent. But when we discussed constraints on the provinces with Mr. Goodale and his parliamentary secretary, Mr. McKay, they both told us that the provinces all agreed to the October 2004 accord, that they had participated enthusiastically in that accord, and that they have no complaints.

So I want to know the real situation, the possibility of coming up with a formula that is consistent with the suggestions made by the provinces two or three years ago to go back to the 10-province standard and to include all sources of revenue.

Mr. Benoît Pelletier: I think my colleague, Michel Audet, would like to add to my answer. However, I would say that in October, we did not think that the equalization system had been reformed. We are still waiting for that. It is true that some financial adjustments were made, and some of them were beneficial to Quebec. It was not a complete failure. However, we really expected that the equalization system would be reformed and that the 10-province standard would be taken into account, as well as all provincial revenues, and so on. As far as I know, none of these matters have been settled.

In my opinion, thinking that equalization alone will rectify the fiscal imbalance is completely incorrect. We have to think about funding not only for health care, which was dealt with to a large extent last September, but also funding for post-secondary education and social programs. We knew that after the federal government gave us funding for health care at the conference last September, it was simply going to reduce the funding for social programs and post-secondary education. That is exactly what it did. So we will have to deal with the problem as a whole, one of these days.

• (1030)

The Chair: Mr. Audet.

Mr. Michel Audet: As regards reforming equalization, I would like to point out that some progress has been made. The federal

government was establishing the equalization formula on the basis of the five-province standard. The variations were significant when a province such as Ontario, which has a great deal of weight, became wealthier or poorer. The corrections introduced proved that the current formula was too sensitive to these phenomena. That is why it has to be broadened, to give a more complete view of the fiscal capability and the revenues of all the provinces, rather than trying to deal with the problem by setting a ceiling.

You are right: in the long term, there will no longer be a link between fiscal capability and equalization payments. After years and years, this will become a type of transfer which, while unconditional, will no longer have any link to the formula whose principles are stated in the Constitution.

The Chair: You have 30 seconds left.

Ms. Judy Wasylycia-Leis: I therefore think that the federal government forced the provinces to accept the October 2004 agreement. They had to take it or leave it. They had a gun to their head, so to speak.

As you mentioned, the provinces unanimously accepted a formula two or three years ago. However, the federal government decided to adopt a different approach. How could it be persuaded to make the changes to the equalization program being demanded by the provinces?

The Chair: Mr. Pelletier.

Mr. Benoît Pelletier: Mr. Chairman, was Mr. Martin really serious when he said that he wanted to undertake the greatest reform in the history of equalization? We are still waiting for this reform.

I see that he has struck an expert panel to examine this issue. We will see where that leads. I honestly believe that the Government of Canada must make this type of choice. I will start by saying that, in terms of equalization reform, last October's conference left us wanting.

I would also say that, in view of the comments you have just made, we must all understand that this is a federation whose partners' interests must be taken into account. Nevertheless, we have to ensure the viability of Canada's federal system. Let us not forget that Canada is a federation, which means that the provinces must not be subjected to a type of fiscal attrition. For Quebec, this involves not only its autonomy and its jurisdictions, but also, to a certain extent, its special nature. Indeed, Quebec's special nature is intimately related to its autonomy.

This means, essentially, that the fiscal imbalance is a fundamental problem in the Canadian context. Personally, I feel that, as "mature" partners, we should be able to find a more permanent solution to the fiscal imbalance problem.

The Chair: Before asking Mr. Bell to make a brief statement, I have two questions for you. I do not often avail myself of this privilege, but I think that it would be worthwhile to hear the answers to these two questions, one of them political, and the other, fiscal.

An agreement was signed with Newfoundland and Labrador and Nova Scotia. Special arrangements have been made with Saskatchewan. Some \$590 million in equalization debt has been forgiven. I think that for British Columbia, the agreement represents \$100 million. There is a possibility, or at least rumours, of an agreement with Ontario as well. That is what we were hearing in Ottawa, only a few days ago.

This is my first question. Do you not feel that you might be the victims of last September's success at the Council of the Federation, where you stood your ground against the federal government? Mr. Martin was bruised, and there was a change in attitude when the second equalization meeting was held. In other words, is this a case of divide and conquer? The premiers of Newfoundland and Labrador, and Nova Scotia, were supposed to be in Halifax. They were no-shows, right after the equalization agreement was signed.

This is my second question. Now that an agreement has been signed with Newfoundland and Labrador and Nova Scotia, and the objectives and very nature of the equalization program have been betrayed, what can we do to fix it? I am asking this question with a view to the recommendations that our subcommittee must make before next June 2.

• (1035)

Mr. Benoît Pelletier: Are we victims of our success last September? I really don't think we are. Last September, we were, in a way, instrumental in having a conference scheduled for October. At the outset, the conference was not in the federal cards.

Mr. Charest was the one who triggered the scheduling of this conference. He convinced his colleagues on the Council of the Federation to force the government's hand so that a meeting would be held in October. In the end, we had nothing to lose with an October conference. We came away with at least \$500 million, because we played hard from the very beginning. That is how you should see it.

That said, we were hoping that the October conference would deal with the fiscal imbalance. However, the subject was equalization, and nothing but adjusting equalization was discussed. Of course, we were disappointed on that score. At the same time, forcing the federal government to discuss equalization reform last October was a good move by Quebec. You at least have to grant us that.

Because of that alone, Quebec can boast about having forced this conference to be held. There will be others, because the debate is far from over. This has earned us the visit of your subcommittee, whose existence is a concrete demonstration of that fact. There is the work that is being done within the Council of the Federation, there is Mr. Martin's panel of experts on equalization, and other things that will take place in the coming months. It is far from over. These are the sinews of war, the heart of the action. All of the partners are lobbying Ottawa to come to a permanent solution.

Of course, we are in a way victims of Ottawa's unilateral decisions. The honourable member mentioned it earlier. When

Ottawa sets an equalization ceiling, that is a unilateral decision. When Ottawa signs agreements with Newfoundland and Labrador, with Nova Scotia, these decisions demonstrate that the current equalization system is not being used as was originally intended.

The equalization principle is a constitutional principle pursuant to section 36 of the 1982 Constitution Act, as Mr. Audet demonstrated earlier. We can't let a constitutional principle which is fundamental for Canada's federation become subject to unilateral decisions by Ottawa. That would make no sense.

The Chair: Thank you, Mr. Pelletier. Mr. Audet has the floor.

Mr. Michel Audet: The second part of your question dealt with the recommendations made by this committee. I believe you have a very important role to play, if only to begin to take a serious look at program review in order to rebalance the funding of the Canadian federation.

This rebalancing, as we said earlier, will consist in a combination of fiscal transfers, of course, which will affect all provinces, and equalization payments, which will go to the provinces with the lower fiscal capacity. It is clear that there must be a balance. We are aware that equalization cannot be the only way, because two or three provinces are not beneficiaries. It is obvious that we are aware of the need for political balance in Canada. So both would apply.

The impression that we now have, in view of the work that has begun, is that faulty assumptions are being used for the equalization formula. The work must be redone, you will have to go back to the drawing board, in order to explain that this is no way to correct the long-term funding of the Canadian federation. As we described earlier, the financial and fiscal transfers, as well as equalization, must be re-engineered in order to ensure a balance among all of the provinces.

• (1040)

The Chair: Thank you, Mr. Audet.

Mr. Bell, a short question, please.

I would also like a short answer, please.

[English]

Mr. Don Bell: I have a question for ministers Audet and Pelletier, based on their comments.

First of all, Minister Audet, you commented that federal transfers have increased since 1998-99. I would just point out that, to my understanding, this was during the same time that the federal government produced consistent, balanced, and non-deficit budgets, I'll call them, and as well reduced the national debt.

The other point you made is that provincial governments don't seem to have any way to pay down their debt. I would point out that my other understanding is that this situation is reversed, that 20 years ago—and you made historical references, both of you—the federal government had a deficit and the provinces didn't. There weren't any provincial offers to help pay down the federal debt, as I understand it, and yet now the reverse is being asked here.

I know that there have been tax cuts by other provinces in recent years, and I'm wondering if there were tax cuts by Quebec during the last seven or eight years. And do you see any inconsistency in provincial budgets being cut, and yet a request, in effect, about a supposed fiscal imbalance, that the federal government should somehow reciprocate the other way?

[Translation]

Mr. Michel Audet: I think my colleague knowledgeably alluded to many of the aspects you just raised.

One thing that must be said about tax reductions is that we live in a competitive economy. We cannot keep the tax burden much higher than the other provinces because we will lose our best resources, human as well as otherwise, as well as business investment.

So we have to face fiscal competitiveness. When adjustments are made to our taxation, it is not—at least this is the case for Quebec—to do the others one better, but rather to make sure we can remain competitive domestically as well as internationally.

I think it is very important to say that our commitment has always been to try to get our tax burden down closer to the Canadian average. That supposes that we have the revenue necessary to allow us to do that. At the present time, our tax level is higher. So we do not want more federal tax transfers in order to decrease taxes, no, it is in order to provide services to the population.

At the same time, and this must be said, we must be aware of the tax burden on businesses and individuals in Quebec if we do not want to find ourselves in a position of weakness both economically and competitively.

The Chair: Thank you, Mr. Bell.

I want to thank you, Messrs. Pelletier and Audet, respectively Minister of Intergovernmental Affairs and Minister of Finance, as well as the teams from your respective departments.

Thank you very much for this great exchange and your high-quality presentations.

Actually, the government of Quebec is getting us used to this very high quality and it certainly was not lacking today. Thank you tremendously for your contribution. Until the next time.

We will suspend the meeting for five minutes.

● (1042)

(Pause)

● (1053)

The Chair: Ladies and gentlemen, if you do not mind getting back to your seats, we will continue our work.

With us we have students in communications from the Université du Québec à Trois-Rivières who are interested in the matter of fiscal imbalance. We welcome them to our subcommittee.

I would also like to welcome Mr. Mario Dumont, Leader of the Action démocratique du Québec, as well as Marc Picard, MNA, and finance critic of the Action démocratique du Québec. It is an honour to welcome you both here today to discuss this important matter of fiscal imbalance.

We have until June 2 next to table a report in the House of Commons containing recommendations for the federal government in order to correct fiscal imbalance in a sustainable way.

I thank you for coming here and contributing to this debate. Messrs. Dumont and Picard, you have 15 minutes to present your points of view and analyses. We will then go around the table for questions and comments from the members from all political parties represented in the House of Commons.

Mr. Dumont, you have the floor.

Mr. Mario Dumont (MNA and Leader of the Action démocratique du Québec, Quebec National Assembly): Thank you.

I would first like to welcome the members of the subcommittee and emphasize the consideration we have for the work you are doing. It is a pleasure to participate in your work concerning a matter which has been given much thought in Quebec, of course. That is true as well for those who are part of the government as for those who are in the ranks of the opposition, and also those who are engaged in politics and are closely following the matter of public finances and the questions surrounding it, amongst others the matter of the hard financial choices governments must make. A lot of work has been done in that respect during the last few years. We do not get the impression it is something terribly new, but when a subcommittee of the House of Commons comes before us, we certainly do have things to say.

As you pointed out, Mr. Chairman, I have with me Marc Picard, who is the MNA for Chutes-de-la-Chaudière and also, within our party, the person overseeing the question of public finances. He will immediately address the matter of transfer payments and questions of financial importance. I will then follow him and address questions more specific to health and R&D.

● (1055)

Mr. Marc Picard (MNA and Finance Critic of the Action Démocratique du Québec, Quebec National Assembly): Because of the provinces' budgetary problems, the government of Quebec charged the Séguin Commission with studying the matter of fiscal imbalance. That commission clearly identified a lack of federal transfers to the provinces as one of the main causes of that imbalance.

In its March 23, 2004 budget, the federal government proposed changes that only perpetuate, if not increase, that imbalance. Those changes do not allow the provinces to increase the funding of their services sufficiently. Federal transfers initially forecast for Quebec decreased by \$716 million in 2003-2004 and \$940 million in 2004-2005.

Federal transfers of some \$8.9 billion in 2002-2003 were decreased to \$8.2 billion in 2003-2004 and \$7.3 billion in 2004-2005. This is a \$1.7 billion decrease over two years. This major decrease weakened Quebec's financial position in a situation where it faces a major increase in the needs of its population.

The negotiation of measures to delay the impact of the decrease in federal transfers only puts the problem back till later. These mitigating measures have led to an increase in federal transfers of \$1.2 billion for 2003-2004 and 2004-2005. However, one must fully understand that Quebec, over the next five years, will have to pay back an amount of \$472 million.

It is clear that these temporary emergency measures will have to be replaced by a fair and equitable sharing out of fiscal revenues. In order to "ensure that provincial governments have sufficient revenues to provide reasonably comparable levels of public services at reasonably comparable levels of taxation" as is set out in section 36(2) of the Constitution Act of 1982.

Nothing in the changes suggested by the federal government shows understanding or a will to find a solution to the fiscal imbalance. No federal proposal improves the standard which is meant to be the crucial parameter of equalization. The fiscal capacity of each province is based on that comparative standard and that is why it must be precise. Presently, the standard is based on the data taken from five provinces; Quebec, Ontario, Manitoba, Saskatchewan and British-Columbia. Seeking fairness would mean broadening that calculation base to include the 10 provinces and that was the standard in place between 1967 and 1982.

Using the five-province standard creates distortions incompatible with our Constitution. For example, according to that standard, 95 per cent of hydro power revenues are included while only 21 per cent of oil revenues are included. That is determined by the mix of provinces included in the standard.

Using the five-province standard instead of the ten-province standard costs \$297 to each citizen and that imposes an additional tax burden on Quebec to the tune of over \$2 billion per year.

The other bone of contention is the tax base. The federal government applies a method based on several concepts that comes out of nowhere and is recognized by no other government. Usually, one applies the residential market place standard. The federal government recognized the deficiency but is still delaying the use of the residential marketplace value to 2009 and is suggesting the 50-50 formula until then. Quebec will thus be deprived of \$2 billion over the next five years.

Another change is necessary: the equalization program must cover all provincial revenues and not, as is the case now, take into account only 50 per cent of sales of goods and services. This deficiency will have cost \$144 million in 2004-2005.

The implementation of the measures proposed by Quebec will require the federal government disburse \$5.2 billion more for the year 2004 in order to improve the revenues of all the beneficiary provinces. If these serious problems which are detrimental to the majority of provinces were to be solved, Quebec would receive an extra \$15.7 billion over the next five years instead of the \$1.7 billion proposed by the federal government's reform.

• (1100)

Even though the \$5.2 billion amount may seem major, we must keep in mind the conservatism of the federal government's estimates.

Indeed, the federal government, since 1997, has been forecasting a balanced budget, whereas the final results set out in the public accounts always reveal very major surpluses. Thus, from 1997 to 2004, the federal government had forecast, for the overall period, an operating deficit of some \$17 billion, while in reality, it had a surplus of over \$54 billion. The fact that the federal government hides its surpluses from year to year has become an open secret.

During that time, what has been happening with provincial finances is exactly the opposite. "*Finance Advisory, The Secret Deficit, The Real Figures, Confusion in the Finance Department, Who is Telling the Truth?, Seeing Things Clearly, No Zero Deficit for Two Years.*" Those are a few titles taken from editorialists and columnists who, during the last year, have been denouncing the trickery, the secretiveness, the Quebec government's creative accounting.

The last Quebec elections clearly revealed to us, once again, the difficulty of presenting a clear and detailed picture of the public accounts to the taxpayers. The saga of the false zero deficit, the increase in the debt load despite the theoretically balanced books, the waltz of debits and credits around the accounting perimeter and the virtual tax decreases are just so many sour notes that increase the population's suspicion of politicians.

Indeed, during the last three years, a similar lack of trust was expressed in the financial leaders of major private businesses because some of them had played fast and loose with the books and betrayed the trust of their shareholders. Following investigations, some major business barons were found guilty of fraud and are now involved in a detailed counting of their days in jail. Finally, strict reforms were implemented in order to increase truthfulness and transparency in the disclosure of accounts.

At Action démocratique du Québec, we believe the time has come to make a clean sweep in order to re-establish taxpayers' trust in our public accounts, and we feel ready to make it harder to indulge in the creative of accounting that has marred public finances.

But why, first of all, should we put so much emphasis on the truthfulness and transparency of public accounts? Because the coming years will force us, as a community, to make logical and difficult choices. The leaders are suggesting policies concerning the debt, health, investments in our infrastructure and others areas. Should we do this on a credible and objective financial basis if we wish to inform the population and get its consent? Putting Quebec's economy on a sound footing becomes more likely if we can count on the informed consent of the taxpayer. Eventually, a better awareness of our real financial situation would help to put the brakes on the demands made by multiple lobbying and pressure groups.

Our party has thus proposed that we should come up with a more adequate definition of what the accounting perimeter should be. For example, Quebec's auditor general, for some time now, has been recommending the inclusion of pension fund actuarial deficits, hospital deficits as well as the amounts required to rebuild our infrastructure. Once these parameters have been properly established, they should be further stabilized in order to facilitate periodical examinations and comparisons.

We also propose including forecasting in the role of Quebec's auditor general and creating a Quebec forecasting bureau. The new mandate would be to offer to elected officials and especially to all citizens, non-partisan, comparable and honest economic and budgetary analyses. This would include demographic forecasting, forecasts on the evolution of program costs as well as those concerning infrastructure rehabilitation.

Let us hope that besides making it more difficult to put up the budgetary smoke screens we have been witnessing, a real picture of Quebec's financial situation will make it embarrassing to resort to the wait-and-see policies and the ad hoc practices that our governments have been using in lieu of proper policies for way too long.

• (1105)

In any case, our wish to anchor our policies in a long-term perspective will be substantiated. We sincerely believe that the same transparency and the same honesty should guide the federal government's public finances.

Mr. Mario Dumont: I would like to come back to the question of health and social programs which are at the heart of the debate. If the existence of a forecasting bureau in Ottawa would lead to a better framework in order to know what the real surplus is, what the real financial situation is, the fact still remains that within the context, there are matters which, taken in isolation, do have a particular impact. Health is the one we notice most because of the aging of our population and the increase in costs which, as we already know, will be major.

The federal and Quebec governments have heaped a lot of praise on the merits of last fall's federal-provincial agreement on health funding in Canada. However, if we look at the situation as a whole over the long term, there is not so much to rejoice about. When the public health system was set up in the early 1960s, the federal government made a commitment to provide 50 per cent of the funds to this new government monopoly through the Canada Health and Social Transfer, leaving it up to the provinces to fund the remaining 50 per cent.

Now, this commitment was never fully met. With the new agreement, the federal government's share could go as high as 25 per cent, which would be practically the same level as 1984, after reaching a low of 11 per cent in 1998. However, if there is one thing that has increased consistently on the federal side, and far beyond the initial commitments, it has to be the controls and interference in the health sector, which is an exclusive provincial jurisdiction. Even as late as December 2003, when everyone was protesting in Quebec, the federal government set up the Health Council of Canada to oversee the provinces in the area of service delivery. Since 1984, the federal government has even been threatening to decrease federal transfers to any province departing from the Canada Health Act. One of the main provisions of that act is to prevent any province wishing to do so from adding the private sector's contribution to health, otherwise the federal government threatens cutting its own meagre contribution.

In the ADQ's opinion, the role of any government should be to offer better services and make available better services at better costs to the public, and not try to police the provinces to prevent sick people from having access to health care. The ADQ believes the time

has come to increase the care offered through a mixed public/private health system.

My goal today is not to convince you but to ask you to put a halt to Ottawa's dogmatic approach and let the population of Quebec as well as the other provinces decide whether they want to put an end to the government health monopoly.

During the next Quebec election, we are going to put it to the population; the party I have the honour of leading will suggest adding the private sector to the health care system. Recent public opinion polls show that over 70 per cent of Quebecers are in favour of those measures.

I do not very often have the opportunity of meeting elected members of all federal political parties at the same table. I will thus take this opportunity to reverse the role of the committee and ask you to answer a very simple question, speaking for each one of your parties.

Even though you are against a public/private mixed health care system, as most have already said many times, if Quebec voters were to vote in a government proposing that kind of change in the health sector, will you respect the democratic choice made by Quebec and allow us to undertake reforms or will you fight to preserve total and complete adherence to the Canada Health Act and thus deny the right of Quebecers to reform their health system?

This question is important and it is directly linked to the question of fiscal imbalance. The federal government cannot dictate the rules in matters of health while leaving it up to the provinces to fund the major part of the expenditures in that sector where expenses are steadily growing. First, under the Constitution, health is a provincial jurisdiction. Then, the federal government is funding only a small part of health expenditures and, ultimately, each provincial government is accountable to its own population for its health system. The population of each province is actually paying the government of each province to have access to health care.

To solve the budgetary dead end that all of the provinces are dealing with in matters of health care, what is needed is a direct transfer of tax points and a unilateral withdrawal from the Canada Health Act.

As for research and development, there is an area where, in our opinion, there is another kind of fiscal imbalance that is mentioned less often but which, for us, is central. Since we are talking about unfair treatment of Quebec by the federal government, I think we must bring up the issue of federal expenditures and their distribution in the area of research and development.

I will use a concrete and very current example for you. After many years of debate and dithering, Quebec finally decided to set up a leading edge medical research centre. The cost for this Centre hospitalier de l'Université de Montréal, CHUM, has been estimated at some \$1 billion.

●(1110)

At this point, the Quebec government is expecting a \$100 million federal contribution. Now, the federal government has been systematically under-investing year after year in Quebec in this strategic field. Ottawa has invested \$49 per person per year in Quebec compared to \$108 in Ontario. The federal share represents less than 40 per cent of public funding for research and development in Quebec as compared to 80 per cent for Ontario.

Another eloquent fact in this matter: Quebec has only 17 of the 122 federal research centres, in other words less than 15 per cent. In the federal capital region alone, Ottawa-Gatineau, only one of the 31 federal research centres is located on this side of the Ottawa river.

This is also an imbalance that should be of concern to us. What Quebec needs to ensure its economic development is not just transfer payments because we are poorer than our neighbours, but also quality investments in leading areas at the same level and for the same amount per capita as our Ontario neighbours. We need such structuring investments.

I will conclude by quoting the former minister of finance of Quebec, Mr. Yves Séguin, who was quite the expert in the area of fiscal imbalance. In the latest Quebec budget, he said:

[...] It is clear that the only sustainable solution to the problem of fiscal imbalance is to come to a new sharing of the tax base between the federal government and the provinces [...]. It is clear, for Quebec, that only that solution would finally end the discussions that have been ongoing for decades concerning the funding of social programs.

So I would ask you to make sure that our respective successors will not be here again many years from now to discuss the problem of fiscal imbalance. There is a holistic and long-term solution to the problem and that is the transfer of tax points.

To conclude my conclusion, I would like to point out that at a time when we are finding out the extent of the horror story stemming from a federal government attempt to buy Quebec public opinion through sponsorship and publicity, which then translated into a financial scandal, all federal MPs are now being called upon to settle our problems. The best way to promote Canada is not by leading friends at the advertising agency to the trough, but rather by settling problems and making sure the system works better. Quebec citizens, just like all the other people in Canada, are competent people who are able to understand that a system that works better is the best publicity.

The Chair: Thank you, Mr. Dumont.

We will proceed with our first round of questioning.

Ms. Ambrose, from the Conservative Party, you have five minutes.

Ms. Rona Ambrose: Thank you, Mr. Chairman.

Thank you, Messrs. Dumont and Picard, for your presentation. You have raised interesting points. Fiscal imbalance is a question that concerns me very much. It is a question that I raise in the House of Commons whenever I have the opportunity.

The Conservative Party, through its leader, Stephen Harper, has pointed out that the widening gap between the federal budget and the provincial ones prevents the latter from making long-term plans and

forces them to always be dependent on transfers to provinces to fund their programs.

It is important for you to know that my party also understands that this dependence on federal transfers allows the Liberal federal government to intrude in an area of provincial jurisdiction. That is why, during our convention in Montreal, the Conservative delegates adopted a motion that reads as follows:

[...] that a Conservative government will settle, jointly with the provinces, the fiscal imbalance problem by increasing the amounts allocated for transfers to provinces, by decreasing the tax burden or by transferring tax points to provinces.

My question is for Mr. Picard and also Mr. Dumont. Could you give us more detail on this idea of a Quebec forecasting bureau?

●(1115)

Mr. Mario Dumont: Firstly, by the sound of the first part of your comments, you seem to be well aware that the people of Quebec want federal parties to take this type of approach. I believe that people do not expect the fiscal imbalance to disappear tomorrow. Nonetheless, they do expect the federal government to set aside the imperialistic approach under which the federal government is the sole decision-maker. It is the federal government that holds federal-provincial meetings and decides on the agenda. The meat of the matter is dealt with unilaterally.

We want a federal government that works towards resolution, as you mentioned, that works towards partnership with the provinces. We should try to work together in order to resolve problems which, ultimately, are those of the citizens. Indeed, it is always fundamentally about citizens, who pay for and receive services, and who want to see their government working in this direction.

I believe that we also expect greater respect for the Canadian Constitution. It appears simplistic, but Quebecers are truly tired, exhausted each time a federal budget is tabled, to hear threats of new intrusions into provincial jurisdictions, of more duplication. I believe that things would be much better if the wording of the Canadian Constitution were respected, if the federal government minded its own affairs honestly and left the provinces to take care of their own. All of this would take place in the context of restoring a fiscal balance, wherein financial pressures and needs would be in better balance with the governments' fiscal capacities.

With respect to the forecasting office, we believe that this idea is good for Quebec. We all know the tune: at the beginning of a new government's mandate, the new administration always says that the previous government left an unexpectedly bad unpredictable financial situation in its wake and that, for this reason, the current government cannot maintain its commitments. We are a little bit sick of that. Obviously, citizens have become very cynical. We believe that the auditor general should be able to turn to this forecasting office, to make sure that the government cannot tinker with its own accounting, cannot decide to exclude public agencies from standard accounting practices and scruting when they run deficits, and reintegrate them when they have surpluses.

We could not appear before you to make this presentation without referring to the fact that at the federal level, there seems to be a king of game going on where the federal government's budget surpluses are underestimated. The federal government meets with the provinces, negotiates on the basis of certain figures, and three weeks following the end of the meeting, announces a federal surplus of several billion dollars more than what was discussed during the meeting with the premiers of the 10 provinces.

There is something unhealthy in all of this. Voters are sick of that. If, at least, we had a reliable forecasting office responsible for presenting a true statement of public finances and of the surpluses that could reasonably be expected, then, in our opinion, that would facilitate subsequent discussions, as Mr. Picard explained to us earlier.

Ms. Rona Ambrose: Thank you.

The Chair: For your information, Mr. Dumont, during the month of February, opposition parties set up a new exercise. All parties choose four independent economists who are not connected to government. Twice during the month of February, these economists appeared before us to talk about quarterly revenue, expenditure and surplus forecasts. We are looking to creation of a permanent office for budgetary forecasts.

Mr. Mario Dumont: Take our comment as an encouragement.

The Chair: Mr. Bell, go ahead.

[English]

Mr. Don Bell: Thank you.

The Chair: You will share your time with Ms. Folco.

Mr. Don Bell: Yes, that's right.

Messrs. Dumont and Picard, you made reference to the political change. You were talking about the need for, provincially, this provisional office. I gather you therefore accept that political parties change, or governments can change by party, and that one party or one government can inherit, in other words, the policies or debts of a previous party, as was the case in 1994, when the Liberal government came to power and picked up the growing deficit that had been there from the Conservative government.

Do you agree that a priority of the federal government should be to reduce the national debt? In all governments, I presume...you know, if you personally have a mortgage, you want to reduce it, if you have a chance, for extra money.

Second, there have been tax cuts by provinces across Canada. At the same time, there have been complaints or suggestions that the federal government should transfer more tax credits to those same provinces. Since there is political independence, if you want to call it, between the two levels, where each government is responsible for its level.... I know there's one taxpayer who pays it, but each government politically is responsible for the level of taxation it gives to provide the services it feels are necessary, within its area of responsibility.

I give you those two questions to respond to.

• (1120)

[Translation]

The Chair: Mr. Dumont.

Mr. Mario Dumont: On the issue of the debt, there should be a debt repayment plan. The list of federal Liberal Party policies which I endorse is not lengthy, but I have always supported that one. It's one of the only ones. I can say it again today.

That being said, as far as I'm concerned, having a debt repayment plan means imposing budgetary discipline to plan for the future. That does not mean you can see debt repayment as an elastic band to be played with 11 months a year, which prevents you from sitting down with the provinces to discuss other problems because you're keeping some sort of surprise for year-end. In that respect, the idea of having a forecasting office makes sense. It would not stop a government from setting up its budget priorities. Instead of acting like a jack-in-the-box at the end of the year and dealing with debt repayment then, it could be stated at the beginning of the year that based on the Canadian government's decisions, some funds would be earmarked for debt repayment to fund past mistakes. That is one thing.

With respect to the leeway the provincial governments have to reduce taxes, you can never stop governments, be they federal or provincial, from working with taxation. Nonetheless, every study on fiscal imbalance has amply demonstrated that there is upward pressure on social spending. Obviously, in principle, health care spending, because of an aging population, does mean more pressure, but not for the federal government. Indeed, no federal department faces the same radical pressure provinces face for external demographic reasons. This is why the federal government has year after year been running a surplus that is greater than its forecasts. Besides, all provinces, save one which is deriving revenue from its oil sales, are facing a difficult situation when it comes to balancing the books.

When the Conference Board, basing itself on provincial and federal government budgetary realities, made projections, it concluded that, all things being equal, if we were to keep to the current course—and this isn't a provincial lobby group: it is clearly an independent organization—the federal government would end up with an extremely high surplus, but not the provinces. On the contrary, they would be running annual deficits.

The Chair: Ms. Folco, you have two minutes, go ahead.

Ms. Raymonde Folco: Mr. Dumont, Mr. Picard, thank you for your presentations.

Before I ask you a question, I simply want to remind you of the powers of the government of Quebec. As a provincial government it can determine its own tax policies, personal and corporate tax rates, and the way in which it wants to use its tax revenue.

I have a chart here according to which if you factor in federal government support for provincial social programs, for over 20 years, the provinces and territories have had total revenues—i.e. independent revenue, federal cash transfers, etc.—that are far superior to those of the federal government. And the assumption is that this gap will continue to grow. According to the figures, for 2005-2006, support for Quebec in the form of the major transfers amounts to \$15.6 billion, or \$2,052 per person.

So these figures do not exactly match those you've just referred to, Mr. Picard, from what I understand. I would like you to react to this comment, Mr. Picard or Mr. Dumont.

• (1125)

The Chair: Mr. Picard or Mr. Dumont.

Mr. Mario Dumont: I'm having a hard time answering your question, because I don't have the chart before me, nor do I know the origin of the figures in it. To my knowledge, the transfers you're describing are not those I'm used to seeing in Quebec budget statements, nor in the most optimistic forecasts made according to the fiscal framework the Liberals referred to during the electoral campaign. Despite their optimism when it came to the collaboration they could expect from the federal government, even they couldn't arrive at such figures. I don't know these figures by heart, but at best, they certainly would not amount to \$15 billion.

As I was saying in answer to the previous question, the splitting of tax revenue between governments must be directly linked to the issue of future spending pressures. At one point, the federal government said that it was going to fund 50 per cent of health care costs. At the time, demographics were in our favour: for each hospitalized senior, there were seven or eight other people to bear the costs. We are moving from a one-to-seven ratio to a one-to-two ratio; that is what the future looks like.

Given these facts, it is obvious there will be enormous financial pressure on those responsible for delivering health care on a daily basis and for dealing with people coming into emergency wards, in other words the provinces. The pressure is already huge and it will increase. In the meantime, the federal government's share has considerably fallen from 50 per cent; it is now far less.

In my opinion, what exacerbates the problem, and I've already referred to it, is the fact that the federal government is not loosening the rules. It is no longer providing the funding, but it won't back down from the ideology according to which there should be no private sector involvement in health care. It threatens the provinces, saying that if ever they were to allow private clinics, it would penalize them by reducing transfer payments. So we now have a federal government that endorses an ideological framework that is stalling progress in the area of service delivery, but which doesn't have the money to fund everything.

The Chair: Thank you, Mr. Dumont.

Mr. Côté, you have five minutes, go ahead.

Mr. Guy Côté: Thank you very much, Mr. Chairman.

Thank you Mr. Dumont, Mr. Picard, for your presentations.

Before I move on to the heart of the matter, I simply want to mention that it is perhaps, not scandalous—that would be too harsh a word—but really unfortunate to hear what Ms. Folco has to say. Even today, she is giving us an eloquent demonstration of the Liberal government's arrogance by denying something which is recognized by all political parties in Quebec, by all parties represented in Ottawa and by groups as diverse as the Conference Board of Canada and labour organizations. Only one party seems to know the truth here, and that's the Liberal Party of Canada. But here, we simply don't subscribe to your version of reality.

That being said, on the issue of...

Ms. Raymonde Folco: You're grandstanding for the cameras, Mr. Côté.

Mr. Guy Côté: That's what you think, Ms. Folco; I don't mind.

The Chair: Please, Ms. Folco, up until now, things have gone rather well during the tour, people have been civilized.

Ms. Raymonde Folco: This gentleman spoke to me, I feel it is my duty to respond.

The Chair: You should not take these things personally, Ms. Folco.

Ms. Raymonde Folco: In that case, nor should people make personal remarks, Mr. Chair.

The Chair: Order, please.

Go ahead, Mr. Côté.

Mr. Guy Côté: That being said, Mr. Dumont, there was talk of creating a Quebec forecasting office. Further to what the chair said earlier, I simply wanted to mention that following two studies carried out by the Standing Committee on Finance, and a mere six weeks after the tabling of the federal budget, forecasters are in agreement that federal surpluses will far exceed the amount indicated in the budget.

You disagree with the current Quebec government on several issues; that is only to be expected. However, in your presentations, you both mentioned that, over the past 30 years, the federal government has made draconian cuts to transfer payments, has taken unilateral decisions to reduce funding, has undertaken piecemeal changes, and has entered into individual agreements. Increasingly, we are faced with a lack of transparency and accountability in a way in which the federal government manages public finance.

I am inclined to ask you the same question that I asked of Minister Pelletier earlier. I would put it to you that your observations today are tantamount to recognizing the impossibility of fully overhauling the equalization and federal transfer system, as well as the impossibility of finding a solution to fiscal imbalance. At the end of the day, are you not making the observation that this is impossible to deal with?

• (1130)

Mr. Mario Dumont: Your opening comments were political in nature. Over the course of the past 30 or 40 years, in Quebec, as elsewhere in Canada, the approach has been one of conflict and confrontation: one side clamoured for endless referendums, the other introduced the Clarity bill.

I believe that these conflicts have done Quebecers a disservice. Today, people feel that this confrontation, which stems from different opinions and two separate visions of Canada, has become stale and mired in, among others, financial scandals. People expect their elected representatives, both in Ottawa and in Quebec, to propose solutions to problems. Today, Quebecers want concrete solutions for their real problems, problems which could be better resolved were we simply prepared to respect the 1867 British North America Act. People are not interested in an ideological struggle like the one that has been going on for the past 30 years, and which has led to two referendums,

Our party has always expressed its willingness to work with whichever party is in power in Ottawa, on the proviso that it be in the spirit of improving the system and solving problems. This liberal federal government has chosen the path of denial. It has denied the existence of problems, denied what it said, and through all the time that it was denying real problems, it was trying to buy public opinion with symbols and advertising campaigns. In short, it was using smoke and mirrors. Obviously, the general public has no time for such an attitude. People want their elected representatives to solve problems; to name problems, to deal with them in a coherent manner, and to find solutions.

The Chair: Thank you, Mr. Dumont.

Thank you, Mr. Côté.

Ms. Wasylycia-Leis, you have five minutes.

Ms. Judy Wasylycia-Leis: Thank you, Mr. Chair, and thank you to Mr. Picard and Mr. Dumont.

My first question concerns equalization. Does your party, the Action démocratique du Québec, accept the principle of an equalization program?

Mr. Mario Dumont: Yes.

Ms. Judy Wasylycia-Leis: Here is the reason for my question: it seems to me that there is a contradiction between your support for an equalization program and your position on our health care system. In fact, both programs are based on the same principles of equality and justice. I would like to know how you explain your support for the principle of equalization and your support for a private health care system, a two tiers system.

[English]

Mr. Mario Dumont: Hundreds of tiers.

Ms. Judy Wasylycia-Leis: Hundreds of tiers. Okay.

Mr. Mario Dumont: That's already what exists.

[Translation]

Ms. Judy Wasylycia-Leis: How do you explain these two positions?

Mr. Mario Dumont: First of all, I feel that the concept of an equalization program exists for a very good reason. In a country like Canada, where there is a diversity of regions and of natural resources, over the decades, a region can experience a great economic boom. Afterwards, the resource is exhausted and another region may experience growth. Over the years and decades, the provinces that find themselves in a better financial situation will support the fiscal capacity of the others. From this comes the idea of

the sharing of wealth in order to give each of the provinces the means to ensure a certain number of services for their citizens and to guarantee the government of each of the provinces a minimal fiscal capacity. In my opinion, this has nothing to do with how a province organizes itself to offer the best possible services, given its financial means.

To get back to the issue of health care, I believe in the importance and the existence of a public and universal system offered by the provinces. For me, that is basic. There are three countries in the world where paying for health care is prohibited: Cuba, North Korea and Canada. If we withdrew Canada from this list, I would not be overly sad. This is where the system goes too far. Maintaining a public system that is as efficient as possible and funding it properly represent a very significant social challenge. However, I think that it is going too far to prohibit a certain number of people from using private clinical services because that goes against the ideology.

Having said that, I do not wish to impose this on the other provinces, but some provincial governments seem to be heading in that direction. This is being discussed in Quebec, Alberta, British Columbia and in Nova Scotia, where the premier is a doctor. In the provinces that want to be more original and innovative, and have a more dynamic health care system that leaves room for the private sector, I don't think that should be banned. I do not think that prevents tax fairness between the provinces. In my opinion, they are two different issues.

• (1135)

The Chair: Ms. Wasylycia-Leis, you have a minute and a half left.

Ms. Judy Wasylycia-Leis: Thank you for your answer. In any case, it seems to me that there truly is a contradiction between your acceptance of equalization and your support for a private health care system.

If you look at the Constitution, it's clear that we have to accept the idea.

[English]

—I'd better go to English for a minute—that you take, in effect, from those who have, for those who have not, to ensure equality of access.

Mr. Mario Dumont: That's equalization.

Ms. Judy Wasylycia-Leis: Yes. But the same principle exists in terms of our universal public health care system. It's to ensure that you've got the same access to the system regardless of your level of income. All the studies in the world show that when you move towards the kind of system you're advocating, you lose that element of universality and access regardless of income.

So I think it's really hard for us to understand the position of your party in this broad context of fiscal imbalance, because there is such a contradiction in your position.

[Translation]

Mr. Mario Dumont: I see no contradiction at all. I think all provinces can share the wealth over an extended period of time.

In fact, the issues that have been raised about the health sector have not been raised for the education sector, for example, where most provinces allow a mixed system, a public system and a private system. Nobody is raising these same issues in the education sector.

It is quite obvious that a huge myth has been created around Canada's health system. My goal is still that of a public and universal system. That is very important to me and I will never sacrifice that. However, I think that prohibiting people from obtaining care is going much too far. That is another debate but it is part of the fiscal imbalance debate.

In terms of equalization, given your interest in this, I will tell you that our party supports it. We go even further. In fact, we are the only party in Quebec that has officially stated that it wants Quebec to become a contributor, to put money in the pot. We are the only party in Quebec talking about that. We want to kickstart Quebec's economy, craft a more aggressive fiscal policy and a structured economic development policy. We think that if Quebec has better strategies, if it develops its hydroelectric capacity and the resources that it should have, then it will be able to put money into the equalization pot. We would be happy to do that.

The Chair: Thank you, Ms. Wasylcia-Leis.

Mr. Dumont, in anticipation of those happy days, I thank you for your excellent presentation. I would also like to thank you, Mr. Picard. Thank you for having contributed to the committee's work.

Mr. Mario Dumont: Thank you to all the committee members.

The Chair: We will break for 10 minutes.

• (1139) _____ (Pause) _____

• (1155)

The Chair: We will now resume our meeting.

I would like to welcome Mr. Laurent Pellerin, president of the Union des producteurs agricoles du Québec, and Mr. Serge Lebeau, research director.

You have 15 minutes to make your statement. We will then move on to a round of questions and comments from the members of each political party. That will also be an opportunity for you to expand on any points in your presentation.

We have a mandate to table a report in the House of Commons by June 2nd. That is the order that we received from the House of Commons. That report will contain recommendations on how to provide sustainable solutions to the problem of fiscal imbalance.

Mr. Pellerin, you have the floor.

Mr. Laurent Pellerin (President, Union des Producteurs Agricoles du Québec): Good morning, Mr. Chairman, members of the committee.

I believe everyone is somewhat familiar with the Union des producteurs agricoles. Our organization represents approximately 45,000 agricultural producers in Quebec.

This morning, we could speak extensively about the situation in agriculture. However, that is not today's topic. Despite that, the numbers that we will be showing you today are a clear illustration of

the current situation in the Canadian agricultural sector and of the links that can be made between that situation and the fiscal imbalance.

I am accompanied by Serge Lebeau, an economist working with the Union des producteurs agricoles. He will be reading the statement that you have before you. You have the French version. I believe that with the tables that we have included in this brief, it will be quite easy to follow, even for those who speak English.

During the second part of the meeting, I will be happy to answer any questions you may have or to expand on Serge's points.

The Chair: Mr. Lebeau.

Mr. Serge Lebeau (Senior International Trade Advisor and Assistant Director, Agricultural Studies and Policies Department, Union des producteurs agricoles du Québec): Thank you, Mr. Pellerin.

Mr. Chairman, ladies and gentlemen members of the subcommittee, I will begin by giving you an outline of my presentation today.

You'll find the outline on the third page of my brief. I will follow it almost to the letter. Some changes were made because we found a few small errors. We apologize for that but we have corrected all of them.

In today's presentation we will mainly use our time to cover two areas: first, the context within which our sector has been evolving, that is to say the fact that since the beginning of this millennium it has been dealing with one of the worst revenue crises in history; then we will speak to the theme of these hearings, that is the fiscal imbalance, by defining it, by demonstrating that it is a very real issue in agriculture, and by describing its impact.

Let me first spend a few minutes on the issue of farm income for Canadian and Quebec producers.

You probably know, as the graph shows, that the Canadian agricultural sector is going through its worst ever crisis. For example, net income for the agricultural sector in Quebec went down by more than 50 per cent between 2001 and 2002. You can also see that for the past 20 years, despite farms getting bigger, net income has not increased, the trend has even decreased.

Figure 2 shows that net farm income in Canada for 2003 was negative for the first time in history. In other words we are not at a very dramatic crossroads.

Now let me speak about fiscal imbalance. From our point of view, there is fiscal imbalance when provinces do not have enough income to meet their responsibilities within their specific jurisdictions and when, on the contrary, the federal government has a surplus compared to what it needs in order to finance its own areas of activity. It is quite obvious that one needn't look to agriculture for the source or origin of the problem.

We will briefly be speaking about the consequences of fiscal imbalance on the agricultural sector.

Overall, we feel that the problem lies in the fact that the federal government, which, in passing, has a fiscal surplus, appears to be more and more unclear on the role it should be playing in the agricultural sector, specifically in how to assist Canadian producers in competing with other countries on a level-playing field.

This unawareness of its role with respect to the agricultural sector is based on the figures shown in figure 3 on table 1.

Figure 3 shows that between the years 1990 and 2000, federal support expenditures for the agricultural sector were split in two, not counting the year 2004-2005, the year of the BSE crisis.

Table 1 shows in relative terms that the percentage of the federal government allocated to the agricultural and agri-food industry went from 4 per cent in 1991-1992 to less than 2 per cent in 2005-2006. Obviously the numbers for 2005-2006 are preliminary numbers.

When the OECD measures support that countries provide to their agricultural sectors, it evaluates total assistance to the agricultural sector in American dollars per capita. From that indicator, support for market prices is subtracted—that's what you see, for example, in the dairy sector—as well as assistance which is not a direct subsidy.

An analysis of table 2 shows us the following. Canada provided \$124 in support per capita in 2002, which is a little less than half of the \$263 that the United States provided and less than the amounts spent by the European Union and Japan. Over a period of more than 15 years, support to agriculture per capita dropped 25 per cent in Canada, while it increased by 75 per cent in the European Union, 31 per cent in the United States and 14 per cent in Japan.

As we saw earlier, Canada had to increase its support to the agricultural sector in 2002 in order to buffer the 51 per cent drop in net income for Canadian producers.

An analysis of this table gives us the following trends. In the long run, total net income in this country will go down, whereas it will go up in the United States. More specifically, Canada is suffering an annual structural loss of Can.\$117 million, whereas our neighbours are seeing an increase of U.S.\$ 881 million.

Since 1980, the largest gap between Canadian and American total net income was between 2004 and 2005. This is due, in part, to the BSE crisis in Canada and, on the American side, by record subsidies to the grain sector, a protectionist policy restricting access to their markets, as well as the deployment of their export energy strategy.

• (1200)

Table 4 is a bit complicated but I will try to summarize it as simply as possible.

This table shows us an overall decrease in public expenditures since 1994, the first year of the fiscal imbalance. For Canada as a whole, the federal government put back 18.2 per cent of agricultural cash receipts into public expenditures supporting the agri-food sector. That is the average for the ten-year period from 1984 to 1994. This contribution dropped to 10.6 per cent for the ten-year period from 1994 to 2004.

The provinces' contributions, for their part, were 11.2 per cent for the first ten years and 7.9 per cent for the second ten-year period. The decrease in public expenditure was felt more strongly on the

federal side. Actually, its expenditures decreased by 42 per cent while provincial expenditures decreased by 29 per cent for the periods under observation.

This situation is reflected in the provincial share of total expenditures used to subsidize provincial agriculture. This share went from 38 per cent to 43 per cent as the provinces had to compensate for the federal withdrawal and still offer first-line services.

The fiscal imbalance certainly has something to do in this picture.

However, despite the federal government's defection, it has been interfering more and more in provincial affairs. The agricultural policy framework is a good example of that practice. However, despite the increase in provincial contributions to public expenditures since 1994, the provinces have been having more and more problems in shouldering their share which is the famous 60/40 ratio. Anytime there is a federal intervention, the provinces have more and more problems to follow. The best example we can give you is the last billion-dollar contribution paid two weeks ago. No province said that it would follow and provide its 40 per cent share. So it is becoming more and more difficult for the provinces to follow the federal government in the area of subsidies to the agricultural sector.

As shown by the aforementioned data, the Canadian agricultural sector gets only about half the support they get in the USA. Will Canadian producers be able to sustain such unequal competition? The answer is self-evident: no. It is not surprising that we just go from crisis to crisis in the field of agricultural income.

The solution is to be found in the implementation of real developmental and flexible programs for greater adaptability to the special features of each province. The way to achieve that has been brought to the attention of the authorities many a time by this country's various agricultural organizations but to no avail.

Agriculture is an area where jurisdiction is shared between the provincial and federal governments. That is why the latter could easily increase its share of expenditures to the provinces while giving them the flexibility they are asking for to ensure the management of the funds.

It has also been proven that programs which are properly adapted to agricultural realities cost the government less than ad hoc solutions to crisis situations.

In conclusion, the decrease in State support for agriculture is first and foremost the result of an ill-informed understanding of the primary importance of that area in a nation's activities, even more so as the federal government has huge financial leeway available thanks to accumulated surpluses due to fiscal imbalance.

The UPA is of the opinion that the present situation is not only detrimental to the development of the industry, but that it also threatens its future. Indeed, the numerous benefits flowing from a prosperous and profitable agricultural sector are essential for any country. To ignore its importance is due to ignorance, pure and simple. Very quickly, just to give a few examples, we could emphasize a country's ability to feed its population independent of foreign diktats for its food basics; upstream and downstream economic activity due to agriculture; the whole economy surrounding the agrifood industry which is dependent on agriculture; the hundreds of thousands of jobs depending on those activities; the occupation of a country's land base and the maintenance of its landscape; the service industries, and I will just leave it at that.

Mr. Chairman, those are the thoughts of the Union des producteurs agricoles. We hope they will serve as an inspiration.

We thank you for listening.

• (1205)

The Chair: Thank you very much, Mr. Lebeau.

We will now proceed with a questions and comments period.

Ms. Ambrose, you have five minutes.

Ms. Rona Ambrose: Thank you, Mr. Chair.

Thank you, Mr. Pellerin and Mr. Lebeau. I appreciated your presentations. I found them very interesting.

The Conservative Party of Canada and my leader, Stephen Harper, have recognized the existence of a vertical fiscal imbalance between the federal government and the provinces for some time now. I know that the fiscal imbalance is the result of federal government policy. The federal government collects more taxes than it requires to meet its needs. This has led to recurring federal government surpluses and provincial deficits.

It is important for you to know that during a recent convention in Montreal, delegates passed the motion stipulating that a conservative government would, together with the provinces, correct the fiscal imbalance by increasing transfer payments to the provinces, reducing the tax burden or transferring tax points.

Mr. Lebeau, what else should the federal government do to address the problem your industry is facing?

Mr. Serge Lebeau: With your permission, I will let the president of the Union des producteurs agricoles du Québec answer that question.

Ms. Rona Ambrose: Thank you.

Mr. Laurent Pellerin: I remind you that agriculture is an area of jurisdiction shared between the federal and provincial governments. What can the federal government do to change the situation? First, the federal government needs to follow what is happening with our main competitor, the United States.

The farmers' job is to compete with the best farmers in the world, especially the Americans. It is an acknowledge fact in Canada that Canadian farmers are able to reach the best standards. Furthermore, we have no trouble competing with our American neighbours.

We want our revenue to come from the market, but unfortunately, because we are neighbours to the United States, we realize that on the other side of the border, market-source revenues are not substantial. We are looking closely at the American government's level of agriculture subsidies. They create a distortion in commodity prices at the farm in Canada. This is an untenable situation for Canadian farmers. The federal government needs to start by acknowledging this distortion, by measuring its impact and then by correcting the problem.

Just from a grain standpoint, Agriculture and Agrifood Canada has concluded that the impact of American subsidies in terms of the drop in grain prices in the North America totals \$25 per metric tonne. Overall, this means an approximate loss of \$1.2 billion annually for Canadian producers.

Our government has acknowledged that American subsidies have had an impact; and the government has measured it. The problem is that it has not done anything to actually fix it.

Producers have no power in this respect and no recourse in order to improve the situation. They just continue to do their work on their farms as best they can. When the time comes to put their grain on the market, they cannot get an adequate price because American subsidies push the market value down to \$25 per metric tonne.

Either the Canadian Government does what needs to be done to make the United States change its level of subsidization—and this is a challenge that we have faced since 1993 with the WTO—or it should offset the shortfall. Producers can no longer live with the situation.

The last round of WTO negotiations in 1993 did not provide the expected results in terms of lowering subsidies. On the contrary—as you saw in the tables that we presented—, American subsidies have continue to go up and the gap between Canadian farmers' income and that of American farmers has remained the same, and even got wider. The Canadian Government really must act.

The federal government is having trouble taking action and addressing the problem because it wants to act in partnership with the provinces and, increasingly, they are tightening their belts due to the current economic situation in Canada. When it comes to historic solutions being put on the table for agriculture, we seem to be at a dead end.

The federal government needs to bring forward meaningful change in order to correct the fiscal imbalance, so that the provinces have enough flexibility to enable them to do what the federal government either cannot or will not do.

• (1210)

The Chair: Thank you, Ms. Ambrose.

[English]

Monsieur Bell, five minutes. You can't share your time now.

Mr. Don Bell: No, I have it all now.

Thank you, Messrs. Pellerin and Lebeau. My question follows along Ms. Ambrose's line.

You were saying in your statement, Mr. Lebeau, that this is the worst crisis your sector has had in terms of revenue for the farmers, with a 50% reduction in 2001 and 2002. Or at least I thought I heard 2001 and 2002, but 2003—

Mr. Laurent Pellerin: The worst one was 2003.

Mr. Don Bell: It was the worst.

My understanding is that the primary responsibility for agriculture is federal, and you're talking about the subsidies in the States. They're federal, as I understand it. They're not state subsidies. Is that not correct?

Mr. Laurent Pellerin: The majority of the money in the U.S. comes from the federal government. There is no doubt about that.

Mr. Don Bell: If that's the case, with regard to your reference to Canadian provinces being cash-strapped, and the imbalance, the imbalance doesn't directly affect your sector. You're expecting, I presume, that the support is going to come from the federal government, and the federal government would do that from the resources it would have with whatever surpluses, if there are surpluses. I would think your argument would be that more of those surpluses should be directed to addressing agricultural issues rather than non-agricultural issues, such as paying down the debt or other priorities the government has chosen, which would include fiscal transfers to the provincial governments.

[Translation]

Mr. Laurent Pellerin: Yes. That's an excellent question. Basically, the federal government has a mass of available money, and the provinces also have an amount of available funds. However, the provinces don't have enough to do what they have to do to fulfil their responsibilities, while the federal government enjoys surpluses or non-allocated money in terms of the work that it has to do. Either the federal government will have to take action in shared areas of jurisdiction in order to address what we are asking it to correct, or, it should transfer tax points to the provinces, as Ms. Ambrose mentioned earlier, to enable them to have the flexibility they need to do what the federal government can't or won't do unilaterally.

You made a comparison with what is going on in the United States by saying that given that it's the federal government which contributes primarily there, the federal government should do likewise in Canada. If we were to accept this argument, yes, the federal government could contribute more substantially. It could quite simply bring its contribution level back to what it was between 1985 and 1995. In doing so, it would roughly double its contribution to Canadian agriculture. It would have to be flexible about how it would do this... Agriculture in Canada, from British Columbia to Prince Edward Island, is vastly different. So, it's unrealistic to think that one single federal program could cover all the very different realities that Canadian farmers face from one coast to another.

Fraser Valley, in British Columbia, and the province of Newfoundland are very different when it comes to agriculture. Prince Edward Island has extremely specialized potato production. Alberta is extremely specialized in cattle. When an embargo is placed on beef, you simply can't claim that Newfoundland will be affected. It's mainly Alberta that will be affected as well as the other cattle raising provinces. However, if there were to be an embargo on

potatoes, like there was two years ago, Alberta would not be affected nor would British Columbia, but the maritime provinces would be. So, in my opinion, it would be unwise to think that one single framework for a federal government contribution would be able to make up for these discrepancies.

Besides, in our document, we refer to Canada's Agricultural Policy Framework. However, under the agreement which enabled the development and the implementation of this Policy Framework, which came as a result of a meeting between ministers of Agriculture held in Whitehorse in June 2001, the first couple of paragraphs stipulate that this agreement must be developed in partnership with producers and the provinces—which wasn't the case—and that it must be flexible, to enable provinces to adequately contribute in their particular fields while respecting shared areas of jurisdiction between the federal and provincial governments. The Whitehorse agreement clearly indicated in its first couple of paragraphs what the Agricultural Policy Framework should do to better respect the work of all parties. So if we add our current concern, that is the fiscal responsibilities or the tax room of each level of government, it would have been far better had this framework been developed in partnership and provided the provinces with enough leeway to carry out their responsibilities in their own areas of jurisdiction, which they are currently unable to do. The provinces are hamstrung, while the federal government has financial leeway. So rather than enabling the federal government to properly meet its responsibilities, this additional leeway is enabling it to encroach on areas of jurisdiction that are quite simply not its own.

• (1215)

The Chair: Mr. Côté, you have five minutes.

Mr. Guy Côté: Thank you, Mr. Chairman.

Thank you, Mr. Pellerin and Mr. Lebeau, for your presentations.

Over the course of the morning, several witnesses have spoken about the decrease in transfer payments, the tightening of employment insurance rules, and you have added the decrease in agricultural support over the past 15 years. These are some of the methods that the Liberal government in Ottawa used to eliminate its budget deficit.

Your documents clearly show how the provinces and Quebec increased its support to the agricultural sector over the same period of time. I'm tempted to call this the "trick" that the federal government often uses. It establishes shared-cost programs, it creates needs, especially in the provinces, and then it withdraws from the funding of those programs and leaves it up to the provinces to provide enough funding for the needs that it created. Sometimes it is doing this to meet the provinces' demands, but often the federal government is trying to increase its own visibility and, in so doing, it is encroaching upon provincial jurisdictions.

You showed us quite clearly how the situation in agriculture can vary throughout the provinces, both in terms of the crops and various types of farm animal production and in terms of the specific circumstances of the operations. Without a doubt the federal government has some catching-up to do in agricultural support.

Is this decrease in agricultural support still a part of the federal government's fiscal policies? I'm sure that if we were to put the question to the departments, they would tell us that they are trying to catch up at this very moment. If they were, how long would it take to obtain the same level of support that was provided to agriculture in 1986, for example, the first year in figure 2 of your brief?

• (1220)

Mr. Laurent Pellerin: I am also the first vice-president of the Canadian Federation of Agriculture. We prepared a small assessment of financial needs over the past two years and a forecast for the year 2005. The Standing Committee of Finance met extensively with the Canadian Federation of Agriculture and this study was given to them. We compared the gap between net income over the past three years, including this year—I'm talking about forecasts for this year—and the average net income over the past 10 years. In the table that we showed you, you can see that the 10 last years were not the best in terms of net income for Canadian agricultural producers. We're on a downward slope, no doubt about it. Net income for each of the last three years was \$1.9 billion under the average for the past 10 years. That means that in 2003, we were \$1.9 billion short of the average net income for the past 10 years.

In 2004, we were still \$1.9 billion short and we forecast that for 2005 we will still be short \$1.9 billion compared to the average over the last 10 years, an average which is already very low. That means that over three years, Canadian agriculture, Canadian agriculture producers, are \$5.7 billion short of a net income that is comparable to the average over the past 10 years.

The Chair: Per year?

Mr. Laurent Pellerin: \$1.9 billion per year amounts to \$5.7 billion over the last three years.

The federal government announced an addition of \$1 billion last week. For the funding of Canadian agricultural organizations, \$1 billion is a lot of money. It is good news, but it is only \$1 billion whereas the needs or shortfalls of the last three years represent a total of \$5.7 billion. For 2003 alone, we have a 50 per cent decrease in the net revenue of Canada's farmers. But in terms of net revenue, 2003 is also the worst year of Canada's entire agricultural history. We are talking about a negative net agricultural income for 2003. That means that 250,000 farmers in Canada worked 365 days that year for nil revenue, in other words zero net revenue. It is catastrophic.

We accept lengthy discussions to reach federal provincial agreements; in a shared jurisdiction like agriculture, we asked the provinces to get involved—otherwise, there is no agreement nor any signature—while the provinces are financially paralyzed. That brings us all the way to 2005, even though we have not yet filled the income shortfalls of 2003 and 2004. The federal programs have yet to pay out any cash for 2003 and 2004 because the process you are engaged in with paralyzed partners is an extremely lengthy one. The federal government is forever asking provinces to contribute. As the latter have no money, then there is no agreement unless the federal government decides, as it did a fortnight ago, to proceed unilaterally. In the circumstances, that is probably the quickest way. But you must understand that this offers no firm guarantee for the future to Canadian farmers.

The Chair: Thank you, Mr. Côté.

Ms. Wasylycia-Leis, if you please, you have five minutes.

Ms. Judy Wasylycia-Leis: Thank you, Mr. Chairman. Thank you, Messrs. Pellerin and Lebeau. Thank you to all members of the UPA. You have shown that the crisis in agriculture is affecting all of Canada. It is the same crisis whether you are in Quebec or Manitoba. What are the solutions? It seems to me we should look at three things.

The first aspect is an increase in federal support. That is a totally feasible solution if we consider this year's and next year's forecast surpluses which are about \$8 billion.

The other aspect of the question is that there has to be more collaboration and cooperation between the provinces and the federal government. It seems to me that the latest announcement made by the federal government was a bit arbitrary. The Manitoba government's view is that the federal government did not quite comfort the provinces.

The third aspect is the equalization formula. It seems to me that if we could go back to a more equitable formula...

• (1225)

[English]

I'll have to say it in English, I'm sorry.

It would seem that if you actually returned to a formula that reflected the real meaning of equalization, and we got away from the kind of chart that we saw today from the government here in Quebec, there would be additional resources for provinces like Quebec and Manitoba that they don't otherwise have access to, which would then also help to balance things out on the agricultural side.

Excuse me for my broken French.

[Translation]

I hope you will be able to answer.

Mr. Laurent Pellerin: You're exploring three tracks which, in our opinion, seem the most promising. First, the federal government can respond on its own and bring its contribution back up to the level of the reference years or at least 1995. The average contribution of the decade from 1985 to 1995 would be an even better comparison if we go by the figures provided.

There also must be a partnership with the provinces. It's not enough to ask them for a 60/40 contribution in terms of percentage and for them to come up with their 40 per cent share, you also have to see if they can actually pay out that 40 per cent contribution.

The announcement made two weeks ago was for an amount of \$1 billion with a 40 per cent contribution coming from the provinces. So \$1.666 billion should have been made available to Canadian producers. The same day, or the next day, the 10 provinces issued a press release saying they would not contribute the 40 per cent share requested. So we're back to \$1 billion. So Canadian agricultural producers are not going to be given \$1.6 billion.

Then you raised the matter of equalization, a sharing between the provinces based on a 60/40 ratio. Is it imperative for this ratio to be 60/40? When you deal with a trade crisis on the international level like the mad cow crisis, is it reasonable? Trade is a Canadian government responsibility, not a provincial one.

Is it reasonable to ask provinces to cover 40 per cent of the losses incurred in the cattle and other ruminant industry because of the BSE crisis? We don't think so. This is a trade crisis. It should be the responsibility of whoever, at the federal level, is responsible for international trade. It's the responsibility of the Government of Canada and it's up to it to cover those losses.

To give you an idea of the scope of the problem, the \$1 billion amount announced 10 days ago represents a \$10 to \$15 per acre support payment for Manitoba's grain producers, for the Canadian West, where farmed acreage is huge. In Quebec, when a producer has 1,000 acres, that's a lot. In Manitoba, some producers have up to 5,000 or even 10,000 acres. You do the math. We're not talking tens of thousands of dollars per producer.

Planting season is here. Western Canadian banks say that 30 per cent of their producers won't be able to go ahead with planting because they don't have the financial resources. They're sent a meagre \$15 an acre cheque while it probably costs five or six times more to go ahead with planting.

In the cattle industry, the \$1 billion amount announced means a contribution of some \$20 per head. You're losing about \$500 per head because of the BSE crisis. You can see that all that is totally disproportionate.

If the question of fiscal imbalance between the federal government and the provinces were settled, either through the transfer of tax points or otherwise, that would give the provinces some leeway to respond adequately to the revenue crisis the grain and beef industries are going through. Those are surely the two most affected sectors at this time.

• (1230)

The Chair: Thank you, Ms. Wasylycia-Leis.

Mr. Bell, you have three minutes.

[English]

Mr. Don Bell: Thank you.

The issue I've heard, that in addition to the provincial governments needing the...well, the provincial governments not having the \$400,000, to add to the \$1 billion that you talked about. So you're also, in addition to what Ms. Wasylycia-Leis referenced, needing, if I understand it....

Because of the differences, as you pointed out, and as I heard in our full finance committee, and the diversity among agricultural needs, whether it's the farmers or the cattle producers across the country, what we really need is to somehow develop even more flexibility in the federal programs, to acknowledge those differences better than they do now.

Mr. Laurent Pellerin: Yes.

Mr. Don Bell: The programs do it, but I've heard, from the other sets of hearings we've had, that even more flexibility for the uniqueness is needed. Is that a fair statement?

Mr. Laurent Pellerin: There's no doubt about that. We need more flexibility at the federal level to make sure that the delivery of those programs, if there is a federal decision on money, is at least flexible enough that each province can flow this money to the sector in their province where they have bigger troubles. For instance, Prince Edward Island probably needed last year some money in the potato sector, because the price was very low. In Alberta, don't ask them where the money will go, because there's no doubt about it, the beef farmers in Alberta need a lot of money. That's where the large yards are and where the large losses are.

You talk about \$400 million, on the \$1 billion. It's not 40% of \$1 billion, it's 40%, the share of the province, above the billion. If 60% is \$1 billion, 100% is \$1.666-something-billion—

Mr. Don Bell: So it's \$600,000.

Mr. Laurent Pellerin: —which was supposed to be the announcement of two weeks ago.

When they asked me, after the announcement, "Is the announcement good news, Mr. Pellerin?", I said, yes, if the provinces go with this amount, it will cover the \$1.9 billion that we said was a loss for each of the last three years.

So \$1.6 billion on \$1.9 billion, we were not that far. But now it's not \$1.6 billion, it's \$1 billion, on \$1.9 billion. It's 50% of what the need was. So it's a lot less than what was expected and needed by Canadian farmers. On top of that, they will spread money everywhere—to hog farmers, to poultry, and so on—so that everybody will receive some of that money. In fact, we should have concentrated this money on beef and grain.

Mr. Don Bell: For clarification, that goes back to your original statement, if I may, where you said that the agricultural sector gets about half of the funding it needs for its producers.

Mr. Laurent Pellerin: Yes.

Mr. Don Bell: Thank you.

The Chair: Thank you, Mr. Bell.

Madame Ambrose, pour trois minutes, s'il vous plaît.

[Translation]

Ms. Rona Ambrose: Thank you, Mr. Chairman.

[English]

I'm going to ask a question in English for my home province of Alberta, where agriculture also is, as you know, a very important issue. But agriculture also is a very important issue for our party, the Conservative Party. I wanted to note to you that we were the federal party that pushed for an emergency debate in the House of Commons on the issue of BSE in particular, led by our leader, Stephen Harper. Almost all of our members were present to articulate many of the issues that you have raised here.

On a personal note, I grew up with farmer grandparents, on both sides, and heard from my mother for years about how important farming is, that is really is the backbone of our nation.

One of the issues we're facing in Alberta right now, and in the rest of Canada as well, is the BSE issue. We are seeing a lot of innovation in domestic markets in Alberta for the development of slaughterhouse capacity. I wonder if you would comment on the situation here in Quebec, if there's any progress being made on this issue to develop domestic capacity.

• (1235)

Mr. Laurent Pellerin: I was not aware that you were from Alberta. Your French is a lot better than my English.

Ms. Rona Ambrose: Merci.

[Translation]

Mr. Laurent Pellerin: In Quebec, the producers quickly looked to slaughtering capacity to try to get out of this crisis. In fact, Quebec agricultural producers, in June 2004, bought the Billette slaughterhouse, the only major abattoir for retail beef. More recently, a purchase contract was signed for the Colbex-Levinoff slaughterhouse, an abattoir used for cull cows and old steers. It is used for slaughtering all Quebec's cull cows and a good number of culls from Ontario and the Maritimes. So it is considerable volume.

I have reminded Mr. Mitchell and other liberal ministers more than once that it would wise to think about increasing slaughtering capacity in Canada. We never should have developed beef and pork production, for example, without at least having the independence we need to proceed with slaughtering domestically rather than exporting live animals to the USA. That kind of leeway leads to the creation of more jobs here and makes it easier to deal with embargos like the one we are under right now. So it is a good idea to increase our slaughtering capacity. Nevertheless, I remind Mr. Mitchell that on its own, that measure would not be enough to increase revenue for agricultural producers. We also have to look at who owns the slaughterhouses and the beef processing capacity. The same logic applies for pork.

As for the slaughterhouses in western Canada, even if they are bigger and a lot more efficient, as long as they are owned by Cargill or other huge multinational corporations, the profits will be exported elsewhere and that is clear. The purchase of the two Quebec slaughter houses for young steers and cull cows allows us to confirm that there is enough money in the system to pay producers properly. The Canadian consumers that you represent continue paying at least as much if not more for their beef as before May 20, 2003. However, what the producers are getting is laughable. So the money is floating around somewhere in the system.

Ms. Rona Ambrose: Thank you.

The Chair: Mr. Pellerin, before giving the floor to my two colleagues, I would like to put a question to you.

Has any settlement been reached in the matter of the slaughterhouse in the Drummondville area specialized in cull cows?

Mr. Laurent Pellerin: With regard to the one in Saint-Cyrille-de-Wendover, the Fédération des producteurs de bovins du Québec with the support of the UPA signed a contract. Ownership takes effect on January 1, 2006. All the conditions concerning the purchase and management of the business were settled on Good Thursday and the announcement was made the following Thursday.

The Chair: There was talk about a 45¢ a pound floor price. Where are we at today?

Mr. Laurent Pellerin: During the year of transition, which started last December and will end December 31 next, the floor price is 42¢ a pound. The market is paying for the first part, which is about 26¢ a pound or a bit more, for the better animals. Quebec's Minister of Agriculture, Ms. Gauthier, had offered to cover the difference for part of the year. Producers should start getting their cheques during the next few days. As of May 1, we are talking about 32¢ a pound and as of September 1, 42¢ a pound. We had asked the federal government to cover the shortfall, but it is very hesitant in getting involved in a floor price. In any case, that is not what is important for us. What is important is to get the money and as I said earlier, the flexibility we need to cover that shortfall and reach the minimum price.

You probably remember that we asked the Canadian government to set a floor price for cull cows, steers and all animals affected by the BSE crisis. I can tell you today that if that had been done, the slaughterhouses would have the money they need to meet those floor prices. We would not have endangered anyone. It is always both revolting and disappointing to see that they do not hesitate putting Canadian agricultural producers in danger but that they abstain from treating the slaughterhouses or the processors or the distributors the same way. If those floor prices had been established, Canadian producers would have been well treated; they would not have had to face the catastrophic effects of the crisis, at least not as intensely. The slaughterhouses would have kept on operating and consumers would have kept on eating Canadian beef and paying the same price they are paying today. We would not have gone through the catastrophe that we have been facing for the last two years.

• (1240)

The Chair: Thank you.

Mr. Côté, you have three minutes.

Mr. Guy Côté: Thank you, Mr. Chairman.

Mr. Lebeau, your conclusion earlier was:

[...] the decrease of State support for agriculture stems first and foremost from a total lack of understanding of the primary importance of this area of activity for a nation [...]

You almost made a Freudian slip before: you were going to say "incompetence". I understand that you did not say that. On the other hand, I can allow myself that luxury.

Effectively, in managing the whole agricultural file, the federal government was totally incompetent. I have only to think of its failure to act instead of regionalizing health exclusion areas. We mentioned the management of the mad cow crisis and cull cows in Quebec. If there is anything affecting our farmers, it has to be cull cows.

The federal government did invest some funds at the last minute but it was only a drop. You addressed it briefly in English when you said that little amounts of money were scattered left and right and did not necessarily go where they should have. Could you come back to that in French? I would appreciate.

Mr. Laurent Pellerin: I have often said that the key...

The Chair: You do not have to engage in politics, Mr. Pellerin. I know that you do quite a lot of that at the UPA.

Mr. Laurent Pellerin: We are trying not to engage in politics. Especially these days, we are all better off for not engaging in politics.

On many occasions, since May 20, 2003, I have said that, from where we stand, the BSE crisis was not managed in the best way and I can repeat that here today.

However, some people did work extremely hard. I would like to mention Mr. Bob Speller who submitted a report and made recommendations together with the members from all parties that worked at consulting Canadians. All Canadian agricultural organizations signed the Speller report introductory page, thus endorsing the recommendations in the report.

The federal government's take on the matter did not often adequately translate what was happening during that crisis and in the world of agriculture in Canada in general. But we must make amends and thank those who deserve it; just pay attention to the press release concerning the latest \$1 billion announcement made by Mr. Mitchell: it is the first time, in the many years I have been reading them, that a press release or any other communication from Agriculture and AgriFood Canada gives such a good description of the situation Canadian agriculture producers are going through.

If you have an opportunity of reading it, you will see that it mentions catastrophe, the worst crisis in our history and their interpretation of the tables we showed you the same way we have been interpreting them for the last four or five years. This is the first time during the last 20 years that Agriculture and AgriFood Canada has been able to look at these things with the same eye as the common man. That has not happened often. I am mentioning that today and I think this is probably the beginning of something more interesting. To date, we have not won our case.

The Chair: Thank you, Mr. Côté. As for what you have said, all the better if we are starting to use the same language, but deeds will have to follow quickly.

Mr. Laurent Pellerin: You know, Mr. Loubier...

The Chair: He is unbelievable...

Mr. Laurent Pellerin: ... the proof is in the pudding.

The Chair: That is true, sir.

Ms. Wasylycia-Leis, if you please, three minutes.

Ms. Judy Wasylycia-Leis: It would seem our challenge is to get the federal government to walk the walk. That is a beginning, isn't it? [English]

It's a beginning.

[Translation]

However, we have a lot to do. Everyone here knows there's a crisis in agriculture. I want to know how much time we have to secure a better future for our agricultural industry. How much time do we have left before the family farm dies out, before all those disastrous changes take place? If we don't see to the changes you've recommended, how much time do we have to secure a future for Canada's agricultural sector?

•(1245)

Mr. Laurent Pellerin: Let's go back to the third chart on table 3 concerning the evolution of Canadian agricultural income over the last 20 years as compared to American agricultural income.

If we had given you other charts to complete that information, you would realize that in any case agricultural producers are living off the same income, whether they're in the U.S.A or in Canada. They need the same amount of money to survive. As the Canadian producers don't have comparable income to that of the American producers, the debt load of Canadian producers has doubled during the last 20 years while the Americans' has decreased.

With that kind of a trend, where income is on a downward spiral... Ontario is probably going to serve us a telling illustration because last year, this year and next year the producers have had and will have negative income both in fact and in forecast, for those three consecutive years. Ontario is the most important agricultural province in terms of sales. It has the highest sales figure in Canada.

Look at the average age in Western Canada. With farmers whose average age is over 60 years, how long do we have left to send a positive message to producers and reverse those trends; we don't have much time.

Right now, we have to discuss with beef producers to give them a bit of hope as to the future of that production. What with the non-opening of the border, the failure we witnessed last March 7th, we don't have much positive leeway with our beef producers.

What are we to say to our young people who want to get into farming, today and tomorrow? The leeway is rather thin. It takes people who are extremely convinced, optimistic and maybe even a bit naive to involve themselves in a financial risk like that one.

We have to change course right now, not 10 years from now. For the first time, Canada's agricultural producers are reading events the same way. There is a consensus.

The Chair: Thank you, Ms. Wasylycia-Leis.

I have one last question for you, Mr. Pellerin. Most federal stabilization programs are based on the last five years, minus the worst and the best year. With three years of negative income, it must be getting hard to subtract the best and the worst year. That means that with the last three years, agricultural stabilization income is going to be a bottomless pit from one year to the next.

Mr. Laurent Pellerin: We have a five-year agreement. This is the third year. The first two years were catastrophic. This program is leading nowhere. It must be subject to an in-depth review. I refer you once more to table 3. It's an approach where the comparison is always based on the average of the latest years.

Look at Quebec's curve. Income stabilization is always on a downward curve. We won't get out of it with this kind of program.

The Chair: It's unbelievable.

Messrs. Pellerin and Lebeau, thank you so very much for your excellent presentations. Rest assured that we will seriously consider your views. This throws a new light on federal and provincial participation in these programs. It puts a light on another consequence of the fiscal imbalance.

Thank you so very much for your brilliant contribution to our exercise. We will come back at 2 p.m.

The meeting is adjourned.

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