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**Submission to the  
House of Commons Standing Committee on Finance  
in regards to Bill C-18**

***An Act to amend the Federal-Provincial  
Fiscal Arrangements Act***

**Hon. Norman Betts  
Minister of Finance  
Government of New Brunswick**

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I am appearing this morning, along with my Atlantic colleagues, in regards to Bill C-18, *An Act to amend the Federal-Provincial Fiscal Arrangements Act*.

Bill C-18 relates specifically to the ceiling on the Equalization Program. The ceiling is a longstanding concern to New Brunswick, since its inception in 1982-83.

Atlantic Premiers, and Finance Ministers, are gravely concerned about the potential impacts of the ceiling on equalization, and have called upon the federal government for its permanent removal.

Concerns about the ceiling, and its potential impact, are not limited to equalization-recipient provinces. At the August, 2000 Annual Premiers Conference, premiers joined together to issue a call for removal of the ceiling on equalization payments, in concert with other fiscal reforms.

In effect, Bill C-18 would amend the Act such that the ceiling on the Equalization Program would be removed for 1999-2000. While I view this as a positive step, I am disappointed that the ceiling on equalization has not been permanently removed. In fact, the proposed change in Bill C-18 would not even allow for equalization entitlements to grow up to the level of growth of the economy for 2000-01 and future years, as has historically been the case.

The federal government introduced the ceiling on equalization in 1982-83 as an affordability measure. While cognizant of the perils of open-ended programs, New Brunswick has opposed this measure since its inception, particularly given the unique, and critical, role that the Equalization Program plays within the federation.

The Equalization Program was introduced in 1957, and has become a central feature of our federation. The 1997 Report of the Auditor General of Canada reaffirmed that Equalization is a vital feature, and one of the main successes, of the Canadian federation.

The purpose of the Equalization Program is to raise, to a standard level, the per capita revenue-raising capacity of recipient provinces, such that all provinces have the ability to provide reasonably comparable levels of public services and taxation to their citizens. It is through this program that the playing field is leveled somewhat among provinces.

The importance of the Equalization Program is underscored by its inclusion in amendments to the Constitution in 1982. Section 36(2) states:

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

The ceiling on equalization payments violates the spirit and intent of the constitutional commitment, by limiting the capacity of the Program to achieve its fundamental objectives.

When the ceiling applies, equalization-recipient provinces receive entitlements that are less than what is determined by the formula. Formula-determined entitlements are scaled back to the ceiling level on a per capita basis. As a result, recipient provinces are no longer equalized to the level of the designated program standard, resulting in a widening of fiscal disparities that the formula is designed to reduce.

Prior to 1999-2000, the ceiling applied in four fiscal years - 1988-89, 1989-90, 1990-91 and 1993-94 - and removed in excess of \$3 billion in formula-determined entitlements from equalization-recipient provinces. For New Brunswick, this resulted in reductions to formula-determined entitlements exceeding \$190 million.

Leading up to the 1999 program renewal, the ceiling level was determined in a relatively consistent manner. First, a base year was established, in which the ceiling on equalization could not apply. In the base year, recipient provinces were guaranteed their formula-determined entitlement. Then, the ceiling level for future years was established based on the cumulative rate of growth in the economy from the base year, applied to the base year entitlement level. The base year entitlement closely mirrored formula-determined entitlements.

The 1999 equalization program renewal represented a departure from past practice. The ceiling was again re-based, to 1999-2000. However, unlike past practices, an arbitrary ceiling level of \$10 billion was established for 1999-2000, with future years' entitlements permitted to grow up to the rate of growth in cumulative GDP from the fixed, base year level. As a result, the ceiling could apply in the base year, as well as future years. Under current legislation, for 2000-01, the ceiling level is estimated at \$10.8 billion, based on the current GDP growth projection of 8.4%.

This change was implemented in large part due to affordability concerns of the federal government. It was also intended to address concerns expressed previously by the Auditor General of Canada as to the uncertainty associated with a base year entitlement that changed as new data became available.

It should be pointed out that this change resulted in a substantial ratcheting down of the ceiling level for 1999-2000 and future years. In fact, it resulted in an unprecedented reduction to the ceiling level.

If past practice had been followed, the ceiling would not apply in 1999-2000. Formula-determined entitlements for 1999-2000, which are currently estimated to be slightly below \$10.8 billion, would serve as the base for establishing the ceiling level for future years. Given the GDP growth projection of 8.4%, the ceiling level for 2000-01 would be in the order of \$11.7 billion, as opposed to \$10.8 billion under current legislation.

Bill C-18 proposes to remove the fixed ceiling level of \$10 billion for 1999-2000. As a result, entitlements for the year in question would be based on the latest estimate of formula-determined entitlements, which, as noted previously, is \$10.8 billion. The removal of the ceiling for 1999-2000 would be consistent with past practices, whereby the ceiling could not apply in the base year.

However, under Bill C-18, the ceiling level for 2000-01 and future years would continue to be calculated using the \$10 billion fixed level for 1999-2000, and not the latest formula-determined entitlement. As a result, the 2000-01 ceiling level under this Bill would be \$10.8 billion, based on 8.4% GDP growth. Given that entitlements for 1999-2000 are currently estimated at just below \$10.8 billion, this would allow for minimal program growth, far below the rate of growth of GDP. In contrast, past practice would have allowed for program growth of up to the growth rate of GDP from the 1999-2000 base year entitlement.

It is conceivable that, under the proposed Bill C-18, entitlements for 2000-01 could be restricted to a level below that of 1999-2000 formula-determined entitlements. This would result in a ceiling allowing for negative growth, as opposed to growth, on a year-over-year basis. This situation cannot be permitted to happen.

Given current circumstances, there is a very strong likelihood of the ceiling applying for 2000-01 and, possibly, future years. At the same time that less-affluent provinces are facing the possibility of reductions to formula-determined entitlements, the federal fiscal outlook is very positive, now and for the foreseeable future.

To put the impact of the ceiling on equalization in perspective, the ceiling for 1999-2000 is currently reducing New Brunswick's formula-determined entitlement by \$50 million, pending the adoption of Bill C-18. In today's terms, \$50 million provides New Brunswickers with approximately 11 days of health care. It provides for in the order of 1,000 nurses. It translates into a further 25 kilometers of new, four-lane highway. From a revenue perspective, it translates into more than 5 percent of provincial personal income tax revenues.

Bill C-18 is all the more troublesome given statements by the Prime Minister at the September, 2000 First Ministers Meeting. It was noted, in a communiqué emanating from that meeting, that "the Prime Minister agreed to take the necessary steps to ensure that no ceiling will apply to the 1999-2000 fiscal year. Thereafter, the established Equalization formula will apply, which allows the program to grow up to the rate of growth of GDP".

As I noted previously, Bill C-18 is a positive step in that it removes the ceiling for 1999-2000. However, it does not uphold the commitment of the Prime Minister. It is also inconsistent with past practice, by not allowing entitlements to grow up to the level of growth in the economy.

The proposed removal of the ceiling for 1999-2000, under Bill C-18, sends some important messages:

One, it recognizes the importance of the Equalization Program to the less-affluent provinces, and its role in ensuring that the constitutional commitment can be better met.

Two, it recognizes that the arbitrary ceiling level of \$10 billion was set too low. This level was established at a time when program entitlements were underestimated considerably, which had a direct bearing on the establishment of the ceiling level.

And, three, it indicates that the program, for 1999-2000, is affordable to the federal government, without the need for an equalization ceiling.

By extension, this would suggest that allowing the program to grow with GDP from the 1999-2000 formula-determined level is affordable to the federal government. Gross domestic product is a commonly used indicator of economic growth and prosperity. Since

the inception of the ceiling, both GDP growth and growth in gross national product have been used as the federal affordability measure.

New Brunswick strongly believes that, on principle, the ceiling on equalization should be eliminated, and we will continue to pursue the permanent removal of the ceiling on equalization. In the context of Bill C-18, New Brunswick would support an amendment that would remove the ceiling for the duration of the current equalization renewal period, as an interim measure.

Barring its removal, modifications should be made to Bill C-18 such that program entitlements for 2000-01 and future years can grow up to the rate of growth of cumulative GDP from the formula-determined 1999-2000 level.

I thank you for the opportunity to appear before the Committee today, and I trust that my concerns, and those of my Atlantic colleagues, will be given due consideration.

