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MEMORANDUM

To: Stakeholders, *Work Research Foundation*

Date: March 19th 2007

From: Ray Pennings
Vice-President, Research

Re.: **The Federal Budget, 2007**

Following is the Work Research Foundation's analysis of the Government of Canada's Budget for fiscal year 2007-2008, released by the Hon. Jim Flaherty, Minister of Finance, on Monday, March 19th 2007. We do not address all matters raised in the federal budget. The *Work Research Foundation* is particularly concerned with the impacts of budgetary policy on the institutions and associations between the individual and government (the state). In addition to matters that touch upon these, we will pay some attention to macro-economic matters that affect all Canadians.

Two Lenses

There are two lenses through which the *Work Research Foundation* looks at and analyzes the federal budget:

1. The task of government is neither minimalist (that is, only a narrow focus on essential duties such as security, safety, and core government services) nor expansionist (where government is prepared to jump in and solve every problem for which there is political advantage in addressing). The state is a guardian of the public good but should defer to the other institutions of civil society who are often better placed to deal with particular issues.¹
2. Economic thinking has been plagued by a "short-termism," the correction of which requires significant rethinking in the markets, what we measure and value as a society, and in government's approach to political economy.² We acknowledge that the Government of Canada went through a paradigmatic shift

¹This is more fully developed by WRF's Senior Fellow, Jonathan Chaplin, Director of the Kirby Laing Institute for Christian Ethics (Cambridge, U.K.), in his inaugural address "Sphere Sovereignty and Canadian Public Life" (Found at: <http://wrf.ca/fellows/senior.cfm?ID=3> or by contacting the *Work Research Foundation*).

²This concept is more fully developed by WRF's Senior Fellow, Jonathan Wellum, CEO of AIC Limited, in his address "Short-Termism and Some Significant Challenges to Capital Markets" (Found at: <http://wrf.ca/fellows/senior.cfm?ID=1> or by contacting the *Work Research Foundation*).



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from short-termism to long-termism in its management of the federal treasury and the demands upon it with the 1995 federal budget, more than twelve years ago. This was achieved by cutting up to 70% from federal departments (Transport Canada), by shrinking the federal public service overall, the Canadian Health and Social Transfer, the implementation of a clawback to OAS for high-income senior citizens, and by keeping the GST in place. Later, the Government of Canada announced and implemented a rise in Unemployment Insurance (now, Employment Insurance) premiums and a gradual rise in contributions to the Canada Pension Plan. As a result, by 2000, the Government of Canada was running with a balanced budget.

The present government is keeping the federal treasury on a policy of long-termism. In November, 2006, Finance Minister Flaherty announced *Advantage Canada* as “a strategic long-term economic plan designed to improve our country’s economic prosperity both today and in the future.” Building on this framework, the budget proposes concrete actions in each of these categories which the government believes will provide the tools to compete globally.

The *Advantage Canada* Framework

The *Advantage Canada* framework focuses on creating five Canadian advantages as pillars for improving Canadian quality of life.

a. Tax Advantage

Advantage Canada argued the need for both general and business tax relief. There are various measures which take strides toward this including a child tax credit, changes to age and limit amounts which will particularly assist small business owners, farmers and fishermen, and older workers. On the business side, overall reductions in tax rates, incentives for new business investment and changes to the treatment of capital costs allowances will provide assistance to many firms.

However, tax competitiveness is not achieved only on favourable macro-economic numbers. Government also has a responsibility create a framework in support of institutions and associations’ carrying out their respective responsibilities in society. In the 2006 budget, the elimination of tax on capital gains on securities donated to charities was a significant positive step in giving the charitable sector additional tools to raise support. The Child Tax Credit announced also provided valuable support for a vital social institution – the family – to continue playing a positive role. By giving income splitting to senior citizens, the government has recognized that most Canadians live in households with shared expense burdens. This recognition needs to be extended to all Canadians and our tax system needs to be further reformed to allow for income splitting and better address the realities of families across the income and age spectrum.

b. Fiscal Advantage



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Advantage Canada called for the elimination of Canada’s “net debt” in less than a generation. This laudable goal was to be achieved with spending discipline, resolving the fiscal imbalance so that provincial governments had the resources to address their responsibilities, and committing to passing the interest savings on to Canadians through tax cuts.

A centerpiece of this budget is the addressing of the fiscal imbalance over the next seven years. The aim of changing the complex array of inter-governmental transfers to a more principled approach in which the roles and responsibilities, together with the fiscal resources, for each level of government is better understood is a welcome step. There is a caution, however, in that overall federal expenditures are projected to increase by \$10.3 billion in 2007-2008 and an additional \$6.9 billion in 2008-2009. Although the bottom line numbers reflected as percentages of GDP are presented favourably in the budget documents, the net result remains that government is growing at a faster rate than inflation. Canada’s new social architecture requires a focus on the other institutions of society and less reliance on government.

c. Entrepreneurial Advantage

At the Work Research Foundation, we believe “markets to be the best way – no, the only *sane* way—to structure interactions in economic life.”³ As such, steps to remove red tape and provide incentive for investment and entrepreneurship are welcome, including the proposal to consider a single market regulator.

We do caution, however, that entrepreneurialism is about more than dollars. A successful business is as much a product of intellectual capital, social capital, human capital and spiritual capital as it is about physical capital. Further, entrepreneurialism entails a myriad of relationships, networks, and associations among people. From decisions taken on the basis of handshake or a telephone conversation to those involving formal, contractual agreements, people – human beings – are involved. Their relationships to each other, from informal networks to more formal associations and organizations, are the basis of a healthy entrepreneurial culture of trust, fairness, and the creation of “win-win” situations for all concerned.

d. Knowledge Advantage

Advantage Canada targets the creation of the “best-educated, most skilled and most flexible workforce in the world.” This will entail investment in advanced education, research and development, and spending on high technology, but it also requires attention to investments in training in the skilled trades and assisting entry into the work force.

³ For expansion on this, see WRF Senior Fellow Gideon Strauss (also editor of our flagship journal, *Comment*) in “Market economy – Yes! Market society – no!” available at <http://wrf.ca/comment/article.cfm?ID=225>



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Too many secondary and high school teachers and guidance counselors know too little about the opportunities in the skilled trades or they are prejudicial in encouraging students into the professions over the skilled trades. Unfortunately, all too many Canadians have not acquired basic job skills necessary to acquiring and holding a job. Canada needs investment in broadest spectrum of jobs and skills and to assist more Canadians to enter the work force with incentives for training and on-the-job learning to becoming contributing members of Canadian society. The best social program is gainful employment.

Canada presently suffers from a severe shortage of skilled workers in the construction trades, especially in industrial construction with industrial construction projects already announced for the next ten years valued at well over \$100 billion. This demand for and shortage of skilled workers requires tax incentives to entice journeypersons and apprentices to travel to projects away from home, and huge investments in training apprentices. *Canada skilled work force is ageing, and it is incumbent on government and industry to assist and facilitate a transfer of knowledge from a generation of skilled workers nearing the end of their careers to a generation beginning theirs.*⁴ The increase of the expense deduction for long haul truckers' meals is a welcome move for that industry, but there are various measures that would equalize the tax benefits for mobile workers that would be beneficial to the construction industry. While the steps announced for the recognition of foreign worker credentials may provide some immediate relief, there are longer term issues facing workers in the skilled trades which remain outstanding.

e. Infrastructure Advantage

The *Work Research Foundation* issued a study of Canada-U.S. trade, the significance of the metaphor of "trade corridors" for understanding of that trade, and included recommendations in respect of the physical infrastructure of trade corridors as well as the statutory-regulatory and business infrastructure of trade (*Greenlighting Trade: A Trade Corridors Atlas*. Found at: <http://www.tradecorridors.com/>). The provision of more stable predictable funding for other levels of government, the investment in border crossings, and the \$1 billion funding designated the Asia-Pacific and Corridor Initiative are all positive contributions in this areas.

Key Spheres and the Budget

Work

⁴ The *Work Research Foundation* conducted research on behalf of and published by the Construction Sector Council as *Working Mobile: A Study of Labour Mobility in Canada's Industrial Construction Sector*. (Found at: http://www.csc-ca.org/pdf/WorkingMobile_Report_E.pdf).



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In last year's federal budget, the Government announced that workers in the skilled trades would have the ability to claim a deduction on their tax return. This deduction has been left in place, thus recognizing the contribution that the skilled trades make in building and maintaining Canada's physical infrastructure, as well as their contributions in raising families and building communities. The announcement of an additional \$500 million for training and the Working Income Tax Benefit to help people over the "welfare wall" and strengthen incentives to work for lower income Canadians are both significant and welcome steps that will assist Canadians in acquiring the skills and jobs they need.

Families

A number of policy changes were announced that will support families:

- For the first time, senior citizens will have the opportunity to engage in "income splitting" in order to reduce their overall income tax payable as a household;
- The increase of spousal and other amounts will result in more equity among families and eliminate the "marriage penalty" that has long existed in the system.
- The Government did not announce similar income splitting for Canadians who are not yet senior citizens. We hope that in future the Government will extend income splitting to all Canadians, therefore assisting households who opt to have one parent stay home and to live on one income;
- A new Child Tax Credit of \$2,000 will provide up to \$310 per child of tax relief to more than 3 million Canadian families. The Government has also kept in place the refundable tax credit for child care of \$100 per month for each child under the age of six years. These policies recognize the importance of supporting parents as they raise the next generation of Canadians;

Communities

The addressing of the fiscal imbalance and changes to the Gas Fund will provide both provincial and municipal governments with additional resources to address important issues of concern in their communities.

Trade Associations and Worker Organizations

The investment of \$500 million additional per year for workplace training and the initiative to create a new labour market program provide an opportunity for industry groups and labour unions to help shape programs that are more responsive to the current needs of their sector.

Charities

Last year, the Government announced the elimination of taxation of capital gains on private securities donated to charities. This year the elimination of the capital gains tax



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for charitable donations of publicly listed companies to private foundations will be of benefit to the charitable sector.

Conclusion

Many will dice the numbers and slice the politics of this budget. The long-term question is how this budget will contribute to the shaping of Canadian society. Our social architecture is changing. Resources and responsibilities are being transferred to institutions and organizations between government and the individual. By giving income splitting to senior citizens, the government has recognized that most Canadians live in households with shared expense burdens. This is a start, but we should go much further down this road. Families, businesses, sectoral councils, charitable organizations, and others must be provided with resources and be able to carry out an even greater role in shaping society. This is a good thing for long-term prosperity and human flourishing in Canada.