INSIDE POLICY

THE MAGAZINE OF THE MACDONALD-LAURIER INSTITUTE

FEBRUARY, 2014

Budget making

Best if feds, provinces and territories moving in same direction

Stanley Hartt

Also in this issue: ***Munir Sheikh*** *includes tax expenditures in new measure of the size of government* • ***Audrey Laporte*** *examines the economics of health care delivery* • ***Donald Barry*** *says Keystone backers will get approval by earning "social license"* • ***Alex Wilner*** *on counterterrorism's challenges* • ***Bobbe Wood*** *on how increasing medical research can make Canada more productive and wealthier* • ***Andrew Griffith*** *examines citizenship issues* • ***Senator Stephen Greene*** *offers a prescription for enhancing the Upper Chamber's credibility and effectiveness* • ***Benjamin Perrin*** *recommends a revised approach to prostitution* • *and more*

Inside Policy

The Magazine of the Macdonald-Laurier Institute

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The Macdonald-Laurier Institute is grateful to Intuit Canada for their support of *Inside Policy* magazine.

Editor's message

Welcome back. We are into our second full year of publishing *Inside Policy* and we look forward to delivering yet more provocative, insightful commentaries and analyses of public policy challenges.

This issue has fourteen very interesting policy pieces. It begins, however, with **Brian Lee Crowley**, Managing Director of the Macdonald-Laurier Institute (MLI) addressing the issue of editorial independence in an article that relates a regrettable episode with one of our now former corporate supporters.

Stanley Hartt, a man with first-hand experience in the complexities of budget-making, demonstrates why the feds and the provinces need to have a good understanding of each others' goals and intentions as they begin crafting their respective budgets.

So that we can have a better sense of just how much the government is intervening in the functioning of the marketplace, **Munir Sheikh** factors in tax expenditures in a new measurement of the size of government.

Health policy expert **Audrey Laporte** suggests that it's time to put economics before politics in health care delivery. Though she sees an important, continuing role for government in a universal-access system, she offers a provocative view of what an economically rational health care system might look like.

With opponents expressing the view that Canada has not been pulling its weight on climate change, professor **Donald Barry** suggests that the key to gaining approval for the Keystone pipeline is for the project's backers to earn their "social license."

Alex Wilner notes that the war against terrorism is never-ending. This means we must recognize the need for on-going counterterrorism measures and accept that there will be challenges translating the strategy into meaningful and lasting successes.

In advocating for greater investment in biomedical research, **Bobbe Wood** cites several recent studies which demonstrate how cardiovascular research has not only extended and improved lives, but has also made us a more productive and wealthier society.

Mike Priaro makes the case for partial upgrading of raw bitumen in Alberta. As the Government prepares to table revisions to the *Citizenship Act*, **Andrew Griffith** looks at longer-term citizenship issues, including integrity, fairness and competitiveness. Senator **Stephen Greene** offers a prescription for enhancing the Upper Chamber's credibility and effectiveness. The senator offers some intriguing recommendations aimed at reducing partisanship and reinforcing the Senate's effectiveness and legitimacy.

In view of the recent Supreme Court ruling which found that existing criminal code offences related to prostitution infringe upon the *Canadian Charter of Rights and Freedoms*, **Benjamin Perrin** examines how other jurisdictions have addressed this particular challenge and offers recommendations for how Canada should overhaul its approach.

We also have insightful MLI commentaries on: how to deal with traffic congestion; NAFTA (is it falling short of its potential?); the CPP (does it really need to be fixed?); and Aboriginal services.

Enjoy these articles and remember that we welcome feedback.

James Anderson, Managing Editor

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Air Canada's Maple Leaf Lounges now a no-fly zone for *Inside Policy*

Carrier discontinues circulation of magazine due to disagreement over article characterizing Canada's aviation policy as protectionist

Brian Lee Crowley

As readers can attest, *Inside Policy* — published by the Macdonald-Laurier Institute (MLI) — seeks to stimulate substantive discussion of public policy issues by providing in-depth analyses and provocative commentary. In the eight issues since the magazine's launch, our expert contributors have addressed some of the most relevant and important challenges confronting governments at all levels.

Our sponsors and advertisers have provided financial and other support that has facilitated MLI's goal of delivering the insightful and provocative public policy research and analysis that has been so evident in *Inside Policy*. Without their sincere commitment to promoting substantive discourse on public policy challenges, we could not have accomplished what we have to this point. We have been very grateful for both their support and their respect for the principle of editorial independence. No sponsor or advertiser has ever made their support of the magazine contingent on having influence over the editorial content of the magazine.

Until recently.

In November, 2013, Inside Policy published an article by transportation policy expert Mary-Jane Bennett. Ms. Bennett's article offered constructive recommendations for how the federal government could deliver on its speech from the throne commitment to reduce "geographic price discrimination." She focused on cross-border airfare differentials, noting that as Canadian travelers cross the border for cheaper fares, the loss to Canada is large – in jobs, GDP and tax revenue. Ms. Bennett suggested that a policy change to stabilize the price difference could lead to as many as two million cross-border air shoppers commencing their trip in Canada, rather than crossing the border to avail themselves of cheaper US tickets. Ms. Bennett asserted that a reduction in the tax portion of an airline ticket — the major factor in the cross-border airfare discrepancy — could be key to solving the problem. In the process of making the case for a policy change on the tax portion of airfare tickets, Ms. Bennett also noted that "Canada's inherently anti-competitive air policy is a major reason for the difference in the base fare," which was described as a secondary factor in the cross-border price discrepancy.

Air Canada — which was never mentioned in Ms. Bennett's article — took such offence at the article's description of Canada's aviation policy that they notified MLI that they would be discontinuing their modest but nonetheless valued support of *Inside Policy*. Air Canada's complaint was as follows:

"The [Bennett] article incorrectly states that "Canada has the reputation of having the most restrictive and protectionist attitude to reciprocated air agreements in the developed world" and goes on to incorrectly allege that there is a "net benefit" test that is applied by the federal government in negotiating air bilateral access agreements... In fact, the World Economic Forum ranks the developed nations of the world every year on air access and Canada consistently places in the top 10%. Moreover, while there is a 'net benefit' test in respect of foreign investment, there is no

such legislative or policy requirement in respect of Canada's negotiation of reciprocal air agreements."

There is no dispute between Air Canada and MLI over whether such statements appeared in the article. In fact, for clarity's sake, below is a relevant excerpt from Ms. Bennett's commentary:

Canada has the reputation of having the most restrictive and protectionist attitude to reciprocated air agreements in the developed world. Before a foreign carrier is allowed access to Canada, it must meet the test of being 'a net benefit to Canada.' The secrecy behind this test, the lack of transparency and the weighting of 'benefit' instead of 'opportunity' would simply not be tolerated in the United States, according to former Assistant Deputy Secretary of Transportation, Andrew Steinburg in 2009.

Not only did Air Canada express disagreement with the characterization of Canada's aviation policy, but their complaint asserted that they "do not like to have factual errors in the public sphere." We have a careful quality control process before we publish articles under the MLI name, and we felt confident that the claim of factual error was not correct, but because of MLI's commitment to accuracy and reasoned public debate, we took the complaint seriously and immediately went looking again to see if the evidence confirmed and supported the assertions made in Ms. Bennett's article.

As we wished to maintain our previously positive relations, the Macdonald-Laurier Institute, as publishers of *Inside Policy*, responded quickly to Air Canada's complaints.

First, MLI provided Air Canada with evidence of seven other recognized air travel policy experts, officials or executives who had expressed views similar to those of Ms. Bennett. Below are two such examples provided to Air Canada by MLI:

1. John R. Byerly, former Deputy-Assistant Secretary for Transportation Affairs for the United States — possibly the most qualified critic in international air agreements in North America — claimed Canada represented the 'old way' of doing business and said "I shudder to think that the United States would revert to such an anachronistic, anti-competitive, anti-consumer, anti-growth policy."

2. A 2008 study by the International Institute of Transportation and Logistics Inc. entitled: Analysis of Canada's Bilateral Air Services Agreement claimed:

"Transport Canada officials in charge of bilateral air services agreements are not ready to accept Open Skies if there is a risk for the Canadian flag carrier (Air Canada) to lose traffic to foreign carriers, even where Open Skies are shown to be a net benefit to the Canadian economy as a whole."

"While the U.S. was signing liberal bilaterals, the Canadian government continued to pursue a traditional and restrictive international aviation strategy, protective of its flag airline interests at the expense of consumers and the national economy."

"It is clear that Canada's bilateral negotiating process has been heavily tilted in favour of protecting carrier interests."

As a second gesture, since we like nothing better than to stimulate debate, MLI offered Air Canada an opportunity to present their perspective on Canada's aviation policy. They were invited to submit their own commentary on Canada's aviation policy in which they could, if they so chose, use the opportunity refute the seemingly widely-held view that successive governments – Conservatives and Liberals alike — have implemented restrictive aviation policies and regulations.

Despite our best efforts to reach a reasoned compromise that would not undermine the integrity of our work, Air Canada management rebuffed all our overtures. It was suggested by Air Canada that the article should have been shown to them prior to publication, a suggestion which — for the record — could not be acceptable to any publication that wishes to retain its integrity. Air Canada insisted, in the face of voluminous evidence to the contrary, that the claims in the article were factually incorrect and also made it clear that they did not regard Ms Bennett as a person qualified to comment on these matters, demonstrating a disregard for her law degree and her nine years of service as a board member of the Canadian Transportation Agency which — it should be noted — included involvement in airline restructurings. And so, despite considerable effort on the part of MLI to salvage the relationship, we were informed that Air Canada's support for the magazine — which had taken the form of permission to have the magazine distributed in the airline's Maple Leaf lounges — would be terminated.

We thought it was important to inform the readers of *Inside Policy* of these developments for several reasons.

First, because we are saddened that Air Canada has rejected our good faith offer to allow Air Canada to make a reasoned contrary case in our pages. Instead, Air Canada has opted to respond with a measure which amounts to punishing the Institute for our effort to stimulate discussion of public policy through the use of independent commentary by recognized experts. Second, because we believe it is important that it be known that the Macdonald-Laurier Institute — which has worked hard to establish a solid reputation at home and abroad - will continue to do what it has always done: to speak out clearly and fearlessly in the pursuit of the very best public policy for Canadians. And third, because a free press is at the heart of what it takes to have a thriving democracy and it is important that people recognize the subtle ways in which such things can be put at risk.

This regrettable episode reminds us of how grateful we should be for those who do support — with sincerity and conviction — informed, independent discussion of public policy. The government and Canada's parliamentarians are constantly working to craft policy responses to economic, social and environmental challenges. Informed, open, respectful debate leads quite naturally to a refinement of ideas.

It is only through this path that we will find the policies that will make our country stronger. Thank you to the many individuals, corporations and associations who have supported and continue to support the efforts of the Macdonald-Laurier Institute and *Inside Policy* magazine.

Brian Lee Crowley is managing director of the Macdonald-Laurier Institute.

Budget making process requires provinces, feds to understand each others' goals and intentions

Stanley H. Hartt understands the complexities of budget-making. In this commentary he examines the high degree of inter-dependence between federal and provincial governments on fiscal and taxation matters and demonstrates why Canada's two senior levels of government need to have a good reading of the intentions of the other as they begin crafting their respective annual budgets.

Stanley H. Hartt

When international institutions like the International Monetary Fund (IMF) or the Organisation for Economic Cooperation and Development (OECD) focus on Canada's fiscal health, they appropriately look at the federal government's debt and deficit, in absolute terms and as a proportion of GDP, as well as the prospects for improvement. They also examine the "general government" position and outlook, taking into account political subdivisions (in our case, the provinces) and public social security funds.

How a country is really doing is best judged by studying the aggregate picture of fiscal balances. The efforts of a fiscally virtuous federal government can easily be negated by profligacy among provincial treasuries (and vice versa). This can have an offsetting effect on net stimulus intended to be provided to the economy and on the stability of price levels at any given time.

Even if all levels of government were intent on rowing in the same direction, the structure of our federal-provincial fiscal arrangements represents a complexity when all regions of the country are not doing equally well. The federal dominance of the national taxation base has led to the evolution of a system of transfers from the federal fisc to those of the provinces.

Equalization is enshrined in Section 36 (2) of the Constitution Act, 1982 as "payments to ensure that provincial governments have sufficient revenues to provide reasonably comparable levels of public services at reasonably comparable levels of taxation." In addition, the Canada Health and Canada Social Transfers make up a huge proportion of provincial financial resources for health care, post-secondary education, social assistance and social services, early childhood development and child care.

But the interdependence does not end there. To some extent, the federal and provincial levels of government compete for the same tax dollar and, from time to time, the space created by tax rate reductions offered by one level is simply occupied by the other. Privatizations contemplated by either level through the sale of Crown assets is often stymied by fear of "tax leakage" — i.e., a private sector entity paying taxes on its profits to the other level of government which previously went only to the owning government. Pressure to "harmonize" both income and sales tax bases is always present if for no other reason than to ease compliance by taxpayers and collections under federal/provincial co-operative agreements.

Little wonder, then, that Canada's two senior levels of government need to have a good reading of the intentions of the other as they begin crafting their annual budgets. The practice has developed for Ministers of Finance to meet in December to share their views on the policy mix which is guiding their preparations.

These meetings can be friendly and professional (even when disparate views are expressed) or, more commonly, vituperative settings for divergent political agendas. Attempting to score political points and pointing fingers of blame at the other level of government is a Canadian sport which has become a highly-developed tool in the hands of skilled practitioners, to the detriment of taxpayers and the public.

The most recent meeting of ministers was no exception: a controversy emerged over whether the Canada Pension Plan should be enhanced at this time. On the one hand, most provinces wanted the plan enriched by hiking both employee and employer mandatory contributions because middle class Canadians aren't saving enough to retire comfortably. The federal stance was that any payroll tax is inadvisable at a time when employment and economic activity are fragile.

If Canadians aren't saving enough, they said, the way forward should focus on financial literacy to encourage savings by way of the available tax-assisted retirement savings plans and tax-free savings account, as well as the development of pooled registered pension plans.

Also irking many provincial ministers was the change in the method of calculating the Canada Health Transfer after the expiry of the Chretien-era ten-year plan as of April 1, 2014. Switching from a formula which combined elements designed to equalize the value of transferred tax points in less-wealthy provinces to a pure per capita basis benefits some provinces (notably Alberta) and harms others (most significantly Ontario) in relative terms. Was the design of the transfer scheme on a going-forward basis intended to rein in a "tax-and-spend" Ontario government that, in the eyes of a federal government determined to return to fiscal balance by 2015, is the antithesis of fiscal prudence?

It would be helpful to recall that, from time to time, better instincts do prevail.

> *How a country is really doing is best judged by studying the aggregate picture of fiscal balances. The efforts of a fiscally virtuous federal government can easily be negated by profligacy among provincial treasuries (and vice versa).*

The harmonization of the retail sales tax bases among the federal and several provincial governments using value-added principles was initially resisted by the provinces for fear of political backlash at the time the GST was first implemented. It provides an example of how provinces can come to see the general good — in this case, the desirability of a policy structure which balances taxation between income and consumption levies, particularly with the system of exemptions and credits which mitigates the most regressive features of consumption taxes generally and which, by exempting saving and investment from consumption taxation and creating room for lower marginal income tax rates, promotes economic growth. The result was better for the stability of both federal and provincial revenues.

Not all memorable federal-provincial co-operation has been in the field of taxation or related to budget-making. Another example of such co-operation occurred in 1985 and 1986. Canada experienced a flight-to-quality financial crisis resulting from the failure of two banks and the government-assisted rescue of several others.

Subsequently, the federal government moved to dismantle the so-called "four pillars" of financial institutions and to permit each to own and engage in the activities of the others. The principal motivation here was to mitigate the disintermediation of the banking system in raising debt capital.

But when the big six banks acquired the leading investment dealers, the question arose as to how these new combined entities would be regulated. In a masterpiece of co-operation, the then-federal Minister of State for Finance, Tom Hockin, negotiated a landmark agreement with his Ontario counterpart, Monte Kwinter.

Finance Minister Jim Flaherty and his provincial/territorial counterparts, December, 2011.

The agreement drew a neat and clear distinction between what constituted banking (to be regulated by the Office of the Superintendent of Financial Institutions) and what comprised securities activities (to continue to be regulated by the various provincial securities regulators). It can even be said that the Hockin/Kwinter Accord is in large part responsible for Canada's top performance during the global financial crisis which began in 2008. The Accord prevented banks from adopting the leverage practices of their investment banking subsidiaries, unlike their counterparts in the United States after the elimination of the *Glass-Steagall Act.*

Of course, various provinces, including Ontario, have now signed on to the establishment of a Cooperative Capital Markets Regulator, as a means of moving Canada towards a single securities regulation regime. The federal Minister of Finance has extended an invitation to all provinces and territories to participate. So co-operation is possible even in very contentious policy areas where differences of ideology about the role of the state persist, but where the interest of taxpayers eventually takes on the prominence it deserves.

Federal-provincial co-operation happens more often than we hear about, and is not so unnatural as some would have us suppose. Regular and continuous dialogue and consultation, agreeing upon national objectives while taking into account regional disparities, is not beyond the abilities of prudent managers of our economy to achieve.

At the moment, a great opportunity presents itself for co-operative planning to foster the development of our northern resources. When Cliffs Natural Resources Inc. announced its abandonment of plans to build a massive chromite mining project in what is known as Ontario's "Ring of Fire," it seemed the natural consequence playing out of so many competing and apparently irreconcilable differences. But it would be foolish to give up on the effort to open access to this remote region to permit the exploitation of its vast mineral wealth and to bring employment and prosperity to its isolated communities, including First Nations.

There is undoubtedly a role for the Federal Economic Development Initiative in Northern Ontario (FedNor) in providing organizational arrangements to encourage the construction of essential infrastructure and logistical support to turn some of the smaller projects, which are still being promoted by entrepreneurial mining companies in this huge territory, into reality.

Although this potential natural resources bonanza falls primarily within provincial jurisdiction, Prime Minister Harper is on record saying that the federal authorities will continue to take an interest in assisting with "regulatory approval processes, … infrastructure investments and … making sure First Nations continue to benefit."

The same could be argued for creative contributions from the Economic Development Agency of Canada for the Regions of Quebec in relation to prospective investment in the area contemplated for mining development under Quebec's "Nord pour tous" plan, (known as "Plan Nord" under the previous government). Will we seize this enormous potential? A great country requires its leaders to surmount the political divisions that separate them and exercise their authority bearing the optimization of the country's economic prospects in mind.

Stanley H. Hartt, OC, QC is a lawyer, lecturer, businessman, and civil servant. He currently serves as counsel at Norton Rose Canada. Previously Mr. Hartt was chairman of Macquarie Capital Markets Canada Ltd. Before this he practised law as a partner for 20 years at a leading Canadian business law firm and was chairman of Citigroup Global Markets Canada and its predecessor Salomon Smith Barney Canada. Mr. Hartt also served as chairman, president and CEO of Campeau Corporation, deputy minister at the Department of Finance and, in the late 1980s, as chief of staff in the Office of the Prime Minister.

Tax expenditures must be included when calculating size of government

In modern societies there is considerable interest regarding the question of the size of government as indicative of the extent to which the government intervenes in the functioning of the marketplace to achieve outcomes different from what the markets would produce. Here, Munir Sheikh provides estimates of the size of government by taking into account the existence of tax expenditures, possibly the first time such an attempt has been made.

Munir A. Sheikh

Governments across the world play pervasive roles in achieving a range of objectives. The indicator generally used to reflect on the size of government is direct government expenditures as a share of gross domestic product (GDP). However, this measure understates the true size of government in the presence of tax expenditures: governments often simply allow selected citizens to keep some of the monies they would otherwise have paid in taxes if they themselves used those monies for things the government would otherwise have provided directly.

If a government converts a direct expenditure into a tax expenditure program, the result would be less government expenditure, less taxes and a smaller government without there being any difference in the extent of the role government plays. This is clearly an inappropriate outcome. A number of major challenges in estimating tax expenditures explain this state of affairs. However, we should deal with these challenges, rather than avoid them, so that public policies are based on the best possible facts about the most important variables. This paper reports the results of a first such effort with the hope that it would generate a serious debate on estimating the true size of government.

Measurement challenges and potential solutions

The first challenge exists in defining tax expenditure. Since it is a reduction or postponement of a tax, it is important to establish a benchmark tax anchor. We hope this is not controversial in Canada since the Department of Finance has published tax expenditure estimates for many years. However, almost a third of close to 200 individual federal tax expenditures in the personal and corporate income and sales tax bases have no quantitative estimates because, according to Finance, "data are not available to support a meaningful estimate/projection." Because of this, any estimate of overall tax expenditures would understate their true value.

The second challenge is in aggregating individual tax expenditures related to many programs. Department of Finance cautions against aggregating for two reasons: first, "[t]he simultaneous elimination of more than one personal income tax expenditure would generate larger estimates because of progressive income tax rates;" and, second, "given the interaction of certain tax measures, the revenue impact of eliminating two or more measures simultaneously would differ from taking the independently estimated numbers published in this document and aggregating them." These two effects are offsetting but it is not clear to what degree. Fortunately, the OECD provides aggregated numbers for tax expenditures both using Canadian estimates and their adjustments.

(A)lmost a third of close to 200 individual federal tax expenditures in the personal and corporate income and sales tax bases have no quantitative estimates because, according to Finance, "data are not available to support a meaningful estimate/projection."

A third challenge is getting tax expenditures for all Canadian governments. Given the existence of federal-provincial tax collection agreements that make federal and provincial tax systems harmonized to a considerable degree, we can estimate provincial tax expenditures in aggregate, proportional to the federal tax expenditures.

A fourth challenge is getting tax expenditure estimates for tax bases beyond income and sales taxes. There simply is no source of such information for the federal government, which would also lead to an understatement of the true value of tax expenditure.

Finally, there is the question of whether any estimated aggregate value of tax expenditure can be added to direct expenditures to get a more accurate indication of the real size of government. While views on it may differ, we feel we can do such an add-up since tax expenditures are a deviation from a benchmark tax system. Alternatively, one can think of tax expenditures as tax concessions from a benchmark tax system and estimate the truer size of government from the government revenue perspective.

Federal tax expenditure and the size of the federal government

Table 1 provides the distribution of tax expenditures for three years, 2001, 2005 and 2009. The largest increases have taken place in retirement incomes, housing, general business incentives (at the expense of specific tax relief), R&D and work-related incentives. GST-related tax expenditures have actually declined in contrast to income tax-related tax expenditures that have increased significantly.

Table 1: Canadian federal government tax expenditures as a share of GDP (%), 2001, 2005 and 2009

Purpose	2001	2005	2009
Income Tax			
General tax relief	.16	.14	.23
Low-income non-work-related	.02	.02	.02
Retirement	.65	1.87	2.03
Work-related	.12	.11	.12
Education	.12	.11	.12
Health	.24	.25	.27
Housing	.06	.25	.27
General business incentives	1.00	.97	1.10
R&D	.22	.25	.33
Specific industry relief	.21	.02	.07
Intergovernmental relations	1.63	1.56	1.60
Charity	.20	.20	.20
Other	.02	.02	.03
Make-work pay	.00	.01	.16
Total income tax	4.67	5.77	6.54
GST-related	1.11	1.17	.90
Total	**5.78**	**6.93**	**7.44**

Chart 1: Percentage increase in the size of the federal government with the inclusion of tax expenditures

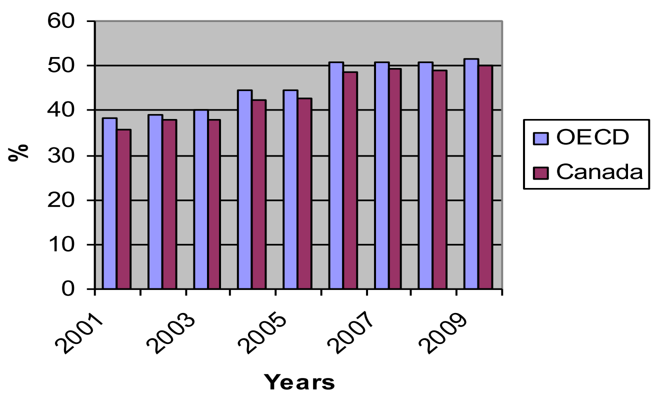


Chart 1 provides estimates of the increase in the size of the federal government with the addition of tax expenditure to direct expenditure. Two estimates are provided: one based on data submitted by Canada to the OECD and the other data adjusted by the OECD. The increase in the size of the federal government, by adding tax expenditures to direct expenditures as a ratio of GDP, is about 50 percent, not a small number.

Chart 2: Estimates of federal and provincial tax expenditure to GDP ratios

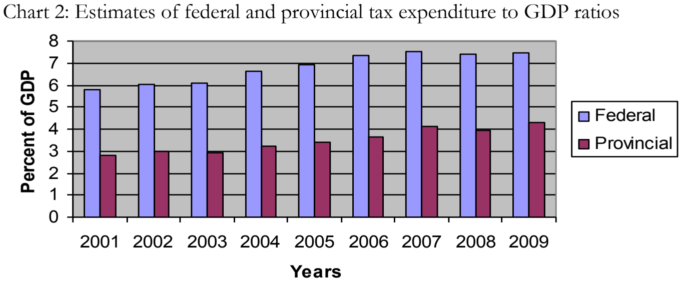
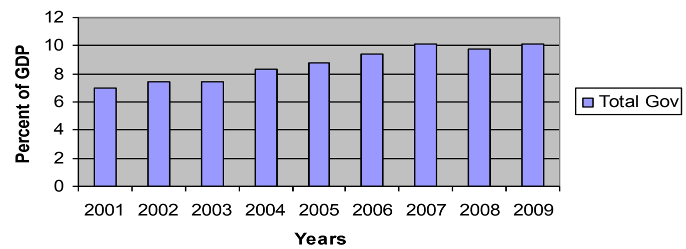


Chart 2 shows the federal and provincial tax expenditure to GDP ratios. The federal ratio is about 7.4 percent and the provincial ratio about 4.3 percent of GDP.

The provincial tax expenditure to GDP ratio is significantly less than the federal ratio because provinces rely much less on income and sales taxes combined.

Chart 3: Tax expenditures for total government income and sales tax



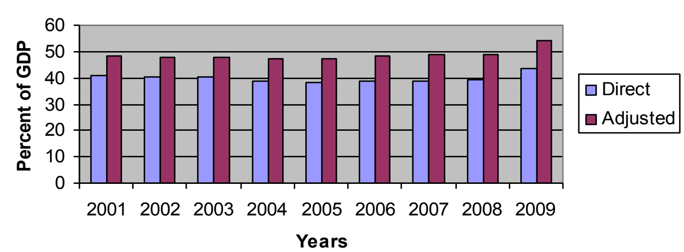
Next, in Chart 3, we add tax expenditures for federal and provincial governments for income and sales tax (removing in the process tax expenditures for intergovernmental transfers, see Table 2).

We find that the share of tax expenditures to GDP rose from under 7 percent in 2001 to over 10 percent in 2009 at the total government level. We have examined changes in tax expenditures in recent years and find the 2009 estimates have not changed materially.

Chart 4 uses information in Chart 3 to estimate the size of government by adding direct expenditures and tax expenditures as shares of GDP. The chart shows that the size of government is about a quarter higher than otherwise including tax expenditures, at about 54 percent of GDP rather than 44 percent of GDP.

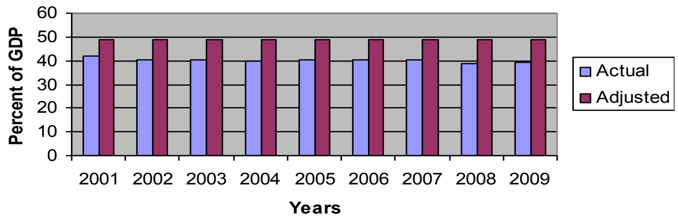
We also do not see a downward trend in the size of government adjusted for tax expenditures in contrast to such a downward trend in the unadjusted size, ignoring 2009, a year affected by increased spending in response to the economic recession.

Chart 4: Direct and adjusted expenditures to GDP ratio



An alternative picture of the true size of government can be developed by using the GDP share of government revenue instead of direct expenditure. The rationale for this is the following: a benchmark tax structure determines the true revenue yield, which is what we need to know but don't; tax expenditures — or tax concessions — tell us the amount of revenue that the tax system collected but is then given back in concessions; adding tax expenditures/concessions to the actual revenue yield, therefore, gives us an estimate of the true revenue yield. The actual and adjusted revenue yields are shown in Chart 5, which conveys the same messages as Chart 4.

CHART 5: Actual and tax expenditure adjusted government revenue



Conclusion

The popular indicator of the size of government, direct expenditure as a share of GDP, understates the true size of government by ignoring tax expenditures as there are major challenges in their estimation.

These challenges must be dealt with to get a truer picture of the size of government. We cannot overcome all of the challenges in view of the many conceptual and data issues but we can make progress. By focusing on tax expenditures in three tax bases — personal and corporate income and sales of goods and services — our estimates show that the inclusion of tax expenditures increased the size of total government in 2009 by over 10 percent of GDP, or about a quarter from 44 percent of GDP to 54 percent of GDP. The size of government adjusted for tax expenditures does not show the downward trend that we observe in the direct expenditure to GDP ratio.

We have also examined changes in tax expenditures in recent years and find they have not changed much since 2009. We believe that the size of government is likely higher than we have estimated since we have no estimates for tax expenditure related to a large portion of tax bases. A similar picture emerges if the size of government is represented by government revenue as a share of GDP.

There are a number of reasons why a better understanding of the size of government and the handling of tax expenditures is important for the appropriate conduct of public policy. While government actions provide many improvements to outcomes in a variety of areas — be they economic, social, environmental or security related — these actions necessitate the collection of taxes that have negative economic effects.

It is important to be fully informed of these costs and benefits while making public policy decisions. At a very basic level, taxpayers have a right to know how much taxes they pay, where the money is spent and what the benefits and costs of taxation and spending are. Transparency and accountability in taxation are important.

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It's time to put economics before politics in Canadian health care delivery

Health policy expert Audrey Laporte suggests that health policy-makers ignore economics at their peril. In a research paper for the Macdonald-Laurier Institute ("How markets can put patients first," released January 16, 2014), Laporte examined some of the key issues that have arisen in the context of health care from an economist's perspective. Among other things, she looked at the mechanics of markets for health insurance and the organization of supply and the nature of demand for health care. Laporte sees an important, continuing role for government in a universal-access system, but offers a provocative view of what an economically rational health care system might look like. Presented below are the Introduction to her paper, as well as selected excerpts. The full paper can be found on the MLI website.

Audrey Laporte

Casual conversation suggests that the chaotic rollout of ObamaCare in the US has become a source of Canadian self-congratulation, a further validation of the superiority of the single-payer structure of Canadian medicare. It shouldn't. If anything it should serve as the impetus for a reconsideration of the problems of the Canadian system, though that will probably not happen. Historically, the tendency among Canadian health policy analysts and policy-makers has been to compare medicare with the US system and to conclude that since we are doing much better than the Americans in so many of the standard metrics used to judge health care systems (notably cost and various measures of access to care), we don't need to consider making any significant changes to the structure of medicare.

This sets the bar far too low. It would be nearly impossible to do worse than the Americans in many aspects of health care delivery, so doing better than they are should not encourage us to rest on our laurels. If anything it should prompt us to stop focusing exclusively on Canada/US comparisons and to compare ourselves with the rest of the world, in which case we are likely to decide that we are at best somewhere in the middle of the pack.

This is not to say that policy-makers are blind to the problems of Canadian medicare. The move to patient rostering and to alternative payment systems, for example, is a response to a problem, often not openly admitted, of access to care and long wait times. Talk about the need to increase the efficiency of the Canadian health care system amounts to tacit admission that perhaps our cost/output record is not as good as we have long told ourselves it was.[1] The drawback with the solutions that have been introduced to tackle problems like wait times is that they are management-based solutions whereas economics-based solutions are needed. To take just one example, whereas many countries have been experimenting successfully with market competition as a mechanism for cost control (Propper 2010), Canadian practice has been to resist any such evolution and to rely on centrally directed reorganizations of the medical org chart.

Economics has, for some considerable length of time, played very little role in Canadian health policy-making. The term economics has, for all intents and purposes, come to mean cost accounting and while cost accounting is essential, the basic insights of economic theory have been set aside in policy-making. Indeed, the very use of the word "theory" has been taken to imply that economic analysis is somehow divorced from reality. It is often claimed that the health care market is so fundamentally different from the market of the introductory economics textbook[2] that economic theory does not apply to health care and indeed, economic analysis should not be given any role in health system design.

In many ways, the exclusion of economic analysis from Canadian health policy-making was formalized back in 1984, in the wording of the *Canada Health Act*.[3] But while the insights of economic theory might be ignored by policy-makers, the starting point of economic analysis, that people respond to incentives, is as true in health care as in any other, more frivolous, area of economic activity.

The rollout of ObamaCare marks a good time to reconsider the basics of medicare, despite the considerable differences between the US system, both pre- and post-ObamaCare, and the Canadian system. This is primarily because many of the problems faced by the two countries are, in their deep structure, the same.[4]

Since we are going to be discussing the role of markets in health care and since we have just referred to the US system, we should make one thing clear. No market-oriented health economist wants to copy the US system. Indeed, a moment's thought would lead such an economist to doubt the word "system" in that context. The US health care system is not a system if that word is taken to refer to a well-functioning mechanism. Rather, it is a Rube Goldberg device, built up over the decades by a process of making quick fixes and then, a few years later, piling on other quick fixes in the hopes of rectifying problems created by the previous quick fixes.[5] While we will be drawing on the US experience for some of the evidence we will adduce for the arguments which we will make below, we intend to discuss market-based health care delivery, and the US system should never be thought of as a market-based system. US health care delivery is the outcome of a massively complicated game, where the players who are most conspicuously absent from the process through which the game's players decide on their moves are patients. A properly designed market system would put patients first.

The first point to make is that economics is not just about adding up the costs of various aspects of care. Rather, it is about the way people respond to incentives, on both the supply and demand sides of any system, whether incentives contained in the signals sent by individuals on the other side of the market or, in cases where the government is heavily involved in the market, incentives contained in the rules and institutional detail imposed by regulators. While institutional detail is important, it is also important to bear in mind what Aristotle said, in the context of proposals that all property should be held in common: while such laws might have a specious appearance of benevolence and seem to promise to eliminate the evils which are manifest in the present system, the true source of the evils is not the system within which men live, it is the wickedness of human nature. People who would abuse one system will abuse others — changing the structure of the system will simply change the specifics of the abuse.

Editor's Note: sections have been skipped in this re-publication of Audrey Laporte's paper. To read the entire paper, please visit the MLI website.

The demand for health care

Canadian attitudes to the applicability of the economic concept of the demand curve to medical care grew up in the 1980s and 1990s around a couple of popular but erroneous notions. One was that patients had no basis for judging the value of the services they received, so that if they had to pay out-of-pocket for care they would tend to cut back on necessary medical care. The other, related assumption was that because of the informational asymmetry between patients and physicians, physicians could manipulate patients into having treatments whose sole function was to increase the incomes of providers — remunerectomies,[15] they were often called. These stylized facts, taken as gospel by many Canadian health planners, were fatal to the idea that a market could work in health care. This in turn was formalized in the *Canada Health Act* banning user fees.

This argument was backed up by the claim, based, as it happened on US, not Canadian research, that roughly 30 percent of medical care was unnecessary.[16] The 30 percent figure relates to the existence of a demand curve for medical care in a direct manner. Standard economic

theory holds that the demand curve for any commodity is downward sloping, where the price of a commodity is on the vertical, and quantity demanded by consumers on the horizontal. The negative slope indicates that at higher prices, all else being equal, quantity demanded will be less and at lower prices it will be more.[17]

While apparently still a mystery to some health policy experts, this relationship is so fundamental to economic theory that it is often referred to as the law of demand. With any commodity, we would assume that the individual is able to assess the benefit he will derive from consuming more or less of that good. The key question is whether this assumption applies to medical care.

Consider, then, the claim that 30 percent of medical care is unnecessary. In the context of a system in which insurance has reduced the out-of-pocket payment by the consumer to a very low level — zero, in the Canadian case — we would expect the marginal units of care to be low marginal value units.[18] Whether the 30 percent number is a reasonable one to use as a stylized fact is a technical matter, but in a system where the price of care out-of-pocket was very low, our starting assumption would be that some units of care will be of very low marginal value, meaning that they add very little to the state of health of patients.

So does the rule that if quantity demanded falls as price rises, apply to health care? And if it does, how does this affect the health of the people paying the bill?

There has been much more research done on the demand for medical care since the RAND Health Insurance Experiment (HIE) of the late 1970s, but the HIE retains iconic status in the literature for a number of reasons. One is that it was as close to a controlled trial as economics ever gets. Some 5800 individuals below the age of 62 in the US were assigned to insurance plans that differed in terms of the patient's out-of-pocket payment: 1294 adults and 599 children were assigned to a free plan, with no out-of-pocket payment, while 2664 adults and 1245 children were assigned to cost sharing plans with various levels of co-insurance (patients were randomized into groups in which the patient paid 25 percent, 50 percent, or 95 percent of the service fee) (Newhouse 1993). The estimated responsiveness of utilization to price was based on comparing utilization across the co-insurance categories.[19] Interestingly, the largest change in consumer behaviour in response to prices was observed in going from a co-insurance rate of 0 to a co-insurance rate of 25 percent — in other words it wasn't necessary to make people pay all that high a price to get them to change their behaviour and lower their demand for low value care (Newhouse 1993).

The RAND researchers also made an effort to determine which types of services were not taken as the out-of-pocket price rose. Medical conditions were categorized, based on the state of medical science in the late 1970s, according to whether formal medical care was regarded as highly effective (pneumonia), quite effective (asthma), less effective (cerebrovascular disease) or rarely effective — but self-care might be effective — (obesity or viral influenza). The researchers then looked at the impact of out-of-pocket payments on the utilization of care for conditions in these categories but did not look at things like whether the individual patient had got all the care normally deemed effective and had moved on to consuming further less effective quantities of care. The conclusion that is usually cited is that co-insurance reduced appropriate and inappropriate (often referred to as necessary and unnecessary) care in equal proportions (Newhouse 1993). Expressed that way, it looks bad for demand theory — people are not being selective in reducing unnecessary care, they are reducing use of all types of care. There are, however, a few caveats.

The first follows from what we have already said about how appropriate care was defined — it was based on chart review rather than actual patient examinations. The second is that in reporting these results the RAND team compared the free care group with all of the co-insurance groups combined. We noted above that the largest effect on utilization came in going from 0 to 25 percent co-insurance; as the appropriateness results are reported we are looking at figures for all of the co-insurance groups combined, so we cannot tell where along the demand curve the reduction occurs. In terms of our definition of demand curves, it would not be surprising if in going to a 95 percent co-insurance level some relatively high marginal benefit services were cut.

Also, the RAND researchers found that, despite the judgments with regards to appropriateness, out-of-pocket payments had virtually no impact on measurable indicators of health. There was a slight improvement in blood pressure among higher risk groups, and an improvement in vision, amounting to going from 20/25 to 20/24 vision for those on the free plan, but overall the conclusion was that there was no measurable effect on health from having to pay out-of-pocket for care (Newhouse 1993).

The RAND results strongly suggest that, at least as of 1981, the reduction in utilization associated with going from free care to a 25 percent co-insurance rate would not noticeably reduce health status, a result which is consistent with the way we have defined the demand curve for medical care. With regards to those cases where there did seem to be a measurable impact on certain health status indicators, the RAND team concluded that it would be much more cost-effective to determine which interventions for which patient groups were really effective and to subsidize them, rather than aiming to provide universal free care (Newhouse 1993).

A much more recent randomization experiment is the 2008 Oregon Medicaid expansion (Finkelstein et al. 2012) in which the state of Oregon decided that it could increase enrolment in the Oregon Health Plan Standard (OHP Standard) by 10,000 people. Because it was anticipated that demand would exceed the number of slots available, Oregon conducted a lottery. Thirty-five thousand individuals out of 90,000 who were eligible for Medicaid coverage were selected and then given the chance to apply for OHP standard coverage.

A 2013 paper looked at the effects of free coverage on roughly 6000 enrolled lottery winners, comparing them with an equal number of controls — individuals who had not been selected in the lottery. It found that Medicaid coverage increased utilization of health care (office visits, prescription drugs received, perceived access to care, and probability of cholesterol screening, Pap smear, mammography in women 50 years and older, and PSA tests in males 50 and older). In addition, the probability of being diagnosed with diabetes was significantly increased among the treatment group. There was no improvement, however, in standard objective measures of health state — blood pressure or high cholesterol, for example — as a result of having Medicaid coverage, nor in the use of medication for hypertension or high cholesterol. They found, in short, no improvement in the measures of physical health which they investigated, although they did find a significant drop in the probability of being diagnosed with depression and, interestingly enough, an increase, relative to the control group, in the probability of reporting that the treatment group's health was the same or better than a year previously (Baicker et al. 2013).

They also found that being enrolled in Medicaid resulted in a significant improvement in financial hardship scores — coverage nearly eliminated catastrophic out-of-pocket medical expenditures and significantly reduced the incidence of medical debt. The authors argue that this is a positive result, since health insurance is a financial product aimed at protecting people from catastrophic medical expenditure and ensuring that their health care providers are paid (Baicker et al. 2013). They have been criticized on various websites[20] for making this argument, but in terms of insurance theory, their statement is correct. The purpose of insurance, as we have said before, is to allow individuals to spread the financial risk of a negative event, like suffering a serious illness.

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These two studies, the RAND HIE and the Oregon Medicaid experiment, both support the view that the extra health care services people will consume when those services are provided free actually don't produce any real change in the health of the population overall. Just because care is "free," we shouldn't assume that people are healthier. This should not be taken to mean that health insurance, properly structured, is not valuable and it should not be taken to mean that charging very high prices out-of-pocket would have no negative health impacts. Clearly neither statement is true.

The role of government in an economically rational health care system

There is no question that there is an important role for government in the health care system but the question is, what is the best way for government to perform that role? Clearly universality of health insurance coverage is desirable so that all Canadians have access to and can afford to have health insurance that covers them in case of serious illness.

This does not mean that we need to have a monopoly public supplier and funder of medical insurance. Universal access to medical insurance does need to be secured through legislation, but that is true whether the system is publicly or privately financed as evidenced by the fact that even now, we rely on the *Canada Health Act* to define the minimum standards and obligations of provincial governments in terms of the provision and funding of physician and hospital services. There is no reason that the minimum standards could not be expanded to include long-term care, home care, and pharmacare services.

Pictured: The Cambie Surgery Centre, a private hospital in Vancouver, BC, bills itself as the most technologically advanced private surgical centre in Canada.

There are those who argue that there is already a significant private provider role on the supply side. However, in reality even though most doctors are, technically, independent practitioners and hospitals are private not-for-profits, government effectively runs the system. There is for example, little scope for hospitals to select the range of services they provide and even less ability to set the prices for their services. In the case of home care, across many provinces there is a mix of private-for-profit and not-for-profit providers that receive public funding to provide care in the community, but patients have little to no choice about which provider provides their care; they must simply accept care from the provider that won the contract from the health region or whichever level of government was responsible for negotiating the contracts with providers that year. If quality of care is poor, patients have little recourse; they cannot seek care from a competitor unless they hire a private provider and pay entirely out-of-pocket.

The emergence of Family Health Teams, as in Ontario, has also tended to include restrictions on the ability of patients to seek care from other providers outside the Team to which they are affiliated. This limits the ability of patients to seek care elsewhere if their GP is unavailable or has provided less than satisfactory care from the perspective of the patient and serves to bolster the income of physicians without increasing the responsiveness of the services they deliver to the care needs of their patients. The function of government should not be to create local monopolies that are not directly accountable to patients.

All providers should be required to meet minimum quality standards. All physicians and nurses for example, should be accredited with their professional colleges and be in good standing to be allowed to practice. All clinics, hospitals, and laboratories, whether public or private, should be regularly inspected and should meet or exceed minimum quality standards set by the government. One could argue that the results of inspections and the records of medical professionals should be publicly reported. There are currently only limited discussions about public reporting of malpractice suits and offenses committed by physicians being made publicly available to patients.

It is interesting to note that restaurants in the city of Toronto and other jurisdictions across the country are inspected and must post the results of their inspections at the entrance to the establishment. We are moving slowly towards comprehensive public reporting of inspection results in the long-term care and community care sectors, akin to what has been pursued in the hospital sector. Governments should continue to do this, as quality control is an important and appropriate role for the state. We could argue that more needs to be done. It is probably fair to say that the health care sector has a distance to go before it reaches the reliability and accountability that has been achieved in other heavily regulated sectors such as the airline industry in which human life is also potentially at stake.

There is also scope for some but not all public provision of health care services, particularly in the case of community general hospitals or hospitals in rural or remote communities. This is akin to the role of Canada Post. There are private courier services that compete in some aspects of the mail delivery market, but there is a basic public provider of service to ensure that mail gets delivered to and can be sent from communities across the country. Similarly, public provision of health care could be expanded or contracted to ensure that necessary services are in place. There is also a case to be made for ongoing government involvement in teaching hospitals, given their role in training and conducting research. Other hospitals and clinics that are private (for-profit and not-for-profit) should be allowed to operate in the marketplace alongside public providers, subject to quality standards set and enforced by the government regulator.

What would an economically rational health care system look like?

The question remains, of course, as to why we would even need to consider changing medicare. The answer lies in something we noted earlier — that we have, for too long, judged the Canadian system's performance solely against the US benchmark, a comparison designed to make any system look good. While Canadian policy-makers do need to look further afield when making international comparisons, we also need to consider the absolute performance of the Canadian system.

On this absolute, as opposed to relative metric, we must face the fact that our system is nothing like as good as we like to believe. (And after all, if it were that good, why has no other country copied it? When not long ago the Swiss were asked in a referendum whether they wanted to switch from their system of competing, regulated insurers to a single-payer system they opted to stay with their existing model, not to change.) We have long waits to get in to see the doctor — that is the motivation for changes to physician payment mechanisms which have been made in a number of provinces recently. And while it is true that most people express satisfaction with medicare, most people have not needed major medical care at any point in their lifetime. Even that is not something the system can reasonably take credit for: steadily improved population health has been more a product of steadily increasing income than of steadily improving medical care. As the population ages the rate of interaction with the health care system will increase, and for that we will need greater efficiency.

Greater efficiency will not come from central managerial decisions, it will only come if we create incentives for greater efficiency at the coalface. That will require patients to give serious thought to whether treatment is necessary and will require that we let physicians organize their practices as they best see fit. The role of policy-makers must be to ensure that the rewards encourage doing the best possible job for the patient (in other areas of economics this is referred to as the incentive compatibility problem). While there are those who object to what they see as the commercialization of medicine, greater efficiency will not come from the bureaucratization of medicine, which moves doctors to payment systems that do not reward effort, and dictates from above the precise mix of personnel which must be in an approved practice.

A health system that takes economics seriously must be structured so that price incentives operate on both demand and supply sides of the market and price signals are sent across both sides of the market. There should always be some element of out-of-pocket payment for medical care, although insurance should be structured so that there is a stop-loss provision or ceiling protecting individuals from massive costs. Out-of-pocket payment must be combined with price flexibility, so that low cost suppliers have an incentive to use their cost advantage to attract patients.

One of the clearest illustrations of the problems that arise in the absence of a proper pricing mechanism comes from the medical arms race period in the US in the 1980s, when the generosity of insurance coverage (often first-dollar coverage, meaning health care was provided at no cost to the patient) was so great that there was no point in suppliers competing through price signals. Instead, hospitals competed through visible indicators of quality — having the latest equipment and specialized services, whether or not they could attract enough patients to run those facilities at optimal scale, and having air ambulances were among the most common. Since patients (operating through their doctors) had no incentive to respond to price competition, hospitals in particular engaged in cost-increasing competition and insurers simply passed these costs on to the sponsoring employers of the plans they were managing.[26]

It is often argued that facing patients with out-of-pocket charges will result in them not having necessary medical care. The results of the RAND Health Insurance Experiment in the late 1970s and early 1980s and the Oregon Medicaid experiment in 2011–2013 cast doubt on this as a general proposition, as does the widespread belief that the US is operating on the "flat of the curve" of medical productivity, meaning that additional applications of current medical technology (as distinct from medical advances) don't really add all that much to the health of the US population as a whole. Still, there is no doubt that responsiveness to price is greatest at the lowest income levels, and it is also true that the lowest income groups tend to have the lowest lifetime states of health,[27] so any rational health care system must include income-based transfers. Should privacy concerns prove manageable, these transfers could be run through the income tax system as a form of negative income tax, and should apply both to insurance premiums and to out-of-pocket payments.

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Income based transfers have been criticized in the past as stigmatizing their beneficiaries. This is because people tend to have the early model of the US food stamp program in mind, under which it was obvious who was a welfare recipient. Payment technology today, however, makes such stigmatization unlikely — a health insurance card could act as a credit card, with part of the bill being paid by the insurer and part by the individual. A low income individual could be given a positive credit on their health payment account, which would mean that the tax system was picking up a certain portion of their out-of-pocket payment. The higher the income the less the credit until at a certain level it phased out altogether. The aim here is not to equalize out-of-pocket payment in dollar terms across individuals but rather to equalize the impact of the out-of-pocket payment, up to some upper limit. This may be a little more complicated than handing over an OHIP card, but the exercise would make the patient acutely aware of the costs involved.

We could think of the out-of-pocket payment as a deductible, but a better way of framing it in the health care case would be as a reference

price. The European evidence shows that in market segments with a reasonable degree of competition the full price (the sum of the reference price and the extra amount the supplier charges) drops quickly to a level only slightly above the reference price, so that the out-of-pocket payment is relatively low.

It is important to note that this happens because consumers are responsive to price and because there are competing suppliers in the market. In the case of medical care, a reference pricing system would give low cost producers an opportunity and incentive to compete on a price basis against high cost producers and the tendency of consumers to move to lower price suppliers would give the notion of price competition teeth. The effectiveness of the reference pricing system in inducing consumers to change suppliers does not depend on the out-of-pocket price being high, but its effectiveness in driving the market price down does depend on there being no barriers to entry by new suppliers other than through quality control, which should be aggressively monitored by government, perhaps on a mystery shopper basis.[28]

Consider the Family Health Teams in Ontario. These are capitated (fixed price per patient) or mixed payment mode practices, which the province decided would be more efficient suppliers of medical care than the fee-for-service practices that had dominated the delivery of physician services. In order to induce physicians to switch to this alternative payment mode, the province had to arrange the payment structure so that physicians would earn more, and hence cost the system more, than under fee-for-service. Since capitated payment reduces the incentive to supply services by eliminating any element of payment based on the quantity of services supplied, the province instituted a system of shadow billing to allow it to monitor the output of the practices.[29]

Family Health Teams (FHT) are also required to run out-of-hours clinics; if any patient registered with one FHT goes to a different Team's clinic, the patient's FHT will be billed the cost of the visit. Patients can be removed from a FHT's list by the FHT if they go to the wrong walk-in clinic. It is worth noting that, back in the 1980s, walk-in after hours clinics were becoming quite common in parts of Ontario, notably Toronto.

These clinics were not approved of by the Ministry or health policy analysts, since they were regarded as entrepreneurial medicine, and obtained their funding as a result of what was regarded by planners as a loophole in the OHIP fee schedule. That loophole was closed and the number of out-of-hours clinics was greatly reduced, despite the fact that there was an obvious demand for their services in parts of the province. Under the rules of OHIP the option did not exist for patients who found it convenient to use such a clinic to pay for its services out of their own pockets.

In a rational system the role of government on the supply side would be greatly reduced. There would still be a need for government-run community and teaching hospitals, but otherwise the organization of practice would be left to the suppliers to determine, since they are the individuals with the greatest incentive for getting it right. Specialty clinics would be permitted, given no particular benefits and faced with no particular hindrance. It has sometimes been argued that specialty clinics will select their service line so as to attract the low cost cases away from hospitals. Whatever the merits of this argument in the present US system (which should be changed so that the implicit cross-subsidy argument no longer works) it makes no sense in the Canadian case to argue that Canadian hospitals should have their beds filled with low cost cases. The essential thing here is that there must be free entry into the market: if that applies then under a reference pricing system, capacity will expand to the efficient level and prices will be driven down to eliminate any monopoly rents. In other words it will attack both the problem of waiting times and rising prices simultaneously.

While a rational health care system must include universal coverage, mandated by law, there is no need for it to be a single-payer insurance system. It is sometimes said that a public monopoly has administrative cost advantages compared to private insurers. In fact, the load administrative costs impose on a system depend on the size of the system. In the US, small employer-based plans tend to be administratively costly, but there are limits to the gains from making the pools bigger; beyond a certain size administrative complexity multiplies rapidly.

The claimed cost advantages of the Canadian single payer system over other countries' multi-payer systems tend to depend on economies of scale, which are exhausted well below the level of the national population (US numbers are distorted by the number of very small pool plans in the US) and also reflect the fact that the primary function of the Canadian payers was simply to write cheques. For much of the history of Canadian medicare the single payer had very little to do, which helped keep costs down. In a rational system there would be competing suppliers, who operated under a set of centrally determined rules.

All of the suppliers would have to offer core major medical coverage, so that no one would be denied necessary medical care for financial reasons, but in a rational system the concept of necessary medical care would actually be defined — have content — and not simply be a buzz phrase.

This was never done under Canadian medicare, primarily because to do so would have been politically courageous, so medically necessary came implicitly to refer to any service which could be performed in a doctor's office, and although provinces have de-listed certain cosmetic services or never listed certain new services (LASIK eye surgery), they have generally done so on an ad hoc basis, behind closed doors. Insurers would be free to cover other services, but those services would not be part of the universal system. Insurers would, however, have to structure their plans on a reference price basis, and would not be allowed to sell insurance that covered payments in excess of the reference price. This restriction already exists in the Australian medicare system.

Insurance would not be employer-provided. Instead, individuals would buy their health insurance the way they buy automobile insurance, or perhaps through health insurance exchanges. This would ensure that individuals who changed jobs would be able to keep their preferred insurance provider.

There would be an income-based negative income tax type subsidy for premiums, phasing out as income rose but not at such a rate as to create a poverty trap situation, so that individuals who lost their job would still be able to stay with their existing plan. Insurance would be guaranteed renewable on both sides, meaning that the insurer and the insured would be locked into the system. This would ease concern that an individual who developed a chronic illness would be denied coverage not in the year in which the condition manifested but in the following year.

To make this economically feasible, individuals would also have to be locked into the system; hence the notion of guaranteed renewability on both sides. The yearly premiums would be structured to contain two parts: one to cover acute illnesses which might strike the individual in that year and another which essentially takes the form of a deposit into an investment account, the funds in which will be drawn upon if and when the individual develops a chronic illness.

An alternative way of looking at the second part of the payment is as a premium insurance: each individual in the health insurance system will be paying into a second insurance plan which pays off if they develop a chronic illness which would force their annually calculated premiums to rise on a permanent basis. In other words, the second part protects the insured against an increase in their actuarially fair premium.

There should always be some element of out-of-pocket payment for medical care, although insurance should be structured so that there is a stop-loss provision or ceiling protecting individuals from massive costs.

An economically rational system would also need to change the way the medical care system is funded. Canadian medicare has traditionally been funded from general revenues. This approach was adopted when the dependency ratio,[30] and in particular the aged dependency ratio, was low. What is referred to as the ageing of the population is a consequence of the conjuncture of the post war Baby Boom and the Baby Bust which followed it, creating a situation in which the ratio of older, non-working individuals to the working population is beginning to increase significantly.

Some Canadian policy analysts have argued that it is fallacious to claim that the aging of the population will raise the cost of the health care system.[31] Whether this argument is true or not, it is irrelevant to the question of the ratio of the number of taxpayers to the number of benefit recipients. This issue, which arises in both Canada and the US, has been termed the problem of health care's unfunded liability, and reflects a broader issue than simply the effect of the ageing of the Baby Boom group.

An economically rational health care system would be structured to minimize the effects of changing age dependency rates. Rather than being a pure pay as you go system, an economically rational system would involve a health savings component, aimed at having working age individuals pre-fund their own later health care expenditures. Pure transfers through the tax system would then be aimed at ensuring that lower income individuals were not disadvantaged in health saving and at ensuring that the benefits of recent economic growth were shared with the older population.

Were the population age distribution to remain stable there would need be no significant difference between the outcomes of this system and those of a pure pay as you go system, but it would cushion the possible disruptions associated with future changes in the population age distribution.

A system which involved individual saving against future health bills and under which core health coverage did not necessarily cover everything that could be done in a doctor's office, as is presently the case, could allow a range of insurance providers to compete to supply coverage. This pattern already exists in some European countries that have universal coverage, so a competitive insurance market would not need to, and indeed should not, look anything like the US insurance system.

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Endnotes

1. It is important to keep cost increases in perspective. Health care is a much more labour-intensive sector than many other sectors of the economy, so costs per unit of output will tend to rise more rapidly than in more capital intensive sectors, where technological change can more easily be incorporated in new capital equipment. What matters is that the cost increase not be increases in what economists refer to as economic rent — payments in excess of the level necessary to induce suppliers to provide specific levels of output. Most of the increase in US costs over the decades has been increases in economic rents. Canada has tended to do better in that regard. Part of the reason for cost increases in Canada lies in the incentives built into the system, which have focused primarily on rewarding finding ways to do more, even at higher cost, rather than on finding ways to do what we already do at lower cost. There is nothing at all wrong with advancing the technological frontier, but there should also be rewards in place for the person who figures out how to cut the cost of things that the system can already do, without compromising quality of care. We must reward medical entrepreneurship along both of these margins.

2. A statement which blithely ignores the fact that what is covered in introductory textbooks is by no means the entire body of economic theory.

3. The wording of the CHA is the shibboleth of Canadian health care debate. The problem is not with the intent of the Act, it is with the assumption that because the Act's intentions are good, the rules set out in it must necessarily and naturally be the right ones to realize those intentions.

4. In addition, the US is a good source of illustrations of some of the points we wish to make. This is a reflection of the old maxim that bad policy makes for good teaching material.

5. Typical of US health policy-making, ObamaCare has deliberately not touched the most important obstacle to rescuing US health care, the tax breaks that lead to most Americans getting (or expecting to get) their health insurance as a benefit of employment, a policy that was the product of a war time ruling about the applicability of wage and price controls to benefits as opposed to cash wages and a tax ruling from the 1950s that meant that employer provided health benefits were not treated as taxable income to employees.

15. In the Canadian literature this term probably dates back to Robert G. Evans (1976).

16. The inappropriate 30 percent figure should not be confused with reports of the proportion of bed blockers in hospital wards. A bed blocker is a patient who needs medical care at a degree of capital intensity beyond that which can be obtained by going to a primary care physician, but does not need hospital level care. They are in hospital because there is no other place for them to get the care they need. Increasingly, bed blockers are elderly patients who could be treated in nursing homes or long term care facilities, but who are hospitalized because of a lack of alternative sites of inpatient care. This type of inappropriate use can often be attributed to a lack of foresight on the part of health system planners.

17. Economists use the term "change in quantity demanded" to refer to a change in consumption that results from a change in price. The term "change in demand" refers to a change due to any other factor — to a change in age, income, or health status.

18. Marginal here does not mean small, necessarily. It is a term economists use to mean "at some margin" — marginal benefit is the benefit to be derived from consuming the last unit of a commodity, where last here really means one more on top of the ones already consumed. Marginal, then, really means additional.

19. There were a couple of other insurance conditions, including an HMO, but we will focus on the co-insurance conditions.

20. See, for example, Tyler Cowen (May 1, 2013), which raises the issue of how the Oregon results would compare with simply giving people cash. See also the comments on the statistical analysis of some of the results by Megan McArdle, (May 13, 2013). For a criticism of this criticism, see Casey Mulligan (2013).

21. See also Ha T. Tu and Jessica May (2007).

22. Under US law at that point in time.

23. The uninsured typically pay the full list price out-of-pocket.

24. Reference pricing can be used for pharmaceuticals under public drug plans in Canada since those do not fall under the Canada Health Act.

25. Martin Gaynor is an expert on hospital economics, who has been an author on a number of studies on the effects of competition on the cost and quality of hospital care in the UK and the US. Since posting the blog post referred to above, he has accepted an appointment as Director of the US Federal Trade Commission's Bureau of Economics. A recent paper considers the effects of market competition in the UK and, according to the abstract, "we estimate the impact of the introduction of competition on not only clinical outcomes but also productivity and expenditure. We find that the effect of competition is to save lives without raising costs" (Gaynor, Moreno-Serra, and Propper 2013).

26. This period brought forth the first era of HMOs, as insurers began to try to restrain costs, but these efforts typically resulted in the insurers being pilloried for putting profits ahead of people's health and well-being, so the insurers essentially gave up and went back to simply passing costs back to employers and ultimately to the insured themselves. A few HMOs survived this period, notably Kaiser Permanente's staff model, which came to be seen as the ideal form of medical care. The Kaiser model proved impossible to translate across the US, however, and in 2013 Kaiser has emerged as one of the highest cost plans offered on California's ObamaCare Health Insurance Exchange.

27. Economists refer to an individual's state of health broadly defined as their stock of health capital — like any capital good it can be built up through investment and maintained at modest costs, but will run down if not actively maintained. As with any investment project it is often the case that the act of investing today has a payoff that is spread out over many future years.

28. See for example, the *Wall Street Journal* article on the subject by Shirley S. Wang (August 8, 2006).

29. The province of New Brunswick, having instituted a system of salaried general practice, is reported to be putting in place a system of monitoring what are termed accountability benchmarks: the number of patients in the practice and the number of patients seen per day along with shadow billing the services provided (CBC News June 20, 2013).

30. The dependency ratio is a ratio of the number of people in the labour force (usually the number of people between the ages of 15 and 64 years) to the number of people not in the labour force (usually those 65 years and older).

31. The standard Canadian reference on this point is Evans, McGrail, Morgan, Barer, and Hertzman (2001).

Markets hunger for Canadian bitumen, not refined oil

Brian Lee Crowley argues that natural resource nationalism causes people to clamour for policies that with a moment's analysis are revealed to be simply wrong. "[C]onsumer advocates and many others believe Canada is somehow "losing out" when it exports bitumen from the oil sands, for example, rather than refined products like gasoline and jet fuel. Many of them look at the discount on Western Canadian oil and, misunderstanding its significance, agitate for that oil to be shipped east where it will prove a boon for consumers. Both ideas are quite wrong," writes Crowley. (For a different perspective, see Mike Priaro's argument in favour of partial upgrading on page 40.)

Brian Lee Crowley

What is it about Canada's natural resources that make normally sensible people take leave of their business and economic senses and clamour for policies that sound good, but a moment's analysis reveals as a fraud and a chimera?

Natural-resource nationalism, the idea that "our" natural resources should go through every stage of processing within Canada, is one such policy. People as diverse as author Jeff Rubin, West Coast newspaper publisher David Black, trade union leaders, consumer advocates and many others believe Canada is somehow "losing out" when it exports bitumen from the oil sands, for example, rather than refined products like gasoline and jet fuel. Many of them look at the discount on Western Canadian oil and, misunderstanding its significance, agitate for that oil to be shipped east where it will prove a boon for consumers.

Both ideas are quite wrong.

Take the oil sands, for example. The oil sands do not produce oil, but a tarry sandy substance called bitumen, which contains oil. To refine the bitumen, you need to upgrade it to a refinable state (so-called synthetic crude); that takes either an upgrader or a coker. To make refined products, then, is an expensive two-stage process compared with ordinary crudes that can go straight to refining.

Even that suggests that one crude is easily substitutable for another. Not so. Refineries are generally designed to handle a particular crude, or more often a blend of crudes with specific characteristics, like their sulphur content. To change from one crude to another often requires a complex and expensive refinery refit.

Put all that in the context of an open North American market for refined petroleum products in which demand has been falling, not rising, uneconomic refineries have been closing (four in North America last year alone) and those remaining have been increasing their capacity to capture economies of scale and compete with imports. Cheap refining capacity, in a perfect illustration of the power of globalization, has been under construction in Asia, with North America part of its target market. The people who are promoting more refining in Canada are therefore doing so in the face of excess local refining capacity that is not especially competitive against rising Asian refiners. These are hardly propitious circumstances in which to build new refineries, or even to spend the billions necessary to wean Eastern Canadian refiners off imported oil and on to bitumen. There are no upgraders east of Alberta, and only one refiner, Imperial in Sarnia, Ont., has a coker.

By contrast, there is spare capacity on the U.S. Gulf Coast that already refines heavy oil products from places like Mexico and Venezuela. That is the business case behind Keystone XL and the rail and barge traffic moving our bitumen south. The case for spending billions to build new refining capacity in Canada is thus weak. If there was money to be made in more Canadian refining, companies would be willing to put billions into it. Instead they often struggle to keep open the refining capacity they have.

What about the idea that the discount that applies to Western Canadian oil products means that eastern consumers would benefit from cheaper gasoline if the oil could be brought east?

This misunderstands both the reasons for the discount and the nature of the market for refined products.

The discount simply reflects our inadequate infrastructure. If the oil cannot reach world markets, that creates a localized oil glut and brings down the local price. Remove the transport bottlenecks, however, get that oil to where the entire world can bid for it, and the discount unrelated to the quality of the petroleum itself will disappear. That's what piping western oil to Montreal or Saint John does: Bring it to world markets because it can just as easily be exported as it can be refined locally. And if it is bitumen in the pipeline, the capacity to process it in the east doesn't exist in any case, except in Sarnia.

As for discounted crude resulting in cheap gasoline for consumers, it is a fiction. Gasoline and other refined products are commodities; those who make them sell them for the prevailing price in an increasingly global market. Cheap local feedstock thus improves the profitability of refiners, and any price differential between Eastern and Western Canada is explained almost entirely by taxes and transportation costs, not the cost of crude.

The failure of the National Energy Program taught us that we get the best value from our resources when we let markets, not politics, guide our decisions. Markets hunger for our bitumen. Refined products are a much different story.

Brian Lee Crowley is managing director of the Macdonald-Laurier Institute. This commentary was published in the Globe and Mail on October 3, 2013.

Trans-Alaska Pipeline System runs 1300 km, from the Arctic Ocean to the Gulf of Alaska at Valdez. The proposed Keystone XL Pipeline project is 1897 km.

Canada's approach to climate change is key to US approval of Keystone

With opponents expressing the view that Canada has not been pulling its weight on climate change policy and the federal and Alberta governments and the oil sands industry still discussing long-awaited oil and gas emissions regulations, Donald Barry suggests that the key to gaining approval for the Keystone pipeline is for supporters of the project to earn their "social licence."

Donald Barry

"I'm going to evaluate this based on whether or not this is going to significantly contribute to carbon in our atmosphere. And there is no doubt that Canada at the source in those tar sands could potentially be doing more to mitigate carbon release….We haven't seen specific ideas or plans."

—President Barack Obama, Interview, *New York Times*, July 24, 2013

To many observers, President Barack Obama's comments represent a shift in policy ahead of his decision on whether to approve the Keystone XL Pipeline project. The pipeline would carry up to 830,000 barrels per day of diluted bitumen from Alberta's oil sands to refineries on the Texas Gulf Coast. But concern over the environmental effects of the project has been a recurring refrain under the Obama administration. The issue is also highly controversial in the United States where it has become entangled in the ongoing power struggle between Republican and Democratic legislators and President Obama's White House. Republicans champion Keystone as an important contributor to US energy security and jobs; many Democrats are concerned about the danger of pipeline spills and even more so about the climate change implications of oil sands operations. Politically, President Obama has little to gain by approving Keystone as few pipeline supporters are likely to be converted to the Democratic cause if he does.

About the only way the Canadian and Alberta governments and the oil sands industry can win the President's endorsement is to reduce the oil sands' footprint — something they have yet to do. Like US supporters of Keystone, they have focused their lobbying efforts on the energy security and job creation aspects of the project while making exaggerated claims about their environmental stewardship. Not surprisingly, their campaign has been ineffective.

In the early 2000s, Ottawa, Edmonton and the industry sought to capitalize on President George W. Bush's push for greater energy security by emphasizing Canada's role as a safe, reliable energy partner. But by 2008, views in the United States were changing. Presidential candidate Obama, with the backing of environmentalists and environmentally-minded Democratic voters, promised to end US dependence on "dirty, dwindling, and dangerously expensive" foreign oil.

Asked whether importing oil sands crude was consistent with this pledge, a campaign advisor replied that if technology failed to reduce carbon emissions an Obama administration would "support resources... that meet our long term obligations to reduce greenhouse gas emissions." It was "an open question" whether oil sands energy would meet those standards.

Prime Minister Stephen Harper's government, which had not delivered on its pledge, made two years earlier, to introduce emissions regulations for the oil and gas sector, proposed a bilateral climate change agreement to protect oil sands exports from possible penalties. In February 2009, Prime Minister Harper and President Obama launched a Clean Energy Dialogue to foster research on emerging technologies in order to reduce greenhouse gas emissions. The centrepiece was carbon capture and storage, an experimental and costly process that would likely be of greater benefit to US coal-fired electric power plants with concentrated discharges than to oil sands operations, the emissions of which are dispersed and thus harder to contain.

At the UN Climate Conference in Copenhagen later that year, Ottawa joined Washington in committing to lower carbon emissions by 17 percent from 2005 levels by 2020. Even with its heavy dependence on coal-fired electricity, which accounts for a third of its emissions, the United States is on course to meet its Copenhagen target.

However, Canada lags behind as a result of oil sands expansion. Although they make up only seven percent of Canada's carbon emissions, oil sands operations are the fastest growing source. While the industry has reduced its emissions intensity, its overall pollution has tripled in recent years as a result of increasing production.

In the meantime, with the Keystone pipeline project in play, Ottawa, Edmonton and the industry set out to "educate" Americans on the importance of oil sands energy to their country.

In 2010, US ambassador David Jacobson told a Calgary audience that "more needs to be done" to reduce the industry's environmental impact. But the Canadians ignored his warning. Instead, they tried to overpower pipeline opponents with a competing narrative focused on energy security, jobs and questionable ethical oil claims. They coopted friendly environmentalists and ignored the rest. An apparently confident Prime Minister Harper pronounced Keystone a "no-brainer." A spokesperson for TransCanada Pipelines, Keystone's builder, agreed saying, "It's what we have been saying all along."

Even with its heavy dependence on coal-fired electricity, which accounts for a third of its emissions, the US is on course to meet its Copenhagen target. However, Canada lags behind as a result of oil sands expansion. While the industry has reduced its emissions intensity, its overall pollution has tripled in recent years as a result of increasing production.

By the fall of 2011, Keystone had become a major political issue in the United States. The US State Department, which had earlier argued that Keystone would have "no significant [environmental] impacts," postponed a recommendation to President Obama until after the 2012 presidential election. This was done in order to consider alternative routes after concerns were expressed in Nebraska over the effects of possible spills on the state's delicate Sand Hills and Ogallala Aquifer.

In an attempt to pressure the administration, Prime Minister Harper warned that the State Department's action had prompted Ottawa to intensify its efforts to sell oil sands crude to Asian markets. Attention centred on Enbridge Inc.'s proposed Northern Gateway Pipeline that would carry diluted bitumen from Alberta to a marine terminal in British Columbia for shipment to China and other Asian countries. Although US supporters of Keystone would echo the prime minister's comments, Gateway had been under consideration since 2006 and had always been seen as a complement to Keystone.

But opposition to Gateway was on the rise. Prime Minister Harper charged that "significant American interests," were preparing to bankroll "environmental groups and others" opposed to the project, presumably to ensure the United States would retain its monopoly on Canada's oil sands crude exports.

Yet, those US interests also supported President Obama's climate change agenda and were against Keystone. Natural Resources Minister Joe Oliver went further, accusing "environmental and other radical groups" of using "funding from foreign special interest groups" to "highjack our regulatory system to achieve their radical ideological agenda."

Image from the Syncrude Canada website, which states: “We understand that we are a large operator in the Canadian oil sands industry and, as such, we must earn our social license to operate by demonstrating sustainable development.”

In January 2012, President Obama, who had said environmental considerations would weigh as heavily as energy security and jobs in his decision on Keystone, rejected the project after Republican legislators, in a budget battle with the administration, forced the passage of a bill that would require him to choose within 60 days. TransCanada responded by dividing the project into two parts: a southern leg that would run from the Midwest oil hub of Cushing, Oklahoma to Gulf Coast refineries, which would not require presidential approval, and a northern leg from Alberta to Steele City, Nebraska, which skirted most of the Sand Hills area. With President Obama’s encouragement the southern section was approved. The proposal for the northern leg would be subject to further State Department review.

While these developments were unfolding, Republican legislators kept pressing the Keystone issue in Congress, and the Canadians continued to make their case. In March 2012, Alberta’s premier, Alison Redford, made the first of several visits to Washington. She extolled her government’s commitment to “environmentally responsible development,” highlighting the province’s intensity-based regulatory approach aimed at lowering emissions by 50 megatonnes per year by 2020. The principal policy instruments are a $15 per tonne carbon tax on big industrial emitters, used to support clean energy projects, together with a $2 billion fund for carbon capture and storage projects.

Prime Minister Harper weighed in again the following month in an address in Washington in which he declared that President Obama’s rejection of the initial Keystone proposal had reinforced Ottawa’s determination to speed up oil sands exports to Asian markets. Still, the Canadians seemed confident that President Obama would approve the project after the presidential election. “It responds to national security concerns and it will create jobs and economic activity in the United States,” said minister Oliver.

Nebraska’s endorsement of TransCanada’s revised Keystone pipeline route through the state and President Obama’s pledge to act on climate change in his Inaugural and State of the Union addresses in early 2013, set the stage for renewed debate. Republican proponents in Congress pressed for quick approval.

Ottawa and Edmonton sought to cast Canada as an ally of the United States on climate change, especially after Ambassador Jacobson followed up the president’s speeches by calling on Canada to “take the lead” in reducing greenhouse gas emissions in order to make it “easier to… find markets for its energy.”

In January 2012, President Obama, who had said environmental considerations would weigh as heavily as energy security and jobs in his decision on Keystone, rejected the project after Republican legislators, in a budget battle with the administration, forced the passage of a bill that would require him to choose within 60 days.

Environment Minister Peter Kent noted that Ottawa was moving in tandem with Washington by improving fuel standards in the transportation sector, and was “very close” to concluding emission standards for oil and gas. Alberta’s international and intergovernmental relations minister found nothing in President Obama’s pledge “that isn’t completely aligned with our commitments.” But an off-message Foreign Affairs minister, John Baird, challenged the Obama administration, claiming — incorrectly — that Canada was on track to “meet or exceed” US measures, and called on Washington to follow Ottawa’s lead in phasing out coal-fired power plants.

Premier Redford returned to Washington in February expressing willingness to work with Ottawa and Washington on climate change policy. In an accompanying article in USA Today she summarized Alberta’s measures, including the carbon tax on big emitters to bring down pollution rates. But the province had to admit that it was “not on the right trajectory” to reach its goal. High costs also forced the cancellation of the second of four carbon capture and storage projects.

Shortly thereafter, the State Department released a revised report on Keystone. The report argued that it was “very unlikely” that pipeline spills would damage Nebraska’s ecology. It estimated that on a life-cycle basis oil sands operations are 17 percent more polluting than conventional crude oil produced in the United States. However, it held that approval or rejection of the project would have little effect on the rate of oil sands development — and thus carbon emissions — because the industry would find other ways to get its product to market, especially by rail.

Ottawa, Edmonton, the industry and their US supporters were quick to claim vindication. Opponents argued that the report's findings were flawed. Keystone alone, they contended, would facilitate a 36 percent increase in oil sands expansion and hence carbon emissions. They pointed to studies that showed rail lacks Keystone's capacity to move oil, and that it is less safe and more polluting. The higher costs of rail transportation compared to pipelines, moreover, would squeeze the industry's profit margins, and by extension federal and provincial taxes and royalties, affecting future oil sands investment decisions. (This helps to explain why the federal and provincial governments and the industry are so intent on securing approval of Keystone.)

The opponents drew support from the US Environmental Protection Agency (EPA), which challenged the State Department's conclusions and recommended that Washington work with Ottawa to reduce oil sands emissions. But Minister Oliver thought Canada's environmental policy was just fine. "I don't see the need for us to do things differently than we're currently doing," he said. "We can stand tall on our record." TransCanada charged that the EPA's recommendation "ignores Canada's fundamental sovereignty."

In an attempt to capitalize on the State Department's report, the federal and Alberta governments expanded their Keystone lobbying campaign, including a series of ads in American publications touting Canadian-American friendship and Canada's reputation as a "world environmental leader."

Prime Minister Harper said that Ottawa and Edmonton were taking a "Team Canada" approach to the project, which he called "vital to both the economic growth and economic security" of the two countries — themes he stressed during an appearance in New York in April. The oil sands industry, too, stepped up its lobbying effort in Washington. "In large part, we go to get the story straight," said a company executive, who complained, "The problem is, environmentalists are not held to the same standard of proof as public companies like us are." But the burden of proof was on the industry. It was enough for protest groups to exploit weaknesses in the industry's case, putting the industry on the defensive and enhancing their credibility in the process.

In a major speech in June, President Obama set out the administration's position, affirming "Our national interest will be served only if this project does not significantly exacerbate the problem of carbon pollution. The net effects of the pipeline's impact on our climate will be absolutely critical to determining whether this project is allowed to go forward."

Minister Oliver asserted that the State Department's report had already settled the issue. If the President's decision were based on "facts and science," he was "comfortable" that Keystone would be approved. Ottawa, Edmonton and TransCanada all echoed the findings of the report.

President Obama went further in an interview with the *New York Times* the following month. He said, "there is no doubt that Canada at the source of those tar sands could potentially be doing more to mitigate carbon release," adding, "We haven't seen specific ideas or plans." It seemed that Ottawa had finally got the message. Although the two countries already had the Clean Energy Dialogue, Prime Minister Harper sent a letter to the President proposing "joint action to reduce greenhouse gas emissions in the oil and gas sector." The step was taken to help sell Keystone to environmental opponents and to protect the industry's competitive position. But it was difficult to see how the two sides could harmonize their policies because the United States does not have an oil sands sector.

Ottawa's cooperative approach did not last long. Minister Oliver tried to shift attention from oil sands emissions to the pollution effects of the coal-fired power sector in the United States. The timing was odd, coming just days before President Obama proposed new draft emission standards for future coal and natural gas power plants, with regulations for existing plants to follow.

Sounding much like President Obama's Republican opponents, Prime Minister Harper issued a direct challenge, telling a New York audience that he would not "take 'no' for an answer," should the President reject Keystone. "This won't be final until it's approved and we will keep pushing forward." The outburst was hard to fathom, unless the Prime Minister had given up on the President in the hope that his successor would give the project the go ahead.

Meanwhile, the government was preparing a new advertising campaign in the United States, Europe and Asia promoting the oil sands as a secure, environmentally responsible source of energy. Even as it did so, Environment Canada issued a report predicting Canada's emissions will exceed its Copenhagen target by 20 percent because of oil sands expansion.

The industry forecasts that output is likely to grow from the current level of 1.8 million barrels per day to 5.2 million by 2030. If production continues on its current trajectory, emissions will increase to almost 14 percent of Canada's total greenhouse gas pollution by 2020, eclipsing gains made in other sectors. By Ottawa's own admission, this is Canada's record.

It has been argued that Canada needs a "social licence" to export oil sands crude. Some observers, often the same ones, claim that a rejection of Keystone based on President Obama's standard would amount to an unfair trade barrier. But as University of Calgary professor Bob Page has observed, "The social licence is being given by the country importing the oil." And many are of the view that Canada has not been pulling its weight on climate change policy. The federal and Alberta governments and the oil sands industry are still discussing long-awaited oil and gas emissions regulations. It is time for them to earn their social licence.

Donald Barry is a professor emeritus of political science at the University of Calgary.

Why even good counterterrorism sometimes falls short

MLI Senior Fellow Alex Wilner, a security and intelligence expert, notes that, unlike traditional wars, the war against terrorism is never-ending. While outright victory against al Qaeda and its friends and allies will prove elusive, this conflict is also unlikely to end in any negotiated settlement. As a result, the best we can hope to achieve is to manage the threat over the long run.

Alex Wilner

This year Canadians will mark a solemn anniversary: the centennial anniversary of World War One. In 1914, the world's most brutal war began. Tens of millions of souls perished. But like all traditional wars, WWI also eventually ended. Canadians mark that date every single year. On November 11 at 11:00 AM, Canadians everywhere stand for two minutes of silence. We do so to recall the terrible sacrifice this country paid during the conflict and to pay tribute to our veterans of all subsequent wars. Eleven AM holds special resonance because at precisely that time, on the 11th day of the 11th month in 1918, World War One officially ended. The Armistice — the agreement signed by Germany and the allies — dictated the terms of the peace.

Think about that for a second: the warring parties sat down, around a table, and negotiated an end to a vicious war. The guns fell silent, the armies eventually packed it in, and the peace held for roughly 20 years.

Now picture that scenario today with an adversary like al Qaeda. Can you imagine two minutes of silence commemorating the end of this conflict? It is impossible to do so: this conflict is so utterly different from traditional war that it is hard to envision any ending at all. There is no way al Qaeda is going to join us at the table to negotiate some form of lasting and meaningful truce. Fanaticism is its raison d'être. But we should not fool ourselves, either. We, too, will prove exceptionally poor negotiating partners. What might we realistically give al Qaeda to ensure an end to hostilities: what piece of land, or foreign community, or policy would we be willing to trade or sacrifice? The bottom line is that this conflict is unlikely to end in any negotiated settlement.

At the same time, outright victory against al Qaeda will prove elusive. It has repeatedly demonstrated its ability to exploit weak and failing states, and to take advantage of civil conflict in order to carve itself new safe havens. It feeds on political instability. Al Qaeda also continues to attract foreign militant groups to its cause, who pick up its flag and mantra as their own. And it also has a knack for recruiting Westerners. The upshot is that the conflict with al Qaeda-inspired, Jihadi-Salafi Islamist militancy, will go on. So, instead of a modern Armistice we are stuck with perpetual counterterrorism. We do our best to destroy them; they do their best to hurt us. In the meantime, terrorism in Canada and abroad remains a persistent if low-level threat and we hone our counterterrorism strategy to better defend our interests. Along the way we will score some victories, like we have by dismantling al Qaeda's core leadership in Afghanistan and Pakistan.

But at other times al Qaeda will regain the momentum, as it did in 2012 by nearly overrunning Mali, and appears to be doing again today in Syria and Iraq. These developments cannot be dismissed. As CSIS noted in 2013, "the oxygen" that al Qaeda has depended upon throughout its history has "been its possession of, or access to, physical sanctuary and safe haven."[1] Al Qaeda's new toehold in Syria, for instance, is attracting scores of foreign jihadists, including thousands from Western Europe, Russia, and the United States. Canadians have not been immune to this siren's call: at least a hundred have travelled to Syria to join rebel groups, and many are suspected of having joined al Qaeda's local franchises.[2] Most notably, Ali Dirie — a self-confessed, convicted, and later released member of the Toronto 18 — recently evaded Canadian authorities despite not having his own passport, travelled to Syria, and died fighting alongside hardcore militant Islamists.

If a settlement is improbable and outright victory over al Qaeda unlikely, the best we can do is manage the threat over the long run. Herein, what does good counterterrorism look like? In my view, counterterrorism has two overarching requirements. First, we need to counter the capability of militant groups; and second, we need to counter the motivation of groups and individuals to facilitate acts of terrorism and political violence.[3] What follows is a summary of these processes along with a discussion of why even good counterterrorism sometimes falls short.

Counter-capability approaches are tactical in nature. The idea is to eliminate the sources of power that allow al Qaeda and other terrorist groups to organize acts of violence. We are talking about the sharp end of the stick, here, the sorts of things we do in order to destroy militant training facilities, or target and eliminate militant leaders, or deter state sponsorship of terrorism. But other, less destructive forms of counter-capability involve strengthening domestic and international institutions that help states better control their territory, or constricting the international financing of militancy, and uncovering, disrupting, and thwarting plots. Each process limits a group's capacity to commit acts of violence.

Alone, however, counter-capability is probably not enough. Terrorism is not just violence, but violence with a political purpose. If we expect to develop strategies that have a lasting effect, we need to challenge the logic and legitimacy of al Qaeda's ideology and goals. Counter-motivation processes help fill the void: they are ideational in nature. The objective is to impede al Qaeda from achieving its larger social, political, and strategic goals, to foster global anti-terrorism and anti-al Qaeda norms, and to champion and reward non-violent alternatives. We are not talking about root causes, per se, but rather about hearts and minds.

> *There is no way al Qaeda is going to join us at the table to negotiate some form of lasting and meaningful truce. Fanaticism is its raison d'être.*

Terrorists lose when the violence they orchestrate no longer resonates with a (purportedly) supportive community. Counter-motivation involves tackling the concepts and rationales that sustain al Qaeda's larger movement. The focus here is on degrading its ideology and on denying terrorism's efficacy for addressing real or perceived political grievances. Importantly, counter-capability and counter-motivation are intertwined. By diminishing a group's capability, for instance, we dissuade participants; and by dissuading participants, we diminish militant capability.

Both processes are built into Canada's Counter-terrorism Strategy (officially released in 2012).[4] The strategy's four pillars — prevent, detect, deny, and respond — are based on the logic of counter-capability and counter-motivation. The buzzword that weaves the four pillars together is resilience: resilience at the community level to repel and reject violent ideologies, and resilience at the national level to defeat terrorists at home and to bounce back, as a free and democratic society, if attacks do take place. Each pillar is also mutually reinforcing.

The message is that terrorists will meet stiff resistance: Canadian security agencies have the mandate and the means to identify and deal effectively with threats. Plots will be thwarted, perpetrators jailed. The strategy's general point is to communicate to would-be militants that they will fail to attract support among other Canadians, that their plans will be foiled, and that Canadians will stand together and resolutely against radicalism, political violence, and terrorism.

In an ideal world, a terrorist contemplating an attack in Canada will realize just how unlikely they are to succeed. And theoretically, a militant who believes they are likely to fail may be less willing to try. But in the real world, things get messy. Even smart counterterrorism can face unintended tradeoffs and runs into the occasional paradox. Expectations then go out the window. Two specific tradeoffs are worth exploring in greater detail.

First, some counter-capability operations are double-edged swords: the benefit we gain is neutralized by an unanticipated cost. Take the US targeted killings program. Targeted killings are the intentional slaying of foreign-based militant leaders and facilitators taken with explicit government approval. Most Canadians are familiar with the US drone program — where remote-controlled aircraft identify and kill individual militant targets overseas, usually in Pakistan, Somalia, Yemen, and Iraq. In November 2013, for instance, Hakimullah Mehsud, the leader of the Tehrik-i-Taliban (TTP, aka, Pakistani Taliban) was killed in a US drone strike in western Pakistan. Hundreds, if not thousands, of such strikes have occurred in recent years. And besides drones, targeted killings are also carried out by Special Operations Forces, like the US raid that killed Osama bin laden in Abbottabad, Pakistan in May 2011.

There is a compelling case to be made that targeted killings effectively degrade militant capability. When leaders are killed, power struggles can erupt — as appears to have happened among TTP members following Meshud's death.[5] And replacement leaders are forced deeper underground, wasting time, money, and energy evading death rather than planning further atrocities. And when skilled facilitators, like bomb makers, are eliminated, a group's competence, capacity, and professionalism may be impaired. Even a group's morale can take a hit, upsetting the recruitment and retention process. Despite significant legal, ethical, and practical concerns, these are some of the likely counter-capability benefits of targeted killings.

But on the flip side, targeted killings — and especially those involving drone strikes — might actually radicalize individuals. That is, they drive rather than diminish recruitment, and motivate people to participate in militancy. This may be especially the case when drones mistakenly kill civilians. For example, Faisal Shahzad, the Pakistani-American who nearly detonated a car bomb in Times Square, New York City, in 2010, justified his recruitment to terrorism by arguing that "When the drones hit, they don't see children."[6] He was out for vengeance, radicalized by a perceived injustice. Now, it is far too easy to oversell this point. A lot of new social science research is going into parsing the counter-capability and potentially motivating effects targeted killings and drones have on militants and their supporters.[7] At the moment, however, we simply do not know enough to come down with definitive findings. But the specific case does highlight the tradeoffs we face when thinking about putting our counterterrorism strategy into practice.

A second paradox worth exploring is that at times our counter-capability operations do not translate into counter-motivations. What we think should influence or deter militants simply does not; our intentions and plans appear to have very little traction. Take airplane and airport security as an example. After al Qaeda turned passenger jets into cruise missiles on 9/11, steps were taken to ensure that such attacks cannot easily happen again. Cockpit doors have been locked. Passengers are extensively screened. Air Marshals sit among us. And the police presence at airports appears robust. In the counterterrorism business, we call this target hardening: we have beefed up our defenses to thwart and dissuade militant attacks on airport infrastructure. At this point commercial aviation is perhaps the most hardened and best protected civilian target.

But time and time again, al Qaeda and other terrorist groups continue to attack airplanes and airports with new devices: 9/11 box-cutters gave way to two British shoe bombs in 2001; then to a shoulder-launched missile attack in Mombasa, Kenya in 2002; then to suicide attacks out of Moscow airport in 2004 and 2011; then to liquid bombs out of the UK in 2006; car bombs at Glasgow Airport in 2007; underwear bombs in 2009; cartridge bombs in 2010; bus bombs at a Bulgarian airport in 2012; and a new and improved underwear bomb that same year.

Despite very low odds of success, terrorists appear hell-bent on attacking civil aviation. Logic tells us that they would be better off focusing their energies elsewhere, on less-hardened "soft" targets. And yet they persist. There is no easy answer for why this is. Perhaps some militants see value in conducting attacks that are nonetheless likely to fail because they equate the sensationalism of the attack as a value in and of itself.

Al Qaeda repeatedly targets commercial aircraft despite a losing track record stretching over a decade, the argument goes, because the plots, even when foiled, generate value (like public fear, political embarrassment, government spending, and so on). If so, this represents a serious conundrum: even al Qaeda's failures can be perceived as successes. This will hamper how we operationlize our counterterrorism strategy.

In sum, we know that we will be facing al Qaeda and its friends and allies for some time yet. Thankfully, we also know what the contours of good counterterrorism looks like: counter-capability and counter-motivation must go hand-in-hand. The problem is that in confronting a complex and evolving security challenge, we may occasionally have trouble translating our strategy into meaningful and lasting successes.

MLI Senior Fellow Alex Wilner lectures at the Munk School of Global Affairs, University of Toronto. Dr. Wilner's research applies traditional theories of deterrence, coercion, and influence to less-conventional contemporary threats like terrorism. He presented a version of this commentary to the annual symposium of the Canadian Association for Security and Intelligence Studies (CASIS) in Ottawa, in November 2013.

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Medical research that can warm an economist's heart

Bobbe Wood, president of the Heart and Stroke Foundation of Canada, asserts that one of the vital elements about biomedical research is that it cannot be turned on and off on a whim. It requires an infrastructure built over many years and it is vital for researchers to know that funding will be there for them to carry out the long-term work that is so fruitful. In making the case for greater investment in research, Ms. Wood cites several recent studies which demonstrate how cardiovascular research has not only extended and improved lives, but has also made us a more productive, and thus wealthier, society, too.

Bobbe Wood

On September 24, 1955, US President Dwight Eisenhower had his first heart attack. He was given the long-standard treatment — enforced bedrest, since there was really nothing else that could be done. It was considered aggressive "treatment" when he was allowed to sit up in a chair after just a month and resumed walking at six weeks.[1]

Forty-nine years later, in September 2004, when former President Bill Clinton, then 56, complained of chest pains and shortness of breath, scans revealed serious blockages in his coronary arteries.

Before he could have a heart attack, he had quadruple coronary bypass surgery and was released from hospital four days later.[2] In February 2010, after some further chest discomfort, he had surgery to install two stents to unblock one of the grafted bypass arteries. He was up and walking two hours later.[3]

Those two famous examples demonstrate how far the knowledge and treatment of cardiovascular disease has come in the lifetime of the baby boom generation. Of course, we don't only have to look south of the border for such examples. Former Prime Minister Jean Chrétien, like Bill Clinton, benefited from quadruple bypass surgery in 2007,[4] as have thousands of other Canadians. In fact, we are all the beneficiaries of the research that led to these and other advances in cardiovascular disease prevention and care, either directly ourselves or by enjoying the healthier and lengthened lives of many of those who are important to us.

We are now learning, however, that the research investments we make into cardiovascular health and disease have another important payback beyond our health. It's in our wealth. Cardiovascular research is one of the best economic investments we can make as a society.

Important work in this area has been done in recent years by economists in several countries, but now Canadian researchers have evaluated the payoffs from cardiovascular disease research in Canada. Their peer-reviewed results, published recently online at CMAJ Open by the Canadian Medical Association, show that investments in cardiovascular research are generating an internal rate of return of 21 percent — a return that will continue in perpetuity.[5] That's payback enough to warm the heart of even the coldest banker or investor.

It's a complex calculation to make, weeding out the impact of Canadian cardiovascular research on the health gains of Canadians and then evaluating what those gains are worth. Building on the work of international researchers, the Canadian team developed a model using Canadian data. From 1981 to 1992, expenditures by public or charitable organizations on cardiovascular research in Canada amounted to $392 million (expressed in 2005 dollars).

Taking a 13 year time lag from when research is done to when it impacts patients, they calculated the health gains of that research from 1994 to 2005 amounted to 2.2 million quality-adjusted life years (QALYs), meaning Canadians' health was improved the equivalent of 2.2 million persons living one additional year in good health with full quality of life. Health economists routinely calculate and monetize QALYs to determine the economic value of treatments and procedures. Doing so in this case produced the 21 percent rate of return.

"It's amazing what the payback is on health research investments in general, and for cardiovascular research in particular, it's extraordinary," said Dr. Paul Grootendorst, an economist and Associate Professor in the Leslie Dan Faculty of Pharmacy at the University of Toronto, one of the co-authors of the study.

Economists like Dr. Grootendorst call knowledge a "freely available capital good," meaning it's something that, once developed, is freely available to everyone indefinitely — it does not get used up. Because of this status, Dr. Grootendorst says governments have an important role in using public resources to create it, as they do for other public goods such as national defence or infrastructure.

There are two specific reasons, he adds, why governments should invest in biomedical research. First, because the result is better health, which is enormously valuable. Second, because any one health research project is an extremely risky endeavour for private investors, with no guarantee of success and, even if it does bear fruit, appropriating the benefits of that knowledge is very difficult.

Important work in this area has been done in recent years by economists in several countries, but now Canadian researchers have evaluated the payoffs, too. Their results ... show that investments in cardiovascular research are generating an internal rate of return of 21 percent — a return that will continue in perpetuity. That's payback enough to warm the heart of even the coldest banker or investor.

However, unlike deciding to subsidize a particular factory or industry, governments don't have to pick the research winners. "With broad research investments, the cream will rise to the top on its own," Dr. Grootendorst says. "The tangible benefits will become apparent by the activities of others who build on the research to create new products or techniques. This is what improves health, adds to our economic activity and increases our standard of living."

A third and more immediate benefit of government investment in cardiovascular research in Canada is that 70 percent of such funds go directly to job creation. Research is a very people-intensive activity, involving a range of positions from doctors and scientists to nurses, medical assistants, statisticians and administrative assistants. They are the type of jobs we always need more of, particularly if we have already made the public investment in the researchers' education.

The findings of the new Canadian study reflect those of earlier work in the US and United Kingdom.

A study in the UK commissioned by the Medical Research Council, Wellcome Trust and the Academy of Medical Sciences found an even higher perpetual rate of return than in Canada.[6] Using a similar methodology to the one in Canada, that study found that each pound invested in cardiovascular disease research by governments and charities produced a return of 39 pence each year forever.

Interestingly, it determined that 30 percentage points of the 39 percent annual return comes from gains in gross domestic product rather than health gains. In other words, more than three-quarters of the benefit was in general economic activity rather than individual health benefits. The results were summed up by Jon Sussex, Deputy Director of the UK Office of Health Economics: "In addition to ways of improving people's length and quality of life, medical research benefits the UK economy. The UK is richer as a result of medical research, as well as healthier."[7]

In the US, studies by leading economists sponsored by the Albert and Mary Lasker Foundation have shown that improvements in health accounted for almost half of the gain in American living standards in the last half of the 20th century.[8] A dramatic reduction in deaths from cardiovascular disease was the leading contributor, leading them to conclude that "the large returns to investment in medical research have come principally from gains against heart disease and strokes."[9]

"There are very significant opportunities to improve the quality of life of patients with this condition," he says. "The cardiac output of patients with AF is substantially reduced, by at least 20 percent. This decreases their capacity for activity, so they do less and can quickly get into a downward spiral of declining activity and diminishing health."

University of Chicago economists Kevin Murphy and Robert Topel have estimated the return on investment in cardiovascular research in the US from 1970 to 1990 averaged $500 billion a year, on the order of 20 times larger than average spending on medical research, a return they call "enormous."[10]

Like the fine print in ads for mutual funds, skeptics might argue that returns on past investments should not be used as a guide for future benefits. Perhaps, they might say, all the big gains in cardiovascular health have been made from those earlier research investments and new ones will not produce similar success. This argument gets perilously close to the thinking of the United States Patent Office clerk who (perhaps apocryphally) in the late 19th century resigned his job on the grounds it could not possibly be interesting because everything important had already been invented.

There are two specific responses to this argument. The first is that we don't need to maintain the same rate of return for future investments to still be worthwhile. A return of a small fraction of 21 percent would be substantial and worthwhile for our health and our economy. US researchers Murphy and Topel themselves point out that the economic gains from prevention and treatment of major diseases are so large that research generating even small progress will almost certainly be a superb investment.[11]

And there is still much progress needed. Despite all the gains we have made, heart disease and stroke remain the leading causes of hospitalization and prescription drug use in Canada, and the second leading cause of death and economic costs. Without further research and progress, this burden will increase dramatically as the population ages and as we face the growing epidemic of obesity and diabetes from unhealthy diets and physical inactivity.

The second, and even more powerful, reason to invest more in research is to ensure the continuation of the world-class work of the dozens of leading cardiovascular researchers in Canada, such as Dr. Andrew Pipe, Chief of the Division of Prevention and Rehabilitation at the University of Ottawa Heart Institute. They already have an idea about the great benefits their research will yield as we understand more about the causes of cardiovascular disease, how to prevent it, how to treat it and how to help people recover to the fullest extent possible.

The work will have wide benefits, says Dr. Pipe. "The great value of research into cardiovascular disease is that when we examine approaches to its prevention we are also addressing the determinants of all other chronic diseases except mental illness.

Approaches to prevent cardiovascular disease also contribute to the prevention of other conditions, including musculoskeletal disorders like osteoporosis and metabolic diseases such as diabetes."

A key point for Dr. Pipe is that we recognize that research does not just involve scientists working in a lab "with boiling beakers and microscopes." Many researchers are examining bio-behavioural approaches to the prevention and management of cardiovascular disease.

Dr. Pipe specializes in finding out how to get patients from one health state to a better one. It has myriad components, one of them being his recognized leadership in developing ways to help patients to quit smoking, in itself the most important thing a smoker can do to improve his or her health.

As our population ages, Dr. Pipe is investigating how to improve the health and lives of Canadians with increasingly common cardiovascular problems, such as atrial fibrillation (AF), a common heart rhythm abnormality. "There are very significant opportunities to improve the quality of life of patients with this condition," he says. "The cardiac output of patients with AF is substantially reduced, by at least 20 percent. This decreases their capacity for activity, so they do less and can quickly get into a downward spiral of declining activity and diminishing health."

Echoing the cautious approach to treating heart attack patients 50 years ago, current recommendations for management of AF make no mention of exercise. "With new research," says Dr. Pipe enthusiastically, "we hope to examine the effect of high-intensity interval training involving short periods of vigorous exercise followed by less intense exercise. We are confident that this can lead to substantial improvement in physical capacity and improve the quality of their lives. Pilot studies have confirmed the validity of this approach."

When research demonstrates clear improvements in the health status of patients, the next step is to influence actual clinical practice. This "knowledge translation" is itself a fertile field for research activity. "We need to identify the most effective and most efficient ways to deliver care in every setting so as to make best use of healthcare resources," says Dr. Pipe. "We need to develop integrated programs of care, involving both patients and practitioners, in order to assure the most beneficial and cost-effective delivery of solutions to contemporary cardiovascular problems."

Though these health and economic arguments for investing in cardiovascular research are compelling, there is a further important reason we should be promoting it. Canada must not build its 21st century economy only on the exploitation of its natural resources. To ensure a diverse and vibrant economy and society, we must also build our investments in economic activity based on knowledge.

Traditionally, the resource sector of the economy has been balanced by a strong manufacturing sector, but that has been in steady decline. While manufacturing accounted for 16 percent of Canadian employment in 2000, a loss of more than 450,000 manufacturing jobs reduced that to 10 percent in 2009[12] and the trend has since continued. A strong science and knowledge-based sector can go a long way to replacing the decline of manufacturing as an economic complement to resource exploitation.

Canada has a solid foundation on which to build even greater excellence in all aspects of biomedical research, including a leading education infrastructure, a strong basic research community, an experienced clinical workforce distributed across the country and across disciplines, a highly qualified and internationally respected clinical and health services research workforce and world-leading expertise in systematic reviews.[13] There is no doubt we have all the ingredients to make biomedical research an important economic sector, while at the same time improving our health, our lives and overall economy.

One of the vital elements about biomedical research is that it cannot be turned on and off on a whim. It requires an infrastructure built over many years and it is vital for researchers to know that funding will be there for them to carry out the long-term work that is so fruitful.

"Consistency of support is fundamental to having progress in research," says Dr. Pipe. "Cadres of researchers can't just be made to appear and disappear. The challenge is to articulate this reality to policy makers who often don't understand how research works and what is required to sustain it. This is ironic given all the rhetoric describing the importance of creating a knowledge-based economy."

We must also ensure that we have the capacity within our healthcare system to translate research findings and progress into real benefit for patients — and thus also benefits to our economic wealth. The studies discussed above demonstrate that the quicker research is translated from bench to bedside, the larger the rate of return.

This requires greater willingness and resources to adopt new techniques and treatments and to educate health professionals, patients and the general public when new knowledge is available.

The studies show these are not just nice things to do, but economic imperatives, while also improving and extending countless lives. Who knows the ripple effect throughout history of even one individual living longer and being able to do more?

There's one other famous example of US presidential cardiovascular disease that many scholars say likely changed the course of world history. Franklin Roosevelt had hypertension for many years, and though the official cause of his death in office in April of 1945 was a stroke, that was no doubt caused by his years of high blood pressure. In the 1940s, there was no effective way to treat it.

At the time of the Yalta conference in February 1945 with Josef Stalin and Winston Churchill to plot the future of the post-Second World War world, Roosevelt was a very sick man and didn't perform well. Many historians believe the post-war world likely would have been very different if he had been healthier and lived longer.[14] He almost certainly would have been if he had had then the hypertension and stroke prevention treatments we have now.

We've come a long way in fighting cardiovascular disease, but we still have a long way to go. It is only through research that we will get there. Who knows how our lives, and indeed our history, will be changed by advances in the future. There's no doubt, however, it will be for the better and we will all be richer for it in many ways.

Bobbe Wood is president of the Heart and Stroke Foundation.

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The question is not how to fix CPP but whether we need to

In the Financial Post (December 12, 2013), MLI senior fellow Philip Cross wrote that while calls for Canada Pension Plan expansion are based on vague feelings of unease about the future, the evidence suggests that doing so could ironically threaten the long-term economic growth needed to secure incomes. Suggesting that "people are genetically programmed to be perpetually anxious about their future standard of living," Cross warns against devising an expanded CPP based on "perceptions of anxiety among people who are worried about their security in retirement."

Philip Cross

There are a lot of specific reasons to oppose the proposed expansion of the CPP — it doesn't target those most in need, it taxes many Canadians who already have adequate savings, it ignores large sources of wealth that could help fund retirement, it penalizes small businesses and youths, and so on.

Let's step back and look at the broader question of what is driving the alleged problem — is it real or is it the result of shaky assumptions?

And what are the broader implications of higher taxes and pension benefits for long-run potential growth, the best assurance of future income security for everyone?

Start with the justification of the perceived problem by Ontario and PEI, the two leading proponents of expanding the CPP. Ontario Premier Kathleen Wynne bases the need to expand CPP on "my understanding that there is a high degree of anxiety among people who are worried about their security in retirement." This ignores that people are genetically programmed to be perpetually anxious about their future standard of living.

The PEI proposal is based on simulations from an academic model that show some middle-class earners will see a drop in income on retiring, although not enough for them to qualify for support from the safety net that the GIS provides for truly low-income seniors.

Let's step back and look at the broader question of what is driving the alleged problem — is it real or is it the result of shaky assumptions? And what are the broader implications of higher taxes and pension benefits for long-run potential growth, the best assurance of future income security for everyone?

This raises the question about the usefulness of models for policy-making. Their recent track record is hardly inspiring. The same models being used to predict a pension crisis decades down the road forecast incorrectly that the welfare reforms of the mid-1990s would aggravate poverty.

Part of the problem is the inability of models to anticipate the complex range of reactions and intra-family transfers that characterize real life. Families, not government, are the quickest to help a member feeling the pinch of lower incomes. Not so long ago, papers were full of reports of how the boomer generation would be on the receiving end of the largest inter-generational inheritance of wealth in history, a transfer not accounted for in models.

Models have proved unable to predict broad changes in the macro-economy, never mind micro changes in household finance. Macroeconomic models famously failed to predict the 2008 recession, partly because of their inability to account for bubbles in the stock market and housing.

In fact, an over-reliance on models contributed much to the recent downturn. After all, it was the notorious Black-Scholes model of options pricing and risk that opened the floodgates to trading in derivatives that helped trigger the financial crisis in 2007. Ratings agencies used statistical models to evaluate sub-prime mortgages packaged as AAA-rated debt, based on historical patterns of default.

Of course, models sometimes can provide useful insights, when their results are supported by theory: The Russian economist Nikolai Kondratieff (of the 50-year 'Kondratieff wave' fame) was executed on Stalin's orders during the Great Purge of 1938 when his econometric model accurately predicted that collectivizing Russian agriculture would result in sharply lower farm output.

Alan Greenspan, former Chair of the Federal Reserve Board, has weighed in on the broader impact of social security benefits on long-term growth, the overarching theme of his new book, *The Map and The Territory.* He is emphatic that rising social security benefits have "crowded out capital investment at a virtual dollar-for-dollar rate that, in turn, has significantly lessened our rate of economic growth."

This is because the increase in social security benefits was used to finance higher current consumption, but every dollar diverted to social security was offset by lower domestic savings in the private sector. This lower private savings rate was reflected in reduced business investment, which led to the long-run erosion of productivity growth and incomes.

Ironically, Greenspan concludes, "the resources required to augment the benefits of the elderly came largely at the expense of the lower income quintile households, almost wholly through suppressed wage rate gains." It is hard to imagine a clearer statement that opposing CPP expansion is not based on ideology, as some critics claim, but because it's a direct threat to higher long-term economic growth that is ultimately needed to secure incomes.

Greenspan frames the fundamental question as "Do we wish a society of dependence on government or a society based on the self-reliance of individual citizens?" This is essentially the question posed by asking whether Canadians want to restructure retirement funding by expanding the CPP or relying on individuals to contribute voluntarily to Pooled Registered Pension Plans. One choice leads to expanding the 'dead hand' of bureaucracy, the other paves the way to increased self-reliance and fosters a spirit of entrepreneurship.

Part of the problem is the inability of models to anticipate the complex range of reactions and intra-family transfers that characterize real life. Families, not government, are the quickest to help a member feeling the pinch of lower incomes.

This is not the time to debate the pros and cons of evidence-based policy. It is noteworthy, however, that proposals to expand the CPP are based exclusively on feelings of anxiety or, worse, on incomplete and misleading models of income dynamics projected decades into the future. It would be folly to risk dampening long-term growth potential on the basis of such flimsy foundations.

Philip Cross is a Research Fellow at the Macdonald-Laurier Institute and the former Chief Economic Analyst at Statistics Canada.

Under construction: The library at Attawapiskat's new elementary school.

Catching up on Aboriginal services is not cheap

In the Ottawa Citizen *(December 20, 2013), MLI managing director Brian Lee Crowley noted that headline-grabbing figures about federal spending on Aboriginal Affairs mean little when one considers decades of neglect and mistreatment of Aboriginal peoples, and the high costs of delivering services to remote regions. Suggested Crowley, "Government spending, rather than a proxy for generosity, however, is actually a measure of our failure to open real opportunities for Aboriginals."*

Brian Lee Crowley

The Fraser Institute got mileage out of its recent survey of government spending on Aboriginal people. Headline-grabbing numbers — per capita spending on Aboriginal Affairs has risen 880 percent from 1950 to the present! — certainly attract attention, but add little to the debate about what governments can and should do with and for Aboriginal people.

Yes, government spending has risen dramatically. Using 1950 as a baseline ensures the comparison captures the rapid expansion of state welfare programming — residential schools, settlement on reserves, income assistance and a major expansion of health care services (not restricted to Aboriginal people, of course) — after the Second World War. Government spending has escalated because governments did a lot more to Aboriginal people, often without their approval.

As my friend and colleague, University of Saskatchewan Canada Research Chair Ken Coates, reminds me however, the past 40 years or so have seen a revolution in the relationship between Aboriginal and non-Aboriginal Canadians that replaced decades of neglect and worse.

There are new programs and services, from support for post-secondary education to the negotiation and settlement of Aboriginal land and legal claims, which were not part of the pre-1970s picture. Aboriginal legal victories produced judgments that must now be honoured.

Federal-provincial gamesmanship has finally started to give way to a greater recognition by provinces of their responsibilities, but catching up is not cheap.

Moreover the fallout of unhappy experiences with treaty implementation, residential schools and long neglect mean that Aboriginal people frequently want to administer their own programs, requiring expensive capacity-creation. Nor do most Aboriginal governments have access to the own-source tax revenues that mostly finance other governments' activities.

At a very practical level, as the Fraser Institute recognizes, the high cost of delivering services to remote reserve communities adds significantly to spending. Providing the most basic services, such as safe drinking water, is hugely higher in northern Ontario fly-in communities than in the south.

Government spending, rather than a proxy for generosity, however, is actually a measure of our failure to open real opportunities for Aboriginals.

Money spent on income support, medical intervention and socio-cultural crises would decline dramatically (and has already done so) when local Aboriginal economies improve. Popular prejudice aside, most Aboriginal communities are determined to shake off the oppressive culture of welfare dependency.

To understand it properly, spending on Aboriginal people needs to be compared, not with spending on the average Canadian, but spending on Canadians similarly situated to Aboriginal people. Well-designed programs concentrate money where the need is greatest.

In this regard, as the funding for education and basic infrastructure shows, federal spending is too low, leaving many Aboriginal Canadians in conditions other citizens would find appalling. By this accounting, government spending is less than adequate, particularly for neglected northern regions.

Canada has long striven to ensure that all Canadians have reasonably comparable opportunities. While Prince Edward Island lacks Alberta's economic strength, federal transfers help the two provinces provide residents with a rough equality of opportunity, a situation that does not hold for the vast majority of Aboriginal Canadians, even with the current level of federal government spending.

The Scandinavian countries do a much better job than does Canada of providing equality of opportunity for Indigenous people and those living in isolated regions.

As we honour our commitments under treaties and the Constitution, government spending has certainly risen. Out of context, that rise can look huge and disproportionate. Placed against the challenge of providing real opportunities for Aboriginal Canadians, it looks very different.

Government spending, rather than a proxy for generosity, however, is actually a measure of our failure to open real opportunities for Aboriginals.

Money spent on income support, medical intervention and socio-cultural crises would decline dramatically (and has already done so) when local Aboriginal economies improve.

No doubt some of the money is poorly spent; of vastly more importance, however, the combination of historical damage to Aboriginal communities, *Indian Act* constraints, misplaced government intervention decades ago, and the realities of location, have left governments and Aboriginal communities struggling to secure what other Canadians take for granted.

One national politician, speaking about the debate over funding for Aboriginal education, said that money was not the solution, but that solutions cost money.

Presenting statistics on Aboriginal funding outside this essential context adds little to our understanding of one of the most important challenges facing Canada today.

As Aboriginal people respond to resource development opportunities, become more entrepreneurial, complete more post-secondary training and education and enter the workforce in greater numbers, government spending on Aboriginal affairs will moderate.

The evidence is already there for those with eyes to see. Until then, creating the possibility for Aboriginal Canadians to enjoy even remotely comparable opportunities with the rest of Canadians will continue to be expensive, difficult and frustrating.

But the cost must be measured against the size of the task and the important progress already made.

Brian Lee Crowley is managing director of the Macdonald-Laurier Institute

The case for partial upgrading of raw bitumen in Alberta

Mike Priaro, an engineer with over 25 years experience in the petroleum sector, lays out a detailed economic argument for why the Alberta and federal governments should require partial upgrading of raw bitumen prior to export. Priaro suggests that the two governments should take steps to legislate, regulate, and/or discourage the export of raw bitumen.

Mike Priaro

"…what's really important to me is that … we process the bitumen from the oil sands in Alberta which creates a lot of jobs, and a lot of job activity, and… that would be a better thing to do than merely sending the raw bitumen down the pipeline."

—the late former Alberta Premier Peter Lougheed in an interview on September 13, 2011.

The transport and export of raw bitumen as dilbit — heavy crude and/or bitumen that has been blended with a dilutant for the purpose of meeting pipeline viscosity and density specifications — is one of the biggest economic and environmental problems faced by Albertans. If all exports were upgraded bitumen and conventional crude, Albertans would have far fewer problems getting export pipelines built and all Canadians, especially Albertans, would obtain far greater economic benefit from the bitumen sands.

The Energy Review Control Board's (ERCB) *Alberta's Energy Reserves 2012 and Supply/Demand Outlook 2013–2022* report conservatively forecasts Alberta petroleum production of 4.2 million barrels per day (bbls/d) by 2022, of which 3.6 million bbls/day is marketable crude bitumen. Of that marketable crude bitumen, only 1.3 million bbls/d, or only 36 percent, will be upgraded bitumen — mainly syncrude — while the remaining 2.4 million bbls/d will be raw bitumen exported as dilbit.

All natural gas producers in Alberta must pay to build and operate gas plants (or pay a processing fee) to remove water, hydrocarbon liquids and other impurities from raw natural gas and to compress the gas for pipelining.

Similarly, Albertans and Canadians must insist that producers of dilbit pay to build and operate plants to remove condensate diluent, and impurities such as fines, sulphur, acidity, heavy metals, salt, asphaltenes, and nitrogen, from the raw bitumen to make it pipeline-quality, and to reduce its viscosity to make it pumpable without requiring diluent thereby making its transport much more environmentally-acceptable.

Partial upgrading of 2.4 million bbls/d of raw bitumen, contained in 3.4 million bbls/d of dilbit, could be accomplished by several dilbit "straddle-plants" near Fort McMurray, Edmonton, Hardisty and/or Empress, AB. These would custom-process multiple streams of condensate-diluted raw bitumen from producers with economies of scale and recycle recovered diluent back to producers. Mixing syncrude and conventional light crudes into the upgraded bitumen further improves pipeline quality.

Large-scale partial-upgrading straddle plants for dilbit are analogous to nine existing large straddle plants in Western Canada located on major gas pipeline systems. These plants are designed to extract incremental amounts of ethane and other hydrocarbon liquids for use as petrochemical feedstock from billions of cubic feet per day of natural gas exports.

Partial-upgrading straddle plants for dilbit will produce off-gases to augment declining supplies of petrochemical feedstock from declining throughputs in existing natural gas straddle plants. In some cases they could be located adjacent to existing natural gas straddle plants.

A dilbit partial-upgrading straddle plant would produce just enough upgraded bitumen to produce pipeline-quality crude when mixed with cleaned raw bitumen. An example of such a process is Universal Oil Products' (UOPs') Catalytic Crude Upgrading process, which utilizes fluidized catalytic cracking to upgrade raw bitumen to pipeline specifications.

A proven, stand-alone, self-fueled process of 98 percent efficiency — compared to the 80-90 percent efficiency (ERCB, *Alberta's Energy Reserves 2012 and Supply/Demand Outlook 2013–2022*) achieved by existing coking-type upgraders, it produces all of its own energy and produces no waste by-products such as petcoke, as do all current upgraders.

The cost of large-scale partial-upgrading straddle-plants for dilbit will be more than recovered by:

- elimination of diluent premium cost above West Texas Intermediate (WTI) estimated at \$6/bbl of bitumen;
- elimination of shipping cost estimated at \$7/bbl of bitumen to import diluent using trans-border pipelines;
- elimination of losses estimated at \$10/bbl of bitumen on diluent sold as dilbit below WTI;
- higher price estimated as several \$/bbl obtained for partially-upgraded bitumen above Western Canadian Select (WCS) price;
- re-cycling of diluent close to the source;
- the need for 30 percent fewer export pipelines;
- re-cycling proprietary diluents back to producers from upgraders within the province would allow the use of more expensive solvents to extract raw bitumen more efficiently, increasing recovery factors and reducing the high Green House Gas (GHG)

emissions of in situ extraction by reducing the amount of steam required;
- lower costs for upgraded bitumen pipelines;
- the higher efficiency of a UOP-type upgrading process;
- economies of scale;
- proportionately smaller volumes to be upgraded;
- less demanding specifications for pipeline-quality crude compared to syncrude;
- lower costs to ship partially-upgraded bitumen by rail car versus raw bitumen or railbit;
- conversion and reversal of diluent import pipelines to export petro-chemical feedstock and upgraded bitumen;
- sale of upgrader off-gases as petro-chemical feedstock;
- value-added at petrochemical plants;
- greatly reduced pipeline and marine shipping environmental risk; and last, but not least
- an enhanced "social licence" to produce the bitumen sands.

Furthermore, bitumen royalty calculations in Alberta are based on the gross revenue of a bitumen project, which is defined as the revenue collected from the sale of bitumen and products (or the equivalent fair market value) less the costs of any diluents contained in any blended bitumen (dilbit) sold.

This calculation effectively subsidizes bitumen producers who produce and sell dilbit. This is to the disadvantage of companies who produce and upgrade raw bitumen. This is also to the disadvantage of Albertans who are denied royalties and to Canadians who are denied the economic benefits of upgrading and refining, petro-chemical industries and their support and service jobs, and government revenues from a wide range of associated taxes.

In total, estimated benefits as a result of partial upgrading of raw bitumen in Alberta are more than $25/bbl of bitumen, not including the benefits noted in points 5 through 18 above.

Refineries in the rest of Canada and elsewhere may benefit from joint investment in large-scale partial upgrading in Alberta instead of spending billions on an upgrading coker to handle smaller volumes of heavier, sour raw bitumen at individual refineries.

There are two or three pilot projects being worked on by small companies. However, there are no commercial partial upgrading operations in Alberta at this time nor has any significant research or development been done in this area by government or academia.

Compounding the problem, many research and policy chairs at the University of Calgary and the University of Alberta are funded by foreign multi-nationals like ExxonMobil, through Canadian subsidiaries. Industry is unlikely to initiate large-scale partial-upgrading of raw bitumen.

Foreign multi-nationals like ExxonMobil, which through Imperial Oil owns 78 percent of the just-commissioned Kearl project — the first bitumen surface strip mine without an upgrader — would rather send cheap, low-royalty raw bitumen to their refineries on the Gulf Coast where the bitumen will be processed into diesel for export at high margins to Latin America. They want to capture all the benefits of raw bitumen at the expense of Albertans and Canadians.

The recent announcement of a second bitumen surface strip mine without an upgrader is a disturbing trend. In October, Canada's largest energy company, Suncor, announced it was proceeding with the Fort Hills bitumen sands surface strip mine project. Fort Hills' $13.5 billion cost will be split by Suncor (40.8 percent), Total (39.2 percent), and Teck Resources (20 percent). It is expected to start production in late 2017 with a design capacity of 180,000 bbls/d.

Suncor says Fort Hills will join ExxonMobil's nearby Kearl project as the second bitumen surface strip mine without an upgrader. Together, at full capacity, they will export a total of 525,000 bbls/d of raw bitumen contained in 750,000 bbls/d of dilbit – coincidentally the capacity of Keystone XL for Canadian production. It means Albertans and Canadians will not benefit from bitumen upgrading, refining, and petro-chemicals.

Based on $50/bbl for raw bitumen and $200/bbl for refined products, assuming $1.25/litre, these projects will cost Canadians $29 billion per year in lost upgrading, refining and petrochemical jobs, profits, royalties, and taxes. And, it means every Albertan will be subsidizing increasing exports of raw bitumen because the cost of diluents in dilbit is deducted when determining market value for royalty calculations.

In the US, exports of crude are prohibited by federal law — unless determined to be in the US national interest — in order to conserve domestic oil reserves and discourage foreign imports.

While Canada does not have an urgent need to conserve domestic oil reserves, exporting raw bitumen as dilbit is not in Canada's national interest from every other possible perspective: energy security, jobs, taxes, royalties, the environment, and to discourage foreign imports, and perhaps ought to be similarly prohibited by legislation in this country.

Alberta's and Canada's governments must legislate, regulate, and/or discourage the export of raw bitumen and encourage building partial upgrading straddle plants by investing in research and development; providing seed money and/or seed volumes; creating crown corporations; initiating joint ventures with refiners and producers; changing bitumen royalty structures to discourage raw bitumen exports; and/or imposing some type of tax or duty on raw bitumen exports.

Mike Priaro, B.Eng.Sc. (Chem. Eng.), worked in facilities, production, operations and reservoir engineering, as engineering consultant, as area superintendent, and in engineering management in Alberta's oil patch for 25 years for companies such as Amoco and PetroCanada. He was awarded Lifetime Membership in the Association of Professional Engineers and Geoscientists of Alberta in 2009. He increased oil production from the historic Turner Valley oilfield and brought in under-balanced drilling technology to drill out, complete and test several of the highest producing gas wells ever on mainland Canada at Ladyfern. He co-authored "Advanced Frac Fluids Improve Well Economics" in Schlumberger's Oilfield Review and developed the course material for the "Advanced Production Engineering" course at Southern Alberta Institute of Technology.

Pictured: Their Royal Highnesses and the Honourable Jason Kenney, former Minister of Citizenship and Immigration with new citizens

Finding the right balance in Canada's citizenship policy

As the Government prepares to table revisions to the Citizenship Act, *building on previous measures to improve citizenship integrity, Andrew Griffith provides a look at longer-term issues. Griffith suggests that we live in a more global world, both economically and socially, and that citizens are increasingly mobile, with many having an instrumental approach to citizenship. Maintaining citizenship integrity, improving fairness, keeping Canadian citizenship competitive with other immigrant receiving countries, and strengthening citizenship understanding in this context will continue to be a challenge.*

Andrew Griffith

As the government prepares to introduce proposed changes to the *Citizenship Act* and continues to deal with the implementation of previous program changes, some longer-term thinking about the key objectives and elements of the citizenship program is in order.

This needs to take into account the focus on economic immigrants, both the traditional skilled worker and trade programs, as well as some of the newer elements that aim to attract more highly educated and entrepreneurial immigrants, like the Canadian Experience Class or the Start-Up Visa program, or other government initiatives to encourage diaspora economic links. Given both the dynamics of an increasingly continental and global economy, and given that higher educational qualifications likely mean more mobile immigrants, citizenship policy will need to take into account this changing mix and focus of the immigration program.

Traditionally, Canadian citizenship policy has balanced facilitation, or making citizenship easier to acquire for new Canadians, and meaningfulness, or ensuring integrity in citizenship tools and processes. Prior to the Conservative government, the overall trend, in both citizenship policy and programs, was towards facilitation. Citizenship, in an almost mechanical and sequential way, followed immigrant selection and settlement services, as part of a straightforward continuum. Notwithstanding this sequence, citizenship, given the relatively easy and short acquisition process, facilitated integration through extension of voting rights and other privileges.

The Conservative government, while remaining within the overall Canadian context, nevertheless made some major shifts towards greater meaningfulness, including: the more comprehensive study guide; Discover Canada; the related more difficult citizenship test; more rigorous application of language requirements; anti-fraud (residency) measures; increased public profile of the citizenship program and ceremonies; and support to the Institute for Canadian Citizenship (ICC) and its various activities. Taken together, these measures addressed weaknesses in the previous approach and improved the integrity of citizenship acquisition.

Similarly, the proposed changes to the *Citizenship Act* will likely also move in this direction, possibly including regulation of citizenship consultants, increased penalties for citizenship fraud, increased and more rigorous residency requirements, more effective revocation processes, and possible elimination of the current "birth on soil" grant of citizenship in favour of a more qualified right, among others.

While looking towards the future is always challenging, some trends are likely to continue, including:

- ongoing economic globalization, possibly leading to further restructuring, inequality and pressure for temporary foreign workers; and,
- ongoing social globalization, enabled by cheap travel, communications, and culture, making identity more fluid and varied.

The implications for citizenship policy are significant with respect to both these trends.

On the economic side, restructuring may lead to further inequality, possibly reducing current levels of support for immigration, including citizenship and multiculturalism, as the current Canadian approach may not be seen as delivering widespread economic benefits. The recent controversy over perceived abuse of the temporary foreign worker program by Canadian companies that replaced skilled Canadian workers with lower-cost foreign workers is a recent example.

On the social side, attachment and belonging may decrease as more people take advantage as opportunities open up to maintain their different identities, running against the wish of many governments to reinforce their respective national identities. Diaspora politics, whether humanitarian (e.g, Haiti, Philippines), "imported conflicts" (e.g., Tamil Canadians), or interest based (e.g., Israel, Ukraine), will likely continue to increase.

As we look at options for addressing these trends, some general principles may be helpful:

- Maintain citizenship program integrity and rigorousness;
- Ensure fairness and comparable opportunity to obtain citizenship among different communities and education levels;
- Maintain competitiveness of Canadian citizenship policies compared to other immigration-based countries;
- Ensure a citizenship focus in immigration, settlement and multiculturalism programs (i.e., permanent, not temporary residents);

Each of these general principles has implications that are worth examining.

On the economic side, restructuring may lead to further inequality, possibly reducing current levels of support for immigration, including citizenship and multiculturalism, as the current Canadian approach may not be seen as delivering widespread economic benefits.

Program integrity

One of the lasting legacies of the department's former minister, Jason Kenney, was greater integrity of the citizenship program. Examples include Discover Canada, a more rigorous and better administered citizenship test, more consistent language assessment, and a more active approach to combatting citizenship fraud, primarily related to residency. From a legislative perspective, imposing a first generation limit on passing on citizenship also reflects greater integrity in ensuring an ongoing connection to Canada and addressing some of the issues related to citizens of convenience.

While future governments may decide to change the content of some of these initiatives (e.g., a broader — or different — focus to Canada's history, society and culture than that in Discover Canada), the general approach of ensuring a more serious approach to citizenship, and greater program integrity, should be maintained as part of good government administration.

Fairness

One of the weaknesses of some of the changes introduced over the past 5 years pertains to implementation short-cuts and approaches that made citizenship less fair and harder for groups with lower educational or language levels (e.g, immigrants or refugees from Afghanistan, Somalia, Cambodia, Burma, Vietnam).

Revising Discover Canada, or writing any new guide, in plain English at the appropriate language level would be one element; ensuring systematic focus group testing of citizenship materials, including test questions, would be another. Broadening settlement services beyond language training to address some of the challenges faced by particular communities in understanding the citizenship study guide and preparing for the test would also improve fairness.

Competitiveness

Canada's balance between facilitation and meaningfulness in relation to other countries is one element in attracting economically skilled and mobile individuals to Canada. Citizenship guides, tests and language requirements are largely not an issue for these groups (although there may be some impact on family members that accompany them). The main factors in relation to the competitiveness of citizenship relate to residency requirements, both with respect to duration of residency required as well as the degree to which absences from residency are handled.

Like all policy choices, it is hard to craft options that address the diverse needs of people applying for citizenship. Immigrants who choose Canada for economic reasons may have a more instrumental view of citizenship, given their mobility options. Providing them greater flexibility, without weakening the meaning of citizenship, or providing additional opportunities for citizens of convenience, will be a challenge.

Given the need to ensure Canadian residency as part of the integration process, there are risks in allowing too much flexibility on absences from Canada. The government has signalled its intent to increase residency requirements, in terms of requiring physical presence and the length of time required (possibly four years out of six). This would still keep us in line with some of Canada's competing countries (e.g., Australia), provided that our processing times shrink drastically and also become competitive.

There may be some mobile professionals (ranging from aircraft pilots to executives) who may require additional flexibility. Future governments will have to decide whether the economic benefits of greater flexibility for mobile professionals, including the economic impact should their families reside in Canada, outweigh any reduced connection to Canada.

Arguments by some that Canada should allow municipal voting for permanent residents, and not require citizenship, are questionable, given Canada's current short residency requirement. Should future governments substantially lengthen residency requirements, or not address current lengthy processing, further pressure on municipal voting may emerge.

From a meaningfulness perspective, and given that voting rights, along with access to a Canadian passport, are the most concrete benefits, it would be preferable to maintain the linkage between citizenship and local voting rights.

Citizenship focus and understanding

Many of the initiatives to improve integrity increase the focus on making citizenship more meaningful. In addition, while the number of special citizenship ceremonies has increased — with ceremonies reinforcing symbols like the RCMP and the military — and the Institute for Canadian Citizenship has developed an active program of enhanced citizenship ceremonies and other activities, there has not been a systematic review of the gaps and opportunities to reinforce this major touchpoint for new Canadians.

There are opportunities, in particular, to strengthen citizenship understanding in Quebec, through a mixture of more intimate citizenship ceremonies (Quebec holds "mega ceremonies" of several hundred, in contrast to the rest of Canada, where the average is more around 50-60) as well as considering whether other initiatives should be considered given that immigration selection and settlement services have been devolved to Quebec and that Canada has few other policy levers to increase federal presence in Quebec.

Another element of citizenship focus is the need for service standards. Current processing time in Canada is over two years; in Australia, it is two months. Surely, both from a service perspective, as well as competitiveness measure, Canada should align its application and business processes around a service standard.

We may not be able to match Australia (though we should ask "why not?"), but we should aim for a service standard of no more than one year.

As governments look at future citizenship and related policy agendas, more creative thinking is required on how to balance citizenship as "place," assuming that citizens remain in their country of immigration, and citizenship as "status," or a more instrumental view of citizenship as a means to secure employment and other rights.

Like all policy choices, it is hard to craft options that address the diverse needs of people applying for citizenship. Immigrants who choose Canada for economic reasons may have a more instrumental view of citizenship, given their mobility options. Providing them greater flexibility, without weakening the meaning of citizenship, or providing additional opportunities for citizens of convenience, will be a challenge.

The upcoming changes to the *Citizenship Act* provide an opportunity for parliamentarians and Canadians to reflect upon the balance question, taking into account integrity, fairness, competitiveness, and improved citizenship understanding.

Andrew Griffith is the author of Policy Arrogance or Innocent Bias: Resetting Citizenship and Multiculturalism. *He is the former director general for Citizenship and Multiculturalism at Citizenship and Immigration Canada. He has worked at Canadian Heritage, Service Canada, Industry Canada and Privy Council Office, in addition to Foreign Affairs and International Trade Canada, where he had a number of domestic and international assignments.*

How the Senate can be effective even if it isn't equal or elected

Senator Stephen Greene has a prescription for enhancing the Upper Chamber's credibility and effectiveness. He asserts that if the requirements of partisanship typically displayed in the House of Commons are replicated in the Senate, then Senate independence, or effectiveness, is gone and, with it, the relevance of the institution. The Senator offers some intriguing recommendations aimed at reducing partisanship and reinforcing the Senate's effectiveness, including its mandate to represent Canada's "regional divisions."

Stephen Greene, Senator

Can the senate be effective if it isn't equal or elected? My quick, short answer is: Yes, but it depends on a few changes.

We all know the dream of the Triple-E — that the senate should be equal, elected and effective. We all understand that provincial equality would require a constitutional amendment; although we also know that we've always had a kind of constitutional regional equality of 30 Atlantic senators; 24 from Quebec; 24 from Ontario; 24 from the West and 3 from the North. Whether you think this suffices for equality unfortunately depends on where you live. Regarding elections, the Supreme Court will tell us later this year if the Government can proceed legislatively or must amend the constitution.

In the meantime, the senate is beset with problems of effectiveness — "the third E" of the Triple-E. Canadians are asking why we have a body that does the same thing as the House of Commons and isn't even elected? Of course, the senate wasn't constituted to do the same thing as the Commons. And the fact we have only one elected House was preferred to the American system that is often seized by gridlock.

I believe Canadians wonder about the senate's effectiveness for two reasons. First, few understand what the senate does, or is supposed to do. And for decades, the senate's performance hasn't added to its reputation as a meaningful body. At times, it seems little more than an appointed copycat of the Commons. Essentially, this is the effectiveness, or relevance, issue.

In 1865, John A. Macdonald tackled the issue of effectiveness in three succinct sentences:

> *"There would be no use of an Upper House, if it did not exercise, when it thought proper, the right of opposing or amending or postponing the legislation of the Lower House. It would be of no value whatever were it a mere chamber for registering the decrees of the Lower House. It must be an independent House, having a free action of its own, for it is only valuable as being a regulating body, calmly considering the legislation initiated by the popular branch, but it will never set itself in opposition against the deliberate and understood wishes of the people."*

Let's examine Macdonald's words. In the first sentence he confirmed the senate's role of "opposing or amending or postponing the legislation of the Lower House." Notice he didn't say, "defeating." One could argue that "opposing" means "defeating" but the third sentence makes clear what his intentions were when he says, "but it will never set itself in opposition against the deliberate and understood wishes of the people."

Notice Macdonald said, "people," not Lower House. Thus he is giving the senate discretion such that if "opposing" can mean "defeating" it can only mean it in exceptional circumstances, not very often, and not when public opinion clearly supports the legislation under review. In other words, the senate's role, because it was to be unelected, is to perform a kind of balancing act.

For me, Macdonald points to a solution to the Senate's modern day effectiveness problem. One is his clear statement, that the senate "would be no value whatever" if it was merely passing Commons legislation without amendment and that it could avoid this fate if it was "an independent House, having a free action of its own." He also says a Senator's job is, "calmly considering the legislation." He knew from experience that the popular branch doesn't calmly consider anything so for the senate he is recommending the antithesis of partisan action and behavior.

I think Macdonald was right: the senate needs to be independent and consequently less partisan to be effective and relevant. The senate might be less independent now than any time in our history if only because there are more senators appointed by the prime minister of the day than at any other time. Certainly most of us, including me, feel a personal loyalty to the person who appointed us that we won't feel for succeeding prime ministers. This is only natural. But there's a problem if that loyalty is so strong that it erodes the ability of the senate to function independently.

At one level, such loyalty is good for the prime minister because his legislation won't be held up. But, when the senate doesn't function independently its relevance is questioned and this can reflect on a prime minister who has appointed most of the senators: Catch-22. Thus, it is both a constitutional duty and a political obligation for senators, especially those in the Government party, to ensure the senate's independence within its constitutional limits.

The first thing all senators should recognize, I believe, is that when they come into the Chamber or sit in committee they should be senators first and party members second. This doesn't mean that anyone's vote will necessarily change as a result of that self-recognition but it acknowledges that the place for partisanship is the Commons, not the senate. Indeed, partisanship is necessary in the Commons because the goal is to put a compelling, cohesive choice before voters. In the senate, partisanship is a barrier to the goal of "calmly considering the legislation," or in other words, to "sober second thought."

For me, Macdonald points to a solution of the Senate's modern day effectiveness problem. One is his clear statement, that the Senate "would be no value whatever" if it was merely passing Commons legislation without amendment and that it could avoid this fate if it was "an independent House, having a free action of its own."

If the requirements of partisanship that are displayed naturally in the Commons are replicated in the Senate, then Senate independence, or effectiveness, is gone and, with it, the relevance of the institution.

Relevance, as well as the perception of it, is important because Canada needs an Upper House. It should not be easy to pass legislation that changes the country. It should be slow and difficult. There should be opportunity, lots of it, to express opposition and to introduce evidence and argument, both contrary and supporting. This is a necessary senate function through its "opposing or amending or postponing" power as Macdonald said.

The power of the House of Commons is so great that, without a senate, Canada could be like a car without brakes going downhill. Until we have senate elections, the senate might be only a handbrake but it still has the potential to slow us down and avert an accident.

There are things the senate can do to diminish opportunities for partisanship and consequently enhance its effectiveness and relevance. Some of these are below. None are new ideas.

The senate was designed to represent the regional "divisions" listed in the Constitution, but its practices have drifted from this orientation.

Instead of caucusing according to regional divisions, senators caucus the way MPs do — with their national parties. For senators to become effective they must reorient their representation from the partisan.

Whether senators attend their national caucus or not, all senators from a region should caucus together, irrespective of party. This would enable senators from a region to work on issues important to a region, like the Constitution mandates, reestablishing the regional representation aspect of the Senate.

Question Period should be reformed, if not eliminated. A friend of mine says it reminds him of pro-wrestling, a shadow of the real thing in the Commons. Like pro-wrestling, it is farcical. Questions dealing with the latest media issue or any issue not on the Order Paper should be ruled out of order.

Question Period is worse than a waste of time. It is a catalyst for partisanship that can make the rest of the session more difficult. It epitomizes how the Senate copies the Commons to its detriment.

The Senate Speaker and Senate caucus officers should be elected by senators rather than appointed by party leaders in the House of Commons. The exception could be the person on the Government side responsible for managing the progress of Government bills in the Senate. Senators electing their own officers is vital for Senate independence from the Commons.

Committee chairs and vice chairs should be elected by senators rather than appointed by Senate Leaders who in turn were appointed by party leaders in the Commons. If caucus officers were elected by senators, the issue of electing committee chairs might be less important. Whether committee chairs should be elected by the committees on which they serve or by the entire Senate is a matter of debate.

The Senate parties sit two sword lengths apart, facing each other, ready for combat. But why, when unlike in the Commons, such combat serves no purpose and encourages the worst?

Instead, we should sit theatre style by region, province or even alphabetically. We should not only be different from the Commons, we should look different.

After we have made these changes and reoriented the Senate towards greater effectiveness, we should open our sessions to television. Proceeding with television before changes are made could increase partisan displays and delay those necessary changes. The Senate should embrace the goal of becoming the most open and transparent political institution in the world.

Partisanship in the Senate is a reflection of longstanding institutional practices that have grown over time. Only senators can change these practices. Indeed, the Senate has been told publicly by the Prime Minister to fix itself. If senators don't, we are helping the abolitionists.

So, can the Senate be effective if it isn't equal or elected? Yes, but it depends on whether senators recognize that their effectiveness depends on the extent to which the institution is independent of the House of Commons and "having a free action of its own," like Macdonald said.

In the 1980s, Stephen Greene served in Canada's foreign service, where he focused on Canada's interests in fishery issues. He later worked as an executive advisor in Atlantic Canada's fishing industry. He was chief of staff to Reform Party Leader Preston Manning from 1993 to 1996. He later worked in the insurance industry. In 2006, he became principal secretary to Nova Scotia Premier Rodney MacDonald. Stephen Greene was appointed to the Senate of Canada in December, 2008.

NAFTA is falling short of its potential

Writing in the Globe and Mail *(January 10, 2014), MLI managing director Brian Lee Crowley suggested that for all its successes, "North America seems to be a perpetual disappointment as economic power blocs go." He points out that the members of the European Union, formerly torn by war, have done much better in creating an enormous and open free-trade area, and an integrated Asia is coming together with the nascent Trans-Pacific Partnership.*

Brian Lee Crowley

Like a hockey player who looks great on paper but never quite lives up to his star billing on the ice, North America seems to be a perpetual disappointment as economic power blocs go.

For all its manifest faults, the European Union has created a vast free-trade area, with open internal borders, free movement of goods, capital and people, and common institutions, where before there had been only bickering nation-states that had dragged the world repeatedly into war.

In Asia, while the institutions lag, the reality is of a vast integrated economic machine where Japanese, South Korean and Taiwanese capital and know-how combine with Chinese, Vietnamese and Indonesian workers and natural resources and complementary economies to create the world's manufacturing centre. The institutions to match Asia's degree of economic integration are now being forged in the Trans-Pacific Partnership (TPP).

But after a few early successes, like the original Canada-U.S. free-trade agreement and its trilateral successor, the North American free-trade agreement (NAFTA), efforts to create the institutions of an economically integrated North America have essentially stalled.

The logic of closer integration is impeccable. The three countries together have much of what a successful industrial economy requires: capital, managerial know-how, entrepreneurism, workers, natural resources, complementary economies. As Mexico modernizes, we increasingly have convergence on democratic values, the rule of law and strong domestic institutions.

Obstacles at the border cost us all dearly. The U.S. reluctance to permit the construction of the Keystone XL pipeline is costing Canada billions of dollars in lost export earnings for no reason that stands up to rational scrutiny. Ditto for rules of origin for pork and beef. Congestion at the U.S.-Canada border alone costs American companies $10-billion annually.

Because of the integration of the North American auto industry, cars repeatedly cross both borders at various stages of production, and costly border delays are, in effect, a tax on our shared industrial production that foreign suppliers do not face. Our failure to match our degree of economic integration with supportive political institutions costs all three nations, and benefits our international competitors.

When you consider the American reliance on Canadian energy, as well as supplies of parts and other inputs in various manufacturing processes, there is hardly an American export that doesn't have a significant Canadian component, and vice versa.

Yet it is not further North American integration that brightens the eyes of decision makers in Washington. That's just boring and unglamorous. If you want enthusiasm, talk about a U.S.-EU trade agreement or the TPP. And unlike Europe, which bargains as a unit, North America's on-again-off-again partners bargain separately.

NAFTA is showing its age. Later trade agreements have dealt with many new issues, and Washington clearly relies on that to modernize relations with its NAFTA partners through the back door. Assuming that Canada, Mexico and the U.S. all join the nascent TPP, for example, any improvements it provides on NAFTA's provisions will automatically apply. But they'll also apply to other TPP members, like Vietnam and Malaysia, and eventually almost certainly China. Not exactly the route to constructing a robust North America that plays to its domestic strengths.

Responsibility can be laid at the door of all three NAFTA countries, but is chiefly down to Washington. While NAFTA enjoys majority support in U.S. opinion polls, it is anathema to the trade unions that swing influence in today's White House. The environmental movement has tied up Keystone XL's approval. Optimistic talk of "reshoring" manufacturing in the U.S. means less sympathy for the idea of shared North American production.

President Barack Obama's foreign policy rightly focuses on Asia, Middle East peace deals and Iranian nuclear capabilities, but in his presidency he has spent a scant few hours in Ottawa. We cannot build an integrated and competitive North America without the energetic engagement of the constituent parties.

There has been progress, like the Beyond the Border initiative. Canada has spent billions on border infrastructure to convince Washington of our bona fides on protecting U.S. security. But these are mostly technocratic adjustments within the existing framework.

Our politicians need to engage the public with a vision of North American leadership in the world, and workable institutions to match. Otherwise we will continue to limp along while our international competitors benefit from our languor.

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How Canada should deal with prostitution

In view of the recent Supreme Court of Canada ruling which found that existing criminal code offences related to prostitution infringe upon the Canadian Charter of Rights and Freedoms, Benjamin Perrin examines how other jurisdictions have addressed this particular challenge and offers some recommendations for how Canada should overhaul its approach.

Benjamin Perrin

The future of Canada's laws related to prostitution has become an urgent public policy issue in the wake of the Supreme Court of Canada decision in *Canada (Attorney General) v. Bedford.* Three prostitution-related offences in the Criminal Code were found to infringe the Canadian Charter of Rights and Freedoms and are to be struck down, effective within one year of the Court's December 20, 2013 decision. Parliament has this limited timeline to adopt any new legislative approach, or else Canada will face the de facto legalization of adult prostitution.

Studies have shown that street-level prostitution is just the tip of the iceberg, with most prostitution occurring indoors. The majority of prostitutes entered prostitution between 14 and 20 years of age, and a disproportionate number of them were sexually abused as children. Substance abuse is significant among street prostitutes; and marginalized women, including Aboriginal women, are particularly vulnerable to prostitution and more likely to face violence (including assaults, sexual assaults, and murder).[1]

Canada is not alone in grappling with how to address prostitution. A number of foreign jurisdictions were examined in the Bedford proceedings. Following a brief discussion of each of these, the following recommendations are made to address prostitution in Canada:

- Canada's objective should be to abolish prostitution;
- prostitutes should not be criminalized, but given help to exit; and
- target criminal laws and enforcement at pimps, traffickers, and johns.

The Netherlands

Since October 1, 2000, the Netherlands has sought to regulate and control prostitution by means of licensing brothels, which are to abide by various health and safety regulations. In *Bedford*, Justice Himel found that this approach has been "moderately successful in improving working conditions and safety in the legal practice of prostitution."[2] She also found that in certain instances access to social services has helped addicted prostitutes overcome substance abuse and exit prostitution.[3]

> *In 1999, Sweden adopted a novel approach to addressing prostitution ... it opted to criminalize the purchasers of sex acts and pimps, but not to criminalize prostitutes themselves. Public awareness campaigns targeted at male sex act purchasers were launched to raise awareness about prostitution and human trafficking, alongside education programs for police about conditions that make women vulnerable to these crimes.*

However, illegal prostitution has flourished alongside this legalized prostitution sector. Justice Himel found:

> Approximately half of all prostitution occurring today in the Netherlands happens outside of this legal sector, and often involves foreign prostitutes providing out-calls set up by telephone and over the internet. Some evidence of the continuing involvement of organized crime in prostitution has emerged in recent years, and new regulatory reforms are being aimed at these syndicates. Recent United Nations reports suggest that there are approximately 20,000 women involved in prostitution in the Netherlands, with two-thirds of them coming from Eastern Europe and developing countries.[4]

New Zealand

Since June 2003,[5] New Zealand has "decriminalized consensual adult prostitution in all forms, and implemented a licensing regime for brothels."[6] A five-year review was completed by the Prostitution Law Review Committee (PLRC),[7] finding an increased likelihood of prostitutes reporting violence to police, and brothels possessing "safer sex" items. Citing this report, Justice Himel found that child prostitution and human trafficking did not appear to increase post-decriminalization in New Zealand.[8]

However, Justice Himel found that despite decriminalization, prostitutes continue to suffer "incidents of violence, threats, forcible confinement, theft, and refusal to pay for services", particularly among street-based prostitutes.[9] This form of prostitution has persisted in New Zealand, despite the hopes of proponents of decriminalization that it would decrease.[10]

Germany

In 2002,[11] Germany decriminalized brothels, abolished mandatory disease screening for prostitutes, and opted to no longer prohibit the promotion of prostitution. Pimping remains a crime, however. A three-year post-decriminalization review[12] concluded the following:

> The German Report states that no measurable improvements are detectable in achieving social protection for prostitutes, improving working conditions, encouraging prostitutes to exit the industry, or reducing crime. However, the fears that decriminalization would open the floodgates to organized crime, human trafficking, or the exploitation of minors have not materialized as a result of the legal changes.[13]

Australia (Queensland)

In Queensland, licensed brothels have been permitted since 1999, whereas escort agencies and street-based prostitution remain illegal. A five-year governmental review[14] of this regime was summarized by Justice Himel as follows:

> The Queensland Report concluded that sole operators, as a result of their complete isolation, are at greater risk of violence than their counterparts in legal brothels. Street-based prostitution, for which the legal reform created stiffer penalties, has been reduced through aggressive policing. According to the Queensland Report, 75 percent of the sex industry has not elected to move into the legal sector, and continues to operate contrary to the law. Decriminalization has not led to an increase in the size of the sex industry.[15]

United States of America (Nevada)

Since 1971, the State of Nevada has allowed licensed brothels to operate, except in Las Vegas. More recently, state law has required condom use during prostitution and mandatory sexually transmitted infection testing of prostitutes.[16] An academic study cited by Justice Himel found "numerous problems with brothel prostitution in the state" but that "[l]egal brothels generally offer a safer working environment than their illegal counterparts."[17] Another study cited by Justice Himel, however, challenged the notion of "safety" in legal brothels, stating: "Usually, however, women mean safe in comparison to other prostitution. Thus the concept of safety is relative, given that prostitution is associated with a high likelihood of violence."[18]

Sweden

In 1999,[19] Sweden adopted a novel approach to addressing prostitution, leaving decades of decriminalization behind. It opted to criminalize the purchasers of sex acts (johns) and pimps, but not to criminalize prostitutes themselves — instead programs exist to help them exit prostitution and alleviate poverty to prevent others from becoming prostitutes. Public awareness campaigns targeted at male sex act purchasers were launched to raise awareness about prostitution and human trafficking, alongside education programs for police about conditions that make women vulnerable to these crimes.[20]

Justice Himel found the following outcomes from Sweden's approach:

> Estimates suggest that the number of women involved in prostitution in Sweden has decreased from 2500 in 1999 to less than 1500 in 2002. The number of women in street prostitution has decreased from 650 in 1999 to less than 500 in 2002. Government reports suggest that there are almost no foreign women remaining in street prostitution, and there is some suggestion that human traffickers may now find Sweden to be an unattractive destination for trafficked women.[21]

In 2010, Sweden completed an independent inquiry, headed by a judge, to examine the impact of its approach in addressing prostitution.[22] Unfortunately, this report was released after the hearings in *Bedford* concluded in 2009 so it was not considered in the case. A summary of the report follows:

> It found that the Swedish model has disrupted organized crime, deterred sex act purchasers, changed public attitudes, and cut street-level prostitution in half. Plus it found no evidence that the problem simply moved indoors as some skeptics had speculated.

Importantly, the inquiry also found nothing whatsoever to suggest that Sweden's abolitionist model had negatively affected those being exploited. It recommended sustaining support for those being sold, creating a national centre against prostitution and human trafficking, and doubling the maximum penalty for purchasing sex acts to up to a year in prison.[23] Sweden's approach is growing in popularity and has recently spread to neighbouring countries like Norway and Iceland, such that it is now called the "Nordic Model."

A way forward for Canada

Decriminalizing/legalizing prostitution has not been the hoped-for panacea for protecting prostitutes. Such an approach could reasonably be expected to maintain street-level prostitution alongside a large illegal indoor prostitution sector, where none of the so-called "protections" exist, while lending prostitution a veneer of legitimacy and social approval by being authorized under law. Instead, a Canadian-version of the Nordic model is the best option moving forward.

Canada's public policy should have as its objective the abolition of prostitution because it is inherently harmful. Exiting prostitution is the only way to truly protect prostitutes and is closely connected to this objective. Support services are needed to help them do so, not the threat of criminal prosecution. Provincial/territorial governments and municipal governments need to do much more to work with non-governmental organizations at the street level to intervene to help prostitutes exit, fund detox facilities to help overcome substance abuse issues, and provide intensive support and assistance for those exiting prostitution to find gainful employment.

Prostitution would not exist without men who are willing to pay for sex acts. Their demand drives prostitution, yet few ever face criminal prosecution in Canada, and most remain completely anonymous. This needs to change. Criminal laws and enforcement should target johns, pimps and sex traffickers. It has also been suggested that they should pay substantial fines that could be used to fund exit programs for prostitutes.[24] There is merit in exploring this idea further.

In closing, Canada's public policy response to prostitution needs to be overhauled. Prostitution is inherently harmful. A Canadian-version of the Nordic model is the most likely to advance the goal of abolishing prostitution and could be constitutionally valid, if implemented properly.

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