

ALBERTA: THE NEW DOMINANT PLAYER IN CONFEDERATION?

Thomas J. Courchene



Alberta's economic and fiscal star is in ascendancy and is likely to remain so for some considerable time, given that it is at the centre of one of the world's premier energy clusters. The intriguing issue is whether the province can parlay this ascendancy into greater political influence in the federation. For this to occur, Alberta will need to frame key aspects of its policies within a context that extends beyond its borders. In selected areas it has done precisely this. Once the bastion of triple-e federalism, or symmetric federalism, Alberta has now embraced asymmetry, thereby helping pave the way for the 2006 federal resolution proclaiming that the Québécois form a nation within a united Canada. Challenges remain, however, and probably none is more complex and delicate than the energy-environment nexus.

La bonne étoile économique et financière de l'Alberta est au zénith et devrait y rester encore longtemps puisque la province se trouve au cœur d'un des premiers réseaux énergétiques du monde. Singulièrement, on se demande toutefois si elle saura profiter d'un tel ascendant pour accroître son influence politique au sein de la fédération. Pour ce faire, elle devra structurer certains éléments clés de ses politiques en fonction d'une conjoncture qui déborde ses frontières. Ce qu'elle a d'ailleurs fait dans quelques secteurs choisis. L'Alberta était le bastion du fédéralisme « triple E », ou fédéralisme symétrique, mais en se convertissant à l'asymétrie, elle a préparé le terrain à la résolution fédérale de 2006 établissant que les Québécois forment une nation au sein d'un Canada uni. Ses défis restent cependant nombreux, notamment celui du rapport complexe et délicat entre énergie et environnement.

While I am a native westerner (Wakaw, Saskatchewan), my hunch is that the principal reason why I was asked to comment on the “new” Alberta was to provide an Eastern (Ontario) perspective. I want to begin on a personal note by congratulating Alberta for its economic and fiscal ascendancy and by proclaiming that this is great news not just for Alberta, but for all of Canada. Indeed, this is great news globally. With huge endowments of fossil fuels in Alberta, Saskatchewan and British Columbia, with uranium deposits in Saskatchewan, with hydro power in Manitoba and with ample potential for grain-based and forest-based biofuels in all four provinces, western Canada is arguably donning the mantle of one of the world's premier energy clusters, even its most stable and reliable one.

Nonetheless, with this energy-anchored good fortune come both opportunities and challenges. While it is probably correct to note that the preponderance of opportunities reside with Alberta and the lion's share of the challenges fall on Ontario and the rest of Canada, this is not universally the case; and, in particular, Alberta's economic and fiscal pre-

eminence does not translate into a corresponding degree of political power and influence, as will be elaborated below.

Turning first to the good news or opportunities, apart from its investment portfolio Alberta is converting a significant portion of its depleting resource assets into longer-term, world-class, human-capital research and industrial clusters in health/medical research, biotechnology and fossil-energy technology, among others. This shift from resource capital to human capital constitutes a key component in ensuring Alberta's long-term sustainability. Moreover, all Canadians will surely welcome these centres of excellence, especially since they are complementary to, not substitutes for, economic and research activity elsewhere in Canada, i.e., they are in the nature of 21st-century “national public goods” with positive externalities for all Canadians. A second and related aspect of ensuring sustainability is to invest the royalties (in excess of those needed for budgetary purposes) in ways and forms that can be called upon to temper the potential for a return to a boom-bust cycle for the province. Appropriately, the

Canada West Foundation (CWF) has spearheaded research and public dialogue in this area.

Another area of opportunity open to Alberta, and again of benefit to all provinces, relates to the advancing of the role of the provinces in the federation. This would involve not only innovations relating to the design and

where “build it and they will come” is likely to be an apt descriptor.

In terms of creative approaches to policies within provincial jurisdiction, Alberta is my choice for the province that will likely lead the way by devolving meaningful powers and taxation to Edmonton and Calgary, the province’s global-city-region corridor, once again

given the genuine concern in the national policy community that the recent immigrant cohorts are not doing as well employment-wise (relatively and absolutely) as earlier cohorts, Alberta may be ready to take the lead in allowing private sector employers to play a much larger role in the immigrant selection process. If potential migrants have a job in hand before arriving in Canada this will certainly enhance their likelihood of prospering economically in our country. Since immigration is a concurrent power under the Constitution (albeit with federal paramountcy), the way is open for Alberta to have a major say in the composition of new entrants into the province’s private sector.

The revitalized annual First Ministers’ Conference, which Quebec helped morph into the Council of the Federation, represent major landmarks in terms of the provinces moving in the direction of adopting pan-Canadian perspectives. Given Alberta’s booming economy and its need to draw upon labour from across the country, the province ought to be, and is, keenly interested in preserving and promoting the internal economic union (as Ontario ought to have been, but wasn’t, when it ruled the roost).

delivery of provincial public goods and services but, as well, the promotion of a pan-Canadian provincialism and an internal economic union so that the provinces can come to grips with ways to internalize some of the cross-province externalities or spillovers of their collective policies and programs. In terms of the latter, the revitalized annual First Ministers’ Conferences, which Quebec helped morph into the Council of the Federation, represent major landmarks in terms of the provinces moving in the direction of adopting pan-Canadian perspectives. Given Alberta’s booming economy and its need to draw upon labour from across the country, the province ought to be, and is, keenly interested in preserving and promoting the internal economic union (as Ontario ought to have been, but wasn’t, when it ruled the roost).

an area of influential research spearheaded by CWF. In the knowledge era, decentralization cannot continue to mean only devolution from Ottawa to the provinces. Canada’s cities are arguably the most fiscally constrained of any cities in developed nations (federal or unitary), an anomaly that is increasingly problematical in an era where global city-regions are emerging as the dynamic motors of the information economy. We need to wholeheartedly embrace the principle of subsidiarity which, in the context of the ongoing democratization of information and technology, means that powers can be successfully be transferred downward and closer to the people by progressively empowering citizens and cities. As noted, Alberta is probably best positioned to lead all provinces in this devolution.

As a relevant aside, I assume that Alberta already selects the foreign professionals for the public sector clusters like health care and medical research. Why not extend aspects of this flexibility to private sector employers, where circumstances warrant?

Shifting the focus from opportunities to challenges, probably none looms larger for Alberta than the environment. Given the dual likelihood that (1) key aspects of environmental policy will be federal policy and (2) Canadians are likely to treat environmental principles as akin to the *Canada Health Act* principles, this sets the stage for Canada’s environmental policy to be viewed by Albertans as the new National Energy Program (NEP). Thankfully, California was first off the mark in unloading its own NEP on Alberta, and in the process effectively conveying the correct message that environmental issues have already transcended east-west Canadian politics. The good news here for Alberta ought to be that it has the fiscal and, perhaps more important, the fossil flexibility (in tandem with hydro and nuclear) to forge its own world-class, environmentally friendly approach to the energy sector, one that would make Alberta a global leader in this area.

The recent Alberta-BC TILMA (Trade, Investment and Labour Mobility Agreement) is a most welcome and significant move in this direction of creating a single inter-provincial market. This is particularly so because TILMA is open-ended in the important sense that other provinces are invited to join in and become full signatories. This is one of those catalytic initiatives

A final, but hardly exhaustive, provincial policy area relates to immigration. Alberta has attracted a huge number of in-migrants from the rest of Canada. Progressively, however, the in-migrants to Alberta will come from all corners of the globe, with exciting implications for the ethnic, cultural, linguistic, religious and, presumably, political diversity of the province. And

But to accomplish this, it will presumably have to work in harmony, energy-wise, with Manitoba, Saskatchewan and BC. This is but another way of saying that while Alberta may own the energy resources it will not be the sole author of the environmental policy relating to its energy sector. Indeed, just as Albertans kept Ralph Klein from flouting the CHA principles in reforming health care, so too will they ensure that Alberta will fall in line with overall national-cum-provincial environmental parameters and principles.

A second ongoing challenge is what I have clumsily termed "Dutch disease plus capitalization." The Dutch disease component is so labelled because it relates to Holland's experience with its North Sea oil. Essentially, the revenues from exports of offshore oil appreciated the Dutch currency, which in turn clobbered Dutch manufacturing. Transferred to Canada, Alberta's energy exports (as well as foreign investment in our energy sector) will lead to the appreciation of the Canadian dollar, which, in turn, will serve to undermine Canada's manufacturing sector. Actually, the dollar's appreciation helps Alberta by tempering the energy boom, since it reduces the amplitude of the Canadian dollar swings in energy prices (relative to US dollar swings).

There is a second-order effect which does affect Alberta's tradables sector. This is that the generalized energy-related overheating of the economy is being capitalized into wages, rents, housing prices and the like. This capitalization, when combined with the exchange-rate appreciation, obviously compromises the ability of Alberta to be competitive in the production of tradable goods. This is no doubt good news for Saskatchewan's tradables producers, since they will share in Alberta's boom.

However, the much greater challenge, even threat, is to central Canadian manufacturing. If there is a tendency for boom-bust scenarios in global energy prices, then our manufacturing sector is likely to fall on hard times. Specifically, the combination of the resulting Canada-US exchange rate volatility of the type associated with the Dutch disease and the high level of north-south trade and integration suggests that manufacturing would arguably be better served by fixed exchange rates with the US or, preferably, a North American version of the

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euro. I hasten to add that Bank of Canada governor David Dodge would earn my vote as the world's foremost practitioner of inflation targeting. The laudatory congratulatory comments from all quarters on the announcement of his retirement are richly deserved. With respect, however, flexible exchange rates are ill-suited to address these energy shocks, which are east-west within Canada, rather than north-south between Canada and the US. The underlying issue here is that the overall size of the Canadian econ-

omy is far too small to accommodate both one of the world's premier energy export clusters and a world-class export-oriented manufacturing sector under Dutch-disease-prone flexible exchange rates.

But since Ontario does not realize this, since Alberta is actually better off with flexible rates and since the mainstream economics profession as well as our business community seems ideologically wed to floating rates, I am left to puzzle where I have gone wrong in my reasoning, all the while witnessing what seems to me to be a decline in central Canadian manufacturing productivity and production.

Given, therefore, our revealed preference for flexible exchange rates, one helpful initiative might be for Alberta to take a page out of Norway's policy book and to invest a significant portion of its energy-related investment portfolio outside of Canada, thereby serving to ameliorate some of the potential for the operation of the Dutch disease.

Turning to the political realm, how does Alberta, as Canada's economic capital and the provinces' fiscal capital, manoeuvre on the political front when it constitutes less than 10 percent of the House of Commons and even less of the Senate? Complicating this is that the national political map tends to be dominated by regional blocs. Not too long ago, Alberta was Reform territory, 101 of 103 Ontario seats were in the Liberal fold, and the Bloc dominated Quebec. Arguably, one of the factors that made the federation work in the days when Ontario was dominant economically was that Ontario MPs, once elected, tended to view themselves as national, not Ontario, legislators. And this disregard for Ontario-related issues crossed party lines: Bay-Street-based finance minister Michael Wilson designated Montreal and Vancouver, but not



Photo by Janelle Schnieder, courtesy Calgary Herald

Construction cranes dot the skyline of downtown Calgary, symbolizing the oil-driven boom in Alberta. The province's ascendancy, writes Tom, is "great news not just for Alberta, but for all of Canada."

Toronto, as international financial centres; the Ontario Liberal MPs were openly hostile toward Ontario's Harris government; successive federal governments were indifferent to the "fair-shares" federalism pleas of Rae, Harris, Eves and McGuinty, and so on. Albertans may object to my positioning Ontario MPs as "national" legislators, but this is largely intended as backdrop to the real issue that may come into play for Alberta: in light of Ontario's (relatively, if not absolutely) diminished economic prospects, will its MPs now adopt (following in the footsteps of Alberta and Quebec) a much more "Ontario first" approach in the corridors of power? And if this comes to pass, it will surely create an even greater wedge between Alberta's economic and

fiscal clout on the one hand and its political influence on the other.

For this, among other reasons, Harper's "open federalism" should be music to Alberta's ears since it recognizes and respects the constitutional division of powers. Quebec likes open federalism because it provides the province with political room to manoeuvre, i.e., to become more of a nation within the Canadian state. Alberta needs open federalism in order to have socio-economic and jurisdictional room to manoeuvre, e.g., to exercise its fiscal flexibility to promote, *inter alia*, its longer-term comparative advantage within NAFTA economic space and even beyond.

While this is arguably part of the grand Quebec-West compromise that

underlies open federalism (and intriguingly recreates a version of Mulroney's Quebec-West bargain), the implementation process is bound to run into difficulties. For example, at the practical or operational level, several developments are serving to complicate the ability of Alberta to manoeuvre as it might like.

One is the reality that Alberta is drawing skilled workers (and unskilled as well) from the rest of Canada, thereby creating challenges for many provinces especially in terms of, for example, maintaining doctors and nurses. But Alberta is not targeting these professionals, per se, since it has to offer these wages to all such professionals in the province. Moreover, there are way more doctors and nurses who have left Canada for the US than will ever be attracted to Alberta.

Analytically, I view this as a non-issue in the sense that it follows directly from the operations of the “Dutch disease with capitalization” discussion. Politically, however, it is a loaded issue and, among other things, it will certainly lead to increased demands for equalization on the part of the poorer provinces in order to enable them to provide comparable levels of public services.

Having broached the equalization issue, there is a problem with the equalization-energy nexus. Specifically, energy royalties serve to drive up the 10-province average for equalization. However, since equalization payments come from Ottawa general revenues and since Ottawa cannot directly access Alberta’s energy rents, it is the case that the residents of the energy-rich “have” provinces do not pay their “fair share” of the equalization that results from energy entering the equalization formula (i.e., Alberta’s share of all-province fiscal capacity is much larger than its all-province share of federal taxes). One approach to this would be to exclude these energy revenues from equalization, but this would generate its own problems by widening the revenue gap between fiscally rich and poor provinces.

This concern over interprovincial fiscal equity is well-nigh intractable—for example, in his recent budget, Finance Minister Jim Flaherty introduced four equalization programs to attempt to come to grips with the issue and only partially succeeded. About a year ago I ventured into this area and tried to make the case for a voluntary interprovincial resource revenue-sharing pool. This attempt failed spectacularly. Not only were there no volunteers, but headlines in Alberta papers claimed that I was proposing another NEP. Undaunted, I have now shifted to a more nuanced (but again likely unsuccessful) approach. It begins by noting that equalization payments are like a

guaranteed annual income (GAI) for the provinces — it brings all of the less-well-off provinces up to some acceptable “standard.” Continuing with the guaranteed annual income analogy, Canadians who have sufficient income that they do not qualify for what passes for a GAI nonetheless do have some other federal transfers that are “income tested” — the Canada child tax benefit, EI payments, old age pensions. The comparable approach for the non-

In the context of the July 2004 Council of the Federation meeting, where all provinces agreed to transfer pharmacare to Ottawa but at the same time recognized that Quebec would maintain its existing program with full compensation, Premier Klein referred to the proposal as “brilliant.” Finally, the formal Quebec “asymmetry rider” attached to Paul Martin’s 2004 health care deal with the provinces would also be available informally to other provinces, in line with the Calgary Declaration.

equalization-receiving provinces would be to “revenue test” their other transfers. Accordingly, I have proposed that horizontal equity in the fiscal federalism context should consider revenue-testing of the vertical transfers (the Canada Health Transfer, Canada Social Transfer, etc.). One approach would be to claw back, say, 15 cents of the value of a province’s vertical transfers for every additional revenue dollar above a certain revenue threshold, say above 110 percent of the national average per capita revenue. At first blush, Albertans would probably rule out such schemes, even though they may have the virtue of falling squarely within Canada’s traditional and accepted approach to redistribution. However, this may not be an appropriate stance for Alberta since the province cannot avoid becoming involved in what is unavoidably a complex strategic game. The challenge will be how to make strategic arrangements, perhaps even concessions, in order to gain more room to flex its economic and fiscal influence in the interests of Albertans (and, one

presumes, Canadians as well) within our federation. The above proposal may or may not qualify as a strategic initiative, but it does illustrate the sort of challenges that Alberta will have to deal with: as Alberta’s economic and fiscal influence spreads well beyond its borders, so must the perspective within which it frames its challenges, opportunities and even responsibilities.

It is important to note that these strategic concessions need not be finan-

cial in nature. Indeed, Alberta’s actions helped paved the way for the 2006 federal resolution that proclaimed that the Québécois form a “nation within a united Canada.” This may seem passing strange since not much more than a decade ago Alberta was the bastion of triple-E federalism (rep by pop in the Commons, equal seats by province in the upper house and equal powers for all provinces). Yet in 1997 Premier Klein, as chair of the First Ministers’ Conference, oversaw the passage in all non-Quebec legislatures of the Calgary Declaration, which replaced the symmetry of triple-E federalism with a recognition of “the unique character of Quebec society” and went on to note that “the legislature and Government of Quebec have a role to protect and develop the unique character of Quebec society within Canada.” On the constitutional front, the Calgary Declaration stated that if any constitutional amendment confers powers on one province, these powers must be available to all provinces. This amounts to de facto *asymmetry* in the context of de jure *symmetry*. In the context of the July 2004 Council of the Federation meeting,

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The purpose of this detour has been to argue or at least suggest that Alberta has played a significant role in the evolution toward open federalism, even to the point of reversing some of its erstwhile stances on key political issues. The larger purpose is that this constitutes strategic behaviour in the above sense, especially since Alberta is the province best situated to be able to take advantage of the resulting flexibility or asymmetry should it so wish.

I want to conclude with a few observations regarding Alberta and taxation. With its Alberta Advantage slogan, the

province is committed to having the lowest income taxes not only in Canada but in North America. By way of an aside, Alberta's move to a flat 10 percent marginal PIT (personal income tax) rate coupled with equal personal and spousal exemptions/deductions is identical to income splitting (for the Alberta portion of the PIT) and, arguably, has influenced the shift to federal income splitting for pensions and the increased interest in income splitting generally. Returning to the Alberta Advantage issue, proof that living next to a low-tax province generates competitive pressures comes from the fact that BC and Saskatchewan have the second- and third-lowest top marginal personal income tax rates in Canada.

However, the real purpose of this focus on taxation is to express a sincere Ontario "thank you" to Alberta and Albertans because of their eschewing provincial sales taxes, whether of the PST or GST variety. Just as Canada can remain more or less competitive with the US in its personal and corporate income tax rates because the Americans do not have a value-added tax, so too the rest of the

provinces can remain tax competitive (or reasonably so) for income taxation with Alberta because Alberta does not have a PST. Were Alberta to have a provincial sales tax, this would allow it to reduce either or both of its personal and corporate income tax rates to levels that would be most problematic for the other provinces. Indeed, there are even suggestions afoot in some quarters that Ottawa should convert some of its cash transfers into a transfer of GST tax points to the provinces, in the hope that Alberta will not take up the tax points!

This is confirmation that our federation will continue to work in weird and wonderful ways, the only change being that Alberta is now about to take centre stage in this evolution.

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